

VALLEY NATIONAL BANCORP
Form 10-Q
May 09, 2018

UNITED STATES
SECURITIES AND EXCHANGE COMMISSION
Washington, DC 20549

FORM 10-Q

(Mark One)

Quarterly Report Pursuant to Section 13 or 15 (d) of the Securities Exchange Act of 1934
For the Quarterly Period Ended March 31, 2018

OR

Transition Report Pursuant to Section 13 or 15 (d) of the Securities Exchange Act of 1934

For the transition period from _____ to _____
Commission File Number 1-11277

VALLEY NATIONAL BANCORP
(Exact name of registrant as specified in its charter)

New Jersey 22-2477875
(State or other jurisdiction of (I.R.S. Employer
Incorporation or Organization) Identification Number)

1455 Valley Road 07470
Wayne, NJ
(Address of principal executive office) (Zip code)
973-305-8800
(Registrant's telephone number, including area code)

Indicate by check mark whether the Registrant (1) has filed all reports required to be filed by Section 13 or 15(d) of the Securities Exchange Act of 1934 during the preceding 12 months (or such shorter period that the registrant was required to file such reports), and (2) has been subject to such filing requirements for the past 90 days. Yes No

Indicate by check mark whether the Registrant has submitted electronically and posted on its corporate Web site, if any, every Interactive Data File required to be submitted and posted pursuant to Rule 405 of Regulation S-T (§232.405 of this chapter) during the preceding 12 months (or for such shorter period that the registrant was required to submit and post such files.) Yes No

Indicate by check mark whether the registrant is a large accelerated filer, an accelerated filer, a non-accelerated filer, a smaller reporting company or an emerging growth company. See the definitions of "large accelerated filer," "accelerated filer," "smaller reporting company" and "emerging growth company" in Rule 12b-2 of the Exchange Act (check one):

Large accelerated filer Accelerated filer Emerging growth company

Non-accelerated filer (Do not check if a smaller reporting company) Smaller reporting company

If an emerging growth company, indicate by check mark if the registrant has elected not to use the extended transition period for complying with any new or revised financial accounting standards provided pursuant to Section 13(a) of the Exchange Act.

Indicate by check mark whether the Registrant is a shell company (as defined in Rule 12b-2 of the Exchange Act). Yes No

Indicate the number of shares outstanding of each of the issuer's classes of common stock, as of the latest practicable date. Common Stock (no par value), of which 331,261,486 shares were outstanding as of May 9, 2018

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PART I - FINANCIAL INFORMATION

Item 1. Financial Statements

VALLEY NATIONAL BANCORP

CONSOLIDATED STATEMENTS OF FINANCIAL CONDITION

(in thousands, except for share data)

	March 31, 2018	December 31, 2017
Assets	(Unaudited)	
Cash and due from banks	\$222,311	\$243,310
Interest bearing deposits with banks	274,349	172,800
Investment securities:		
Held to maturity (fair value of \$2,014,954 at March 31, 2018 and \$1,837,620 at December 31, 2017)	2,048,583	1,842,691
Available for sale	1,843,514	1,493,905
Total investment securities	3,892,097	3,336,596
Loans held for sale, at fair value	8,449	15,119
Loans	22,552,767	18,331,580
Less: Allowance for loan losses	(132,862)	(120,856)
Net loans	22,419,905	18,210,724
Premises and equipment, net	346,700	287,705
Bank owned life insurance	436,334	386,079
Accrued interest receivable	86,804	73,990
Goodwill	1,078,892	690,637
Other intangible assets, net	86,487	42,507
Other assets	612,029	542,839
Total Assets	\$29,464,357	\$24,002,306
Liabilities		
Deposits:		
Non-interest bearing	\$6,124,256	\$5,224,928
Interest bearing:		
Savings, NOW and money market	11,077,789	9,365,013
Time	4,757,801	3,563,521
Total deposits	21,959,846	18,153,462
Short-term borrowings	1,618,416	748,628
Long-term borrowings	2,353,548	2,315,819
Junior subordinated debentures issued to capital trusts	55,109	41,774
Accrued expenses and other liabilities	232,435	209,458
Total Liabilities	26,219,354	21,469,141
Shareholders' Equity		
Preferred stock, no par value; 50,000,000 shares authorized:		
Series A (4,600,000 shares issued at March 31, 2018 and December 31, 2017)	111,590	111,590
Series B (4,000,000 shares issued at March 31, 2018 and December 31, 2017)	98,101	98,101
Common stock (no par value, authorized 450,000,000 shares; issued 331,202,537 shares at March 31, 2018 and 264,498,643 shares at December 31, 2017)	115,824	92,727
Surplus	2,784,194	2,060,356
Retained earnings	199,555	216,733
Accumulated other comprehensive loss	(64,103)	(46,005)
Treasury stock, at cost (12,678 common shares at March 31, 2018 and 29,792 common shares at December 31, 2017)	(158)	(337)

