

VersaBank**First Quarter Fiscal 2025 Financial Results Conference Call**

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Joe Yanchunis

Raymond James — Analyst

Tim Switzer

KBW — Analyst

Andrew Scutt

ROTH Capital Partners — Analyst

PRESENTATION

Operator

Good morning, ladies and gentlemen. Welcome to VersaBank's First Quarter Fiscal 2025 Financial Results Conference Call. This morning, VersaBank issued a news release reporting its financial results for the first quarter ended January 31, 2025. That news release, along with the Bank's financial statements, MD&A, and supplemental financial information, are available on the Bank's website in the Investor Relations section as well as on SEDAR+ and EDGAR.

Please note that, in addition to the telephone dial in, VersaBank is webcasting this morning's conference call. The webcast is listen-only. If you are listening to the webcast but wish to ask a question in the Q&A session following Mr. Taylor's presentation, please dial in to the conference line, the details of which are included in this morning's news release and on the Bank's website. For those participating in today's call by telephone, the accompanying slide presentation is available on the Bank's website. Also, today's call will be archived for replay both by telephone and via the Internet beginning approximately one hour following completion of the call. Details on how to access the replays are available in this morning's news release.

I would like to remind all listeners that the statements about future events made on this call are forward looking in nature and are based on certain assumptions and analysis made by VersaBank management. Actual results could differ materially from our expectations due to various material risks and uncertainties associated with VersaBank's businesses. Please refer to VersaBank's forward-looking statement advisory in today's presentation.

I would now like to turn the call over to David Taylor, President and Chief Executive Officer of VersaBank. Please go ahead, Mr. Taylor.

David Taylor — President & Chief Executive Officer, VersaBank

Good morning, everyone, and thank you for joining us for today's call. With me is our Chief Financial Officer, John Asma.

Before I begin, I will note that you will see a change in a number of terms we use to describe our business. With the start of a new fiscal year and the context of the evolution of the bank, including the US bank acquisition, we have taken the opportunity to update the manner in which we are describing our asset and deposit classes.

The first quarter of fiscal 2025 has been a tremendously busy and eventful one in terms of moving our strategy forward. We signed our first RPP partner in the United States following the US bank acquisition; we completed a very successful \$86 million capital raise, including full execution of over-allotment option to support our US RPP opportunity; we aligned the structure of DRT Cyber to position our digital deposit receipts for renewed opportunity and our cybersecurity service business for planned divestiture; and we accomplished all of this as we achieved yet another record for total assets.

Let me start with the signing of our first US partner post-US bank acquisition. We are thrilled to partner with Watercress Financial, a rapidly growing point-of-sale originator of home improvement loans in the US. Watercress has proven track record of originating high-quality consumer loans through its expanding network of contractors nationwide. It's no accident that our first partner finances the

home improvement sector, as that has been our biggest driver of significant growth in our Canadian business in recent years. Immediately following the agreement, we provided our first tranche of funding, and shortly thereafter our second. Importantly, the program is functioning just as it should and meeting both our partner's and our expectations. We expect our funding with Watercress to steadily expand throughout the year and contribute meaningfully to US growth this year. We are working with multiple other firms in our robust pipeline to add them as our next partners and we are confident that these can be finalized quicker now that we have been through this once. Moreover, with the program now formally functioning in the United States under our US license, we have further evidence of its value for potential new partners.

John will run through Q1 numbers in detail in a few minutes, but I want to highlight a few items to provide some perspective on the quarter:

One, from a consolidated perspective, the quarter reflects the start-up nature of the US operations. That is essentially full cost ahead of any generation of revenue and profits from our US RPP. Specifically, we had close to a full cost load but a de minimis revenue, as we signed our first US partner only at the very end of the quarter.

Two, our Canadian digital banking operations continues to demonstrate the power of the operating leverage in the business; in particular, the power of our receivable purchase program at scale to drive efficiency and return on common equity. I will note here that our Canadian banking operations bear the vast majority of our corporate overhead costs, including our public company costs, so as an indicator of its true potential efficiency and return on equity of our US business, it is actually significantly

understated. And as the US business is expected to be even more efficient than the Canadian business at scale.

