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CORPORATE PARTICIPANTS

Andrew R. G. Moor *Equitable Group Inc. - President, CEO & Director*

Ron Tratch *Equitable Group Inc. - Senior VP & Chief Risk Officer*

Tim Wilson;Chief Financial Officer

CONFERENCE CALL PARTICIPANTS

Cihan Tuncay *Stifel Nicolaus Canada Inc., Research Division - Analyst*

Geoffrey Kwan *RBC Capital Markets, Research Division - Analyst*

Graham Ryding *TD Securities Equity Research - Research Analyst of Financial Services*

Jaeme Gloyn *National Bank Financial, Inc., Research Division - Analyst*

Stephen Boland *Raymond James Ltd., Research Division - MD & Equity Research Analyst*

PRESENTATION

Operator

Good morning, ladies and gentlemen. I'd like to welcome shareholders and analysts to Equitable's Second Quarter 2020 Conference Call and Webcast. Later, we will conduct the Q&A with participating analysts on the call. Before we begin, I'd like to refer you to Slide 2 of the presentation regarding the company's caution regarding forward-looking statements. This presentation and comments may contain forward-looking information, including statements regarding possible future business and growth prospects of the company. You are cautioned that forward-looking statements involve risks and uncertainties, including those introduced by the current global COVID-19 pandemic. Certain material factors or assumptions were applied in making these statements and could cause results or performance to differ from forecasts or projections expressed in these statements. Equitable does not undertake to update any forward-looking statements except in accordance with applicable securities laws.

This call is being recorded for replay purposes on July 29, 2020, at 8:30 a.m. Eastern.

It's now my pleasure to turn the call over to Andrew Moor, President and CEO of Equitable Bank. Please proceed, Mr. Moor.

Andrew R. G. Moor - *Equitable Group Inc. - President, CEO & Director*

Thank you, Chris. Good morning, everyone, and welcome. Tim Wilson, Chief Financial Officer of the Bank; and Ron Tratch, Chief Risk Officer of the bank, are also participating today. While Tim and I will deliver prepared remarks. Ron is available for Q&A.

Since the last conference call, business conditions look a lot more encouraging as we will discuss in detail this morning. Our earnings rebounded nicely, and we anticipate with all the usual forward-looking caveats, earnings increasing sequentially in each of the next 2 quarters. We've seen ample liquidity deposits at rates historically attractive against benchmarks. The housing market has been resilient in the face of the broader economic backdrop, which will likely have a positive impact on realized losses.

Our early efforts to transition our customers from a period of mortgage deferral back to their regular payments are showing very positive results. Our actions have helped to increase our capital ratio, with the bank's 14% CET1 being right at the top of our target range. And changes in consumer behavior in response to the pandemic, play to our strengths and capabilities in digital banking.

None of this is to deny the real challenges ahead posed by the continuing uncertainty created by COVID-19. And but I feel we are in a strong position to address these challenges and ultimately emerge in a stronger strategic position than prior to the pandemic.

Our presentation this quarter will focus on changes and developments since our last call, including those that affect our view of the future. To start, adjusted Q2 earnings per share were 68% above the level we recorded in Q1, and ROE snapped back to 13.8%. Across all parts of the bank, employee productivity and efficiency remained industry-leading amongst Canada's Sched I banks. This underscores our team's resilience under extraordinary circumstances, that in the early days of the COVID lockdown included an unprecedented volume of customer requests for systems.

Now that lockdown restrictions are easing, a small number of employees opted to return to equitable offices earlier this month. And starting in September, we will begin to gradually migrate the rest of our team, assuming it's safe to do so.

As we discussed last quarter and along with other banks, we provided mortgage deferrals to help our customers through a period of temporary loss of income. Equitable has been proactive in working with our customers to make the return to a more normal environment, a slope rather than the clip being talked about in some quarters. Deferrals peaked at 20% of total loan balances, amounting to $5.6 billion. As of mid-July, those levels have dropped to 6%, total loans were $1.7 billion. We provided a view on the expiry profile of their main deferrals in our MD&A. The progressive reopening of the economy suggests that many of our customers will be able to stay current with their payments once their deferral period ends.

We did not end Q2 with our usual lending growth mindset, but Equitable served its part to keep the economy moving as all of the bank's retail and commercial businesses continue to provide capital for household formation and business purposes.