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Total Shareholders' Equity	3,245,003	2,533,165
Total Liabilities and Shareholders' Equity	\$29,464,357	\$24,002,306
See accompanying notes to consolidated financial statements.		

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VALLEY NATIONAL BANCORP
CONSOLIDATED STATEMENTS OF INCOME (Unaudited)
(in thousands, except for share data)

	Three Months Ended March 31,	
	2018	2017
Interest Income		
Interest and fees on loans	\$237,586	\$ 174,353
Interest and dividends on investment securities:		
Taxable	21,323	17,589
Tax-exempt	5,721	4,031
Dividends	1,939	2,151
Interest on federal funds sold and other short-term investments	926	331
Total interest income	267,495	198,455
Interest Expense		
Interest on deposits:		
Savings, NOW and money market	22,317	10,183
Time	14,616	9,553
Interest on short-term borrowings	5,732	3,901
Interest on long-term borrowings and junior subordinated debentures	17,232	12,950
Total interest expense	59,897	36,587
Net Interest Income	207,598	161,868
Provision for credit losses	10,948	2,470
Net Interest Income After Provision for Credit Losses	196,650	159,398
Non-Interest Income		
Trust and investment services	3,230	2,744
Insurance commissions	3,821	5,061
Service charges on deposit accounts	7,253	5,236
Losses on securities transactions, net	(765)	(23)
Fees from loan servicing	2,223	1,815
Gains on sales of loans, net	6,753	4,128
Bank owned life insurance	1,763	2,463
Other	7,973	4,296
Total non-interest income	32,251	25,720
Non-Interest Expense		
Salary and employee benefits expense	93,292	65,927
Net occupancy and equipment expense	27,924	23,035
FDIC insurance assessment	5,498	5,127
Amortization of other intangible assets	4,293	2,536
Professional and legal fees	17,047	4,695
Amortization of tax credit investments	5,274	5,324
Telecommunication expense	3,594	2,659
Other	16,830	11,649
Total non-interest expense	173,752	120,952
Income Before Income Taxes	55,149	64,166
Income tax expense	13,184	18,071
Net Income	\$41,965	\$ 46,095
Dividends on preferred stock	3,172	1,797
Net Income Available to Common Shareholders	\$38,793	\$ 44,298

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Earnings Per Common Share:

Basic	\$0.12	\$ 0.17
Diluted	0.12	0.17
Cash Dividends Declared per Common Share	0.11	0.11
Weighted Average Number of Common Shares Outstanding:		
Basic	330,727,412	63,797,024
Diluted	332,465,522	64,546,266

See accompanying notes to consolidated financial statements.

