MidWestOne

2nd Quarter 2017 Earnings

July 31, 2017 at 12:00 PM Eastern

CORPORATE PARTICIPANTS

Charles Funk - *President and CEO*

Kent Jehle –*Chief Credit Officer*

Katie Lorenson – *Chief Financial Officer*

Kevin Kramer – *Chief Operating Officer*

PRESENTATION

Operator
Good afternoon and good morning, and welcome to the MidWestOne Financial Group Inc. Second Quarter 2017 Earnings Conference Call. All participants will be in a listen-only mode. Should you need assistance, please signal a conference specialist by pressing the star (*) key followed by zero (0). After today's presentation there will be an opportunity to ask questions. To ask a question, you may press star (*) and then one (1). To withdraw your questions, you may press star (*) and two (2). Please also note today's event is being recorded. At this time, I'd like to turn the conference call over to Mr. Charles Funk, President and CEO. Sir, please go ahead.

Charles Funk
Thank you very much, Jamie. Good morning or good afternoon, to everyone. I will begin as I normally do with the forward-looking statement, which simply says this presentation contains forward-looking statements relating to the financial condition, results of operations, and business of MidWestOne Financial Group, Inc. Forward-looking statements generally include words such as believes, expects, anticipates, and other similar expressions. Actual results could differ materially from those indicated. Among the important factors that could cause actual results to differ materially are interest rates, changes in the mix of the Company's business, competitive pressures, general economic conditions, and the risk factors detailed in the Company's periodic reports and registration statements filed with the SEC. MOFG undertakes no obligation to publicly revise or update these forward-looking statements to reflect events or circumstances after the date of this presentation.

And with that, I will again say thank you for joining us on the call this morning. We felt like the second quarter was definitely progress, it was definitive progress. I think we're beginning to gather some momentum in our Company and our numbers are reflective of that. And I think the numbers also reflect lots of hard work by many individuals over the last 24 months. We still have a few challenges, which I will outline, but there were certainly a lot more positives in the second quarter. To briefly review by the numbers, the return on assets is approaching 1%, return on tangible equity at roughly 11.9%, certainly within our strategic comfort zone of 11% to 14%. And the efficiency has come down a little bit quicker than we'd forecast, 58.5% for the quarter. There were a few recoveries of nonaccrual loan interest income that helped during the quarter. We also had a small one-time adjustment positive from our DP core provider in the neighborhood of $150,000.

Talking for a minute about the balance sheet. A good quarter for loan growth, albeit late loan growth and you can see that in the discrepancy between the ending balance and the average balance, as I think we did preview that on the last earnings call last quarter. The last 2 weeks of June were very, very busy times for large loan closings and a couple of those were large, large balance transactions. We continue to see good commercial real estate volume from the Twin Cities footprint and really steady continued activity in Florida and in Iowa City. And as we reflected in the earnings release, we had about $20 million in loans from our new Denver office, which basically just opened on May 1st. And I will also say that almost all of that growth was in C&I loans, which we really appreciate.

The pipeline is starting out to be decent in the third quarter in terms of loan growth. I would say it's not quite as visible as it was a quarter ago, but nevertheless, we do expect loan growth this quarter. And in fact, the loan growth, we have had some loan growth during the month of July.
I would say that I'm not really all that concerned about our ability to grow loans. I think we've

proven we can do that, and I think we will continue to move the needle forward in loan growth. In terms of deposits, a little more concern there. I think there was some seasonal outflow during the second quarter, and we did see a few of our larger core accounts that use money, commercial enterprises that use money for various reasons. I would attribute that a little bit to the business cycle. I think that the largest challenge we have as a company right now is in continue to grow our core deposits and, because we need our core deposit growth to continue to support our asset generation, and as I said, I'm not as concerned about our ability to generate good quality loans.

