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PRESENTATION
Operator

Good morning, ladies and gentlemen, and welcome to the Reliant Bancorp's Fourth Quarter 2018 Earnings Conference Call.

Hosting today’s call is DeVan Ard, Reliant’s President and Chief Executive Officer. He is joined by Dan Dellinger, Chief Financial Officer; Louis Holloway, Chief Operating Officer; and Alan Mims, Chief Credit Officer, who will be available during the question-and-answer session.

Please note Reliant Bancorp’s earnings release and supplemental financial information are available on the Investor Relations page of the company’s website at www.reliantbank.com. Today's call is being recorded and will be available for replay on Reliant Bancorp’s website approximately an hour after the conclusion of the call. (Operator Instructions)

During this call, Reliant Bancorp may make statements which constitute forward-looking statements. All forward-looking statements are subject to risks and uncertainties and other facts that may cause actual results and performance or achievements of Reliant Bancorp to differ materially from any results expressed or implied by such forward-looking statements. Many of such factors are beyond Reliant Bancorp’s ability to control or predict, and listeners are cautioned not to put undue reliance on such forward-looking statements.

Additional factors which could affect the forward-looking statements can be found in Reliant Bancorp's annual report on Form 10-K, quarterly reports on Form 10-Q and current reports on Form 8-K filed with the SEC.

Reliant Bancorp disclaims any obligation to update or revise any forward-looking statements contained in this presentation, whether as a result of new information, future events or otherwise.

In addition, these remarks may include certain non-GAAP financial measures as defined by SEC Regulation G. A presentation of the most directly comparable GAAP financial measures and a reconciliation of the non-GAAP measures to the comparable GAAP measures is available on Reliant Bancorp’s website, again at www.reliantbank.com.

I will now turn the presentation over to DeVan Ard, Reliant Bancorp’s President and CEO.

DeVan D. Ard - Reliant Bancorp, Inc. - Chairman, President & CEO

Thanks, good morning, everyone. Thanks for joining us on this morning’s call to review our results for the fourth quarter and the full year 2018. We appreciate your continued interest in our company. We had a very strong quarter and recorded record net income, loans, deposits and assets for our fourth quarter and for the year ended December 31, 2018.
Our fourth quarter net income attributable to common shareholders was up 257% to $4.1 million and EPS was up 177% to $0.36 per fully diluted share compared to the fourth quarter of last year. Our strong earnings growth was due to the contribution from the Community First merger we completed at the beginning of the year, combined with growth in loan volumes and earning assets, higher noninterest income and improved asset quality.

A major contributor to our earnings growth in 2018 was consistent growth in loans and a shift in mix towards a more profitable variable rate lending.

Total loans grew 59.4% from December 2017 to a record $1.2 billion at year-end 2018. Loan production remained strong in the fourth quarter, with $104 million in new loans, an increase of 23% over the same quarter last year.

This was our 14th consecutive quarter of loan growth, and that growth has been focused on building relationships with customers in Middle Tennessee and Chattanooga. We experienced loan growth across our markets, including solid contributions from our new offices in Murfreesboro and Chattanooga. We opened our Murfreesboro office late in the third quarter, and our Chattanooga office opened midway through the fourth quarter. We’re also starting 2019 with a strong and diverse pipeline for new loans that we expect will sustain growth in the first quarter.

As I reported last quarter, we continue to experience strong competition for loans across our markets. Our loan portfolio is built on solid underwriting and risk management practices. We remain focused on lending to quality home builders, real estate developers and small to midsize business customers. At the end of the fourth quarter, we had branches in 7 counties, with Nashville, Davidson County at the core, and we believe we are well-positioned to capture our share of the robust growth in our markets without reducing our focus on quality credits. Dan will provide more details about our superior credit metrics that are a critical part of building our existing loan portfolio, and a significant factor in maintaining our base for future earnings.

The economy in the greater Nashville area remained strong going into the new year. We have one of the lowest unemployment rates in the nation and our local market is growing by about 100 net new persons per day. In recent months, Nashville was named as the new Operations Center of Excellence for Amazon, that will add about 5,000 high-paying jobs, and another 600 quality jobs are projected to be added by E&Y in Nashville. E&Y will add about 200 technology-focused jobs and another 400 tax-related positions to their existing Nashville office that employs about 300.