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VALLEY NATIONAL BANCORP
CONSOLIDATED STATEMENTS OF COMPREHENSIVE INCOME (Unaudited)
(in thousands)

	Three Months Ended March 31,	
	2018	2017
Net income	\$41,965	\$46,095
Other comprehensive income, net of tax:		
Unrealized gains and losses on available for sale securities		
Net (losses) gains arising during the period	(20,929)	1,307
Less reclassification adjustment for net losses included in net income	548	13
Total	(20,381)	1,320
Non-credit impairment losses on available for sale securities		
Net change in non-credit impairment losses on securities	(268)	113
Less reclassification adjustment for accretion of credit impairment losses included in net income	(16)	(87)
Total	(284)	26
Unrealized gains and losses on derivatives (cash flow hedges)		
Net gains on derivatives arising during the period	1,960	127
Less reclassification adjustment for net losses included in net income	1,036	1,475
Total	2,996	1,602
Defined benefit pension plan		
Amortization of net loss	112	59
Total other comprehensive (loss) income	(17,557)	3,007
Total comprehensive income	\$24,408	\$49,102
See accompanying notes to consolidated financial statements.		

VALLEY NATIONAL BANCORP
CONSOLIDATED STATEMENTS OF CASH FLOWS (Unaudited)
(in thousands)

	Three Months Ended March 31,	
	2018	2017
Cash flows from operating activities:		
Net income	\$41,965	\$46,095
Adjustments to reconcile net income to net cash provided by operating activities:		
Depreciation and amortization	7,247	6,260
Stock-based compensation	7,395	4,127
Provision for credit losses	10,948	2,470
Net amortization of premiums and accretion of discounts on securities and borrowings	8,495	6,043
Amortization of other intangible assets	4,293	2,536
Losses on securities transactions, net	765	23
Proceeds from sales of loans held for sale	237,360	161,325
Gains on sales of loans, net	(6,753)	(4,128)
Originations of loans held for sale	(227,660)	(112,682)
Losses on sales of assets, net	97	34
Net change in:		
Fair value of borrowings hedged by derivative transactions	—	(454)
Cash surrender value of bank owned life insurance	(1,763)	(2,463)
Accrued interest receivable	(691)	(1,429)
Other assets	19,480	(7,103)
Accrued expenses and other liabilities	(15,295)	(35,145)
Net cash provided by operating activities	85,883	65,509
Cash flows from investing activities:		
Net loan originations and purchases	(475,346)	(323,470)
Investment securities held to maturity:		
Purchases	(52,945)	(52,160)
Maturities, calls and principal repayments	58,227	77,141
Investment securities available for sale:		
Purchases	(174,047)	(207,402)
Sales	38,625	—
Maturities, calls and principal repayments	60,858	50,543
Death benefit proceeds from bank owned life insurance	560	1,998
Proceeds from sales of real estate property and equipment	7,378	4,970
Purchases of real estate property and equipment	(4,260)	(5,627)
Cash and cash equivalents acquired in acquisition	156,612	—
Net cash used in investing activities	(384,338)	(454,007)
Cash flows from financing activities:		
Net change in deposits	241,541	(399,567)
Net change in short-term borrowings	219,809	564,004
Proceeds from issuance of long-term borrowings, net	—	200,000
Repayments of long-term borrowings	(50,000)	—
Cash dividends paid to preferred shareholders	(3,172)	(1,797)
Cash dividends paid to common shareholders	(29,611)	(29,012)
Purchase of common shares to treasury	(2,083)	(2,151)
Common stock issued, net	2,521	1,246

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Net cash provided by financing activities	379,005	332,723
Net change in cash and cash equivalents	80,550	(55,775)
Cash and cash equivalents at beginning of year	416,110	392,501
Cash and cash equivalents at end of period	\$496,660	\$336,726

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VALLEY NATIONAL BANCORP
CONSOLIDATED STATEMENTS OF CASH FLOWS (Continued)
(in thousands)