With that said, we did see a couple of very, very nice core deposit wins during the quarter; accounts that were in the $5 million to $10 million range. One of those won't close until, ah, either close in July or will close early in August. And more notably, these wins were in two of our smaller markets, which I appreciate very, very much. I would give some guidance. I think our loan-to-deposit ratio is likely to head higher in the near term. It wouldn't surprise me if it goes into the low 90s. Our comfort level has always been in the 80s, but we certainly feel like we have the liquidity to support a loan-to-deposit ratio in the low 90s and I suspect that's probably where it's headed over the next quarter or so. In terms of the net interest margin, we, the core margin, of course we've got the accretion income in there. The core margin we calculate to be up 2 basis points to 365. With the recovered interest on loans, it was 372. And that would be part of the core margin. We think that the core margin has hung in there pretty well. And, you know, the pricing remains very, very competitive on high-quality loans. I would say that on some of the medium-quality loans, the pricing seems to be a little bit more reasonable, but the loans that are really strong quality deals, there's no shortage of lenders at the table. We've had to sharpen our pencil. We've let some go. We continue to see a few deals that are priced in the 3s for 5 years. By and large, we pass on those. No change there.

In terms of deposits, our cost of funds, you notice, was up 3 basis points during the quarter. Our core accounts have moved very little, if any. CD rates certainly going higher at the margin, and I don't think that's unexpected. I think where the change is, and we may have talked about this in the last call, but certainly we saw more of it in the second quarter, is the large depositors who keep their balances in either repo or money market accounts or whatever. They are definitely rate sensitive. And if, you know, when the Fed raised rates we had to adjust some rates. That doesn't get reflected, perhaps at the margin on the core accounts, but some of the larger depositors are definitely rate sensitive and I think that would account for most of the 3-basis point increase in our cost of funds. I think a little bit of our ability to maintain margin depends on core deposit growth to support loan growth. If we have to start going into that, into some of the alternative sources for loan growth, that would put pressure on our margin. But I'm not forecasting that. I am saying that we have to grow core deposits and that's probably the major push in our Company today.

In terms of noninterest income, and I'll go in no particular order here. I think we talked in the last earnings call that we did hire a new leader for our home mortgage center and I'm very, very pleased with this leader. I think the progress is a little harder to see in our income statement, because there's always been, there has already been a fair amount of progress in expense control, as he approached some of the low-hanging fruit. You won't see it yet in terms of a lift in revenue, but that will come. I think it probably comes as this year unwinds, I think you'll see a little bit of it in the third quarter. You'll see more of it in the fourth quarter as we get a better margin and more per loan in terms of loan generation that we have. I will also add that we've added a few producers in the Twin Cities area, which let's just say, they're good team members, they understand the importance of cross-sell and wallet share, and we're looking very, very hard to add a producer in our Florida footprint and eventually in our Denver footprint. We would hope

to roll those out sometime over the balance of this year. You won't see a lot of progress in our numbers from the home mortgage center, but I'm very, very pleased and positive over the next 18 months that that will start to show a discernible difference in our income statement.

Wealth management had a good quarter. The trust department continues to be very consistent. They're a steady grower. The investor center, which is our brokerage, had a nice rebound. They're almost to budget, and we're beginning to see a little bit of traction in the Twin Cities and continue to work very hard to add producers in the Twin Cities in the investor center. I will say that the Department of Labor ruling has had a negative impact both on top line and bottom line revenue in this department and there's really nothing we can do about that, but we continue to support the efforts to reverse this ruling. Insurance is a very small piece of the pie, but our insurance agency had the best six months they've ever had, and all three entities in wealth management had a nice quarter. Service charges are a little bit under our projections and there's really no specific reason why, but we continue to pay attention to that to get our arms around fee waives which there may be a few more of those than we would like, but the miss there wasn't a great miss. Our expenses, very, very good news on expenses. I think there are a few more efficiencies yet to come over the balance of 2017. But I think now we're getting to the point where we just need to manage our expenses very closely and if we do that, these numbers should take care of themselves.

