Conference Call First Quarter 2019 Financial Results

February 27, 2019

Caution Regarding Forward-Looking Statements

In this document and in other documents filed with Canadian regulatory authorities or in other communications, we may from time to time make written or oral forward-looking statements within the meaning of applicable securities legislation. Forward-looking statements include, but are not limited to, statements regarding our business plan and financial objectives including statements contained in our 2018 Annual Report under the heading “Outlook”. The forward-looking statements contained in this document are used to assist readers in obtaining a better understanding of our financial position and the results of operations as at and for the periods ended on the dates presented and may not be appropriate for other purposes. Forward-looking statements typically use the conditional, as well as words such as prospect, believe, estimate, forecast, project, expect, anticipate, plan, may, should, could and would, or the negative of these terms, variations thereof or similar terminology.

By their very nature, forward-looking statements are based on assumptions and involve inherent risks and uncertainties, both general and specific in nature. It is therefore possible that the forecasts, projections and other forward-looking statements will not be achieved or will prove to be inaccurate. Although we believe that the expectations reflected in these forward-looking statements are reasonable, we can give no assurances that these expectations will prove to be correct. Certain important assumptions by us in making forward-looking statements include, but are not limited to, our estimates and statements regarding our business plan and financial objectives including statements contained in our 2018 Annual Report under the heading “Outlook”.

We caution readers against placing undue reliance on forward-looking statements when making decisions, as the actual results could differ considerably from the opinions, plans, objectives, expectations, forecasts, estimates and intentions expressed in such forward-looking statements due to various material factors. Among other things, these factors include: changes in capital market conditions, changes in government monetary, fiscal and economic policies, changes in interest rates, inflation levels and general economic conditions, legislative and regulatory developments, changes in competition, modifications to credit ratings, scarcity of human resources, developments with respect to labour relations, as well as developments in the technological environment. Furthermore, these factors include the ability to execute our plan and in particular the successful reorganization of retail branches, the modernization of the core banking system and the adoption of the Advanced Internal Ratings-Based approach to credit risk (the AIRB approach).

We further caution that the foregoing list of factors is not exhaustive. For more information on the risks, uncertainties and assumptions that would cause our actual results to differ from current expectations, please also refer to the “Risk Appetite and Risk Management Framework” section of our 2018 Annual Report, as well as to other public filings available at www.sedar.com.

We do not undertake to update any forward-looking statements, whether oral or written, made by us or on our behalf, except to the extent required by securities regulations.

NON-GAAP MEASURES

Management uses both generally accepted accounting principles (GAAP) and non-GAAP measures to assess the Bank's performance. Results prepared in accordance with GAAP are referred to as "reported" results. Non-GAAP measures presented throughout this document are referred to as "adjusted" measures and exclude the effect of certain amounts designated as adjusting items. Adjusting items are related to restructuring plans and to business combinations and have been designated as such as management does not believe they are indicative of underlying business performance. Non-GAAP measures are considered useful to readers in obtaining a better understanding of how management analyzes the Bank's results and in assessing underlying business performance and related trends. Non-GAAP measures do not have any standardized meaning prescribed by GAAP and are unlikely to be comparable to any similar measures presented by other issuers.

Operator

Welcome to the Laurentian Bank Financial Group conference call. Please note that this call is being recorded. I would now like to turn the meeting over to Ms. Susan Cohen. Please go ahead, Ms. Cohen.

Susan Cohen, Director, Investor Relations

Good morning and thank you for joining us.

Today's review of the first quarter of 2019 results will be presented by François Desjardins, President and CEO, and François Laurin, Executive Vice President and CFO. All documents pertaining to the quarter, including Laurentian Bank Financial Group's news release, investor presentation and financial supplement can be found on our website in the Investor Center.

Following our formal comments, the senior management team will be available to answer questions and then Francois Desjardins will offer some closing remarks.

Before we begin, let me remind you that during this conference call, forward-looking statements may be made, and it is possible that actual results may differ materially from those projected in such statements. For the complete cautionary note regarding forward-looking statements, please refer to our press release or to Slide 2 of the presentation.

It is now my pleasure to turn the call over to François Desjardins.

François Desjardins, President and Chief Executive Officer

Thank you, Susan and good morning everyone.

The road to becoming a better and different bank - one that is relevant to today's customers and one that delivers higher performance than historically - is an exciting, challenging and, sometimes bumpy one.

I am happy to report that during the last quarter, we made significant progress on key initiatives that will propel our organization in the coming months and years.

We successfully completed phase one of the Core Banking implementation and now all B2B Bank and most of Business Services products, which had been on our legacy system, are on the Temenos T24 system. This is no small feat and is very exciting for us. Going forward, modern technology will be the foundation of our platform and this will significantly reduce implementation costs and time to market. In short, we are now building on solid ground.

This also paves the way for digital implementations. We will soon be ready to offer digital banking and deposit products through B2B Bank advisor and broker networks – complementing the existing product line and generating opportunities to grow the number of pan-Canadian banking customers, in addition to unlocking a new source of funding for the Group.

This initiative required a coordinated effort from team members across the Group and I wish to personally thank everyone involved for their contribution.

We also celebrated the grand opening of the first advice lounge located at our Montreal corporate Offices. This new concept focusses our team solely on financial advice, improves the customer experience and lowers operating costs. We plan to replicate this concept in a prominent location on Montreal's south shore within the year.

We have had strong growth in higher-margin loans in Business Services, in line with our efforts to evolve the portfolio mix. In the first quarter, we generated sequential growth of 3% excluding loan sales and are on target to achieve low double digit growth in our commercial loan portfolio in 2019.

With respect to residential mortgages, growth has been below our historical levels as we have been prioritizing loans to business customers. We believe that borrowers are beginning to adapt their behavior to the new regulations and higher rates, and when combined with strong renewals, we expect to resume growth during 2019.

Nonetheless, our financial performance for the first quarter was below expectations. A key element was lower capital market driven revenues which impacted earnings by about $0.12 per share compared to the fourth quarter of 2018 and about $0.15 per share compared to the first quarter of 2018.

I would like to add that in the first quarter of 2019, an additional provision for credit losses of $4.5 million was recorded against the same single syndicated commercial exposure that we mentioned last quarter. Excluding this amount, PCL's would have been $6.0 million, a continued testament to the quality of our underwriting and credit risk management. As a reminder, 98% of the loan portfolio is collateralized.

However, as we have previously stated, short-term performance through transformation, does not follow a straight line and would be impacted by the investments we are making in the business - and we are continuing to invest in 2019. This is contributing to a higher than usual expense run-rate as we are managing two core banking systems side by side as well as incurring higher regulatory and other transformation related costs.

We also have increased costs related to labour relations. Since the end of the collective agreement in December 2017, we have incurred extra legal expenses and higher costs associated with our contingency plan in the event of a work conflict which amount to approximately 3 million dollars on an annual basis. Furthermore, we have been managing the Bank's balance sheet very conservatively, with a strong capital position and higher than normal liquidity levels. Our prudent liquidity management translates into an estimated 7 million dollar reduction in net interest income on an annual basis.

Management believes that it is in the best interest of all concerned to promptly reach an agreement – but the agreement must allow the Retail Services branch network to be relevant to the needs of today's customers and be financially sound. Our intention has been clear and consistent through this entire process - we wish to offer employees competitive working conditions and reward their performance. We also wish to focus on advice and allow for operational flexibility, including streamlining non-core administration activities, as we continue to transform. As a reminder, of the 3,700 Laurentian Bank Financial Group team members, the unionized workforce accounts for less than 1,200 who are located only in Quebec and are concentrated in Retail Services Operations and Support Groups.

The bad news is that these investments and expenses weigh on our short-term results. The good news is that we continue to move forward and many of these expenses will not recur over time as we build a renewed and profitable financial institution.

As previously disclosed, we will be transforming all remaining branches to the advice-only operating model by year-end, hence eliminating all cashier positions. Furthermore, the continuation of our transformation initiatives, including our investments in technology, are allowing us to further streamline our operations, particularly regarding certain back-office functions that support Retail Services activities. As such, we expect to reduce the Group's headcount by about 10% or about 350 employees over the next twelve months. Management always prefers to proceed with voluntary pre-retirement packages and natural attrition. Based on our previous experience, we are confident that these changes will optimize the Retail Services branch network operations and better position the Group to provide value-added services to clients.