	Three Months Ended March 31,	
	2018	2017
Supplemental disclosures of cash flow information:		
Cash payments for:		
Interest on deposits and borrowings	\$58,881	\$56,735
Federal and state income taxes	8,843	1,599
Supplemental schedule of non-cash investing activities:		
Transfer of loans to other real estate owned	\$145	\$4,813
Transfer of loans to loans held for sale	—	103,884
Acquisition:		
Non-cash assets acquired:		
Investment securities held to maturity	\$214,217	\$—
Investment securities available for sale	308,385	—
Loans	3,744,682	—
Premises and equipment	62,066	—
Bank owned life insurance	49,052	—
Accrued interest receivable	12,123	—
Goodwill	388,255	—
Other intangible assets	45,906	—
Other assets	98,134	—
Total non-cash assets acquired	\$4,922,820	\$—
Liabilities assumed:		
Deposits	\$3,564,843	\$—
Short-term borrowings	649,979	—
Long-term borrowings	87,283	—
Junior subordinated debentures issued to capital trusts	13,249	—
Accrued expenses and other liabilities	26,848	—
Total liabilities assumed	4,342,202	—
Net non-cash assets acquired	\$580,618	\$—
Net cash and cash equivalents acquired in acquisition	\$156,612	\$—
Common stock issued in acquisition	\$737,230	\$—
See accompanying notes to consolidated financial statements.		

VALLEY NATIONAL BANCORP
NOTES TO CONSOLIDATED FINANCIAL STATEMENTS
(Unaudited)

Note 1. Basis of Presentation

The unaudited consolidated financial statements of Valley National Bancorp, a New Jersey corporation ("Valley"), include the accounts of its commercial bank subsidiary, Valley National Bank (the "Bank"), and all of Valley's direct or indirect wholly-owned subsidiaries. All inter-company transactions and balances have been eliminated. The accounting and reporting policies of Valley conform to U.S. generally accepted accounting principles (U.S. GAAP) and general practices within the financial services industry. In accordance with applicable accounting standards, Valley does not consolidate statutory trusts established for the sole purpose of issuing trust preferred securities and related trust common securities. Certain prior period amounts have been reclassified to conform to the current presentation.

In the opinion of management, all adjustments (which include only normal recurring adjustments) necessary to present fairly Valley's financial position, results of operations and cash flows at March 31, 2018 and for all periods presented have been made. The results of operations for the three months ended March 31, 2018 are not necessarily indicative of the results to be expected for the entire fiscal year.

In preparing the unaudited consolidated financial statements in conformity with U.S. GAAP, management has made estimates and assumptions that affect the reported amounts of assets and liabilities as of the date of the consolidated statements of financial condition and results of operations for the periods indicated. Material estimates that are particularly susceptible to change are: the allowance for loan losses; the evaluation of goodwill and other intangible assets, and investment securities for impairment; fair value measurements of assets and liabilities; and income taxes. Estimates and assumptions are reviewed periodically and the effects of revisions are reflected in the consolidated financial statements in the period they are deemed necessary. While management uses its best judgment, actual amounts or results could differ significantly from those estimates. The current economic environment has increased the degree of uncertainty inherent in these material estimates.

Certain information and footnote disclosures normally included in financial statements prepared in accordance with U.S. GAAP and industry practice have been condensed or omitted pursuant to rules and regulations of the SEC. These financial statements should be read in conjunction with the consolidated financial statements and notes thereto included in Valley's Annual Report on Form 10-K for the year ended December 31, 2017.

Note 2. Business Combinations

On January 1, 2018, Valley completed its acquisition of USAmeriBancorp, Inc. (USAB) and its wholly-owned subsidiary, USAmeriBank, headquartered in Clearwater, Florida. USAB had approximately \$5.1 billion in assets, \$3.7 billion in net loans and \$3.6 billion in deposits, after purchase accounting adjustments, and maintained a branch network of 29 offices. The acquisition represents a significant addition to Valley's Florida franchise, specifically in the Tampa Bay market. The acquisition also brought Valley to the Birmingham, Montgomery, and Tallapoosa areas in Alabama, where Valley now operates 15 of its branches. The common shareholders of USAB received 6.1 shares of Valley common stock for each USAB share they owned. The total consideration for the acquisition was approximately \$737 million.

Merger expenses totaled \$13.4 million for the three months ended March 31, 2018, which primarily related to salary and employee benefits and professional and legal fees included in non-interest expense on the consolidated statements of income.