Understandably, overall growth decelerated in Q2 as a result of the COVID-induced market slowdown, temporary job loss impacting some potential borrowers' ability to participate in the market and our tighter risk tolerances. Total loan principal was still up $912 million or 3% within the quarter to a record $27.6 billion.

Tim will discuss credit quality metrics and allowances in his remarks. But as a reminder, as is our practice, we adjusted our underwriting criteria in March in light of the uncertainty related to house prices and to protect the bank against what we saw as elevated risk. These actions include implementing a reduction in maximum LTVs are intended to uphold the quality of the bank's asset base, but of course, had a bearing on loan and revenue growth.

Looking at asset categories, our homegrown prime single-family business saw a new origination record in Q2 at $308 million, 26% or $64 million higher than the previous record set in Q3 2019. As a reminder, our Prime business is fully insured against credit loss and spread has been wider than was typically the case over the last few years. As a result, we have chosen to be very constructive in this market.

Our Challenger Bank accumulation businesses also continue to build demand in their markets. Looking ahead, we believe loan balances for reverse mortgages and our CSV line of credit will grow, while loan balance in most of our established businesses will be relatively stable to the 2020.

I'll turn to single-family as the exception. As a result of market conditions and our risk appetite I just described, originations will likely remain subdued. We currently expect the portfolio to contract slightly from Q2 to the end of the year. There are certainly some upsides to this view, but that's not our base case.

Companies also counts on us for the great digital banking services. In Q2, we achieved the outstanding growth in EQ Bank account openings, powered by the appeal of banking on Canada's first born in the mobile age all digital platform. Our digital customer referral program, the innovations we continue to introduce and our competitive interest rate.

Over the past year, new customer account openings increased 52%. And in the second quarter, we saw even more dramatic growth as the openings were almost 3x higher than the average over the past 12 months.

Leading Challenger Banks around the world are seeing great growth in the current environment, and the result of Canada's Challenger Bank mirrors that global experience. In June, EQ Bank's deposits surpassed $3 billion to finish the quarter at $3.3 billion, 46% above last year as a result of these account openings and higher balances in existing accounts. Getting to the $3 billion milestone this quickly, is proof positive that we can deliver a better experience by enabling customers to bank on their terms.

Canadians are more value conscious than ever and more open to embracing new systems of technology-enabled banking. That's good for Equitable because our digital offerings provide both great value and simple elegant technology experience. By challenging the status quo of additional banking practices, we're winning hearts and minds by combining the-money making capabilities of a high interest savings account, with the bill paying options of a checking account, all minus the service fees.

Earlier this month, we introduced EQ Bank's joint savings account, allowing up to 4 account holders to share on these advantages. As you know, setting up a joint account is a painful process of most Canadian banks and usually requires a branch visit. Working from the premise, there needs to be a better way, the EQ team has done an outstanding job of creating a simple, intuitive, fast and completely virtual sign-up process. This is the kind of Challenger-based innovation that makes banking better for Canadians, and I'm really enthused about this latest development, which I urge everyone to try.

Canadian's told us that the product they wanted most was joint accounts, and the response we've had so far suggests we've created something that is really capturing their attention.

Digital banking is becoming more popular with Canadians of all ages. But recently, we've noticed that the most significant new account opening growth is in the 18- to 25-year-old cohort. From a social perspective, this is good as young people are forming the savings habit and building a solid financial foundation.

From our perspective, we like the idea of building customer relationships for life, from youth to retirement. Our EQ international money transfer service is adding to the fast-growing uptake of our services. I still feel we've not really delivered a message of how good this service is, but if you're looking to send money overseas, EQ has a fantastic way to do so. We also (inaudible) referral service on May 14, and since then over 4,000 customers have signed up for a recommendation by friends and family, about 6x more than was typical for our manual referral program. The big picture is that one of the advantages that large incumbent banks have over Canada's Challenger Bank is the cost we have to incur to attract new customers. We are clearly seeing this acquisition cost drop, and this improves the relative economics of our bank going forward.

Between EQ Bank, Equitable's extensive network of independent investment advisers and financial planners and our strategic partnerships, we continue to attract all the deposit volumes we need to fund our growing business. Retail and securitization funding markets have proven to be much more liquid and efficient than we had expected earlier in the crisis. Flows in both markets have been relatively uninterrupted and very cost efficient. As GIC rates consistently decreased from mid-March onward at a much faster rate pace than relevant benchmarks.