This Bank has never been in a better financial position, in terms of its solid capital and liquidity levels; it continues to have an industry low loan loss provision – a testament to the quality of our underwriting and credit risk management; and it has never been stronger in terms of its processes and technology.

We remain confident that the investments we are making will improve efficiency and position Laurentian Bank Financial Group for sustainable growth and performance in an industry that is rapidly evolving. In

this age of disruption, it seems necessary to take a step backwards to ensure many steps forward. Although the road is and will continue to be bumpy, we are certain that the initiatives of our transformation plan will ultimately create long-term value for our shareholders. For this reason, Management remains committed to achieving our mid-term targets.

And now, I would like to turn the floor over to François to provide a more in depth review of our financial results for the first quarter of 2019.

François….

Francois Laurin, Executive Vice President, Finance, Treasury and Capital Markets, and Chief Financial Officer

Thank you, François.

Good morning everyone.

I would like to begin by turning to slide 16 which highlights the Bank's financial performance. Adjusted net income of $44.7 million, EPS of $0.98 and ROE of 7.3% in the first quarter of 2019 were lower year-over-year and sequentially.

Reported earnings for the first quarter, as outlined on slide 17, were affected by adjusting items totalling $4.4 million after tax or $0.10 per share, and are largely related to restructuring charges and business combinations. Restructuring charges resulted from the optimization of our Retail Services activities, as well as from the reorganization of retail brokerage activities, and mostly related to salaries, provisions for lease terminations and professional fees.

The drivers of our performance begin on slide 18. Total revenue in the first quarter of 2019 amounted to $242.3 million, a decrease of 9% compared to a year earlier. Net interest income fell by 3% and other income fell by 21% compared to a year earlier.

Net interest income decreased by $6.0 million compared to a year earlier and was impacted by lower year-over-year loan volumes and higher liquidity levels, partly offset by higher margins on loans to business customers. In addition, we have gradually increased the duration of our deposit portfolio to strengthen the Bank, which has also impacted our funding costs.

As shown on Slide 19, NIM increased to 1.80% in the first quarter of 2019, up 3 basis points year-over-year and quarter-over-quarter mainly due to the greater proportion of higher-yielding loans to business customers. This is evidence that we are successfully implementing our strategic plan to evolve the bank mix towards higher margin commercial loans. As at January 31, 2019, commercial loans accounted for 36% of our loan portfolio, compared to 34% a year earlier and residential mortgage loans accounted for 49% compared to 50%.

As we completed the optimization of our commercial loan portfolio over the past 4 quarters and resumed net growth in our commercial loan portfolio in the first quarter of 2019, we expect NII to gradually increase and NIM to modestly improve as our business mix continues to evolve.

Other income, as presented on Slide 20, totaled $69.7 million, and decreased by $18.6 million from a year ago. Of this amount, $12.4 million or about two thirds of the decline, was market-related. Specifically, fees and commissions on brokerage operations decreased by $3.6 million, mostly resulting from lower activity levels in fixed income, equity and underwriting due to poor market conditions, particularly in the first two months of the quarter. Looking forward, the pipeline remains strong and we expect revenues to increase when market conditions become more favorable. Other market related revenues, including securities gains and income from treasury and financial market operations were also affected and decreased by a combined $7.3 million compared with the first quarter of 2018. This decline was mostly driven by lower gains on inventory held for brokerage activities, as well as by lower realized gains on treasury portfolios. Commissions on sales of mutual funds fell by $1.5 million due to a combination of

lower sales volumes and lower market values. Other income was also impacted by a decrease in fees and commissions on loans and deposits of $4.4 million compared to a year earlier. This was mainly driven by lower deposit and payment service charges as clients gradually modify their banking behavior.

Slide 21 highlights adjusted non-interest expenses of $179.2 million, which rose by $6.2 million or by 4% year-over-year. Salaries decreased by $1.6 million year-over year, mainly due to lower pension costs and lower performance-based compensation. Premises and technology costs increased by $1.7 million largely due to higher technology costs to run concurrent core-banking platforms and to enhance IT service levels and security, as well as higher amortization expense for the completed Phase 1 of the core-banking system. These costs were partly offset by lower rent expenses following the move to our new Montreal corporate office. Technology costs are expected to decline as we gradually retire our legacy platforms.

Other adjusted non-interest expenses of $38.1 million increased by $6.0 million compared to the first quarter of 2018. Higher regulatory expenses, including increases in deposit insurance costs and other costs related to various compliance and regulatory-risk projects and higher professional fees and labor relations costs related to the renegotiation of the expired collective bargaining agreement contributed to the increase. The adjusted efficiency ratio was 74.0% in the first quarter of 2019. As previously mentioned, this ratio is expected to remain high over the next few quarters. Operating parallel core-banking platforms, managing matters related to the expired collective bargaining agreement and implementing new regulatory requirements such as IFRS guidelines, anti-money laundering and other regulatory risk-related projects are necessitating additional expenditures. However, the investments that we are making are expected to allow us to work towards our efficiency objective of 63% in 2021.

Slide 22 highlights our well diversified sources of funds. In the first quarter of 2019 the Bank continued to align its funding mix and levels with its asset levels. Deposits stood at $28.2 billion, up 1% sequentially. Personal deposits totalled $21.4 billion, up $0.4 billion compared with October 31, 2018, as deposits from branches increased 3% and deposits from independent brokers and advisors increased by 1%. Furthermore, Slide 23 shows that more than 3 years ago, we made the strategic decision to increase our broker sourced non-redeemable GIC's while reducing our high interest investment accounts. We will continue to prioritize higher quality term funding sources.

I would like to add that our liquidity position continues to be strong and well above our internal and regulatory requirements and that our liquidity portfolio is largely highly rated government securities.

Slide 24 presents the CET1 ratio, under the Standardized Approach, of 8.9% at January 31, 2019 and highlights our strong capital position.

Turning to Slide 26, total loans decreased by 7% year-over year and by 1% sequentially and reflects the continued optimization of our portfolio mix to better position the Bank. It should be noted that we sold non-strategic and low margin commercial loans totalling $708 million in 2018 and an additional $105 million in the first quarter of 2019 which concludes the realignment of our portfolio. In the first quarter, commercial loans increased by 2% sequentially and 3% excluding loan sales, mainly due to inventory financing volumes and real estate financing loans. We are on target for low double digit growth in this portfolio in 2019. The residential mortgage loan portfolio declined by 11% year-over-year, as we focus on higher-yielding commercial loans and in part, due to the strategic decision in November 2017 to no longer accept broker referrals in the branches as well as changes in regulation, including the impact of B-20.

Slide 27 provides a deep dive into our residential mortgage loan portfolio. While there seems to be an industry-wide slow down in mortgage growth, our strategy is to seek profitable niches, such as the high end of Alt-A business. As at January 31, 2019, our Alt-A portfolio totalled $1.3 billion and continues to represent 8% of the total mortgage book and 4% of the total loan portfolio. Within the overall residential mortgage portfolio, mortgages in the GTA represent about 22% of the portfolio and the GVA accounts for 4%. Overall, this portfolio is high quality as evidenced by very low loss ratios and low LTV's as well as high credit scores.

Slide 30 highlights our commercial loan portfolio which is pan-Canadian with a US presence. It is well diversified, has a track record of strong credit quality and is positioned for sustainable profitable growth.

Turning to slide 31, credit quality remained good. The provision for credit losses, under IFRS 9 amounted to $10.5 million and was $1.5 million lower than a year ago and $7.1 million lower than in the fourth quarter of 2018 when a $10.0 million provision was taken against a single syndicated commercial exposure. Of note, the provision for credit losses in the first quarter of 2019 included $4.5 million related to this same exposure. The loss ratio of 12 basis points in the first quarter of 2019 continues to reflect the good underlying credit quality of the portfolio.

Impaired loans are shown on Slide 32. Gross impaired loans increased by 5% sequentially, essentially as we are now including $15.0 million of insured residential mortgage loans to align this disclosure with the new stage 3 definition of IFRS 9. Excluding this adjustment, impaired loans would have decreased by 4% since October 2018. The net impaired loan ratio stood at 43 basis points under IFRS 9 compared to 42 basis points in the fourth quarter of 2018 under the previous definition and we remain well provisioned.