I want to take a minute and talk about asset quality, which was better. We calculate that the net charge-offs were a little bit higher. They were at 17 basis points for the quarter. We did, I feel like I should point out that when we had the charge to the provision in the fourth quarter, we did impair one loan and that was charged-off and that was fully accounted for in the loan loss reserve. If you take that out it was a 10-basis point quarter, but the reported number was 17 basis points. And we calculate that we're running at about 15 basis points for the calendar year 2017 and 11 basis points if you exclude what we'd already provided in the reserve. Looking ahead, based on what we know now we think 10 to 12 or 13 basis points should catch it for the balance of this year in terms of net charge-off. And there's been a lot of progress on the nonaccrual and problem credits. The large Iowa City credit that we've talked about for 18 months is still on nonaccrual, but it's fair to say that we all believe that they sit in a much better place today than at any time in the last 18 months. That said, we've left it on nonaccrual out of an overabundance of caution. In terms of agriculture, which I think everybody wants to know about. It depends where you sit in the state of Iowa right now, which is where our Ag loans are. If you're sitting down in Oskaloosa, which is the Southern part of our Iowa footprint, they need rain and there's a little bit of stress there. The bulk of our Ag loans in our Iowa footprint are in Central and North Central Iowa, where they have really very good growing conditions. They've had ample amounts of rain, a little bit of hail damage, but by and large the crops are very, very good in that part of the footprint.

As we've said before, the balance sheets continue to weaken in agriculture. I don't think that's unique to MidWestOne and our borrowers. We will be doing mid-year farm visits in the next month or two. And I think we just continue to see, to have an abundance of caution. We have run stress tests. We're in the process of running another stress test on our Ag portfolio. I don't think that will be much different than the stress test we ran 12 months ago. But I think most of the migration in Ag continues to be from pass to watch. There haven't been that many credits that have migrated to substandard or worse. The news there really isn't a lot different other than the crop update.

We have, we are getting to resolution on a loan that really has been a problem loan since our 2008 merger and it's been a TDR, probably for the last 4 or 5 years. And we expect some

resolution on that, although we're not sure how much. There was some resolution during the second quarter. There will be more during this quarter. There is a chance that we might get a nice interest recovery, but we'll have to see how it plays out. But the bottom line is we're fully secured, we will not take a loss on this credit. The only question is when does the whole thing go away.

In terms of our historical level of reserve on non-acquired credits has been in the 140 to 150 level, it's at 120 right now. That's supportable, by the way, in our internal calculations. But those of you who have been exposed to our Company for a period of time, we like to run in the 140 to 150 range, there will be some effort to get the reserve to that level over the next 6 to 12 months, but it's hard to be more specific in that. If we get some of these interest recoveries that we're talking about, some of that will go straight to the reserve and we just think that shouldn't be taken as alarm, it's just taken that we'd like to build the reserve a little bit more, even though our internal calculations support where it is right now.

I will also talk about the FDIC loss share exit. We think that will be a modest positive going forward. I think there will be a little positive that comes from that during Q3. How much, we don't know, but we feel very, very good about getting out of that arrangement.

In summary, Florida, Denver, the Twin Cities are going very well. Iowa City is going well. And I would say that the rest of our footprint, as we've said before, roughly 30% to 35% of our footprint is exposed to small town America and small town America is just not doing as well right now as other parts of, as more metro populations. In terms of M&A, a fair amount of effort and discussion on M&A this quarter, probably the most active in terms of discussion and running numbers as we've had in a while. I would say that we see prices as being very aggressive in the community banking space. nothing’s really changed other than there is a lot of discussion and it’s taking more and more of our time, but certainly, there is nothing imminent that we would want to discuss on this call.

In terms of capital, I think we're in good shape on capital. Our tangible, ah, tangible equity at between 8.8% and 8.9%, that's as strong as it's been for a while. The dividend increase at mid-year is a little bit unusual for us. We typically do all of that in January. But given where we sat in January, we wanted to have a dividend increase. But we decided that because we've shown so much progress in the Company, we wanted to do another, a little bit and we did $0.02 and we did that at the last board meeting.