Three, I noted on our last call that there are a number of favourable trends that we believe will support incremental expansion of our net interest margin in 2025. While NIM on credit assets continues to be dampened by the lag effect of the atypical inverted yield curve that existed throughout fiscal 2024, we began to see small sequential increases in NIM on credit assets in Q1. This was driven to a large extent by the cost of funds catching up to yields as market interest rates decline. Notably, with an outsized proportion of term deposits coming due in the near term, as well as continued expansion of our insolvency trustee deposits, we expect further declines in our cost of funds in the near term.

And finally, our EPS for the quarter reflects the significantly higher number of shares outstanding in Q1 as a result of our December capital raise. In fact, the weighted average shares of Q1 was 12% higher than Q1 last year. And this is, of course, ahead of being able to put that capital to work, as we have now started to do. As a reminder, this provided a 30% increase in our capital base, which we deploy at approximately 12x or more at around 2.5% spread. That is very accretive.

I'd now like to turn the call over to John to review our financial results in detail. John?

John Asma — Chief Financial Officer, VersaBank

Thanks, David. Before I begin, I will remind you that our financial statements and MD&A for the first quarter are available on our website under the investors section as well as on SEDAR and EDGAR. All

of the following numbers are reported in Canadian dollars, as per our financial statements, unless otherwise noted.

Starting with the balance sheet, total assets at the end of the first quarter of fiscal 2025 grew 15% year over year and 3% sequentially to a new high of just under \$5 billion. Cash and securities were \$545 million, or 11% of total assets, up from 6% in Q1 last year and level with Q4 of last year ahead of expected deployment in Q2. Book value per share increased to a record \$16.03, our CET1 ratio increased to 14.61%, and our leverage ratio was 9.67%, with both remaining above our internal targets.

Total consolidated revenue was \$27.8 million compared with \$28.9 million last year. The small year-over-year decrease was driven by lower overall net interest margin as well as lower non-interest income. Consolidated non-interest expense was \$15.7 million compared with \$12 million in Q1 of last year and \$19.4 million for Q4 of last year, which included one-time expenses mostly related to acquisition. The year-over-year increase reflects incremental operating costs associated with VersaBank USA operations and higher operating cost to support current and anticipated increased business activities ahead of any revenue generation. As a reminder, DRT Cyber expenses are included in consolidated net interest expense and totaled \$3 million for the quarter, which were elevated and I will describe in a moment.

Looking at the income statement on a segmented basis, the vast majority of revenue was, of course, driven by our digital banking operations, and within that, our Canadian banking operations, as we didn't fund our US partner until the end of the first quarter. Revenue for the Canadian business operations was \$23.8 million, up slightly from Q4 of last year. Net income for the Canadian banking

operations was \$8.8 million, or \$0.30 per share. Revenue for US banking operations was \$2 million and income from the US banking operations was \$103,000.

Within DRTC, the cybersecurity component generated revenue of \$2 million, up from \$1.9 million in Q1 of last year. Net loss was \$757,000, impacted by higher operating expenses related to the onboarding support costs for new cybersecurity offerings. Within DRTC, Digital Meteor revenue was \$342,000 and net income was \$33,000.

Our credit asset portfolio grew to a new record, \$4.35 billion at the end of Q1, driven once again by our receivable purchase program, which increased 10% year over year and 3% sequentially to \$3.4 billion. Our RPP portfolio represents 79% of our total credit asset portfolio at the end of Q1, up slightly from the end of Q4.

David previously mentioned changes to the naming of our asset categories. One of those changes was to simplify the commercial real estate portfolio and public sector and other portfolio to the combined multi-family residential loans and other portfolio. Our multi-family residential loans and other portfolio grew 5% year over year to \$928 million. We are seeing the ramp-up of our CMHC-insured loan program, which drove a 2% sequential increase in multi-family residential loans and other portfolio. We currently have \$231 million outstanding at the end of the quarter. As a reminder, our multi-family loans and other portfolio is primarily business-to-business mortgages and construction loans for residential properties. We have very little exposure to commercial use properties.