We continue to expect that over the medium-term, the loss ratio will gradually move higher to reflect our changing business mix. Nonetheless, with our current portfolio mix, conservative provisioning and a portfolio that is 98% collateralized, we expect that the loss ratio will remain below other Canadian banks.

Turning to Slide 33, we continue to work towards our 2021 medium-term growth targets and financial objectives.

To conclude, we are confident that our transformation plan and the strategic initiatives that we are implementing will lead to sustainable profitability and create long-term value for our shareholders.

Thank you for your attention and I will now turn the call back to Susan.

Susan Cohen, Director, Investor Relations

At this point, I would like to turn the call over to the conference call operator for the question-and-answer session. Angele?

Operator

Our first question comes from Meny Grauman of Cormark Securities.

Meny Grauman, Cormark Securities

Good morning. A question on the headcount reductions. I'm wondering if that decision complicates negotiations in terms of the collective bargaining agreement.

François Desjardins, President and Chief Executive Officer

Well, today's announcements are consistent with our transformation plan and should be of no surprise to anyone that we're moving towards focusing on advice and reducing headcount in more administration positions. This is consistent with the messaging that I've given outside and inside our walls. Obviously, we need to simplify and streamline our operations and processes, and it is a big part of our transformation.

We had already announced that we were moving to a 100%-only branches and that's a continuation of those announcements. In short, the plan is to build the bank for the next decade and that's what we're moving towards. In terms of negotiations with the union, we're still working very hard to get to an agreement and we hope that we'll do so in the next few weeks.

Meny Grauman, Cormark Securities

Okay. And then, just wondering, for a while now you've talked about balance sheet conservatism. And I'm just wondering, how to reconcile that with, you know, you have sustained very low and pretty impressive loan-loss provision. So, how do those two come together? It would seem like if I just looked at your credit performance that there's no worries at all out there, that things are very benign. And so, why take a more conservative approach to your balance sheet, given the credit environment that continues to go your way?

François Desjardins, President and Chief Executive Officer

There's no link between the credit balance sheet and what we're doing on the capital and liquidity levels. We are maintaining a strong capital position with market volatility, and as we continue to increase loans to business customers in the bank mix and pursue our plan. From a liquidity standpoint though, because there was an end to the collective agreement at the end of December 2017, we started building a higher liquidity profile as part of our business continuity plan, which has to be operational and financial. This is just normal course when you have to build and prepare for the worst of times while still hoping for the best of times.

Meny Grauman, Cormark Securities

Okay. And then, finally, just a question on fee income. I understand the weakness in the market-related fee income; but if you look across the lines, definitely non-market-related fee income is also under pressure. I'm looking specifically at a drop in fees and commissions tied to loans and deposits. And I'm wondering, can we see an improvement in those fee income lines before we see a material improvement in loan and deposit growth, or are those two just hand in hand and the fee income line will only improve once the loan growth starts to look better?

François Desjardins, President and Chief Executive Officer

I'll ask François Laurin to give some colour on that.

Francois Laurin, Executive Vice President, Finance, Treasury and Capital Markets, and Chief Financial Officer

Yes. Meny, François Laurin here. On the lending fees, some of the reasons of the decline is the fact that the NCF and the equipment inventory financing business is a margin business and there's no other income fees involved in that business as our mix evolved with this, so that's one reason. The level of BA's as well has been a bit lower and that attracts also some fees to the business versus only NIM. So, we should see – from a commercial perspective, we look at NIM and other income together to evaluate the profitability, not just the lending fee. It's a combination of both NIM and other income because of the nature of the business.

And then when we see clearly that business going up. As for deposit service charges, their continued trend downward follows the consumers' modification of their behaviour. And we're also constrained with the rollout of our advice-focused retail strategy owing to the lack of progress on the collective agreement. So, we don't see necessarily growth there. But as we explained before, we need to ponder this with the reduction of expense and our growth – our efficiency ratio improving over time. So, the revenue will be lower but the expenses will be as well in order to improve the efficiency ratio. That's how we look at it. Does that answer your question Meny?

Meny Grauman, Cormark Securities

Yes. Thank you very much.

Operator

We'll go ahead with our next question from Doug Young of Desjardins Capital Markets. Please go ahead.

Doug Young, Desjardins Capital Markets

Hi. Good morning. Just to kind of frame the quarter here. I mean you had adjusted EPS of $0.98. I think François you mentioned capital markets being down year-over-year was about $0.15. You had an additional provision of $0.05. So, if you kind of normalize for those two, you get to $1.18. And I guess if capital market results don't improve and the PCL rate stays at 12 basis points, you get to about $1. Is that – again I'm just trying to get a sense, is that the bracket we should be thinking about in terms of the earnings power? And that's assuming, obviously, expenses don't improve. But I'm just trying to get a feel as to – because the numbers on the adjusted EPS are jumping around quite a bit, so I'm just trying to get a sense of what we should be thinking.

François Desjardins, President and Chief Executive Officer

Yes, thanks for the question. And it is why we gave a little bit more colour and numbers this quarter to try to help you out here. Looking at this quarter, we are impacted by capital markets revenue and by that the added provision to the single loan loss that we mentioned last quarter. Looking at the run rate, we are running at a lower performance for two reasons. 2019 continues to be a year of investment in the business and labour relations costs. So, if we're looking forward, what we should expect is capital markets revenues to come back. Although we might not make up everything we lost in the first quarter, we might make up some, but we believe the capital markets revenue will bounce back in future quarters.

We're also working towards the labour relations agreement which would eliminate the extra cost that we disclosed this quarter, as liquidity levels would go back to normal and, of course, costs related to managing the negotiations itself disappear. As we have been mentioning 2019 is a year of investment. And we'll continue to keep our expenses high in the next few quarters. But the announced efficiency initiatives that we announced today will contribute to a gradual improvement in our expense rate.

Of course, the end game here is a totally renewed, much more cost-effective digital retail bank where transactions are fully automated and where we focus our people on advice. So, we should continue to see investments – expenses linked to investments, but those will pay off as they disappear. And as things get automated, ultimately this is how we get to our medium-term objectives which management remains committed to.

Doug Young, Desjardins Capital Markets

And can you quantify what the labour – and you probably said this, but what the labour relation agreement costs were?

François Desjardins, President and Chief Executive Officer

Yes. The liquidity alone is about $7 million on an annual basis impact on revenue. And the other costs - security, legal, etc., are about $3 million on an annual basis, so about $10 million in all.

Doug Young, Desjardins Capital Markets

Okay. And then just a few other cost-related questions. I mean there is – you started amortizing the new core banking system cost. Can you quantify what that is? And I don't think you're fully amortizing it because I think the Phase 2 isn't done yet. Just wondered what would be the forecast once that's done as well?

François Desjardins, President and Chief Executive Officer

I'll ask François Laurin to give some colour if he can.

Francois Laurin, Executive Vice President, Finance, Treasury and Capital Markets, and Chief Financial Officer

You're right in the sense that it's partially starting to be amortized. But on an annual basis, it would be around $5-ish million at this point.

Doug Young, Desjardins Capital Markets

Okay. And what will it peak out at once the phase 2 is done?

Francois Laurin, Executive Vice President, Finance, Treasury and Capital Markets, and Chief Financial Officer

Less than $10 million.

Doug Young, Desjardins Capital Markets

Okay. But then you're going to get some savings from I guess getting rid of the legacy system, is that correct as well?

Francois Laurin, Executive Vice President, Finance, Treasury and Capital Markets, and Chief Financial Officer

Operating – well, some depreciation, but mostly operating and maintenance costs of the old legacy that will be withdrawn.

François Desjardins, President and Chief Executive Officer

Obviously, new core banking gives us also some other expense reductions once it's all said and done. It's not just the costs of running two systems. It's different IT teams. It's doubling up of certain costs or back-office costs. But also cost of opportunity where our people are doing manual transactions instead of giving advice.