In summary, I would say the Company is coming together pretty well. We still have the potential to put up a nice second half of the year. I think our best days are yet ahead of us. I do want to take a minute and talk about Denver, because Denver has exceeded our expectations at 6/30, and we've put this in the earnings release, $21 million in loans, $11 million in deposits. They currently sit at $28 million in loans and $17 million in deposits. And what I really appreciate about our Denver folks, our commercial bankers and our treasury management person, is that they're really doing a good job of funding the loan volume that they're bringing to the table. And they are cheap deposits and they're doing a very, very nice job of that. As I've made a few calls, it's a very high caliber of customer that they're bringing to the bank. Almost all of it's C&I. I think Denver is way ahead of the schedule that we'd laid out. The goal is for them to have a breakeven run rate by the end of this year, and that's well ahead of what we expected whenever we first came to the table. We’ll see if we can achieve that, but that's the stretch goal that we've put in front of them for right now.

Again, I would say the two things we're working the hardest on is to make sure that we get

momentum in all of our markets on core deposit growth. And the second would be to build the loan loss reserve to a little bit more robust level that's more in keeping with our numbers. Those of you who've been with us for a while will remember when it was just the old MidWestOne, we consistently ran in the 145 to 160 as a percentage of our loans, and while we realize we won't get back to that point in the short term, we just think that our Company operates a lot better if we can figure that out and still deliver the returns that shareholders expect.

With that, we will turn it to the Q&A. I do have Katie Lorenson is joining us by telephone, our Chief Financial Officer. I have our Chief Credit Officer, Kent Jehle and our Chief Operating Officer, Kevin Kramer, in the room here in Iowa City. And with that, Jamie, I will turn it back to you for the Q&A.

QUESTIONS AND ANSWERS

Operator
Ladies and gentlemen, at this time we will begin the question-and-answer session. To ask a question you may press star (*) and then one (1). If you are using a speakerphone, we do ask that you please pick up your handset before pressing the keys to ensure the best sound quality. To withdraw your question you may press star (*) and two (2). Once again, that is star (*) and then one (1) to join the question queue. Our first question today comes from Jeff Rulis from D.A. Davidson. Please go ahead with your question.

Matt Yun
Good morning. This is Matt on for Jeff. My first question is about loan growth. I believe in the past you guys gave guidance of 4% to 5% loan growth for the year of 2017. Do you still think that number is attainable?

Kevin Kramer
Thanks Matt, this is Kevin Kramer. Yeah, as we roll into, you know, halfway through the year, we had a slow start on loan growth in the first quarter. We reported second quarter, as we had earlier reported, was much stronger. It's now normalized that we do think we're going to be on a growth rate of 3% to 5% each quarter. As you look at the way the year-end wraps up, yes, it's attainable. It will be a little bit of a stretch to hit that guidance we provided at the beginning of the year, but the momentum is definitely there and we're definitely on a run rate for 4% to 5% at this particular point. But the way pipeline looks, it’s definitely attainable.

Matt Yun
Sounds good. And one more question in regards to the core margin. Could you give, sorry if I missed it, but could you give a run rate on where you expect that going in the future?

Kevin Kramer
Go ahead, Katie.

Katie Lorenson
I'll take this question. Again, we saw the core without those one-times from the nonaccrual adjustments, we saw the core move from 363 to 365. We've kind of talked all year about how we expect that to be pretty stable, with the bogey being the deposit cost of funds. I would stick with that guidance of stable at the core of 360, mid 360s.

Matt Yun
Thanks for the color. I’ll step back.

Charles Funk
Thank you, Jeff.

Operator
Our next question comes from Andrew Liesch from Sandler O'Neill & Partners. Please go ahead with your question.

Andrew Liesch
Good morning everyone.

Charles Funk
Good morning, Andrew.

Andrew Liesch
I just wanted to touch on expenses here. The core, I mean, backing out the depreciation and the amortization, what, about $19.2 million. It sounds like there may be some more efficiencies ahead, maybe a little bit out. Could it get south of $19 million or is that sort of a good way to build off of?

