

FIRST BUSINESS FINANCIAL SERVICES, INC.

Form 10-Q

October 27, 2017

UNITED STATES

SECURITIES AND EXCHANGE COMMISSION

Washington, D.C. 20549

FORM 10-Q

☒ Quarterly Report pursuant to Section 13 or 15(d) of the Securities Exchange Act of 1934

For the quarterly period ended September 30, 2017

OR

☐ Transition report pursuant to Section 13 or 15(d) of the Securities Exchange Act of 1934

Commission file number 001-34095

FIRST BUSINESS FINANCIAL SERVICES, INC.

(Exact name of registrant as specified in its charter)

Wisconsin

39-1576570

(State or other jurisdiction of incorporation or organization) (I.R.S. Employer Identification No.)

401 Charmany Drive, Madison, WI 53719

(Address of Principal Executive Offices) (Zip Code)

(608) 238-8008

Registrant's telephone number, including area code

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

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

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

Large accelerated filer ☐	Accelerated filer ☒	Non-accelerated filer ☐	Smaller reporting company ☐	Emerging growth company ☐
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(Do not check if a smaller
reporting company)

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

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

The number of shares outstanding of the registrant's sole class of common stock, par value \$0.01 per share, on October 20, 2017 was 8,759,673 shares.

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PART I. Financial Information

Item 1. Financial Statements

First Business Financial Services, Inc.

Consolidated Balance Sheets

	September 30, 2017 (unaudited)	December 31, 2016 (unaudited)
(In Thousands, Except Share Data)		
Assets		
Cash and due from banks	\$ 20,685	\$ 14,596
Short-term investments	52,511	62,921
Cash and cash equivalents	73,196	77,517
Securities available-for-sale, at fair value	131,130	145,893
Securities held-to-maturity, at amortized cost	38,873	38,612
Loans held for sale	—	1,111
Loans and leases receivable, net of allowance for loan and lease losses of \$19,923 and \$20,912, respectively	1,446,790	1,429,763
Premises and equipment, net	3,048	3,772
Foreclosed properties	2,585	1,472
Bank-owned life insurance	39,988	39,048
Federal Home Loan Bank and Federal Reserve Bank stock, at cost	5,083	2,131
Goodwill and other intangible assets	12,735	12,773
Accrued interest receivable and other assets	32,228	28,607
Total assets	\$ 1,785,656	\$ 1,780,699
Liabilities and Stockholders' Equity		
Deposits	\$ 1,423,724	\$ 1,538,855
Federal Home Loan Bank advances and other borrowings	167,884	59,676
Junior subordinated notes	10,015	10,004
Accrued interest payable and other liabilities	17,252	10,514
Total liabilities	1,618,875	1,619,049
Stockholders' equity:		
Preferred stock, \$0.01 par value, 2,500,000 shares authorized, none issued or outstanding	—	—
Common stock, \$0.01 par value, 25,000,000 shares authorized, 9,016,345 and 8,959,239 shares issued, 8,758,923 and 8,715,856 shares outstanding at September 30, 2017 and December 31, 2016, respectively	90	90
Additional paid-in capital	78,353	77,542
Retained earnings	95,785	91,317
Accumulated other comprehensive loss	(370)	(522)
Treasury stock, 257,422 and 243,383 shares at September 30, 2017 and December 31, 2016, respectively, at cost	(7,077)	(6,777)
Total stockholders' equity	166,781	161,650
Total liabilities and stockholders' equity	\$ 1,785,656	\$ 1,780,699

See accompanying Notes to Unaudited Consolidated Financial Statements.

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Consolidated Statements of Income (Unaudited)

	For the Three Months Ended September 30, 2017 2016		For the Nine Months Ended September 30, 2017 2016	
	(In Thousands, Except Per Share Data)			
Interest income				
Loans and leases	\$17,686	\$18,016	\$53,492	\$55,161
Securities	771	698	2,326	2,102
Short-term investments	177	184	488	533
Total interest income	18,634	18,898	56,306	57,796
Interest expense				
Deposits	2,708	2,870	8,039	8,961
Federal Home Loan Bank advances and other borrowings	763	453	2,185	1,425
Junior subordinated notes	280	280	832	835
Total interest expense	3,751	3,603	11,056	11,221
Net interest income	14,883	15,295	45,250	46,575
Provision for loan and lease losses	1,471	3,537	5,699	6,824
Net interest income after provision for loan and lease losses	13,412	11,758	39,551	39,751
Non-interest income				
Trust and investment services fee income	1,653	1,364	4,930	3,981
Gain on sale of Small Business Administration loans	606	347	1,501	3,854
Gain on sale of residential mortgage loans	—	198	26	540
Service charges on deposits	756	772	2,287	2,247
Loan fees	391	506	1,525	1,791
Increase in cash surrender value of bank-owned life insurance	314	244	940	730
Other non-interest income	619	209	1,931	914
Total non-interest income	4,339	3,640	13,140	14,057
Non-interest expense				
Compensation	7,645	7,637	24,710	24,454
Occupancy	527	530	1,521	1,538
Professional fees	995	1,065	3,046	2,888
Data processing	592	623	1,810	1,971
Marketing	594	528	1,546	1,710
Equipment	285	292	868	913
Computer software	715	539	2,037	1,607
FDIC insurance	320	444	1,081	989
Collateral liquidation costs	371	89	556	204
Net loss on foreclosed properties	—	—	—	93
Impairment of tax credit investments	112	3,314	338	3,520
Small Business Administration recourse provision	1,315	375	2,095	449
Other non-interest expense	760	317	2,404	1,574
Total non-interest expense	14,231	15,753	42,012	41,910
Income (loss) before income tax expense	3,520	(355)	10,679	11,898
Income tax expense (benefit)	936	(3,020)	2,812	957
Net income	\$2,584	\$2,665	\$7,867	\$10,941
Earnings per common share				

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Basic	\$0.30	\$0.31	\$0.90	\$1.26
Diluted	0.30	0.31	0.90	1.26
Dividends declared per share	0.13	0.12	0.39	0.36

See accompanying Notes to Unaudited Consolidated Financial Statements.