So, as the new system gets automated and as digital gets rolled out, really putting the power of self-serve in the hands of our customers for manual transactions, that does reduce significantly the cost structure for administrative costs of the bank.

Doug Young, Desjardins Capital Markets

And just I guess you had the new digital bank offering coming in and you've got the reduction of the workforce. Have those costs already been taken related to those two items as well, or are those additional that we should be expecting the next few quarters?

François Desjardins, President and Chief Executive Officer

François?

Francois Laurin, Executive Vice President, Finance, Treasury and Capital Markets, and Chief Financial Officer

The cost of digital? Well, some of them will be capitalized. But obviously – are you talking about, Doug, in terms of operating expenses?

Doug Young, Desjardins Capital Markets

Yes, I mean the reduction of the workforce, the restructuring charge, is that all taken in this quarter already? I guess that's the first. And then there's going to be costs around the digital offering that you're coming out with B2B. I don't know if that's already been kind of factored into your expenses.

Francois Laurin, Executive Vice President, Finance, Treasury and Capital Markets, and Chief Financial Officer

Well, obviously, our cost structure today includes the fact that we have people dedicated to those functions and projects.

Doug Young, Desjardins Capital Markets

Okay. And then just – if I can just finish off, I mean the AIRB conversion process, you haven't changed the timeline for adoption of that. I'm just trying to get a sense of how it's going – how the dialogue with OSFI is going. My understanding is this is an iterative process and so they're in the offices and working with you. Just kind of trying to get a sense of where you stand with that process. Thank you.

François Desjardins, President and Chief Executive Officer

I'll ask Liam Mason to give some information about that.

William Mason, Executive Vice President, and Chief Risk Officer

Good morning Doug and thanks for your question. I mean OSFI has a defined approval process where you must submit a pre-application, you have to – they want to see progress on the models. We have near-term meetings with OSFI reviewing the models.

We are progressing on our established timeline as we've disclosed. And we continue to believe that there's a substantive benefit to the bank. CET1 on a standardized basis versus AIRB is dramatically different. There's at least 200 basis points of improvement in our CET1 from this. So, we're progressing on the AIRB project as expected right now.

Doug Young, Desjardins Capital Markets

And this is a Q4 – this is at tail end of 2020, still that's when it's expected to be done?

William Mason, Executive Vice President, and Chief Risk Officer

That's the timeline we're working to. What I would say is it's subject to OSFI approval. And so, we have to go back and forth to make sure they're comfortable with all of our submissions. But that's the timeline we're working to.

François Desjardins, President and Chief Executive Officer

If I might add, the implementation of IRB initiative and this has been the case for all financial institutions - even though the project might be done at the end of 2020, the benefit is gradual over 2021, 2022, 2023 and that's where you can see improvements in CET1 and obviously, redeployment of that capital into growth or other means.

Doug Young, Desjardins Capital Markets

Thank you.

Operator

Ladies and gentlemen, if you find that your question has been answered, you may remove yourself from the queue by pressing start two. And we will now take our next question from Sohrab Movahedi of BMO Capital Markets. Please go ahead.

Sohrab Movahedi, BMO Capital Markets

Thank you. Maybe I'll just start-off with Liam. Liam the benefit from the AIRB conversion, is that – how much of that benefit gets enhanced or reduced as the mix of the portfolio goes towards commercial away from residential?

William Mason, Executive Vice President, and Chief Risk Officer

Sohrab, good question and good morning. The AIRB benefit really depends upon your mix of business. And some types of business receive more AIRB benefit than others. But right now, our estimate is well in excess of 200 basis points of benefit from AIRB. As François just indicated though, that will be phased in over the years of 2021 2022 in terms of timeline.

Sohrab Movahedi, BMO Capital Markets

So, in other words, the fact that for example you're guiding towards higher loan losses given the mix of the portfolio towards commercial will have no bearing on the AIRB benefit you're expecting?

William Mason, Executive Vice President, and Chief Risk Officer

You have to think about it in two contexts. Obviously, we're under IFRS 9 now, so we have to look at the IFRS 9 ECL. That drives your loan-loss provisions. The AIRB standards while they leverage some similar models are slightly different. And it's the combination of the two that gives you sort of your capital stack, your loan reserve plus the capital against your exposure. But at this juncture, we have no change in our expectation and it's still well in excess of 200 basis points – or in excess of 200 basis points benefit from the AIRB.

François Desjardins, President and Chief Executive Officer

Okay. And if I may add on that. Whether it be on personal or commercial lending, IRB is beneficial when your book is conservative in nature. And as we've been repeating for a long time, our book is. We're a conservative bank in terms of our lending practices. And that's applying standard methodology to calculating capital is punitive for a conservative bank because when you move into IRB, you re-evaluate based on real risk. And that's how you calculate a new RWA. And of course, that translates into revised capital. So, as long as we're moving the mix, it doesn't impact that much because we're not moving our risk profile of these books.

Sohrab Movahedi, BMO Capital Markets

Okay. Thank you. And while we're on the commercial, maybe obviously good growth. You're expecting it to be a driver of volume growth. How much of that is coming from syndicated credit as opposed to I guess self-originated credit? If you can give us a little bit more color around which geographies or what type of loan, business loan, business lending you're doing over here to drive this growth?

François Desjardins, President and Chief Executive Officer

I'll ask Stéphane Therrien to add some information here.

Stéphane Therrien, Executive Vice President, Personal and Commercial Banking

Thanks for the question Sohrab. In terms of geography, here's how you should look at it, more than 50% of our book is outside of the province of Québec. So, we're really a national player and now a player also in the States. I would say that the majority of our deals are self-originated versus being syndicated or being invited into a syndicate. So, that's how you should see our book right now.

Sohrab Movahedi, BMO Capital Markets

And can you just comment how much would be out of the US versus Canada?

Stéphane Therrien, Executive Vice President, Personal and Commercial Banking

The supplementary information is on page 17 and you have a graph in the investor presentation that we have today.

Sohrab Movahedi, BMO Capital Markets

Okay. That's helpful. Those are the types of trends you expect to continue or expect that to pick up? Like, is that current mix between Canada, US, sustained mix you're going for? Or are you trying to grow US faster than Canada?

Stéphane Therrien, Executive Vice President, Personal and Commercial Banking

I think, right now, we're definitely winning a lot with our latest acquisition that was mainly in the States, so I would see that percentage growing with time.

Sohrab Movahedi, BMO Capital Markets

And then just one last one for me. François, was the tax rate abnormally low this quarter?

Francois Laurin, Executive Vice President, Finance, Treasury and Capital Markets, and Chief Financial Officer

You could say that, yes. Based on lower domestic profitability – it's basically because of the lower profitability of the domestic Canadian business that we have, compared to the non-Canadian. So, we should expect more like 20% in the next few quarters.

Sohrab Movahedi, BMO Capital Markets

So, as the profitably in Canada rebounds, so will the tax rate, is that what's happening?

Francois Laurin, Executive Vice President, Finance, Treasury and Capital Markets, and Chief Financial Officer

Yes, exactly. That's exactly it.

Sohrab Movahedi, BMO Capital Markets

Okay. Thank you.

Operator

And we will now take our next question from Darko Mihelic of RBC Capital Markets. Please go ahead.

Darko Mihelic, RBC Capital Markets

Hi. Thank you and good morning. I'm going to start, I guess, my question more basically on the expense level. When I look at the expenses at around $179 million, I'm wondering if you would just offer us – is that a good run rate to go from here, just to help me out? Because the efficiency ratio doesn't matter much to me, given where revenues could bounce around. I'm just more interested in just the base level of expenses, let's call it $180 million per quarter, is that a good idea for the rest of this year?

François Desjardins, President and Chief Executive Officer

François?

Francois Laurin, Executive Vice President, Finance, Treasury and Capital Markets, and Chief Financial Officer

Yes. Clearly, as we mentioned, we entertained more expenses in years of investment as we have now. And we expect that the ongoing level of non-interest expense, Darko, will remain at a similar level over the next few quarters as we continue to invest.

And we explained today some numerical evidence of what we intend to have as benefit going forward post certain activities and implementation of measures. And it's still working towards our 63% by 2021, we're still confident with that.