This makes funding very cost competitive. The government has moved to inject liquidity into the banking system early in the crisis, further increased our level of comfort in the intervening months. Our instinctive response to the emergence of the crisis in March was to increase the size of our liquidity portfolio. And we took the additional step of ensuring $687 million alternative single-family mortgages as soon as CMHC expands its insurance eligibility criteria on March 20. The insurance came into force in Q2 and created an equivalent amount of additional liquidity. Tim will walk you through a cost-benefit analysis of this insurance in his remarks. For the bottom line being that it provides net funding cost and capital benefits through 2024, but had a negative impact on earnings in the most recent quarter of $0.20 a share. This drag is expected to reduce to $0.09 in Q3 and $0.01 in Q4 but turning positive in subsequent quarters.

We're protecting the bank and its depositors by maintaining a strong capital position. By quarter-end, positive earnings, coupled with slower risk-weighted asset growth of the bank's CET1 ratio to the top end of our target range of 14%, up 90 basis points year-over-year and 50 basis points from March. The insurance on $687 million of single-family assets contributed about 30 basis points to that increase. This capital benefit is driven by the fact that the insurance eliminates the credit risk on these assets for Equitable. So they became 0% risk-weighted after being insured. But our CET1 and total capital ratios are at the high end of the Canadian banking industry, and we expect them to increase from here.

Planned dividend increases are on hold for now because of regulatory guidance from OSFI to the banking industry. Even so, our most recent dividend declaration was 12% above last year. Our low payout ratio, which was 12% in Q2, shows that we have room to maintain our dividend and still build capital organically.

All in all, we do not foresee a reasonable scenario under which we will need to raise additional equity capital to support our existing businesses. Equitable is soundly capitalized coming into this pandemic and is even more so today.

Tim will now comment on quarterly financial results in more detail. Tim?

Tim Wilson;Chief Financial Officer

Thanks, Andrew, and good morning, everyone. As Andrew mentioned in his opening remarks, Equitable's earnings rebounded in Q2 compared to Q1. On an adjusted basis, net income grew 64% and ROE improved to 13.8% from 8.4% in Q1. This is one of those quarters when reported earnings and ROE were actually higher than adjusted numbers since the reported figures include $4.4 million of net mark-to-market gains. And for greater clarity, both reported and adjusted results include the impact of loss provisions in every quarter.

While earnings were up sequentially, they were down 10% from last year, which was our best second quarter on record. There were 2 primary reasons: the insurance premiums that Andrew mentioned and elevated PCLs. If the economic outlook remains stable and borrowers behave as expected, PCL should reduce in future quarters and cause earnings to increase from Q2 levels.

Digging a little deeper into PCLs. In the second quarter, we've recorded $8.8 million of credit loss provision, with $5.4 million of that relating to stage 1 and 2 loans. As a reminder, stage 1 and 2 provisions are expected future losses on performing loans. We modeled these expected losses based on our current book of business and macroeconomic forecasts. So why were stage 1 and 2 provisions elevated in Q2? During the quarter, forecast for several macroeconomic variable, including real GDP and unemployment, deteriorated, triggering a migration of $3 billion of loans from stage 1 to stage 2. The migration happened because the risk of default on these loans increased according to our model. Because we base stage 1 allowances on expected losses over the next 12 months and stage 2 on the lifetime of the loans, this migration caused allowances to grow by $13.3 million. As an offset, the loss we expect to incur on defaulted loans, otherwise known as the loss given default, decreased for stage 2 due to improved house price forecasts. Lower loss given default caused a $7.9 million decrease in allowances with the net change being $5.4 million.

On Slide 13 in our deck, we present PCLs and ACLs by business line. All of our businesses contributed to the elevated PCLs, but all were down significantly from Q1. The ACL for each also increased and remain adequate in the view of our management team. We ensure that these allowances reflect a range of potential outcomes as required by IFRS 9, and we modeled 5 different economic scenarios with forecasts provided by Moody's analytics and use a weighted average of those scenarios to determine our allowance. On Slide 13, we included the base case of our forecast at June 30 as compared to March 31, and it shows the deterioration in 4 of 5 key variables. Only HPI improved. There is, of course, a high degree of uncertainty in forecasting, particularly right now. But we compared Moody's forecast to those provided by a range of other economists, and the estimates we use appear to be in line, but on the conservative side. If those forecasts do not change and the behavior of our borrowers is as modeled, our PCLs should decline in future quarters. On the other hand, if they deteriorate, our PCLs will be elevated and if they improve, our PCLs will decline even further. I will also highlight that since our PCL is based on a weighted average calculation across economic scenarios, we will have over reserved by $7.8 million if the economy simply follows our base case.