In January, Volkswagen AG announced that Chattanooga will be home to the company’s first electric vehicle manufacturing facility in North America, with an estimated investment of $800 million and the creation of 1,000 jobs. General Motors also announced that their plant in Middle Tennessee in the Spring Hill area will manufacture the Cadillac XT6, the company’s first electric SUV, adding approximately 200 jobs and a $300 million investment. The GM plant is located in Maury County, a market we acquired with Community First and is a major contributor to Williamson County as well. We believe this additional growth in high-quality, high-paying jobs in our primary markets will drive increased demand for loans in the commercial and residential sectors.

As we mentioned last quarter, we opened our first branch in Rutherford County in the city of Murfreesboro. Rutherford County has a deposit base of $4.6 billion and is home to a strong and diverse economy that includes one of the state’s largest universities, with about 22,000 students, and Nissan’s automotive assembly plant. We’re very pleased with the community’s positive response to our new branch in Murfreesboro, and believe it will be a solid contributor to our loan and deposit growth in 2019.

Our new branch in Chattanooga also contributed to our growth since its opening. With almost $8 billion in deposits, Hamilton County presents us with a significant opportunity for growth in core deposits. We remain very positive about our future as we enter 2019. We have a robust and diverse loan pipeline. The economy across our markets remain strong and growing. We believe that Reliant has additional opportunities to grow organically and through potential acquisitions within our footprint.

Our credit quality is sound, and we have a strong capital position to support our continued growth. Also during 2018, our Board of Directors increased our cash dividend in recognition of our growth and record earnings performance. I want to thank the entire Reliant team for their continued contributions to our results. Our employees work with our customers every day to meet their banking needs. During the past year, they’ve played a very important role in building and cultivating customer relationships that have resulted in our exceptional loan and deposit growth, and we have similar expectations going into 2019.
I'll now turn the call over to Dan Dellinger, our CFO, to review our fourth quarter results in more details.

James Daniel Dellinger - Reliant Bancorp, Inc. - Executive VP & CFO

Well, good morning, everyone, and thanks, DeVan. One of the key drivers of our solid earnings performance for the quarter and for the year is related to the growth in our loan portfolio. As we noted last quarter, loan demand ramped up late in the third quarter and continued into the fourth quarter. With the expected seasonal slowing of loan demand, our fourth quarter loan production remained strong at $104.1 million, a 23% increase over the same quarter of 2017.

Our loans were up 59.4% to $1.2 billion in the fourth quarter of 2018, compared with the fourth quarter of last year. Loans were up 3.1% or 12.4% on an annualized basis since the third quarter. As we have noted in the past, many of these new loans were not fully funded at the origination date, but they represent future growth and at the same time, as the projects are built out, and the loans are funded. At December 31, our top 10 closed new construction loans had $42 million left to fund.

Fourth quarter loan demand for new loans was led by CLD at 38%; C&I at 28%; consumer and 1-4 family loans at 22%; and CRE at 12%. The majority of our loan growth is driven by commercial construction activity and positive economic trends in Middle Tennessee and Chattanooga.

Our organic loan growth has been in the low double digits over the past year and we expect similar growth over the next several quarters.

I wanted to pick up on DeVan’s comments about asset quality and how it’s shaped our loan growth and our earnings performance in 2018. We experienced a solid improvement in our asset quality throughout this year. This was reflected in Reliant’s nonperforming assets to total assets improving to 0.30% in the fourth quarter of 2018, down from a low of 0.46% in the fourth quarter of last year. Total nonperforming loans declined 18.7% to $4.2 million at year-end 2018.

In the fourth quarter, we had net charge-offs of $82,000, and of course, for the entire year 2018, we had net recoveries of $125,000.

Additionally, [credit side] assets declined 19% or $3.2 million from the third quarter, with most of the decline coming at no loss to the bank. At year-end, we had 1 property of $20 million and other real estate owned. Our allowance for loan loss has increased over the past year from 189% for nonperforming loans at year-end 2017 to 269% at year-end 2018.

Our credit team remains focused on high-quality loans while aggressively pursuing loans that demonstrate early weaknesses.

On the deposit front, we were successful in expanding our deposit base through organic growth with the acquisition of Community First. Total deposits rose 62.7% for the year to a record $1.4 billion. Deposits grew 3% from the third quarter, or 12.1% on an annualized basis.