François Desjardins, President and Chief Executive Officer

Of course, Darko, you have to take into consideration that what I said earlier about the cost of labor relations would disappear with an agreement. So, that's about $10 million. And, of course, you have to take into account the reduction in headcount that we announced today as well.

Darko Mihelic, RBC Capital Markets

And why does the – I mean, I understand that there'd be a $10 million benefit, given the drag of liquidity and the cost. But is it possible that the agreement results in higher base employee costs?

François Desjardins, President and Chief Executive Officer

We're not foreshadowing that at all. We need to move forward in agreement that is sound for the bank. Now, carrying this level of expenses is not easy. And if we thought that we could resolve this sooner, we would have. But negotiations have to come to fruition. And we need to have a deal that is beneficial for the bank and its employees.

Darko Mihelic, RBC Capital Markets

Okay, understood. And my last question is sort of twofold. When I look at the – I guess, the whole building, a stronger foundation, as I look at that there's a lot of work I think that you have to do in simplifying your Retail Services. And you want to shift to a focus on advice. And it looks like it's going to take you all the way through to 2021 to sort of complete that.

And I just wanted to touch on the movement, I guess, away from mortgages towards more commercial. I mean, one of the things that I always think about with a bank is, you're building an expensive retail base and you want scale. And mortgages not only bring you a high ROE product, they also bring you a good touch with the customer in deposits and the ability to cross-sell into deposits.

So, I'm a little confused with – shifting the portfolio mix to sort of optimize margin, I suppose makes sense. But to optimize ROE, I would have thought that you would want to increase your mortgage balances and thereby help your deposit franchise and overall healthy ROE. So, can you help me understand, when I look at Page 26, why an optimal portfolio mix would have less mortgages and more commercial?

François Desjardins, President and Chief Executive Officer

Sure. Well, first of all, one of the things you said was mortgage have a high ROE. That's only true if you can securitize it on the basis of portfolio insurance or have insured mortgages. And you know the rules around insurance have radically changed the marketplace.

So, you're right, mortgages can attract customers to the business. But cross-selling other products and making them real long-time customers with other products and Visa cards and mutual funds and deposits, has to be the goal.

Now, we made the choice, for example, to stop referrals to the branch network from mortgage brokers, because over time – over the last decade or so, what we saw is that the retail branch network, which is an expensive piece of real estate to operate, was more used as a mono line administrative sector to bring in mortgages and to not cross-sell them and see them leave once again.

So, this refocus of the branch network has to be, and I think that is true for all financial institutions, is if it's operating a retail branch network, it has to be bringing in more deposits than it has loans. And part of the deposit base has to go to fund other pieces of business in the spectrum. Mostly, it's Business Services operations and our retail branch network has more loans right now than it has deposits. I know we haven't disclosed those numbers, but they are the numbers that we disclosed in 2016. And it's been getting slightly better, but it's still upside down.

The same can be said for the B2B business. One of the reasons why we're rolling out digital is to be able to cross-sell our mortgage customers with real banking products. And we didn't have those products on the shelf and so we're about to launch those through our adviser and broker network. So, yes, absolutely mortgages are important. But I would say that more important than that is growth of mortgages that is also something that we can convert into real, either digital Pan-Canadian or real branch-based advice-based customers is the plan.

Now the move from personal loans to commercial is not a choice. We want to grow both portfolios. But what we've said is, we want to grow the Business Services loan portfolio faster than the personal loan portfolio. Why? Because we feel that the ratio is off balance. We havereally big mortgage books as compared to other lending books that we have. So, we have to work on Visa cards and we have to work on building those cross-sell relationships. And also, we have to allow for growth in higher-margin products and help our business customers. And that really puts money on the bottom line and uses our capital effectively.

Darko Mihelic, RBC Capital Markets

Okay. Thanks very much, François.

François Desjardins, President and Chief Executive Officer

If I might add something, Darko. A big piece of the puzzle for us here, as you were saying in your – the first part of your question is about our branch network and it would take us a long time to get to full digital. That is true, full digital. But the moves that we're making right now to focus our branches on to advice-only, gets us partly there.

We've launched a new model at our Montreal corporate offices where there is no more money except for the ATMs, 22 advisers. So, a really big improvement in terms of how we use the space and really great reaction from customers. I think that this is really the way to go.

And the question is, will we open another one soon? Yes. We'll have a second one during the year. These are really interesting hubs. And for the rest of the branch network, we're moving to advice-only which reduces costs and starts that movement in towards that advice-only space.

Darko Mihelic, RBC Capital Markets

Thanks, François for answering my question. It's helpful. I guess, in the end, we're all curious about, at least I'm very curious about is, the answer to the dilemma of growing the deposits, right? Is the new branch – is there something with the new branch, the new digital banking that can really grow out your personal deposit balances?

François Desjardins, President and Chief Executive Officer

Well, that's the expectation. We've curtailed ourselves for a long time to think that Retail Services was just branch banking in Quebec. And for the last two quarters what we've been saying with bringing Craig Backman on board to lead personal digital banking is to say, sure we're going to operate the branch network where we're going to give advice to our customers in Quebec, that's fine. But from a deposit-raising perspective, we feel that the Laurentian Bank brand is really strong outside Quebec - much stronger than most people would think. We have not run a branch outside of Quebec except for Ottawa since 2003. And our brand is four times to five times better recognized than any of our smaller competitors. So, rolling out digital products - mostly basic banking and deposit products across Canada, we feel we have a great opportunity there in the next months and years.

Darko Mihelic, RBC Capital Markets

Okay. Thank you very much.

François Desjardins, President and Chief Executive Officer

You're welcome.

Operator

And your next question will come from the line of Richard Roth of TD Securities. Please go ahead.

Richard Roth, TD Securities

Hi. Good morning. Just first a small question. You mentioned $4.5 million. Is that extra provision related to that one commercial account that was booked this quarter?

François Desjardins, President and Chief Executive Officer

Liam?

William Mason, Executive Vice President, and Chief Risk Officer

Yes. Good morning, Richard. Yes, the $4.5 million as François Laurin mentioned is related to the exposure we disclosed last quarter.

Richard Roth, TD Securities

And do you see any potential for further provision? Or are you pretty confident now that you've sort of recognized all that needs to be recognized there?

William Mason, Executive Vice President, and Chief Risk Officer

Again, good question. The lending team continues to work on remediation of the account. We – as I disclosed sort of last quarter, we advised that the information last quarter was very preliminary. And when we released it we were taking $10 million. We believe that we're provisioned appropriately given the additional $4.5 million, but I'm sure you'd appreciate these exposures evolve. We're fully comfortable with where we are. The syndicated committee needs to work on it but never say never.

Richard Roth, TD Securities

Absolutely. Okay. And then with respect to other income, I guess, you guys cite market conditions as the primary driver for the sharp decline. What's – we haven't – we didn't really see that big of an impact from your peers, so what's unique about your business lines in other income that would make you more susceptible to sort of the market downturn we saw in November December?

François Desjardins, President and Chief Executive Officer

François?

Francois Laurin, Executive Vice President, Finance, Treasury and Capital Markets, and Chief Financial Officer

Sure. Basically, the volatility of the market. Our niches are in the small-cap equity market in terms of investment banking and trading and advisory, so we saw lots of volatility there and also – and much less origination and underwriting in corporate going to market and very little in the small cap market. And we don't play in the cross-border facilities and equity facilities.

On the fixed income side, where our strength is in the provincial and government bonds and money markets and you may have seen that the spread – the credit spread of provinces versus Canada - went very wide in December. So, November, December, there was not much take-up of those in our trading book. We got hit negatively on those. So, since January everything is more business as usual. But November, December, we're hit on those fronts for us.

Richard Roth, TD Securities

Okay. And how do – now that we have sort of two months now of a recovery January February, how do things look?

Francois Laurin, Executive Vice President, Finance, Treasury and Capital Markets, and Chief Financial Officer

On the fixed income side, since January things are more business as usual as we've seen before. The spread has come down on the provinces and then the activities are healthier now both on trading and underwriting.

And on the equity side, the pipeline is very strong, but the conditions have not yet come back to where they were before October. So, still working on that.

Richard Roth, TD Securities

You've seen a bit of a rebound, but not a full recovery?

