LAURENTIAN BANK

CONFERENCE CALL

TRANSCRIPT

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PRESENTATION

Operator

Good afternoon, ladies and gentlemen. Welcome to the Laurentienne Banque conference call.

I would now like to turn the meeting over to Madame Gladys Caron. Please go ahead, Madame Caron.

Gladys Caron, Media and Investor Relations

Merci. Bienvenue. Good afternoon everyone. Our press release was issued today on Canada newswire and is posted on our website. This afternoon's overview of our second quarter 2010 results will be provided by our President and CEO, Rejean Robitaille, as well as by our CFO, Michel Lauzon. Other members of our senior management team are also present on this call to answer any questions. You will find their names and titles on slide 18 of the presentation available on our website. Mr. Robitaille and Lauzon will refer to that presentation throughout their speeches.

During this conference call forward-looking statements may be made and if 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 prefer to our press release or to slide two of the presentation. I will now turn the floor over to Mr. Robitaille.

Rejean Robitaille, President and Chief Executive Officer

And thank you, Gladys. Good afternoon, ladies and gentlemen. So the second quarter, 2010 was another very solid quarter for Laurentienne Banque and I'm very satisfied with our results. We maintained our momentum with strong year-over-year growth in our profitability and in our balance sheet. Owing to numerous growth and development initiatives that are gaining traction, revenue increased substantially, demonstrating our capacity for organic growth. Net interest income was significantly higher than a year earlier, benefitting from the improvement in net interest margins, as well as from volume growth. We were particularly pleased with our level of non-interest income, given that income from securitization fell sharply but was replaced by other sources of revenue.

This testifies to our ability to diversify our revenue base, producing earnings, with—which are core and sustainable. Furthermore, our strong positive operating leverage generated a considerable improvement in the bank's efficiency ratio. Overall credit quality has stabilized in the quarter as retail portfolios are clearly showing signs of improvement. We continue to progress in a sustainable manner and are well positioned to benefit from improving economic conditions.

As shown on slide three of our PowerPoint presentation, for second quarter of 2010, earnings per share increased by 39 percent year-over-year to $1.06, with net income of $28.3 million. Return on equity reached 10.9 percent in the second quarter of 2010, compared with 8.5 a year earlier. These strong results were achieved despite higher loan loss provisions and as previously mentioned, significantly lower securitization income.

Turning to slide four; after six months, management believes that the bank is well positioned to meet the 2010 objectives set at the beginning of the year. Our business plan, in a more supported economic environment, in conjunction with our solid capital base, provide the flexibility to prudently continue to deliver growth.

I will now call upon Michel to provide you with a more in depth analysis of our financial performance. Michel?

Michel Lauzon, Chief Financial Officer

Thank you Rejean. Financial highlights of the second quarter of 2010 can be found on slide five. We are particularly pleased that the total revenue increased by 15 percent year-over-year. This was driven by 25 percent rise in net interest income. The provision for loan losses; 16 million, was equal to the provision in the first quarter of 2010, but 4 million higher than in the first quarter of 2009.

Higher expenses, associated with various initiatives to support business development, pushed non-interest expenses up by 8 percent year-over-year. In the second quarter of 2010, diluted EPS and ROE reached $1.06 per share and 10.9 percent respectively, compared with $0.76 and 8.5 percent in the second quarter of 2009.

Delving deeper into the results, I will discuss the main drivers of the bank's performance during the second quarter of 2010. Firstly, net interest income of 117.6 million in the second quarter of 2010 increased by 23.6 million from the second quarter of 2009. Strong year-over-year loan and deposit growth, as well as margin expansion contributed to this performance.

As highlighted on slide six, a net interest margin at 2.10 percent was 18 basis points higher than a net interest margin of 1.92 percent earned in the second quarter of 2009. The combination of the low interest rate environment in the second quarter of 2009, which significantly hampered profitability and the re-pricing initiatives undertaken last year to strengthen margins contributed to the improvement. The margin was three basis points lower than in the first quarter of 2010, mainly due to changes in business mix and pressure on pricing.

Secondly, while other income was $60.5 million in the second quarter of 2010 was very similar to the 60.7 million recorded in the second quarter of 2009, its composition was very different. Securitization income of $300,000 in the second quarter of 2010 was $8.3 million lower than in the second quarter of 2009. This was a result of lower securitization gains ensuing from the tighter—tightening of credit spreads, as well as the effect of mark to market revaluations on retained interest and related economic hedges.