Looking at impaired loans. They were $23.1 million higher at March 31, primarily as a result of a newly impaired and low LTV $17 million commercial loan in Alberta. We do not expect any losses on that loan. Impaired balances also included a $39 million loan on a commercial property in Vancouver that defaulted last year. In early Q3 of this year, the property was sold and the proceeds were used to fully discharge the loan such that Equitable recovered all outstanding principal and accrued interest. This experience serves as a reminder of why we focus on lending against well-located, high-quality properties. Actual losses and write-offs in Q2 amounted to $4.2 million or just 6 basis points of total loan assets. We've included both qualitative and quantitative information on our approach to lending and risk management in the MD&A, beginning on Page 27, and we'd be happy to answer any questions you have on this call.

Moving on. The change analysis slide in our deck quantifies the quarter 1 to quarter 2 impact of various drivers of our profitability. One of those drivers was a decrease in total operating costs, which were down $2.1 million from Q1 as we held the line in all expense categories. Our efficiency ratio followed suit. It was down to 39.2% from 43.4% in Q1, as lower noninterest expenses were assisted by higher fair value income. We remain focused on our long-term objectives and are pushing forward with the digitization of our bank and our service offerings. In other words, even in this COVID environment, we will continue to invest in our strategic priorities. That said, look for expense levels in Q3 and Q4 to be roughly consistent with Q2.

On NII, Q2 was up 4% year-over-year, driven by 11% growth in our average asset balances and despite a 12 basis point drop in our NIM. NIM was also down by 7 basis points sequentially. The decrease in NIM was largely as the result of ensuring $687 million of alternative single-family mortgages in Q2, and occurred despite the higher spreads that we have been seeing on originations and renewals in both our commercial and single-family businesses, particularly since the middle of March.

As Andrew mentioned, this insurance will provide funding costs and capital benefits to Equitable over the lives of the insured mortgages. However, there was a mismatch in the timing of the costs and the benefits. The insurance premiums are amortized into income on an aggressive profile, that being over the remaining contractual term of the mortgages. The funding cost and capital benefits, on the other hand, are realized over the initial term and subsequent renewal periods. So most of the premiums will be expensed in Q2 and Q3 of this year, while the substantial benefits are realized over a period of years. The net mismatch in Q2 was $4.7 million and resulted in a 7 basis points drag on NIM.

We've provided the expected net benefit by quarter on Slide 16 of our deck. We anticipate that the net pretax cost will be in the range of $2 million next quarter and will disappear almost entirely by Q4. The economics will then reverse next year and be in the range of $1 million to $1.5 million of additional pretax profit per quarter. We believe this is a good investment even if it does weigh slightly on quarterly results this year.

Further on NII, we had some dynamics with our CMHC floating rate securitization that contributed to lower NII in Q2. Related to the timing of when the rates were set and also the fact that floating rate liabilities are priced off SEDAR, where the loans are priced off prime and those rates were disconnected for part of the quarter. And finally, we held the EQ Bank HISA rate at 2% for competitive reasons and to encourage balanced growth, while consumers were actively shifting to digital channels. This is an investment that continues to cost us some short-term NII, but a substantial long-term franchise value. There is an opportunity to reduce this rate. These dynamics with our floating rate assets should dissipate next quarter and help our earnings by at least $0.10.

That's my report. Now back to Andrew for final comments.

Andrew R. G. Moor - *Equitable Group Inc. - President, CEO & Director*

Thanks, Tim. Equitable marked its 50th business anniversary in July, was coincidently named one of the best workplaces in Canada by Great Places To Work. Would have been nice to celebrate this occasion without pandemic disruptions since the accomplishments by generations of Equitable employees deserves recognition and praise.

We devoted a slide in our deck to calling out just a few of our milestones over the past 5 decades. From our humble trust company beginnings in Hamilton, to our place as Canada's Challenger Bank today, we have made a difference to the lives of hundreds of thousands of Canadians, and we are grateful for the opportunity to serve them from coast to coast.