Francois Laurin, Executive Vice President, Finance, Treasury and Capital Markets, and Chief Financial Officer

Yes.

Richard Roth, TD Securities

And I guess when I look – yes, when I look at other line items like commissions on sale of mutual funds and stuff, I would have expected given your transition to advice-only that these lines would be increasing rather than contracting, what's sort of – what am I getting wrong there?

Francois Laurin, Executive Vice President, Finance, Treasury and Capital Markets, and Chief Financial Officer

Sales on commission is very dependent on market value because the fees you earn there and the portfolio are based on the value of the portfolio. So, obviously, November, December and then the first quarter that even if you had an increase in volume, we have a decrease in value, so that decrease the fees that we earned related to those factors, Richard.

Richard Roth, TD Securities

Sure. But even, let's say, fee on investment accounts, which did sequentially increase, it's still down 20% year-over-year. I guess, what I'm trying to say is that, if you're converting an entire branch from transactional business to advice business, like shouldn't you see like substantial increases in income generated from those venues?

François Desjardins, President and Chief Executive Officer

I'll ask Stéphane Therrien to give you the lay of the land from a Retail Services point of view.

Stéphane Therrien, Executive Vice President, Personal and Commercial Banking

Thanks for your questions. Obviously, when we meet a client for advice, it's not to sell them necessarily mutual funds, right? So, with all the turmoil that has happened in the market, I should note that as well that our branch deposits have increased. So, it's the arbitrage or the right advice at the right time for the right customer.

So, a lot of our customers, I would say that lately have preferred to go solely on deposits than on GICs. And this is what you're seeing in terms of for the first time in a long time that our deposit level at retail have lately increased 3% quarter-over-quarter and 1% year-over-year.

François Desjardins, President and Chief Executive Officer

If I might add a couple of things on that. Of course, resetting the objectives for our retail branch network is not done overnight. We're seeing early signs like growth in deposits, which we haven't seen in a long time. So, that's very encouraging. And we do expect this to happen over time. I might add as well that the labor situation has been distracting to our managers and staff. And this we hope to get resolved very soon as well.

Richard Roth, TD Securities

Okay. Thanks, guys.

François Desjardins, President and Chief Executive Officer

You're welcome.

Operator

We will now take our next question from Marco Giurleo of CIBC. Please go ahead.

Marco Giurleo, CIBC World Markets

Marco Giurleo: Hi. Good morning.

François Desjardins, President and Chief Executive Officer

Good morning. I just wanted to follow-up on the line of questioning for the expenses. François, you mentioned $180 million as an appropriate run rate for expenses. So, just tying your commentary about the 10% headcount reduction, what type of impact will that have on the adjusted expense line? Or do you see that being redeployed elsewhere in 2019 keeping that run rate at around $180 million?

Francois Laurin, Executive Vice President, Finance, Treasury and Capital Markets, and Chief Financial Officer

The impact would be a reduction of expenses of $15 million to $20 million, to be implemented gradually over time.

Marco Giurleo, CIBC World Markets

Sorry, that's the impact from headcount reductions?

Francois Laurin, Executive Vice President, Finance, Treasury and Capital Markets, and Chief Financial Officer

Yes.

Marco Giurleo, CIBC World Markets

Okay. So, $15 million to $20 million annualized impact?

Francois Laurin, Executive Vice President, Finance, Treasury and Capital Markets, and Chief Financial Officer

That's it.

Marco Giurleo, CIBC World Markets

Okay.

Francois Laurin, Executive Vice President, Finance, Treasury and Capital Markets, and Chief Financial Officer

It should be implemented over the next 12 months.

Marco Giurleo, CIBC World Markets

All right. And then if I just look at the trajectory of expenses through say 2021. On slide 6, you have the timeline for your core banking system implementation and you show Phase two being implemented – the end of Phase two being implemented at the end of 2021. So, should – is that at the point we should expect a step-down in the expense line? And what type of impacts do you see from eliminating one of your – from eliminating your legacy platform and just running with the new system?

François Desjardins, President and Chief Executive Officer

You're right. Certainly, we're going to see a reduction in expenses when the second phase of core banking is implemented. But we don't have to wait that long to see a gradual expense reduction as we're going along. We've already implemented Phase 1. Business Services is on a new platform already. So, we will see some reductions in expenses as we're going along in the next couple of years. I could add – ask Deborah Rose to add some color on that if you wish?

Deborah Rose, Executive Vice President, and Chief Operating Officer

Sure. So, as François mentioned, what we have remaining to do is to convert a small portion of Business Services accounts – would be bank accounts, business deposits line of credit and then the Retail Services accounts. And as François mentioned, as we're doing that, we're also retiring some of the legacy systems. And all of that has been built into and factored into our 2021 objectives for the efficiency ratio.

Marco Giurleo, CIBC World Markets

All right. My second question is with respect to your syndicated loan exposures. There's been a few mentions over the past years about just exposures and the provisions that you've had to take against those exposures. So, just wondering what percentage of your portfolio is syndicated; and would you be able to tell us how many loans that exposure consists of?

François Desjardins, President and Chief Executive Officer

I'll ask Liam Mason to comment on that.

William Mason, Executive Vice President, and Chief Risk Officer

Sure. I mean, just Marco a couple of general comments. Our appetite for borrower – individual borrow limits is quite conservative and we did have some hiccups a number of years ago. But our appetite and volume in terms of borrow limit is much smaller than it's been traditionally. We now have borrow limits of about $40 million. Overall, our syndicated loans amount to 10% or about $1.2 billion. But it's a diversified book and we have very conservative and tight underwriting standards. And I think that's reflected in the good years that we've seen in terms of PCLs. We would view this as an isolated incident in terms of this, given the accounting discrepancies. And you've seen some other banks that have participated in this facility release also and point out that it's a surprise to them as well.

Marco Giurleo, CIBC World Markets

All right. And just a final question on liquidity. François, you've said a few times today that you have a very strong liquidity position, in part you've mentioned that you're holding more liquidity than you need to because of what – the negotiations with the union. But in light of OSFI's newly proposed liquidity requirements released earlier this month I was wondering if you could comment on your – well, on the impact that these new requirements might have on your liquidity position. Would you need – would you be able to reduce your liquidity based on these new requirements?

François Desjardins, President and Chief Executive Officer

I'll ask François Laurin to comment on it.

Francois Laurin, Executive Vice President, Finance, Treasury and Capital Markets, and Chief Financial Officer

Marco, it's still too early to determine the final impact given the ongoing consultations between the parties involved. The consultation is still due to commence in March. We know – clearly, we know that our LCR level is at the very high-end of the big six banks disclosure ratios. And our internal liquidity metric is even more conservative than the LCR. So, obviously two things that underlies our prudent approach towards managing liquidity and we continue to prioritize term funding and further diversify our source of deposits and including the launch of the digital bank that we mentioned earlier. And given that our strong liquidity and diversified funding, we're confident that we can adapt to that new regulation and would not have a material impact on profitability at this point based on what we know.

François Desjardins, President and Chief Executive Officer

So, the short answer to the question is yes, we would be able to reduce our liquidity and eliminate $7 million worth of impact on the bottom line.

Marco Giurleo, CIBC World Markets

Okay, perfect. Thanks. That's it for me.

Operator

And we'll go ahead with the next question from Gabriel Dechaine of National Bank. Please go ahead.

Gabriel Dechaine, National Bank Financial

Good morning. I want to follow-up on this liquidity stuff. Firstly, the mechanics. So, are we – is your balance sheet still going to be adjusted for the additional liquidity you're taking on? And where am I going to see that; is it you keep taking loans down and replacing those with cash, or are you going to take on wholesale deposits or something just to build up a nice liquidity buffer?

François Desjardins, President and Chief Executive Officer

No. Gabriel, this is François Desjardins. What we're disclosing is that this is already built into our results and it has been built into our results since December of 2017. We started building more liquidity into our balance sheets when we saw what was happening in the wake of Home Capital, but not to the levels that we have now. When the end of the collective agreements occurred, as part of normal business continuity planning, we need to build ourselves a buffer over and above normal liquidity levels. And that's what we've been carrying ever since.