Revenue from treasury and financial market operations also declined by 1.4 million to 4.6 million. On the other hand seasoned commissions on loans and deposits rose by 3.9—3.8 million, sorry, year-over-year and income from credit insurance and sales of mutual funds each increased by 0.8 million over the same period. In other words, the more volatile securitization income was replaced by more stable and core revenues which we consider to be notable achievement. In addition, improved market conditions resulted in revenues from brokerage operations increasing by 3 million.

Thirdly, as highlighted on slide seven, the provision for loan losses amounted to $16 million in the second quarter of 2010, unchanged from last quarter, but higher than the 12 million recorded a year ago. The year-over-year increase largely reflects losses associated with the limited number of commercial loans and mortgages which, in most cycles, tend to lag the economic recovery. Higher loan volumes also impacted the level of provisions.

During the quarter the credit quality of our consumer loan portfolios demonstrated improvement which resulted in the reduction in the loan loss provisions allocated to these portfolios.

Slide eight highlights the credit quality of the loan portfolio. Gross impaired loans of 161.9 million at the end of the second quarter of 2010 increased by 4.6 million from the end of the first quarter. This increase largely results from the previously mentioned deterioration in a few commercial and real estate loans which was partially offset by improvement in retail loan portfolios. Net impaired loans stood at 37.8 million, as at April 30, 2010, compared to 36 million as at January 31, 2010.

Nonetheless the ratio of gross impaired loans to total loans and BAs (phon) and reverse repos remains at an acceptable 92 basis points. Therefore, while we continue to closely monitor market conditions, the credit quality of our loan portfolio remains satisfactory in the quarter.

As presented on slide nine, deficiency ratio for the first six months of 2010 was 68 percent. Specifically in the second quarter of 2010 the ratio was 69.4 percent, which was a significant improvement from the 73.7 percent a year earlier. The strong positive operating leverage of 6.7 percent in the second quarter of 2010 contributed to this improvement.

One of the main drivers of the bank's improving results is loan and deposit growth, as highlighted on slide 10. Total loans and BAs rose by 2.4 billion or 16 percent over the last 12 months. Contributing to this growth were residential mortgages which increased by 1.8 billion or 28 percent, benefitting from the effective distribution channels and strong underwriting activity. Personal loans were virtually unchanged year-over-year, as solid growth in investment loans and home equity lines of credit were more than offset by the impact of our strategy to further reduce our exposure to point of sale financing.

While total deposits increased by 1.5 billion over the last 12 months, thanks in large part to the success of B2B Trust's high interest investment account, the rate of growth slowed sequentially. This was a result of the bank actively managing its liquidity levels to meet its funding requirements and its focus on pricing. That being said, retail deposits continue to provide a stable and diversified source of funding at comparatively attractive rates. A conservative loan portfolio, prudently managed liquidity and a solid base of personal retail deposits positioned the bank well for the future.

I would also like to point out that at the end of the second quarter, our capital position remained strong with a tier one capital ratio of 10.9 percent and a tangible common equity ratio of 9 percent, which reflects the high quality of the bank's capital.

We will now turn to the performance of our business segments on slide 11. All our business segments reported strong revenue growth and we were particularly pleased with the exceptional growth in income for the real estate and commercial segment and from B2B Trust.

Slide 12 shows that total revenue in retail in SME Quebec, in the second quarter of 2010, rose by 7 percent compared to a year ago, reaching $111.4 million. This increase was a result of higher loan and deposit volumes and higher fee income. However, net interest margins were under pressure during the quarter, due to low interest rate environment and sustained competition on fixed term retail products. Loan loss provisions increased by 3.4 million and $11.5 million, largely owing to one commercial account, although the credit quality of retail loan portfolios improved during the quarter. Non-interest expenses rose by 5 percent year-over-year to 87.3 million, mainly as a result of increases in salaries and employee benefits and staffing levels. Net income in the second quarter of 2010 reached 10.1 million, 3 percent higher than a year earlier.

Slide 13 highlights the results of the real estate and commercial segment. Total revenue increased by 38 percent to 29.1 million in the second quarter of 2010, mainly as a result of higher loan volumes and improved margins, owing to repricing (phon) measures initiated last year. Loan losses rose modestly to 4 million in the second quarter of 2010, compared to 3.2 million in the second quarter of 2009 as a result of provisions being recorded on certain deteriorating accounts as well as higher loan volumes. However, the overall credit quality of the portfolio remains satisfactory considering the economic slowdown last year and we are cautiously optimistic about credit quality in the commercial book for the remainder of the year.