More importantly, our cost rates -- cost relationship deposits, checking, savings and money market accounts, grew 4% during the quarter or 16% annualized. Our continued success in growing deposits during the fourth quarter was partly attributable to our new regional branches in Murfreesboro and Chattanooga. Our Chattanooga deposits were up 43% since the second quarter of 2018, while our Murfreesboro deposits jumped 86% over the same period. Reliant posted record net income of $14.1 million for 2018 or 94.4% from $7.2 million in 2017.

The key drivers for our growth in net income were the completion of the Community First merger, growth in noninterest income and lower provision for loan losses, growth in noninterest income and lower income tax expense. Fourth quarter net income was up almost 257% to $4.1 million compared with $1.2 million in the fourth quarter of last year. Our excellent performance compared with the fourth quarter of last year was due to the same factors, plus significantly lower merger-related expenses in 2018 compared with 2017, when we were finalizing the Community First merger. We believe our solid performance since last year highlights our organic growth and strong economy that is driving our growth metrics.

With that overview of our growth in net income, loans and deposits, I wanted to review in more detail from our -- give more details on our statements of operations and balance sheet. Net interest income rose 52.3% to $13.6 million, up from $8.9 million in the fourth quarter of last year. Key drivers were solid growth in interest fees on loans and higher income from our investment portfolio.
The majority of the increases were due to the growth of average earning assets of 52.8% or $1.55 billion. Most of this was due to organic loan growth, with average loans up 59% to $1.2 billion during 2018. The acceleration in our loan growth was highlighted by average loans growing 20.1% on an annualized basis since the third quarter, compared with average earning assets growing 11.6% on an annualized basis for the same period.

On a linked-quarter basis, interest income rose 5.1% to $18.5 million but was offset by a 19.1% increase in interest expense. Over the past quarter, funding cost increased due to a rise in deposit rates, competition in our market for deposits and higher Federal Home Loan Bank borrowing costs. We also added $11.6 million in subordinated debt as part of the Community First merger that contributed to our growth in interest expense compared to the fourth quarter of last year.

Our net interest margin improved to 3.82% at the end of fourth quarter, up 5 basis points from 3.77% in the third quarter of this year--of last year, sorry, and up 3 basis points from the fourth quarter of last year. After removing the effect of purchase accounting adjustments, our net interest margin was 3.7% for the fourth quarter of 2018, up 3 basis points from the third quarter and down 4 basis points from the fourth quarter of 2017.

Loan yields, excluding fees, in the fourth quarter of 2018 were up 27 basis points from the third quarter of 2018 and up 72 basis points from the fourth quarter of 2017. Loan betas improved on a linked-quarter basis as we began to see a lift in our fixed rate yields and our variable portfolio benefited from an increase in short-term rates.

Weighted average yield on loan production in the fourth quarter rose to 5.6%, an increase of 33 basis points from the third quarter of 2018. Loan accretion from the Community First merger added 13 basis points to our fourth quarter margin compared to 10 basis points in the third quarter. In both the fourth quarter and the third quarter of 2018, we have unused state tax credits. These credits increased our margin by 22 basis points in the fourth quarter and 10 basis points in the third quarter. One of these loans was originated in the fourth quarter, the entire tax credit was realized in that quarter. On a go-forward basis, we expect these credits to influence our margin by approximately 8 basis points per quarter.

Deposit costs grew 22 basis points to 1.44% in the fourth quarter from 1.19% in the third quarter of 2018. They were up 48 basis points from the fourth quarter of 2017. Our deposit betas rose in the fourth quarter, as deposit rates continue to be pressured by competition. As we enter 2019, we believe the deposit betas will slow as we get closer to normalization of rates in our local markets. Our margin has also been affected by the increase in borrowing costs to the Federal Home Loan Bank, the assumption of subordinated debt from the Community First merger and the incremental cost of interest rate swaps that were added in the second and third quarters of 2018.

Total funding cost increased to 1.54% for the fourth quarter of 2018, 20 basis points over the third quarter of 2018; 57 basis points over the fourth quarter of 2017. The total notional value of interest rate swaps were $60 million in the third quarter of 2018 and $30 million in the second quarter of 2018, the remaining $60 million in the fourth quarter of 2018.

Interest rate swaps reduced our NIM by 2 basis points in the fourth quarter and 3 basis points in the third quarter. As of December 31, 2018, 37% of our loan portfolio geared adjustable interest rates, up from 35% at the end of the third quarter. New loan production was more focused on variable rates, with 68% of the fourth quarter’s production gearing adjustable rates. Competition for high-quality commercial fixed rate loans is fierce in our market, although pricing has shown improvement over the past quarter.