I think that in the last few quarters you've been asking how come liquidity has been impacting how much. I thought it would be just fair to give you how much that is impacting our net interest income to keep that on the books. Our responsibility of course is the safety and soundness of our institution and our customers and that's a normal course. But going forward, once – we're working towards an agreement with the union – once that is behind us, normally we should be able to take that down to a normalized level and see the benefit on NII and the bottom line. That's the message.

Gabriel Dechaine, National Bank Financial

Okay. So, you've been running at these levels you're just quantifying it now. Maybe a stupid question on my part, but what is the length between the union negotiation and the uncertainty there and having to maintain higher liquidity? I can come up with my own ideas, but I just – it's not painfully obvious I guess.

François Desjardins, President and Chief Executive Officer

Well in a work conflict situation the worst-case scenario is some of the operations get stopped or halted, etc. And of course, this bank has to fund itself. So, there might be more volatility in terms of the ability of the bank to continue its regular branchoperations. Obviously, this is not 1984 anymore. 96% of all transactions are done outside of branches. So, the customer base,, in terms of a work conflict should be largely unaffected. But we have to take no chances and we're just being prudent by managing this at a level that's higher than normal.

Gabriel Dechaine, National Bank Financial

So, moving on to other expenses. Regulatory and compliance costs have been moving higher. And maybe they're not linked. But the message I was getting from you last year was that in the wake of the mortgage issues, you were seeing an imminent rise in these types of costs. And it appears to be the case that you're incurring these costs. Are they connected? Or – and if not what's driving them? And how I guess secular are these types of costs?

François Desjardins, President and Chief Executive Officer

No, they're not. But I'll ask François to give some indication of what these expenses are.

Francois Laurin, Executive Vice President, Finance, Treasury and Capital Markets, and Chief Financial Officer

We've been mentioning that we're in years of investment. So, we have higher advisory service fees related to the implementation of our new core banking system, the development and implementation of digital solution, the adoption of AIRB as well as all other fees that we incur to the reorganization, optimization and simplification of Retail Services as well as what we mentioned earlier, professional fees and labor-related costs as well as all other regulatory cost implementation, whether it's the deposits insurance costs and other projects like the conversions to IFRS 9, IFRS 15 and other – all other similar regulatory expenses that are not project-driven but expense – OpEx-driven. So, that's a mix of all those things that we have been incurring and when we say investment, we mean not only CapEx, but P&L investment to improve our processes and everything else.

Gabriel Dechaine, National Bank Financial

Okay. And just to clarify and this is in relation to Darko's question on that expense line item, $179 million. I'm not quite sure I got the message there and maybe you can help me. Is that the number you expected to be kind of flat for the rest of the year $179 million or $180 million or so, or does it go up despite the labor cost reduction from that severance charge?

Francois Laurin, Executive Vice President, Finance, Treasury and Capital Markets, and Chief Financial Officer

Aside from the reduction we mentioned, this should be mostly salary, we're talking here other expenses, this should be at a very similar level over the next few quarters.

Gabriel Dechaine, National Bank Financial

Okay. All right. And then if next year you have the union negotiation all tied up then they go down that's possibly the case?

Francois Laurin, Executive Vice President, Finance, Treasury and Capital Markets, and Chief Financial Officer

They're linked to our regulatory process and investment. So, we said 2018 and 2019 are years of investments, so you should see starting somewhere in 2020 a reduction of those.

Gabriel Dechaine, National Bank Financial

Okay.

François Desjardins, President and Chief Executive Officer

Gabriel, if you look at the rest of the year, these would be flat. We would save a portion of $10 million linked to the labor situation. And gradually, like François just said, $15 million to $20 million of annualized expenses linked to the announcements we made for headcount reduction today.

Gabriel Dechaine, National Bank Financial

Thank you.

François Desjardins, President and Chief Executive Officer

You are welcome.

Operator

We'll go ahead with our next question from Scott Chan of Canaccord Genuity. Please go ahead.

Scott Chan, Canaccord Genuity

Hi. Good morning. I just want to go to the US balances and I'm assuming that's mostly NCF and inventory finance. And going through the MD&A, you kind of talked about inventory financing being kind of a key growth driver at commercial. And we saw the largest sequential increase this quarter in terms of the US balance as $1.4 billion to $1.8 billion. Can you maybe talk about that business particularly? And kind of what's supporting that incremental growth?

François Desjardins, President and Chief Executive Officer

I'll ask Stéphane Therrien to answer that.

Stéphane Therrien, Executive Vice President, Personal and Commercial Banking

Yeah, you're right. We're really happy with this acquisition. We got a team of seasoned lender all specialized in that industry with a lot of relationships. The reason why that business was up for sale was lack of liquidity to continue to grow. And when we did the acquisition, that's exactly what we said that what we were bringing to the table - the liquidity tthey needed to continue their growth. And they've been delivering according to plan and we're really happy with this.

Scott Chan, Canaccord Genuity

And we see the growth on the US side, but what about on the Canadian side, is it growing as well?

Stéphane Therrien, Executive Vice President, Personal and Commercial Banking

Stéphane Therrien: Yeah. But it's smaller, right? Northpoint's overall balance sheet is 10% in Canada. So, yeah, we're seeing similar growth, but obviously on a smaller scale.

Scott Chan, Canaccord Genuity

Okay. And if I go to page two on your sup, like under interest expense, under other, we saw a sequential increase of about $10 million quarter-over-quarter. And I just want to clarify kind of what maybe that other – like what's involved in that other and why was it increased so much quarter-over-quarter, other interest expense.

Francois Laurin, Executive Vice President, Finance, Treasury and Capital Markets, and Chief Financial Officer

François Laurin here, Scott. Some of the other expenses includes taxes, insurance, training expenses, recruitment and administration expenses. We don't detail all of those. But basically, that includes all of these basic items under that caption.

Scott Chan, Canaccord Genuity

So, like looking forward is that – like it was a pretty big jump after it kind of being stable or kind of growing with the book. Like is that Q1 number like more representative, or is it kind of going back to more average level?

Francois Laurin, Executive Vice President, Finance, Treasury and Capital Markets, and Chief Financial Officer

Sorry, Scott you said you were on page two?

Scott Chan, Canaccord Genuity

Page 2 of the supplemental, under interest expense, so like other interest expense.

Francois Laurin, Executive Vice President, Finance, Treasury and Capital Markets, and Chief Financial Officer

I'll get back to you for specific, Scott, on that one. Sorry about that.

Scott Chan, Canaccord Genuity

Okay. No problem. Thank you.

Francois Laurin, Executive Vice President, Finance, Treasury and Capital Markets, and Chief Financial Officer

Next question.

Operator

We will take the next question from Sumit Malhotra with Scotiabank. Please go ahead.

Sumit Malhotra, Scotiabank

Thanks. Good morning. And sorry about before guys. I had to switch lines briefly. My first question is going to be on credit and it's most likely for Liam. So, first quarter that you're reporting this under IFRS 9, we see a $2 million release from the non-impaired stage 1, stage 2 portfolios combined. Just as we get used to you reporting under this standard, I wanted to ask you whether it was – mechanically or formulaically were there specific factors that resulted in the release in this initial quarter from that aggregate portfolio?

William Mason, Executive Vice President, and Chief Risk Officer

Sumit, thank you for your question, and good morning. I think you have to be careful. We're really talking IAS 39 to IFRS 9. As you understand two different models. So, some of it is in terms of the transition

between those and shake out as we formalize our methodology. As you know, we gave a range last time. In terms of the release, we've done a scrub and a calibration of our models this quarter. That's why we gave a range last time and tightened those up. And I think what you'll see right now – and some of that is just stabilizing of the numbers over the last sort of a trend. So, we're very comfortable with where we are with the numbers now and building a base and have the calibration. So, I would not put too much credence in the change Q1 to Q2 – sorry Q4 to Q1.

Sumit Malhotra, Scotiabank

Sumit Malhotra: Nothing to read into right now from a release from that?

William Mason, Executive Vice President, and Chief Risk Officer

No, not at this juncture. I think when you're implementing – and that's why we gave the range last quarter. We're within the range but you've got some puts and takes as you finalize your models.