Turning to the income statement. Our digital banking operations, net interest margin on credit assets, that is excluding cash and securities, was 2.36%. That was 27 basis points or 10% lower on a year-

over-year basis and 1 basis points or 1% higher on a sequential basis, primarily due to the lag effect of the atypical inverted yield curve that existed throughout 2024, which dampened the RPP portfolio margins. Net interest margin, including the impact of cash, securities, and other assets, was 2.08%, which was primarily due to higher than typical liquidity in the first quarter of fiscal 2025 but still remaining among the highest of the publicly traded Canadian Schedule I banks.

Our provision for credit losses, or PCL, in Q1 increased this quarter to 0.09% on average credit assets compared to negative 0.01% last year and with a 12-quarter average of 0.02%. The increase this quarter was due to changes in forward-looking information used in our credit risk models.

I'd now like to turn the call back to David for some closing remarks. David?

David Taylor — President & Chief Executive Officer, VersaBank

Thanks, John.

2025 is off to a great start and unfolding on plan. Looking ahead, we expect another year of solid growth in credit assets. We will increasingly benefit from the operating leverage of our business model as those assets scale. We still expect minimum of low double-digit growth in our Canadian assets with potential upside from increased consumer spending in the lower interest rate environment. That said, we could see this growth dampened if the recent tariff situation is prolonged and meaningfully impacts consumer spending in Canada.

We expect to begin to see a more meaningful contribution of our growing CMHC-insured multi-family residential loan business in our opportunistic real estate portfolio. These zero-risk weighted loans

require no capital and generate a very attractive spread. We are still targeting \$1 billion in commitments by the end of fiscal 2025, although the pace of drawdowns on commitments to date has been slower than expected. Each of these will drive greater efficiency, growth and profitability and higher return on common equity as we continue to capitalize on the operating leverage of our business model. We also expect to see the continuation of several favourable trends that support net interest margin. The yield curve has returned to its normal upward slope. While there's still a lag effect in the very near term, we will see benefit thereafter, increasing in 2025. In addition, we should continue to see the benefit of our low-cost insolvency trustee deposit business as bankruptcy activity in Canada continues to increase.

In the United States, we're off and running with our first partner post US bank acquisition with the benefit of USD\$86 million in capital we raised in December. We have a robust and growing pipeline, as our discussions with both potential partners and others in the industry continue to validate that our RPP is both a unique and very attractive solution for companies who finance big-ticket goods and services at the point of sale. We will grow our US RPP business as quickly as our balance sheet capacity permits. And I will note here, at this time we do not expect tariffs to have any negative impact on the ramp up of our US RPP business. In fact, the uncertainty in the markets could make our RPP solution even more attractive as alternate sources of funding get more expensive.

Finally, we continue to be very encouraged by our favourable stance of the Trump administration on digital assets, which we believe will be very beneficial for our proprietary digital deposit receipts, or DDRs for short, and we are now actively pursuing this renewed opportunity. Our DDRs are highly-encrypted digital assets based on a one for one on actual deposits that combine the safety of a traditional banking with the efficiency, cost savings, security, and flexibility of blockchain technology.

This uniquely provides superior security, stability, and regulatory compliance compared to conventional alternatives. Importantly, our DDRs are backed by the Bank's very own military-grade cybersecurity technology, which we call VersaVault. We have a tremendous head start, having successfully completed a pilot program with our proprietary DDRs provided a secure representation of federally-regulated bank deposits on the Algorand, Ethereum, and Stellar blockchains.

Our DDRs have the potential to be an ultra-low-cost source of deposits funding for VersaBank as well as any bank that uses our technology while enabling consumers and businesses to confidently engage in the rapidly developing field of digital commerce. To pursue this opportunity, we have transferred the intellectual property and other resources related to DDRs to our wholly-owned subsidiary exclusively for DDR assets. The name Digital Meteor is indicative of the potential for DDRs to significantly disrupt the conventional banking deposit framework.

With that, I'd like to open up the call for questions. Operator?

Q & A

Operator

Thank you. Ladies and gentlemen, we will now begin the question-and-answer session. Should you have a question, please press the star followed by the one on your touchtone phone. You will hear a prompt that your hand has been raised. Should you wish to decline from the polling process, please press star followed by the two. If you are using a speakerphone, please lift the handset before pressing any keys.

The first question comes from Joe Yanchunis at Raymond James. Please go ahead.

David Taylor — President & Chief Executive Officer, VersaBank

Go ahead, Joe.