Along the way, we have followed our own path to challenge the status quo and a small but meaningful way, made banking better for Canadians. We've now made challenging a serial preoccupation, and unlike those early days, we've got a lot more muscle to put behind our efforts. I'm of a view that Equitable has what it takes to become an even more powerful force for good in our industry. And I'm really excited about our future plans for innovation and service in all parts of our bank.

I think Canadians are ready for change. We're seeing that with the adoption of EQ Bank services, growth in deposits through our fintech partnerships and the emergence of our decumulation businesses, the way I think about this is that we are a catalyst for change in banking that creates value for Canadians from all walks of life. While we're taking all the necessary precautions to manage successfully through this health and economic crisis, we're not losing sight of the future. Digitalization of our services will continue, as will our advocacy efforts in favor of open banking and our commitment to adding value to customers, shareholders, employees and our broader community of partners.

In closing, Equitable has adjusted well to new realities. With strong capital liquidity positions, the bank is prepared for a range of downside scenarios but also for economic recovery. We expect earnings to grow from the improved levels of Q2, and we know that our award-winning digital capabilities, cloud infrastructure and incredibly dedicated workforce will continue to give us the advantage we need to challenge and succeed.

This concludes our prepared remarks. As a reminder, Ron Tratch, Chief Risk Officer of the bank is here with Tim and I to answer your questions. And with that, Chris, please open the lines for Q&A.

QUESTIONS AND ANSWERS

Operator

(Operator Instructions) Your first question comes from Stephen Boland of Raymond James.

Stephen Boland - *Raymond James Ltd., Research Division - MD & Equity Research Analyst*

Not usually the first one. Maybe you could just talk about the leasing portfolio? And I guess, the allowances, they still remain fairly high. And again, is that driven by the macro modeling or is there something specific in the portfolio or the age of the portfolio that makes the allowances remain so high compared to the other portfolios?

Andrew R. G. Moor - *Equitable Group Inc. - President, CEO & Director*

Steve, you're always first in our minds. So we appreciate you came first up this time. I think Ron has spent more time with that book, and I wonder if Ron can drill into that question.

Ron Tratch - *Equitable Group Inc. - Senior VP & Chief Risk Officer*

Yes. So Steve, the allowances that we took are relatively similar quarter-over-quarter with the degradation of few of the macro factors causing us to take incremental additional allowance. But no, the losses don't really relate to any idiosyncratic specific lease-level issues. They're mostly and primarily driven by the degradation in the macroeconomic factors. Tim had commented that our loss given default was a net gain across the entire book. But in that business, HPI forecast don't really benefit it. So it is primarily a function of the macroeconomic factors at the broader economy level.

Stephen Boland - *Raymond James Ltd., Research Division - MD & Equity Research Analyst*

Like at the age of the portfolio, does that matter at all in terms of deciding that allowance? Like if you have more equity in the lease, your loan to value, theoretically, I guess, would be lower, right, like if there is a cushion. So is that kind of relevant?

Ron Tratch - *Equitable Group Inc. - Senior VP & Chief Risk Officer*

Yes. So I mean they are leases. But if you think of it in long term, in terms of effective amortization, yes. So as the lease does get further into the term of the lease, the balances do come down fairly rapidly, obviously. So -- but quarter-over-quarter, we wouldn't see big changes in that effective duration of the book. So that wouldn't be what's driving big changes quarter-over-quarter. If you went over an extended period and weren't adding a considerable level of new leases, I think that could become a bigger factor, but not quarter-over-quarter with what we're -- our results are today.

Stephen Boland - *Raymond James Ltd., Research Division - MD & Equity Research Analyst*

Okay. And just my second question would be just, Andrew, maybe on the strength of the originations in the commercial book. I know there was some -- you mentioned one secured loan for $60 million. Maybe you could just talk about the environment right now? How competitive it is? Are the big banks circling or not -- or the bigger banks? Maybe just spend maybe a minute on that.

Andrew R. G. Moor - *Equitable Group Inc. - President, CEO & Director*

Yes. I think we're pretty optimistic about our commercial book. It seems like competition is less, as the normal spreads seem to have increased a fair bit, and our team is extraordinarily well-organized. So we're seeing some pretty good opportunities right now with better loan metrics than would be the case. I think we talked more about that at the last quarter, but we did change our lending appetite in the commercial area and made it more conservative in face of uncertainty. But despite that, we're seeing good opportunities. So it feels like a good place to be. And similarly, in the multi side of our business, we're pretty optimistic about where that's going currently.