Sumit Malhotra, Scotiabank

And maybe staying with you since we had this discussion last time. The way that the additional provision on the syndicated loan is being talked about today it's almost as if it's a one-off. But I mean as the portfolio shifts more towards commercial lending and away from the low loss rate of mortgages, I think it's reasonable to expect there are going to be a few bumps in the roads so to speak. So, when you think about IFRS 9, and again as we get more comfortable with that, you had indicated that getting to a normalized provision rate of 20 basis points was a reasonable expectation. So, why is it that it sounds like this provision that you took this quarter, which even still only got you to 12 basis points, seems like it's being characterized as a one-off? Am I reading you correctly on that?

William Mason, Executive Vice President, and Chief Risk Officer

You are reading – we believe this loan to be a one-off, Sumit, very much because of the special circumstances around it. We do have very conservative and disciplined underwriting processes. That said, we have indicated – I mean, I'll say two things. One we have indicated that as our mix slightly edges towards commercial, we will have slightly more volatility. But also, IFRS 9 based on – you have the benign scenario, you have your base scenario, you have the adverse scenario, and as expectations work just from the methodology, and I think you've heard this from other banks, the basic methodology itself can drive more volatility in general. So, I just but right now our guidance for PCLs remains the same consistent with what we've indicated before.

Sumit Malhotra, Scotiabank

Thanks for that.

François Desjardins, President and Chief Executive Officer

Sorry, Sumit, the bottom line here is that and we have been indicating over I think the last three years that we should be moving upwards in terms of our loan losses over time. This has not occurred. We continue to see really low loan losses. We continue to have the same message, because we don't want you to be surprised at one point. But this one loan here is a real one-off that is surprising to the syndicate. Over the next few quarters, don't expect the loan losses to go up as sharply. What we're indicating is that over time, as the loan mix is changing or the environment changes, we might see some higher loan losses over time.

William Mason, Executive Vice President, and Chief Risk Officer

But I would add to François' comments, we also expect higher margins commensurate with that uptick.

Sumit Malhotra, Scotiabank

That makes sense. I'll wrap it up with one for François Desjardins. I mean another trade off, if you will, of commercial growth getting stronger where the mortgage book is being repositioned is potentially you're going to see more of a drawn on capital. And the last couple of quarters, your CET1 ratio has been flatter in terms of the sequential move kind of in the same range anyway. I guess, François, the question to you would be, even versus your other standardized peer, you've been managing with a lower CET1 ratio for some period of time. Just remind us how are you thinking about the range on CET1, and where would you classify your position relative to that today?

François Desjardins, President and Chief Executive Officer

Yes. A couple of quarters ago we moved the CET1 ratio range to 8.3% to 8.7%. That is still our range and has not moved up. We said that we would be running at the higher end of that range. And, of course, with the changes in the mix and moves that we made last year, we've been running slightly above that range. But one of the reasons why this range is the way it is, is because of the conservatism of the lending book. So, this is something that we don't take out of a hat. We calculate this as being what is required for managing the risk of the organization.

So, over time as there is a shift towards commercial, that might still go up. But for the time being, we're comfortable with this range. And of course, we're above the range right now, so there's room there. The other thing I might add is that running at a higher level of capital is also to give us some flexibility in terms of the portfolios but also in the investments that we're making in software.

As you know, software implementations are really day one very punitive on CET1 regulatory capital. An investment in software hits the P&L over time through amortization but hits the capital ratio as it is immediately deducted from the capital ratio day one as the spend is made. So, the investments that we've been making over the last year, we're still making – does eat away at the regulatory capital ratio. And we have to maintain those as we're going forward. Liam, do you want to add something?

William Mason, Executive Vice President, and Chief Risk Officer

Yes. I think with the sort of low, I mean, I think you have to look at us on an apples-to-apples basis with everyone else. And think about us in terms of an AIRB equivalent in excess of 200 basis points above that. So, if you did that, we're at an AIRB equivalent of 10.9% and we're not a DSIB, with all of the obligations with DSIB. And so, apples-to-apples and we're probably well above – we're above 10.9% if you really adjust for what our expectations are. So, I'd take a little umbrage with the – operating at low versus peers. You put us on a like-for-like basis, we are very strong from a capital perspective.

Sumit Malhotra, Scotiabank

Well, that's a good way for us to go to this next point and maybe wrap it up is for a variety of reasons, the earnings power of the company on a per share basis has been on a decline for the past year. And yet when we look at your capital deployment actions, you have still raised the dividend along with the Q4 and the Q2 results. Many of your peers across the sector, including some that historically have not done so, have been allocating capital to share repurchases. I hear your umbrage, Liam, and I guess I'd say to you if the company is so confident in their capital position in what's been a difficult period for shareholders, wouldn't some of that deployment be better served for them in buying the stock at significant discount to book if you are confident in both capital and the return to higher profitability?

Francois Laurin, Executive Vice President, Finance, Treasury and Capital Markets, and Chief Financial Officer

I think there's a difference between being confident and having it being required for us to achieve our plans. Capital deployment in investments that we're making and in the growth that we're projecting is important. So, of course when we get into IRB implementation that – what Liam is talking about is there's a potential for capital release at that point or capital redeployment. But for the time being, we're at 8.9% with a range of 8.3% to 8.7%. It's strong. And we look at dividend hikes and share buybacks as options every quarter. But for right now, this is not the plan.

François Desjardins, President and Chief Executive Officer

I would say from a dividend perspective, we're in the middle of a transformation which should result in improved efficiency and profitability. So, I'm sure we have a high payout ratio right now. But as profitability returns, the expectation is that the dividend payout goes back to its range. Of course, we believe that the level of earnings that we have this quarter doesn't reflect the future earnings power of the corporation. To me, there's a very big difference between run rate expenses or operational expenses and what we're doing now which is investing in ourselves in this age of disruption. Shareholders are investing in Laurentian because they believe in the endgame. We're resetting this bank and rebuilding it for the next decade. This is a huge undertaking. And I'm not going to be shy about the fact that we believe that this is the best strategy to get to higher value for shareholders over time.

Sumit Malhotra, Scotiabank

No. Look I hear you and will stop here. Like it's obviously somewhat philosophically here, I think the dividend increases in the last couple of quarters while earnings power has been under pressure you did – you could say it's a way to reward long-term shareholders. And other might say you're not necessarily getting value for it in the stock. And as I say with – I've never met a CEO who's happy with the way share price is trading. And I think in your case the qualm would be some of that capital deployment maybe would be better share for shareholders relative to the stock. And that's where I wanted to take your temperature on how much excess capital and deployment ability you have. But that was really the gist of the discussion, so thanks for that.

François Desjardins, President and Chief Executive Officer

Well, as you can see in our yearly proxies, the management team and in particular myself own a significant number of Laurentian Bank shares. So, the goals of the shareholders and our goals are extremely aligned. So, our belief in this long-term strategy is to build wealth for long-term value. And if I look back at the share price – of course, never there's a CEO that's happy with the share price. But when we launched the plan, as you remember, we wanted to get to profitability to a level that would push the price of book over one on a sustainable basis and hopefully somewhere in between 1 and 1.5 depending on market conditions. That's still the goal.

Sumit Malhotra, Scotiabank

Thanks for your times guys.

François Desjardins, President and Chief Executive Officer

Thanks, Sumit.

Operator

Ladies and gentlemen, this concludes the Q&A session for today. I'd like to hand it back over to Mr François Desjardins for closing remarks please.

François Desjardins, President and Chief Executive Officer

Well, thanks everybody for your questions. Our determination to build a better and different financial institution has not wavered. And we look forward to reaping the benefits of the investments that we're making in our business. 2019 will be a year in which we complete important elements of our plan, including the implementation of most of core banking, the launch of digital banking and the transformation of our branches to the advice-only model. Transformation is not easy, but rewards those who have the courage to persist through the headwinds. We're convinced that our efforts will ensure that our organization remains relevant and profitable in the months and years to come. I will now turn the call back to Susan.

Susan Cohen, Director, Investor Relations

Thank you for joining us today. Should you have any further questions, our contact information is included at the end of the presentation. Our second quarter 2019 conference call will be held on 30th May and we look forward to speaking with you then. Have a great day.

Operator

Ladies and gentlemen, this concludes today's call. We thank you for your participation. You may now disconnect your lines and have a wonderful day everyone.