Katie Lorenson
Hey Andrew, this is Katie. I think with Denver, it definitely does not get south of that number. Our projections without Denver had it just right around the $19 million, maybe slightly under by the end of the year. But again, with Denver coming in at a run rate of $300,000 to $400,000 of expense per quarter, we're going to creep back over that number. Again that's excluding the amortization, as you noted.

Andrew Liesch
Right. Okay. That's very helpful. And then along the, following up on the core margin, as this loan growth that came on later in the quarter, I would imagine the earning asset mix might look better this quarter. Do you think maybe a little bit more than just mid-360s just simply because of the math of the earning asset mix?

Katie Lorenson
Yeah, we could see it go up again. I, my caution comes with the deposit cost of funds, which I mean, the increase is modest this quarter by 3 bps, but it is increasing every quarter, but yeah, I think we, depending on how that mix changes, it's stable to maybe slightly increasing.

Andrew Liesch
Okay. Very helpful. Thanks so much.

Katie Lorenson
Um hmm.

Charles Funk
Thank you, Andrew.

Operator
Once again, if you would like to ask a question, please press star (*) and then one (1). Our next question comes from Nathan Race from Piper Jaffray. Please go ahead with your question.

Nathan Race
Hey guys. Good morning.

Katie Lorenson
Good morning.

Charles Funk
Good morning Nathan.

Kevin Kramer
Good morning.

Nathan Race
Just following up on the commentary on the margin going forward, just thinking about deposit costs and pricing at this juncture. Can you kind of just give us an update in terms of where you guys are seeing the most pricing pressure across the footprint? It sounds like some larger relationships are also driving the increase. Just any guidance in terms of what we can expect for deposit costs in the back half of the year would be helpful.

Charles Funk
Well, I think that depends on what happens with the core accounts. And you know how it works, Nathan, if, when one or two banks raise the savings account rate or the interest checking rate and all these rates, then people follow. As of yet, we haven't seen that. There's been a lot of talk. I don't know if it's true or not that the large banks will lead this time. We haven't seen that in our footprint. We do notice in Iowa that there's a little bit of pressure now coming from the credit unions, but interestingly enough from what I can tell, it's not on their core accounts, they're creating new accounts, which is very positive because you don't have to go in and raise your core rates.

I think a lot of it depends on when the first domino falls with the core rates, then there you go. It's going to be all banks, not just ours, that have to respond. Now having said that, I'll go back to my comments that the large borrowers are already there. We’re probably okay right now, but if the Fed raises rates again, they're going to want 10 to 15 to 20 basis points of that increase. And those are the deposits that are $5 million to $10 million and larger. That’s kind of where we are. The CD thing, you know, that's not surprising and that's a small part of our cost of funds and that basically builds over time, but really doesn't have much effect from one quarter to the next. I would expect behavior similar to what you've seen. But that all changes if the Fed raises rates again or if somebody decides that the core rates need to go up. Sorry for the long answer, but it's a complicated question.

Nathan Race
No, I appreciate that color. That's helpful. And just maybe switching gears, going back to your commentary on the M&A discussions during the quarter. It's obviously encouraging to hear that discussions are picking up of late. Can you kind of just provide maybe some additional color in terms of where, in terms of the geographies where you guys are having a pick-up in conversations and maybe just provide some color around the size of depositories that you're talking to of late?

Charles Funk
On the small side in both Minnesota and Iowa and one that was out of footprint that quite frankly, is an attractive opportunity. I'm just not sure it's for us and we've sort of put that one on

hold for the time being. But really in Minnesota and Iowa and one out of footprint.

Nathan Race
Okay. Got it. I appreciate all the color guys. Nice quarter.

Charles Funk
Thank you.

Operator
Once again, if you would like to ask a question please press star (*) and one (1). Our next question comes from Brian Martin from FIG Partners. Please go ahead with your question.

Brian Martin
Hey guys.

Charles Funk
Hi Brian.

Kevin Kramer
Hey Brian.

Brian Martin
Hey Charlie, just your last, on that last question on the M&A. I mean, the one that you put on hold, is that because the others are more interesting or more, maybe, and I don't want to say further long, but just better opportunities or is it just, it's just the out-of-footprint is less enticing at this point because the opportunities are better?