Operator

Joe, please un-mute your line. You are live.

Joe Yanchunis — Analyst, Raymond James

I apologise. Good morning. Let me start over. So the digital deposit receipts, it sounds like a very exciting opportunity. How should we think about that kind of in the near term? And can you quantify the level of these deposits, say by year end, that you would consider a success?

David Taylor — President & Chief Executive Officer, VersaBank

Well, Joe, what we have in mind is piloting the project again in the United States. We completed the pilot project for what we call VCAD, or CADVs, being a digital representation of deposits with our bank in Canada, and now that we have a national bank license in the United States we plan to do a similar pilot, very soon actually. We're working with the regulators to put that together. Once we've had a successful pilot project, then we'll start raising deposits in this fashion, probably towards the middle to the end of the year. And I think it's an extremely attractive product. It's sort of like the modern day checking account where one of our depositors can pay for some goods or services rather than write an old-fashioned paper check, but transfer a digital deposit receipt that, of course, would be insured, in

that it's a deposit with a national bank, to another person's wallet and thereby transact business, sort of like having a certified check, because obviously they are drawn on our bank and our bank's deposits attracts FDIC insurance. So I think towards the end of this year you'll probably see it rolled out, but right now the plan is just to start a pilot in the United States.

Joe Yanchunis — Analyst, Raymond James

Understood. Well, certainly look forward to seeing how that matures and grows over time. And then if we could just pivot over to the non-interest expenses, should we think about this being the current run rate kind of moving forward where we're at right now?

David Taylor — President & Chief Executive Officer, VersaBank

Yeah, I would. Maybe even a little bit more. One thing that impacts our financial statements is the exchange rate in that the expenses we have in the United States are a lot more expensive now in terms of Canadian dollars, and the salaries, of course, the salaries we are paying on the 14 people we assigned to the US bank are, in terms of Canadian dollars, are a lot more expensive. But yeah, that's what I would do. I'd run at today's rate plus a little more maybe and that's a good number to estimate.

Joe Yanchunis — Analyst, Raymond James

Got it. I appreciate that. And then last one for me here. How should we think about, you know, this growth in the US RPP volume as we move throughout the year? How quickly do you think you can ramp that up?

David Taylor — President & Chief Executive Officer, VersaBank

Well, the first account we signed, Watercress, took a little while to plow through the legal work, but shortly after signing we did the first draw, about \$10 million. We did another draw after that, about \$15 million. And it looks like there's a lot more to come. I would look at it as gathering momentum. The next one is in the hopper and the legal work shouldn't take anywhere near as long. So the original targets I gave for the year were in the order of, ah, I think it was USD\$290 million. I think that's easily attainable just with a few RPP partners, and there's quite a number lined up.

Joe Yanchunis — Analyst, Raymond James

All right. I appreciate it. Thanks for taking my questions.

David Taylor — President & Chief Executive Officer, VersaBank

Thank you, Joe.

Operator

Thank you. The next question comes from Tim Switzer at KBW. Please go ahead.

Tim Switzer — Analyst, KBW

Good morning. Thank you for taking my questions. I have a follow up on kind of the trajectory of the US point-of-sale business and the originations there. Can you provide an update on how the

conversations with some of your newer partners are going and what it's going to take for them to want to launch quicker and start originating loans as soon as possible?

David Taylor — President & Chief Executive Officer, VersaBank

Well, it's sort of a matter of doing the paperwork. We have what we call a master purchase and sale agreement and it's a fairly hefty document. Our partners have and their lawyers have to become familiar with it and interact with us. That's sort of what we have experienced in Canada, too. It's a unique new program and it takes a little while to understand how it all operates. But it's just simply do the paperwork. Everybody seems keen and excited. And in fact, we've talked to some partners have huge potential, some of them dealt with us in the past in Canada, so they're familiar with the bank, they're familiar with the personnel actually. So it'll just do like it did in Canada, it'll start gathering momentum. And we got a little bit of help. The alternative financing is securitizations and I guess, unfortunately, due to market conditions, securitizations are getting a little more expensive, this sort of a flight to quality again, which plays into our hand, but of course it's not so good for the stock market and investors.