Non-interest expenses decreased by 1.3 million to 5.6 million in the second quarter of 2010, owing to the reversal of operational loss provisions and lower variable compensation. Net income increased by 80 percent year-over-year to 13.7 million in the second quarter of 2010.

As shown on slide 14, B2B Trust's revenue increased by 24 percent to $29.6 million in the second quarter of 2010. A significant $5.4 million increase in net interest income was a result of volume growth and recovering margins. Loan losses, which include provisions under investment lending activities, remained low at $500,000 in the second quarter of 2010, compared with 700,000 in the second quarter of 2009.

Higher salary and employee benefits caused non-interest expenses to increase to $12.8 million in the second quarter of 2010, compared with 11.7 million in the second quarter of 2009. Positive operating leverage resulted in the efficiency ratio improving by nearly 6 percent to 43 percent. Net income rose by 45 percent, year-over-year to 11.4 million in the second quarter of 2010.

As can be seen from slide 15, revenues in Laurentienne Banque securities and capital markets grew by 9 percent to $15.3 million in the second quarter of 2010. The continued strong performance of the institutional fixed income division and improving revenues from retail brokerage, as our retail advisor network expands, more than compensated for the decline from other capital market operations. Higher variable compensation costs were largely responsible for non-interest expenses increasing to $11.7 million in the second quarter of 2010, from 9.2 million in the second quarter of 2009. Net income decreased to 2.6 million in the second quarter of 2010, from 3.3 million in the second quarter of 2009.

The other sector, presented on slide 16 posted a negative contribution to net income of 9.3 million in the second quarter of 2010, compared with a negative contribution of 7.4 million in 2009. Net interest income improved to negative 8.7 million in the second quarter of 2010, compared to negative 17.8 million in the second quarter of 2009. Last year higher funding costs and lower margins on liquid assets adversely impacted results. Other income for the second quarter of 2010 was 4—1.4 million, compared to 9.7 million a year ago. The decline was a result of lower income from securitization and from treasury and financial market operations.

This concludes my comments. Rejean will offer some closing remarks.

Rejean Robitaille, President and Chief Executive Officer

And thanks, Michel. So not only were we satisfied with the performance of our second quarter of 2010, but we are proud of our performance over the longer term. Over the past three fiscal years, average annual earnings increased by 20 percent, while average annual growth in loans and deposits has been 9 percent and 13 percent, respectively. This testifies to the effectiveness of our agile business model and our execution. Our performance also benefits from our diversification, both geographic, with about 40 percent of loans originating outside of Quebec and sector (inaudible) with a good business mix. Our diversified portfolios are further strengthened by our prudent approach to risk management, liquidity and capital.

Our focus on our strategy—on our strategy priority, sorry, those being increasing profitability, improving efficiency and developing our human capital, remains unrelenting. These serve to guide our actions and prioritize our investments. These are targeted towards our three growth engines; retail banking, real estate financing and B2B Trust. Within each growth engine, as well as within our growing business segment Laurentienne Banque securities, are numerous opportunities for growth and development. We expect that these opportunities will fuel our future growth and earnings. Moreover, our profitability has been, and we want it to continue to be, core, strong and sustainable. We are confident of our potential, given our effective business model, our clear strategy priorities and our dynamic growth engines. Furthermore, we are determined to continue to develop and grow in order to deliver sustainable long-term profitability.

I will now turn the floor back to Gladys.

Gladys Caron, Media and Investor Relations

At this point I would like to turn the call over to the conference operator for the question and answer session. Please feel free to ask your questions in English or in French.

QUESTION AND ANSWER SESSION

Operator

Thank you. We will now take questions from the telephone lines. If you're using a speakerphone, please lift the handset before making your selection. You may press star, one at this time if you have a question. Should you wish to cancel your question, please press the pound sign. There will be a brief pause while the participants register. We thank you for your patience.

The first question is from Dave Monk (phon) from RBC Capital Markets. Please go ahead.

Dave Mun, RBC Capital Markets

Thanks and good afternoon. Just one quick question for me. Revenues would have been a lot stronger if it wasn't for the decline in the securitization income and in that securitization gain there was a mark to market revaluation on retained interest and related hedges. That negative impact was a lot larger than in prior quarters and I think the last time it was that large was in Q1 '09. Just wondered, can you just remind us what it is that made that so large and if there's something that we can track to help determine the magnitude and the direction of that adjustment? Because I'm not sure if I'm getting the same sort of direction in prior quarters.