Charles Funk
Well, I think a little bit of all of the above. I think certainly, very much more complex than the ones that are in footprint. And for that reason, you know, I'm a big believer that you really should deal with one thing at a time and that's sort of what we're doing right now. There was a deal that hasn't been announced yet, but we were unsuccessful in one part of our footprint. We're continuing to have discussions in our footprint. I think the complexity of the out-of-footprint deal is probably arduous for us to take a step back and see where these other discussions lead us if that helps a little bit.

Brian Martin
Yes, I mean, it seems like the opportunity in Denver is pretty enticing and rewarding, I guess, from the shareholders perspective going forward and a better use at the moment. You've talked a lot about the funding, Charlie. I guess it seemed like when the expansion into Minnesota was going to allow you to kind of make some progress on that front. I mean, how are things trending up on the deposit side up in the Twin Cities market? And I guess, is that, is it going kind of as expected? Is it slower up there? With the, I mean, given all the competition historically that's been in Iowa it seemed like that was going to be a benefit or at least help alleviate some of the pressure, the competitive pressures. Has that kind of been tracking as you guys think or not necessarily?

Charles Funk
May I just be honest with you and tell you it's behind our projections. We're disappointed. We don't have a lot of traction with the exception of couple of our Wisconsin offices that really got into the religion on deposits and they've been out making calls and they've had some, one of the

successes that I detailed came from one of our Wisconsin markets. But in the Twin Cities, we don't have a lot of traction right now. It's not because we're not talking about it, but that's one that we still need to work on and I can assure you that Kevin Kramer and I talk about this every single day. And he gets tired of me talking to him about it, but just an honest answer to your question, Brian.

Brian Martin
Yeah. Okay. All right. And just the part of, maybe just for Katie, just on the margin. Can you just talk about, when you talk about the kind of stability, if you will, in the core margin. Just as you think about if there are further increases versus no increases, just kind of how things trend under both of those scenarios. Is it pretty similar or is it, if you can give contrast if there is?

Charles Funk
Well, yeah, I'll start on that and Katie, I'll let you add if I miss something or you have something to add. I mean, I think the worst possible scenario for us is a flat yield curve and the yield curve gets flatter. All of our ALCO models show that. And, you know, in my 38 years now in banking, I've always observed that the banks I've worked for, the times when our margin was under the most pressure came from when the yield curve got very flat. One of the things I think that could help mitigate that is the fact that our Denver folks are bringing a lot of variable rate things to the table. I think that C&I bent, and Denver will continue to grow loans. They will continue to grow loans and a lot of those will be C&I opportunities. That could mitigate a little bit, Brian.

But I think, if the Fed doesn't increase rates for the rest of this year, I think we can hang in there right where we are unless once the dominoes start to fall, which I've already talked about. I think if the yield curve gets flatter and now, let's face it, our Minnesota bankers have been very successful in commercial real estate and we've been able to get north of 4%. The 4.25% and 4.375% on a lot of the 5-year deals, which we can do just fine with those rates. If those start to come down to where they're 4.10%, or 3.95% or 3.75%, then that's a problem. It's not just a problem for our margin, that's a problem for everybody's margin. Let’s see what happens to the current yield curve. But in general, a flattened yield curve is not our friend, a flatter yield curve is not our friend.

Brian Martin
Gotcha. Okay. All right. And then maybe just, it sounds as though you’re a bit more cautious on credit, Charlie, not saying there is anything bad coming, but I guess, is, would you sense that the caution is more related, it sounds like it's more related to the, I'll call it the commercial portfolio, not the ag portfolio. Does that seem fair? Because it sounds like you're not seeing much migration trends, different migration trends in the Ag book. I guess it seems to suggest maybe it's elsewhere, if there is just a general caution. Is that fair or just maybe if you can just talk about kind of the methodology to kind of rebuild the reserve to historic-type of levels?