The following table sets forth assets acquired and liabilities assumed in the USAB acquisition, at their estimated fair values as of the closing date of the transaction:

	January 1, 2018 (in thousands)
Assets acquired:	
Cash and cash equivalents	\$156,612
Investment securities held to maturity	214,217
Investment securities available for sale	308,385
Loans	3,744,682
Premises and equipment	62,066
Bank owned life insurance	49,052
Accrued interest receivable	12,123
Goodwill	388,255
Other intangible assets	45,906
Other assets:	
Deferred taxes	8,698
Other real estate owned	4,073
FHLB and FRB stock	38,809
Tax credit investments	20,138
Other	26,416
Total other assets	98,134
Total assets acquired	\$5,079,432
Liabilities assumed:	
Deposits:	
Non-interest bearing	\$887,083
Savings, NOW and money market	1,678,115
Time	999,645
Total deposits	3,564,843
Short-term borrowings	649,979
Long-term borrowings	87,283
Junior subordinated debentures issued to capital trusts	13,249
Accrued expenses and other liabilities	26,848
Total liabilities assumed	\$4,342,202
Common stock issued in acquisition	737,230

The determination of the fair value of the assets acquired and liabilities assumed required management to make estimates about discount rates, future expected cash flows, market conditions, and other future events that are highly subjective in nature and subject to change. The fair value estimates are subject to change for up to one year after the closing date of the transaction if additional information (existing at the date of closing) relative to closing date fair values becomes available. As Valley continues to analyze the acquired assets and liabilities, there may be adjustments to the recorded carrying values. However, Valley does not expect significant future adjustments to the recorded amounts at January 1, 2018.

Fair Value Measurement of Assets Acquired and Liabilities Assumed

Described below are the methods used to determine the fair values of the significant assets acquired and liabilities assumed in the USAB acquisition.

Cash and cash equivalents. The estimated fair values of cash and cash equivalents approximate their stated face amounts, as these financial instruments are either due on demand or have short-term maturities.

Investment securities. The estimated fair values of the investment securities were calculated utilizing Level 2 inputs. The prices for these instruments are obtained through an independent pricing service when available, or dealer market participants with whom Valley has historically transacted both purchases and sales of investment securities. The prices are derived from market quotations and matrix pricing. The fair value measurements consider observable data that may include dealer quotes, market spreads, cash flows, the U.S. Treasury yield curve, live trading levels, trade execution data, market consensus prepayment speeds, credit information and the bond's terms and conditions, among other things. Management reviewed the data and assumptions used in pricing the securities by its third party provider to ensure the highest level of significant inputs are derived from market observable data.

Loans. The acquired loan portfolio was segregated into categories for valuation purposes primarily based on loan type (commercial, commercial real estate, residential and consumer) and credit risk rating. The estimated fair values were computed by discounting the expected cash flows from the respective portfolios. Management estimated the contractual cash flows expected to be collected at the acquisition date by using valuation models that incorporated estimates of current key assumptions, such as prepayment speeds, default rates, and loss severity rates. Prepayment assumptions were developed by reference to recent or historical prepayment speeds observed for loans with similar underlying characteristics. Prepayment assumptions were influenced by many factors, including, but not limited to, forward interest rates, loan and collateral types, payment status, and current loan-to-value ratios. Default and loss severity rates were developed by reference to recent or historical default and loss rates observed for loans with similar underlying characteristics. Default and loss severity assumptions were influenced by many factors, including, but not limited to, underwriting processes and documentation, vintages, collateral types, collateral locations, estimated collateral values, loan-to-value ratios, and debt-to-income ratios.

The expected cash flows from the acquired loan portfolios were discounted to present value based on the estimated market rates. The market rates were estimated using a buildup approach based on the following components: funding cost, servicing cost and consideration of liquidity premium. The funding cost estimated for the loans was based on a mix of wholesale borrowing and equity funding. The methods used to estimate the Level 3 fair values of loans are extremely sensitive to the assumptions and estimates used. While management attempted to use assumptions and estimates that best reflected the acquired loan portfolios and current market conditions, a greater degree of subjectivity is inherent in these values than in those determined in active markets.