Rejean Robitaille, President and Chief Executive Officer

Good afternoon, Dave. I think first of all, you're right, we were able to compensate a lower securitization income during the quarter; $8 million, with more core other income. So we're quite proud of that. And, I'll ask Michel to give you a little bit more flavour on the impact on securitization.

Michel Lauzon, Chief Financial Officer

Okay, well thank you Rejean. We did securitize about $182 million of loans in the quarter, basically replacing what was coming back on the balance sheet through repayments and prepayments. That generated a net revenue of roughly $5 million. However, the increase in mortgage rates towards the end of the quarter did mean that we had to revaluate the penalty payments from prepayments that are flowing into the off balance sheet structure of debt (phon). And, as a result, the cash flows going into the structure are being lowered. We had to re-evaluate those hedges at a lower level. And so that generated a little bit of a drag on earnings. As well there were some assumption changes in some of the modelling that we do for that. And that resulted in some cases some gains and in some cases some losses. So, unfortunately I can't give you any more guidance because it is related to market events and client behaviour, but we were—we were impacted a bit more in this quarter which negated narrower gains because the gains we did make on the securitization that we did do were a bit narrower because of compressed spreads between mortgage rates early in the quarter and market rates.

Rejean Robitaille, President and Chief Executive Officer

And also, as we announced that—well, in fact, in our objectives in the beginning of the year, we still think that we will have less securitization revenue going forward, as we already mentioned that before.

Dave Mun, RBC Capital Markets

Great. Thank you.

Operator

Thank you. The following question is from Michael Goldberg from Desjardins Securities. Please go ahead. Mr. Goldberg, your line is now open.

Michael Goldberg, Desjardins Securities

Yes, thank you, a couple of questions. What happened to the high interest savings balances in B2B Trust? Has there been any erosion?

Rejean Robitaille, President and Chief Executive Officer

They—good afternoon, Michael. I ask Francois Desjardins (phon) of B2B Trust to answer that question.

Francois Desjardins, B2B Trust

The answer to that is, no, there has not been any erosion in the portfolio. It's been slightly growing since the beginning of the year.

Michael Goldberg, Desjardins Securities

Okay. And—

Rejean Robitaille, President and Chief Executive Officer

(Inaudible) reduced a little bit the pace of that growth, as you know, because we have still lots of liquidities so make sure that we're putting that cash to work. So, that's one probably explanation, but as Francois mentioned, still very positive on trends on that product.

Michael Goldberg, Desjardins Securities

Okay. Have you sensed though, more intense competition for those high rate balances?

Rejean Robitaille, President and Chief Executive Officer

Francois, once again.

Francois Desjardins, B2B Trust

Well there's more competition out there but we haven't sensed a competition in the sense that would lead to erosion of balances. I think that it's a product that's more popular out there and it's—I think that Canadians are saving a little bit more; at least investors are. And, these types of products are being used as a cash component of their investment portfolios. So, even though there's more offer (phon) out there, that doesn't seem to have an impact on balances at this time. And the outlook, I think is quite positive.

Michael Goldberg, Desjardins Securities

Okay. Now turning to your net interest margin, you talked about pricing pressure and a shift to a somewhat less risk —less rich business mix. Do you think that your net interest margin has plateaued (inaudible)?

Michel Lauzon, Chief Financial Officer

Yes, Michael, I think there's several factors that were impacting the margin in the quarter. The two I mentioned in my speech were tightening pressure on the fixed rate side of the retail products and that is a pressure that has started to build since the beginning of the year and it's continuing. It's being felt both in B2B Trust and in our retail and SME lines of business. The fact that growth has come mostly from the mortgage book, also, it has a slightly less rich margin component, especially with the competition out there. And so it has drifted our margin slightly lower. However, we're carrying a lot of liquidity into the second quarter as it was the case also in the first quarter. We have reduced that liquidity. So, while there's still continuing pressure on the retail side, we should see a little positive mixed shift where we're redeploying liquid assets into loans in the third quarter. But, all in all, the mixed margins should hover plus or minus five basis points around where it is now.

Michael Goldberg, Desjardins Securities

Thank you.

Rejean Robitaille, President and Chief Executive Officer

And based on the fact that we—well we've seen that we have—and we have a lot of volume growth. And the strategy to continue to grow and then develop the portfolios will allow us to generate increasing revenues and reach our potential even if, let's say, we think that the margins should stabilize going forward.

Michael Goldberg, Desjardins Securities

Thank you, very much.