Charles Funk
Well, thank you for asking the question because I wouldn't say it's any more cautious than it was a quarter ago. But what I am saying is, if 9% of our loans are to agriculture. And then if you take the related businesses, you get up to maybe 1/6 of our loan portfolio. I just think anybody who’s involved in agriculture right now, we're in the second or third or fourth year of a tough time. I think you just have to talk about caution. I don’t think it's any more cautious than it was a quarter ago. In fact, you can see in our numbers, we've made a lot of progress in the last quarter. There’s a few light manufacturing companies that Kent's talked about in the past that we continue to keep an eye on. But I wouldn't say more cautious, I would say we just continue to be cautious. We’ve tended to be on the conservative side in terms of where our reserve is

and let me have Kent to finish that answer. But it's a good question and I appreciate you asking it.

Kent Jehle
Brian, I think the only thing I would add with Charlie's comments is on the Ag side and given the fact we are out making our client visits right now. when you see in the state of Iowa, the corn condition good to excellent is under 70%, it's in the upper 60%; that's a little lower than what we've seen in the last couple of years. Soybeans are down closer to 60% good to excellent from that standpoint right now. That's week-old information and we'll have a new report this afternoon. that's leading us towards there could be a little more stress on the cash flow side and that's why we want to be proactive and working with our clients to see how things are shaping up in our footprint as Charlie alluded to with his opening comments, as well. not that we're still very guarded with Ag and we're very proactive and we're trying to identify any of our customers that are under stress and how, what's that going to look like as we get out of harvest and into next year's renewal season.

Brian Martin
Okay. I appreciate it. Thanks Kent. Just a last couple from me, just on the fee income side. Did you guys call out anything that was non-recurring, I guess, you kind of went through it quickly, Charlie. But just I didn't catch if there was anything in that fee income line that was kind of non-core or just unusual in the quarter.

Katie Lorenson
Brian, I'll take that one. This is Katie. There really wasn't anything unusual. We did have our, of course, mortgage servicing right adjustment, which we measure the month before the quarter ends. We had a slight decrease, it was very minimal, like $25,000, but as you recall in Q1, we had a nice positive of around $200,000 flowing through that line item. The decrease you're seeing there in the loan servicing income is really related to that, and that's kind of the only thing that I would point out on the noninterest income.

Brian Martin
Okay. And then just on the Denver operation. You guys, I thought that it was some additional people that may be coming aboard that operation over time in different, maybe just fee businesses, I guess, any updates on that, Charlie? Or just kind of the expense run rate in Denver, does it grow from where we're at today or just how to think about that piece of it?

Kevin Kramer
Brian, this is Kevin Kramer. Yeah, we've had a few enhancements. We brought on another commercial banker. We're actively talking to another portfolio manager as we speak. We're also looking at other fee business opportunities in that market, like mortgage is another area that we're looking into along with SBA. We'll continue, the expense run rate will increase, but from an operations point of view, it will be accretive as we continue to bring more folks on because they can drive, these are folks that drive revenue for the bank. We, that expense run rate we have helps us keep the doors open and run the operation there, but we are looking at a couple of new folks who can provide immediate impact. When I say immediate, in the first two to three quarters that they're onboard to bring revenues to the banks. We'll see a little bit of that. I don't have any exact numbers on what the future run rate will look like for 2018, but as we do the planning later this year, it will go up by a little bit because of the additional production team that we've put in place with the original four.

Brian Martin

Okay. I appreciate the color. All right. I'm going to step back. Thanks for taking the questions, guys.

Charles Funk
Yeah, thank you Brian.

Kevin Kramer
Thank you.

Operator
And ladies and gentlemen, at this time and showing no additional questions, I'd like to turn the conference back over to management for any closing remarks.

CONCLUSION

Charles Funk
Yes. Thank you, again, everyone for joining the call this morning. We feel pretty good about where we are right now, and we look forward to a strong finish to 2017. Thanks for joining us this morning.

Operator
Ladies and gentlemen, that does conclude today's conference call. We do thank you for joining today's presentation. You may now disconnect your lines.