The difference between the fair value and the expected cash flows from the acquired loans will be accreted to interest income over the remaining term of the loans in accordance with Accounting Standards Codification (ASC) Subtopic

310-30, "Loans and Debt Securities Acquired with Deteriorated Credit Quality." See Note 8 for further details.

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Other intangible assets. Other intangible assets mostly consisting of core deposit intangibles (CDI) are measures of the value of non-maturity checking, savings, NOW and money market deposits that are acquired in a business combination. The fair value of the CDI is based on the present value of the expected cost savings attributable to the core deposit funding, relative to an alternative source of funding. The CDI is amortized over an estimated useful life of 10 years to approximate the existing deposit relationships acquired.

Deposits. The fair values of deposit liabilities with no stated maturity (i.e., non-interest bearing accounts and savings, NOW and money market accounts) are equal to the carrying amounts payable on demand. The fair values of certificates of deposit represent contractual cash flows, discounted to present value using interest rates currently offered on deposits with similar characteristics and remaining maturities.

Short-term borrowings. The short-term borrowings consist of securities sold under agreements to repurchase and FHLB advances. The carrying amounts approximate their fair values because they frequently re-price to a market rate.

Long-term borrowings. The fair values of long-term borrowings consisting of subordinated notes and FHLB advances were estimated by discounting the estimated future cash flows using market discount rates for borrowings with similar characteristics, terms and remaining maturities.

Junior subordinated debentures issued to capital trusts. There is no active market for the trust preferred securities issued by Alient Statutory Trust II; therefore, the fair value of junior subordinated debentures was estimated utilizing the income approach. Valuation methods under the income approach include those methods that provide for the direct capitalization of earnings estimates, as well as valuation methods calling for the forecasting of future benefits (earnings or cash flows) and then discounting those benefits to the present at an appropriate discount rate. Under the income approach, the expected cash flows over the remaining estimated life were discounted to the present at an appropriate discount rate.

Note 3. Earnings Per Common Share

The following table shows the calculation of both basic and diluted earnings per common share for the three months ended March 31, 2018 and 2017.

	Three Months Ended	
	March 31,	
	2018	2017
	(in thousands, except for share data)	
Net income available to common shareholders	\$38,793	\$ 44,298
Basic weighted average number of common shares outstanding	330,727,416	330,797,024
Plus: Common stock equivalents	1,738,117	1,749,242
Diluted weighted average number of common shares outstanding	332,465,533	332,546,266
Earnings per common share:		
Basic	\$0.12	\$ 0.17
Diluted	0.12	0.17

Common stock equivalents represent the dilutive effect of additional common shares issuable upon the assumed vesting or exercise, if applicable, of restricted stock units, common stock options and warrants to purchase Valley's common shares. Common stock options and warrants with exercise prices that exceed the average market price of Valley's common stock during the periods presented have an anti-dilutive effect on the diluted earnings per common share calculation and therefore are excluded from the diluted earnings per share calculation. Anti-dilutive warrants and, to a lesser extent, common stock options equaled approximately 2.9 million and 3.2 million shares for the three months ended March 31, 2018 and 2017, respectively.

Note 4. Accumulated Other Comprehensive Loss

The following table presents the after-tax changes in the balances of each component of accumulated other comprehensive loss for the three months ended March 31, 2018.

	Components of Accumulated Other Comprehensive Loss				Total Accumulated Other Comprehensive Loss
	Unrealized Gains and Losses on Available for (AFS) Securities (in thousands)	Non-credit Impairment Losses on AFS Securities	Unrealized Gains and (Losses) on Derivatives	Defined Benefit Pension Plan	
Balance at December 31, 2017	\$ (12,004)	\$ (380)	\$ (8,338)	\$ (25,283)	\$ (46,005)
Reclassification due to the adoption of ASU No. 2016-01	(480)	—	—	—	(480)
Reclassification due to the adoption of ASU No. 2017-12	—	—	(61)	—	(61)
Balance at January 1, 2018	(12,484)	(380)	(8,399)	(25,283)	