Operator

Thank you. The following question is from Sumit Malhotra (phon) from Macquarie Capital Management. Please go ahead.

Sumit Malhotra, Macquarie Capital Management

Good afternoon.

Rejean Robitaille, President and Chief Executive Officer

Good afternoon.

Sumit Malhotra, Macquarie Capital Management

Staying with net interest income on both sides of that equation. For NIM, in particular we can see the decrease in liquid assets or proportion of liquid assets as the quarter ended. We can also see the pressure on our loan yields. It might be very short term, but we've certainly seen an increase over the last month and a half or so in the banker's acceptance rate; both the three month and the one month. I know Laurentienne has a larger proportion of personal deposits, but can you talk about any impact, a tightening prime BA spread is having on your margin and what we can look for going into the second half of the year?

Rejean Robitaille, President and Chief Executive Officer

Okay, Michel will answer that one.

Michel Lauzon, Chief Financial Officer

Yes, we've seen that tightening as well. It's about seven to eight basis points right now, in anticipation will be to the possible Bank of Canada policy shifts, expected early in June. It will all depend on what the reaction from the market is in terms of the prime rate. So, yes, we do have a portion of our assets which are prime based. And some of our liabilities are BA based in terms of being swapped into BAs to fund that book and so a tightening of that spread could be detrimental. But, we expect that spread to probably recover to maybe 180 basis points; 180 to 185. Whether or not that's sustainable over the medium term, that's an open question. As to whether or not the banking market will get back to 25 basis points that was embedded in the widening spreads back in the first quarter of 2009.

Sumit Malhotra, Macquarie Capital Management

And I think Michael Goldberg was asking specifically about a particular segment, but when we look at Laurentienne's loan growth, specifically on the real estate secured side, certainly there's been a lot of press that until very recently we had fixed rates moving noticeably higher. You touched on the potential rate hike that's coming through, the HST, some of the changes to mortgage rules. When I look at the bank having grown resi mortgages 5 percent quarter-over—I mean we can go back a number of quarters here, you've had minimum 3 percent lean (phon) quarter growth in reported resi mortgage balances. How much do you think is still left in the pipeline here? Or is it reasonable to expect a slowdown in the back half of the year in your real estate secured growth?

Rejean Robitaille, President and Chief Executive Officer

Well, we think that there's still a lot of potential for us. We have invested a lot in the past in our business development capacity and I would like to ask Francois Desjardins, head of B2B and Luc Bernard, head of retail to give you a little bit more flavour on this. So Luc if you want to start on the retail in Quebec?

Luc Bernard, Executive Vice President, Retail and SME Financial Services

Sure, Rejean. Let me just say that we're in a very good position right now. Quebec market is a very competitive market. We invest a lot in our branches but strongly in our sales force capacity throughout the years. So, we have a very good organic growth capacity right now and we're capitalizing on it.

Rejean Robitaille, President and Chief Executive Officer

Francois?

Francois Desjardins, B2B Trust

And I'll echo a little bit of the same. We've been working since 2007 to really rebuild, with solid foundations, our business development and marketing activities across Canada for the mortgage product. And, the pipeline seems to be quite strong going forward, regardless of the elements that you mentioned.

Sumit Malhotra, Macquarie Capital Management

I know you've mentioned, I think it's 40 percent of your loan portfolio is allocated to borrowers outside of the province of Quebec. Is it the same mix for the residential mortgage portfolio?

Francois Desjardins, B2B Trust

That's a good question. I would say lower; a lower mix; probably around 25 percent outside of Quebec, 75 percent in Quebec.

Sumit Malhotra, Macquarie Capital Management

Okay, so obviously, B2B and some of the commercial portfolios have been the main products that you've utilized outside of your home province?

Francois Desjardins, B2B Trust

That's right.

Sumit Malhotra, Macquarie Capital Management

Thanks guys.

Réjean Robitaille, President and Chief Executive Officer

Thank you.

Operator

Thank you. Once again, you may press star, one for any questions or comments. We have no further questions registered at this time. I would now like to turn the meeting back over to Madam Caron. Please go ahead.

Gladys Caron, Media and Investor Relations

Thank you all for joining us today. If you have any further questions do not hesitate to contact us. Our phone numbers are listed in the presentation. Thank you.

Réjean Robitaille, President and Chief Executive Officer

Thank you. Good afternoon.

Operator

Thank you. The conference has now ended. Please disconnect your lines and we thank you for your participation—and we thank you for your particip—

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