Operator

Our next question comes from Graham Ryding of TD Securities.

Graham Ryding - *TD Securities Equity Research - Research Analyst of Financial Services*

You've mentioned in your MD&A that your Alt-A volumes were down year-over-year. Is there anything you can quantify there? And maybe is there any color in terms of your prime volumes originated in-house versus third parties?

Andrew R. G. Moor - *Equitable Group Inc. - President, CEO & Director*

Sorry. I think we gave a number for our prime volumes and generated in-house is 300 -- just over $300 million. Tim, Can you?

Tim Wilson;Chief Financial Officer

Yes. Sorry, Graham, you've cut out on part of your question. Do you say Alt-A volumes? And are you thinking about originations?

Graham Ryding - *TD Securities Equity Research - Research Analyst of Financial Services*

Yes, your originations. You said -- you just said they were down year-over-year. Is there anything you can quantify there to give us some context?

Tim Wilson;Chief Financial Officer

Yes. I mean, I'd say this was really a function of the broad market activity levels with an additional effect because of the fact that we tightened our lending criteria, our underwriting thresholds a little bit. But I think if you look at the broad market activity, I mean, in April, it was down, call it, 60% year-over-year depending on the market that you're operating in. So I think you could apply a similar number to originations for us through a good chunk of the quarter.

So again, it was mostly market-driven and the activity levels were down roughly in line with the -- our underwriting and originations were down roughly in line with those activities.

Graham Ryding - *TD Securities Equity Research - Research Analyst of Financial Services*

Okay. That helps. And then you commented that your originations, you expect them to remain subdued. Again, is that because the market is smaller or not there right now? Or are you deliberately pulling back and being more cautious in the Alt-A space?

Andrew R. G. Moor - *Equitable Group Inc. - President, CEO & Director*

I think we're not. Definitely not deliberately pulling back where our teams are really focused on trying to find the right kinds of deals. It's sort of interesting. It does seem like it's day to day. As you know, we prepare these MD&As weeks (inaudible). On the underwriting floor yesterday and we had a good day for submissions yesterday, for example, and the kind of qualitative commentary was that the quality of the deals were quite a bit better than what we have seen a month or 2 ago. So because when we had this -- went through this interruption of income caused by the lockdown, we still saw some decent volumes coming in, but many of the transactions didn't make sense because they've been a breakage of income, and I'm sort of hopeful that, that might reverse over the next few weeks. But it all remains to be a split scene. And I think as you know, we're actually trying to be relatively conservative in providing our forward-looking projections. So certainly, this is a fairly conservative view of the world.

Graham Ryding - *TD Securities Equity Research - Research Analyst of Financial Services*

Okay. Fair enough. And then just one more, if I could. When I look at your allowance for credit losses, they're sort of sitting roughly 3x higher than your 2019 averages for your retail and your equipment portfolios, but your commercial book, the allowances are roughly 1.4x higher. So I'm just wondering, is there any color on why your commercial allowances have not increased as much as those other 2 areas on a relative basis?

Andrew R. G. Moor - *Equitable Group Inc. - President, CEO & Director*

I think, Ron, can you address?

Ron Tratch - *Equitable Group Inc. - Senior VP & Chief Risk Officer*

Yes. So I think the best way to address that is, if you look at the -- or when we look at the actual losses that we realized in commercial because it is a book that is largely contained of a relatively fewer number of large accounts and we really have very few losses. So in the normal course, out of, call it, an abundance of caution, we do hold a greater percentage of reserves than we would see in the normal course in commercial, much more than the 2 basis point average that our book would lose in any given year. So as a result, coming into the COVID pandemic situation, while we have increased the level of reserves for commercial, we've always kept a much bigger buffer to realize losses, just in case there were a few idiosyncratic ones that we couldn't forecast before. So it's not so much -- I wouldn't view it as we have not increased because we think the book is dramatically different, it's just that in good times, we do hold more for commercial. And so we balance that out somewhat in the current environment.