Construction loans normally float with prime and remain relatively profitable for us. In the fourth quarter, 31% of our loan production, or $31.9 million, was construction-related. The outstanding balance of our book of construction loans was $146.7 million, with $110.8 million remaining to be dispersed. Additional drivers affecting our net interest margin since the fourth quarter of last year are the lower federal income tax rate that reduced the tax-equivalent yield in our municipal securities portfolio. Our margin was negatively impacted by a reduction in tax-equivalent yield of 11 basis points compared with the fourth quarter of 2017.

Noninterest income in our retail banking segment was down 8.2% over the third quarter. We experienced 9.8% increase in our service charges from the third quarter to the fourth quarter but reported a gain on (inaudible) in third quarter. For the year, noninterest income from our retail banking segment was up 60.8% from 2017, primarily due to higher service charge income and debit card fees. We benefited from an increase in service charges on deposit accounts with the Community First merger.
Noninterest expenses for our retail banking segment, excluding merger expenses, were up 7% from the third quarter of 2018. The increase was due largely to higher expenses associated with the opening of new branches in Murfreesboro and Chattanooga, $233,000 of increased incentive pay compensation and stock option expense, and $115,000 in nonrecurring expenses.

Our tax expense for the fourth quarter of 2018 decreased 111.5% to a benefit of $59,000 compared to an expense of $519,000 for the third quarter. Our tax expense for the year ended 2018 decreased 29.4% to $1.4 million compared to $1.9 million for the year ended December '17. The main driver of the decreases was the addition of the 2 loans with the significant state tax credit, one of which was originated in the fourth quarter of 2018. Another item that contributed to the decrease when compared to 2017 was the $620,000 revaluation of the deferred tax asset that was recorded in December of last year, of 2017.

Lastly, the bank formed an investment subsidiary and transferred it to the investment portfolio to -- in the fourth quarter of 2018. This further reduced tax expenses by $88,000 in the fourth quarter. In 2019, we expect our effective tax rate to be around 14%.

For purposes of GAAP financial statements, the mortgage operation's revenue and expenses were combined with the bank and the holding company and then netted out as noncontrolling interest of the subsidiary. For the fourth quarter of 2018, the mortgage subsidiary generated a net loss of $1.3 million compared with a net loss of $842,000 for the third quarter of '18 and a net loss of $185,000 for the fourth quarter of 2017. As a reminder, our joint venture partner is solely responsible for funding losses in the mortgage operation.

Gains on sale of mortgage loans sold were down [7.44]% from the third quarter, or down 51.3% compared with the fourth quarter of 2017. Before turning the call back over to DeVan, I want to comment on a few additional balance sheet items.

Investment securities available for sale rose $3.3 million or 1.1% from the third quarter. The yield on investment securities was up 11 basis points from the third quarter to 3.94%. Reliant's total deposits were up 12.1% on an annualized basis from the third quarter to $1.4 billion. Compared with the fourth quarter of last year, total deposits are up 52.8% due to organic growth and the acquisition of Community First. As we have noted in past calls, the competition for deposits is intense in the greater Nashville market, and this has put upward pressure on the rates we pay to remain competitive.

As I mentioned earlier, our cost of interest-bearing deposits was up 22 basis points in the last quarter to 1.41%. Our cost for wholesale time deposits continues to increase at a faster rate than our other interest-bearing accounts due to Fed rate increases.

We're working hard to increase the percentage of noninterest-bearing and low-cost deposits through a combination of incentive plans, treasury management enhancements and efforts in branch openings in high-growth markets.

I will wrap up my review with a few comments about our strong capital position. Reliant's total stockholders' equity was up $58.3 million to $208.4 million in the fourth quarter of last year. Our capital ratios continue to remain very strong, with our Tier 1 leverage ratio at 10.17% and our total risk-based ratio at 13.02%.

I'll now turn the call back over to DeVan.

DeVan D. Ard - Reliant Bancorp, Inc. - Chairman, President & CEO

Thanks, Dan. Before I open the call for questions, I want to highlight our strategy for growth, our focus on loan quality and our outlook for the first half of 2019. As I noted in our third quarter call, our Board of Directors approved an updated strategic plan at new year 2018 that focused on growing Reliant Bank by developing our existing markets to enhance our organic growth potential.