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First Business Financial Services, Inc.

Consolidated Statements of Comprehensive Income (Unaudited)

	For the Three Months Ended September 30, 2017		For the Nine Months Ended September 30, 2017	
	2016		2016	
	(In Thousands)			
Net income	\$2,584	\$2,665	\$7,867	\$10,941
Other comprehensive income, before tax				
Securities available-for-sale:				
Net unrealized securities gains arising during the period	172	81	199	1,317
Securities held-to-maturity:				
Amortization of net unrealized losses transferred from available-for-sale	25	41	79	124
Income tax expense	(76)	(47)	(126)	(555)
Total other comprehensive income	121	75	152	886
Comprehensive income	\$2,705	\$2,740	\$8,019	\$11,827

See accompanying Notes to Unaudited Consolidated Financial Statements.

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First Business Financial Services, Inc.

Consolidated Statements of Changes in Stockholders' Equity (Unaudited)

	Common Shares Outstanding	Common Stock	Additional Paid-in Capital	Retained Earnings	Accumulated Other Comprehensive (Loss) Income	Treasury Stock	Total
(In Thousands, Except Share Data)							
Balance at December 31, 2015	8,699,410	\$ 89	\$ 76,549	\$80,584	\$ (80)	\$(6,310)	\$150,832
Net income	—	—	—	10,941	—	—	10,941
Other comprehensive income	—	—	—	—	886	—	886
Share-based compensation - restricted shares, net	37,708	1	857	—	—	—	858
Cash dividends (\$0.36 per share)	—	—	—	(3,132)	—	—	(3,132)
Treasury stock purchased	(19,819)	—	—	—	—	(454)	(454)
Balance at September 30, 2016	8,717,299	\$ 90	\$ 77,406	\$88,393	\$ 806	\$(6,764)	\$159,931

	Common Shares Outstanding	Common Stock	Additional Paid-in Capital	Retained Earnings	Accumulated Other Comprehensive (Loss) Income	Treasury Stock	Total
(In Thousands, Except Share Data)							
Balance at December 31, 2016	8,715,856	\$ 90	\$ 77,542	\$91,317	\$ (522)	\$(6,777)	\$161,650
Net income	—	—	—	7,867	—	—	7,867
Other comprehensive income	—	—	—	—	152	—	152
Share-based compensation - restricted shares, net	57,106	—	811	—	—	—	811
Cash dividends (\$0.39 per share)	—	—	—	(3,399)	—	—	(3,399)
Treasury stock purchased	(14,039)	—	—	—	—	(300)	(300)
Balance at September 30, 2017	8,758,923	\$ 90	\$ 78,353	\$95,785	\$ (370)	\$(7,077)	\$166,781

See accompanying Notes to Unaudited Consolidated Financial Statements.

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Consolidated Statements of Cash Flows (Unaudited)

	For the Nine Months Ended September 30, 2017 2016 (In Thousands)	
Operating activities		
Net income	\$7,867	\$10,941
Adjustments to reconcile net income to net cash provided by operating activities:		
Deferred income taxes, net	(1,603)	(9)
Impairment of tax credit investments	338	3,520
Provision for loan and lease losses	5,699	6,824
Depreciation, amortization and accretion, net	1,148	1,103
Share-based compensation	811	858
Increase in value of bank-owned life insurance policies	(940)	(730)
Origination of loans for sale	(24,606)	(54,794)
Sale of loans originated for sale	27,244	59,263
Gain on sale of loans originated for sale	(1,527)	(4,394)
Net loss on foreclosed properties, including impairment valuation	—	93
Excess tax benefit from share-based compensation	(59)	(138)
Returns on investments in limited partnerships	92	250
Net increase in accrued interest receivable and other assets	(1,759)	(2,813)
Net (decrease) increase in accrued interest payable and other liabilities	6,739	(2,789)
Net cash provided by operating activities	19,444	17,185
Investing activities		
Proceeds from maturities, redemptions and paydowns of available-for-sale securities	29,802	32,555
Proceeds from maturities, redemptions and paydowns of held-to-maturity securities	2,723	2,906
Proceeds from sale of available-for-sale securities	11,702	2,190
Purchases of available-for-sale securities	(27,125)	(48,229)
Purchases of held-to-maturity securities	(3,016)	(714)
Proceeds from sale of foreclosed properties	—	57
Net increase in loans and leases	(22,530)	(29,962)
Investments in limited partnerships	(500)	(750)
Returns of investments in limited partnerships	—	541
Investment in historic development entities	(417)	(1,488)
Investment in Federal Home Loan Bank and Federal Reserve Bank Stock	(12,223)	