Tim Switzer — Analyst, KBW

Okay. Thank you. As you begin to ramp up the originations in the US business, how should we think about the capacity of the balance sheet, which I think is pretty large now following the capital raise, versus the loans that you want to put into syndication? And what does that mean for like the related fee income?

David Taylor — President & Chief Executive Officer, VersaBank

Well, as we start to approach our budgeted figure, we'll be sharing the loans through the syndication model with other community banks and maybe some investment firms. We're well underway with that with the program. The software is developed, the software works, and it's easily able to look after it, and we've been working with some large investment banking firms to package the participation into a security that hopefully has a decent bond rating. I'm looking for about AA considering our bank is A with unsecured, which gives a favourable risk weighting on a participant's balance sheet, about 20% versus 75%, 100%. So that will make the product even more attractive.

With respect to management fees, we've been targeting around 1%. It remains to be seen. We haven't concluded a transaction yet. But the more attractive the product is, i.e. bond rating and risk weighted at a very low level, the better fees we'll be able to earn, obviously. And the market conditions, too. When the market is frothy, rates are narrow, and we have to sharpen our pencils, and when the rates, as it seems to be happening now, increase a flight to quality versus higher-risk debt, then we do better.

Tim Switzer — Analyst, KBW

Great. Thank you so much.

Operator

And the next question comes from Andrew Scutt at ROTH Capital Partners. Please go ahead.

Andrew Scutt — Analyst, ROTH Capital Partners

Good morning, guys. Thank you for taking my questions. First one for me here, can you just kind of parse out a little bit more the detail of the impact of the flattening of the yield curve, you kind of talked about the roll off of some of the deposits on the book right now, and just kind of what you see, you know, 2025 trajectory?

David Taylor — President & Chief Executive Officer, VersaBank

Yeah. Thanks, Andrew. Last year around this time we were [inaudible] about our deposit rates, that would be Canadian deposit rates, increasing on a margin over the same term Government of Canada bond, and they got to sort of historical highs, 80, 90 basis points of the same term Government of Canada bond. So those GICs, in Canada they call them GICs or CDs, are going through the system now, they're maturing, so the unusually high margin we were paying over the risk-free rate is diminishing in 2025. So that gives us quite a tailwind on margins. Historically we run around a 3% margin. And so you've started to see it inching up a little bit, but we've only had the beginning of the maturities of those higher-priced GICs go through.

The other thing that's helpful for us, but not so helpful for the rest of Canada, is that there's been a huge increase in bankruptcies, about 26% year over year, might even be a lot higher in the next few months, and while that doesn't bode well if the Canadian economy dampens, consumer enthusiasm to buy things and such, it certainly provides us with a lot more economically priced deposits. So, all in all, keeping those things in mind, our margins should widen back up to where they used to be running, around 3%.

Andrew Scutt — Analyst, ROTH Capital Partners

Great. Thanks for the colour there. Second one for me, a little bit of housekeeping. You guys took a bit of a provision in the quarter. I believe it was due to an accounting change. Can you just provide some details there?

David Taylor — President & Chief Executive Officer, VersaBank

Yeah, we have our provisions based on, as all the other banks do, on forward-looking models. It's a provision for expected losses or possible losses and it's driven by a lot of factors. And we're in a little more unstable credit environment both sides of the border, so our models are producing higher provisions than they have historically. Now mind you, they're still only tiny basis points, one or two basis points versus the industry is around 30 basis points, 40 basis points, but that's sort of what happens when you have disruptions in the credit markets, that the models we use and all the other banks use start kicking up increased provisions for losses. No, they're not losses, but they are provisions for losses.

Andrew Scutt — Analyst, ROTH Capital Partners

Great. Thanks for the time this morning and thanks for taking my questions.

David Taylor — President & Chief Executive Officer, VersaBank

Thank you. Look forward to seeing you soon, Andrew, in California. I'll be seeing you in California, right?

Operator

Thank you. We have no further questions. I will turn the call back over to Mr. Taylor for closing comments.

David Taylor — President & Chief Executive Officer, VersaBank

Well, I'd like to thank everybody for joining us today and I look forward to speaking to you at the end of our second quarter. Thank you very much. Have a good day.

Operator

Ladies and gentlemen, this concludes your conference call for today. We thank you for participating and we ask that you please disconnect your lines.