Our new banking centers in Murfreesboro and Chattanooga were part of this plan. We’ve ramped up our call activity, expanded our direct marketing programs and added new lenders in key markets. We’re already benefiting from these activities, based on the acceleration of loan and deposit growth that we experienced in the second half of 2018.
We're also continuing to pursue M&A opportunities. Our focus will be on banks in our existing footprint that can provide scale, growth, core funding and that are a good cultural fit for our company.

Dan highlighted the progress that we’ve made over the past year in improving asset quality. We're in a dynamic growth market, and our team has the opportunity to lend at higher levels. However, we're not chasing higher loan volume by lowering our credit standards. We’ve passed on potential deals that do not meet our underwriting standards and have increased due diligence for many potential credits, evaluating not only the credit quality of the deal but the overall market for new projects that are coming online that might have a future impact on the borrower.

Last quarter, I reviewed our loan due diligence process with the Community First merger. As part of that process, we identified about $2 million in nonaccrual loans, net of purchase discounts; $461,000 in loans 90 days past due; and $1.7 million in ORE. Over the past year, we focused on remediation of those nonperforming assets.

Since the first quarter of this year, we’ve experienced a 34.7% decrease in nonaccrual loans; ORE is down 39.4% from the Community First merger date; nonperforming assets to total assets improved by 20 basis points, all without experiencing significant losses.

Our credit team is led by Alan Mims, who's on the call with us today and will be available to answer your questions.

Another part of our strategic plan relates to the culture of Reliant Bank and how our organizational structure affects our profitability. We have embraced a culture within Reliant that ties our employees to our bank's success. We believe this program will drive future profits as we work together as a team to serve our customers and to build shareholder value.

We remain optimistic about the outlook for our company in the coming months. All of our primary markets are strong, and the addition of new jobs, low unemployment rates and low income taxes in the state are very favorable for future growth. Based on the current trends, we expect continued growth in 2019.

Operator, that completes my remarks for this morning’s call, and we'll now open the call for questions.

QUESTIONS AND ANSWERS

Operator

(Operator Instructions) First, we'll hear from Kevin Fitzsimmons with FIG Partners.

Kevin Patrick Fitzsimmons - FIG Partners, LLC, Research Division - Deputy Director of Research

Dan, it was a little difficult to hear you on some of the details. Did you say the ongoing sustainable tax rate to assume for 2019 was about 14%?

James Daniel Dellinger - Reliant Bancorp, Inc. - Executive VP & CFO

Yes, I did.

Kevin Patrick Fitzsimmons - FIG Partners, LLC, Research Division - Deputy Director of Research

And is that consolidated? Is that bank segment only?
James Daniel Dellinger - Reliant Bancorp, Inc. - Executive VP & CFO

That is consolidated.

Kevin Patrick Fitzsimmons - FIG Partners, LLC, Research Division - Deputy Director of Research

Can you -- is it -- what would you call it on a bank segment only, if we're pulling out the mortgage sub?

James Daniel Dellinger - Reliant Bancorp, Inc. - Executive VP & CFO

It's the same, Kevin -- I'm sorry. So the bank, the retail segment would be 14%.

Kevin Patrick Fitzsimmons - FIG Partners, LLC, Research Division - Deputy Director of Research

For the retail segment? Okay.

James Daniel Dellinger - Reliant Bancorp, Inc. - Executive VP & CFO

Yes, that's right. I'm sorry, I didn't realize -- the mortgage piece doesn't get into that.

Kevin Patrick Fitzsimmons - FIG Partners, LLC, Research Division - Deputy Director of Research

Yes, I strip out the mortgage piece altogether. So I just wanted to be sure on the same basis. So looking back to this past quarter, can you give a little more detail on, pulling out one-timers and looking at banks -- the retail bank segment only, it looks like the tax rate was less than 1%.

How should we look at how much benefit was something permanent that we should be factoring in? And was there any -- if this is coming from the state tax credits, was there any linkage over in NII? So in other words, was the benefit that would normally be coming from NII flowing to the tax line in fourth quarter?

James Daniel Dellinger - Reliant Bancorp, Inc. - Executive VP & CFO

Yes, let me address it this way. So for the calculation of our margin, we do include the effect of the state tax credits. So that's why I commented that for the quarter, it impacted our margin by about 22 basis points. However, as you just noted, it doesn't flow through the NII in dollars. It flows through the taxes on the income statement.

So what happened in the fourth quarter, we originated another CDFI loan for $9 million. We had one that was already on there for $13 million. The $9 million carried a 5% credit, so we took a $450,000 tax benefit, while that flowed in the fourth quarter. That $450,000 was added to the, and at the same time, before calculations on margin. Does it make sense?

Kevin Patrick Fitzsimmons - FIG Partners, LLC, Research Division - Deputy Director of Research

Yes.
So Kevin, this is DeVan. Kind of how this works, and it’s not real obvious, but what we have today is basically 3 of these loans that we’re receiving tax credits on. They total about $45 million. Dan just mentioned the one that was booked in the fourth quarter.

All 3 of those loans carry a note rate of 0%. But what we get is we get a tax credit annually on the outstanding balance that’s equivalent to 5% of the loan balance. That’s obviously after-tax, so basically, it gives us a loan yield pretax of a little over 6%.

And so there’s no -- in net interest income, there’s no impact from having these 3 loans with tax credits on them. If you impute an interest rate to that, it’s about $1,250,000 in the year. So the trade-off is no revenue coming through our margin, but you get an effective yield of about 6% from a tax standpoint. Did you understand that?

Got it, I do, so -- but now looking forward, is there any -- this trade-off between taxes and NII, is this same sort of thing going to be playing out in coming quarters? Is it factored into the 14% or is it not? Is it, was it something we just saw this quarter?

It will play out in coming quarters. The tax benefit is an annual number, so we’ll basically get a 5% tax credit in 2019 on the balance of those loans.

So Kevin, yes, I factored it into the 14% on a go-forward basis for taxes. As far as the margin is concerned, on a reported basis, it will represent about 8 basis points per quarter. So our nominal margin on a go-forward basis should be somewhere around 3.6%.

Got it, okay. That’s very helpful, guys. And could I just -- one quick follow-up, can I ask? I know you guys announced a while back the buyback plan, and all the bank stocks have been hit since then. Can you say whether you guys have been out actively buying back? Or are we not at a trigger point yet where you guys would be contemplating that?

Yes, we’re -- today Kevin, we’re kind of at that trigger point, maybe a little bit below that. We went into a blackout period while the stock was still trading above our trigger point. So depending on what happens over the next few days, we may be in the market buying shares back. I mean, we’re ready to do it. We have everything set up. But until the stock dropped below $22 a share last week, we just didn’t have an opportunity to do it.

Don’t you -- maybe I’m wrong, DeVan, but wasn’t it a 10b5 plan, which you’re not subject to the blackout periods? Or am I wrong on that?

No, you’re not wrong on it. We actually just put the 10b5 plan in place.
And next, we’ll hear from Catherine Mealor with KBW.

Catherine Fitzhugh Summerson Mealor - Keefe, Bruyette, & Woods, Inc., Research Division - MD and SVP

I am going to go -- just one more question on the margin conversation. So just to be clear, so the margin this quarter was 3.82%. And so you’re saying that the impact from this tax benefit is going from 22 bps this past quarter to about 8 bps next quarter. And so all in, you kind of, outside of other adjustments, the margin is basically going from 3.82% to 3.60%, just with the impact of the tax rate and the tax -- I mean, the tax credit kind of normalizing. Is that right?

DeVan D. Ard - Reliant Bancorp, Inc. - Chairman, President & CEO

3.60%. It’s 3.60% to 3.61%.

Catherine Fitzhugh Summerson Mealor - Keefe, Bruyette, & Woods, Inc., Research Division - MD and SVP

I’m sorry. Say that again?

James Daniel Dellinger - Reliant Bancorp, Inc. - Executive VP & CFO

3.60% to 3.61% (inaudible) margin.

Catherine Fitzhugh Summerson Mealor - Keefe, Bruyette, & Woods, Inc., Research Division - MD and SVP

Okay, got it, got it. So the margin goes from 3.80% to 3.60%, and then the tax rate goes from (sub 1%) to 14%, so it kind of nets out?

DeVan D. Ard - Reliant Bancorp, Inc. - Chairman, President & CEO

Yes.

Catherine Fitzhugh Summerson Mealor - Keefe, Bruyette, & Woods, Inc., Research Division - MD and SVP

Okay, okay. All right, great. And then, wanted to see what you thought about the expense growth rate going into this year? I feel like we had higher expense growth this year, just with Murfreesboro and Chattanooga. What are you thinking about an appropriate expense rate for 2019?

DeVan D. Ard - Reliant Bancorp, Inc. - Chairman, President & CEO

Yes, let me try to address that, Catherine, since this is always a little bit confusing with the segment report in our earnings release. And just kind of focus on the retail, the bank segment reported part of that, since the mortgage company noninterest expense is going to bounce around a good bit depending on the amount of volume that they do in lending.

And we did have -- the fourth quarter was up, at the bank level, anyway, and this includes holding company expenses, was up about $670,000 over the third quarter. About $350,000 of that was nonrecurring, so we tried to address some of it in our earnings release. We had some marketing and
promotional and supplies expense related to the new branches. We had a true-up in some of our comp plans for bonuses and incentive pay that occurred based on the bank's performance.

And then, we had about $115,000 in nonrecurring expenses that were related to a couple of M&A opportunities that we looked at. So that gave you about $350,000 in nonrecurring that was about half of that $670,000 increase in fourth quarter.

We're modeling about $10.4 million in noninterest expense in the first quarter of this year. So you'll have kind of a full load of all the expenses, occupancy and personnel, related to Chattanooga and Murfreesboro in there. And then we've made some technology investments as we moved into 2019 as well. But that's $10.4 million in the first quarter, and it will be relatively flat from there on out through the rest of the year.

Catherine Fitzhugh Summerson Mealor - Keefe, Bruyette, & Woods, Inc., Research Division - MD and SVP
Okay, got it. And then maybe one follow-up on the margin with regard to the FTE adjustment?

DeVan D. Ard - Reliant Bancorp, Inc. - Chairman, President & CEO
She just asked about FTE adjustment.

James Daniel Dellinger - Reliant Bancorp, Inc. - Executive VP & CFO
Yes, I couldn't -- what was your question, though, Catherine?

DeVan D. Ard - Reliant Bancorp, Inc. - Chairman, President & CEO
Is about the securities?

Catherine Fitzhugh Summerson Mealor - Keefe, Bruyette, & Woods, Inc., Research Division - MD and SVP
I feel like it -- yes, well, the FTE adjustment, I feel like, bounces around a lot. Just curious -- or maybe not bounces, it's been increasing a lot this year. So how should we think about what level of the FTE adjustment we should be looking at next year?

James Daniel Dellinger - Reliant Bancorp, Inc. - Executive VP & CFO
Catherine, I think that's probably going to range around 10 to 11 basis points, just based on our portfolio yields, NIM.

Operator
(Operator Instructions) And next, we have Joseph Fenech with Hovde Group.

Joseph Anthony Fenech - Hovde Group, LLC, Research Division - Managing Principal & Head of Research
DeVan, I guess on the loan growth outlook, some management teams are getting on fourth quarter calls and just cautioning on loan growth for this year, but not really based on what they're seeing in their markets, just on the headlines they're reading about a potential slowdown in GDP growth.
It sounds like you feel like your markets are still very well insulated from the projected trends in the economy more broadly, you continue to deliver on that growth we've seen the past few years. Is that a fair assumption? Any caveats to that? Or you feel like you can deliver on what you have done the past few years, this year?

**DeVan D. Ard - Reliant Bancorp, Inc. - Chairman, President & CEO**

I think we can. The economy in the Middle Tennessee area and in Chattanooga looks like it has still got a good bit of momentum. We had a good year in 2018, and we’re kind of looking at somewhere between 12% and 13% growth. That’s point-to-point growth.

If you look at our average outstandings from the third and the fourth quarter, you saw it’s a big [increase]. We were up about 5% in terms of average outstandings in our loan portfolio. I think part of that, Joe, was good new production, but we’ve also seen in the last, I’d say, 3 to 6 months, a kind of a slowdown in some of the payoff activity that we experienced in 2017 and part of 2018. As rates have moved up, it’s just less and less attractive to refinance loans.

So that activity has slowed down as well. We’ve hired some new lenders. We’re getting some good traction in Chattanooga and Murfreesboro, that we really didn’t have last year, without having a full-service banking center. So I think that 12% to 13% increase on a point-to-point basis in 2019 is attainable.

**Joseph Anthony Fenech - Hovde Group, LLC, Research Division - Managing Principal & Head of Research**

Okay. And then how much of that projection, DeVan, is that constrained at all?

(technical difficulty)

**Joseph Anthony Fenech - Hovde Group, LLC, Research Division - Managing Principal & Head of Research**

Yes, can you hear me?

**DeVan D. Ard - Reliant Bancorp, Inc. - Chairman, President & CEO**

Yes, I can hear you.

**Joseph Anthony Fenech - Hovde Group, LLC, Research Division - Managing Principal & Head of Research**

Okay. Is that loan growth projection constrained at all by expectations on the funding side? In other words, like if the funding environment were what it was 2 to 3 years ago, where do you think you could kind of comfortably grow loans? I'm just trying to get a sense for where the economy, just from a demand standpoint, where things stand relative to 2 years ago, taking the funding component out of it for a second, if that makes sense.

**DeVan D. Ard - Reliant Bancorp, Inc. - Chairman, President & CEO**

Yes, it does make sense. I think the forecasted growth rate that we have, at least for the next 12 months anyway, is not constrained by the funding side. If you look at our earnings release and look how we broke out the deposit categories, one of the more encouraging things to me was that the low-cost deposit accounts, what I always talk about as relationship accounts, we actually grew at a faster pace in the fourth quarter than we grew loans.
Now it's not as cheap as it has been, but I think we've got a -- I think we've still got an opportunity to grow deposits. We are in markets in 2019 that we just really kind of barely scratched in 2018. I talked about the Murfreesboro and Chattanooga combined, they have about $11 billion in deposits in those markets.

And we've been pretty aggressive in doing some advertising and direct marketing and doing some deposit specials in those markets, and are seeing some good results from that. So I don't anticipate funding in 2019 to be a constraint on our ability to meet our loan targets.

Joseph Anthony Fenech - Hovde Group, LLC, Research Division - Managing Principal & Head of Research

Okay, so it's not like you'd be growing 15%, 16%, 17% because of funding. 12% to 13% is what you see as sort of a legitimate growth rate the market is offering you within the credit standards that you have?

DeVan D. Ard - Reliant Bancorp, Inc. - Chairman, President & CEO

Yes, that's correct. That's right.

Joseph Anthony Fenech - Hovde Group, LLC, Research Division - Managing Principal & Head of Research

Okay. And then I guess, lastly for me, just on the margin, fair to say that for the faster growers like yourselves, that a pause by the Fed could kind of have a disproportionate benefit to you all as the asset side maybe catches up a bit and the funding side slows a bit. Are you really seeing 2019 as, if the Fed does take a pause here, to year-over-year able to show some decent margin expansion?

DeVan D. Ard - Reliant Bancorp, Inc. - Chairman, President & CEO

Yes, I think that's a fair assessment. We still saw deposit rates going up in the fourth quarter, and we're modeling higher rates in the first quarter this year. But when I look at, let's say, a comparison between December and January, I know it's just 1 month, but we -- typically through 2018, we saw increases every month. In January to December -- excuse me, December to January, it's been pretty flat. So I'd say absent a rate increase, I would expect to see deposit increases moderate some.

On the other hand, when I look at our loan yields, they have been moving up. That's a combination of new loan production at higher rates and maturing term loans that we have a chance to reprice up. We've got quite a few of those coming up in 2019 as well.

But we did -- our loan production in the first quarter of 2018 was at an average -- a weighted average rate of 5.12%. And we moved that up to 5.60% in the fourth quarter. So that's a significant increase in production. A lot of that fourth quarter production has not actually hit our books yet in terms of funding because it was construction related.

So yes, I think there is an opportunity, if rates stay stable, for us to see some expansion in our margin. I don't know that I would see it much in the first quarter, Joe, but certainly, second quarter and maybe going forward.

Joseph Anthony Fenech - Hovde Group, LLC, Research Division - Managing Principal & Head of Research

Yes, I was going to suggest that maybe first quarter looks a bit like the fourth quarter. And then if there is a pause in March, second and third quarter is where you start to see that pick up.
DeVan D. Ard - Reliant Bancorp, Inc. - Chairman, President & CEO
I think that's right.

Operator
And at this time, it doesn't appear that we have any further questions from the audience. I'd like to turn the floor back to management for any additional or closing remarks.

DeVan D. Ard - Reliant Bancorp, Inc. - Chairman, President & CEO
I appreciate everybody's support. Thanks for joining us today.

Operator
All right. Ladies and gentlemen, that does conclude our conference for today. Thanks for joining us. You may now disconnect.