Tim Wilson;Chief Financial Officer

And just to build on that for a second, Graham, there are really historically, 2 major components to the commercial allowance, one was a purely modeled component and the other is the buffer, the overlay that Ron was talking about. When you fast forward to a year like 2020, that model component is responsive to changes in the economic climate and borrower behavior. The buffer portion actually doesn't move with those macroeconomic changes. So because that portion was held relatively steady, you don't see that same 3x increase that you see in our other portfolios.

Graham Ryding - *TD Securities Equity Research - Research Analyst of Financial Services*

Got it. Okay. So on a relative basis, you have a bigger buffer in your commercial than you do on your retail?

Tim Wilson;Chief Financial Officer

Exactly.

Operator

(Operator Instructions) Your next question comes from Cihan Tuncay of Stifel.

Cihan Tuncay - *Stifel Nicolaus Canada Inc., Research Division - Analyst*

Just wondering on the CMHC insurance that you purchased. Was that the maximum amount of mortgages that qualified under their revised turns? Or could there potentially be any more approved mortgages going into that kind of product in future quarters?

Andrew R. G. Moor - *Equitable Group Inc. - President, CEO & Director*

Essentially, it's the maximum amount that was available to us. We wouldn't think there's going to be much more available. There may be small amounts. But by and large, we felt this was ample enough -- ample for us and kind of close to the amount that made sense on a sort of economic trade-off basis, it could be more expensive to get different types of loans. We were sure these were the ones that made sense from a kind of NPV perspective.

Cihan Tuncay - *Stifel Nicolaus Canada Inc., Research Division - Analyst*

Okay. And just on the reduction in noninterest expenses. Trying to get a sense of whether or not -- how much of that was really just pushed out to next year or are these kind of lasting cost cuts that you've taken? And with that, I know a lot of the investment was in the digital infrastructure, will some of those cost reductions that you're taking in IT, have any impact on your own internally generated origination volume in the future just from an IT infrastructure perspective?

Andrew R. G. Moor - *Equitable Group Inc. - President, CEO & Director*

No. The way we sort of thought about the world is that some of our projects, and I think we've talked perhaps a little more about this in the last conference call. So we were planning to be in the covered bond market this year, and we were planning to advance our AIRB program quite aggressively. Both of those programs because of the impact of COVID and kind of the dynamics around those were sort of pushed off a bit. So that's one of the areas where we didn't invest as much as we would have came into the year thinking.

But on the other hand, we're seeing lots of opportunity around digitalization. And so we're continuing to invest for the -- in digitalization. I wouldn't say we're at a higher level than expected to run, but we certainly haven't dialed that back very much. So our costs shouldn't affect long-term origination volumes at all. But those 2 programs will get deferred into later.

Cihan Tuncay - *Stifel Nicolaus Canada Inc., Research Division - Analyst*

Okay. And just one more quick question. Tim, in your comments, you alluded to the fact that with the growth you're seeing in EQ Bank deposits, you're still maintaining some kind of interest rate. At what point do you think that you will get enough momentum behind deposit growth in that product to start seeing declines in deposit costs?

Tim Wilson;Chief Financial Officer

I think we're getting sort of close to that point, frankly, certainly something that will be an active conversation with quarter end behind us. The way we think about this, roughly speaking, and it's -- there's a bit of art or science, but roughly speaking, we think there's about $1,000 NPV value in a new customer. So you can see just holding that break for a little period, doesn't -- is a good acquisition kind of cost. We would have perhaps spent $300,000 to $400,000 more on interest in, say, June than we would have expected that we could have done if we dropped rates to more market competitive rates. But then in contrast, we added an extra $9 million of NPV from having that broader customer base. So that appeared to be a pretty good investment in that period. We think as the summer is here now, probably people are less focused on banking more and focused on being outside. The value of those incremental accounts that you pick up is starting to reduce and as we're increasing our product set as well, that's also leading to kind of good inflow of customers. So those are some of the things we're considering is how -- if we reduce rates, how much does that slow down customer acquisition? What does that mean on a kind of NPV view of the world franchise value of the world. Clearly, one of the nice things about the EQ Bank franchises we've now built it. As we get into certain scales, as we add new innovations, that thing spread across a wider customer base, which is just making us more and more productive. So that gives us an exciting opportunity every time we think about new initiatives, you divide those by a larger customer base and they certainly start to make sense. So I think you'll see some really interesting things coming on the product side over the next year or so.

Operator

Your next question comes from Jaeme Gloyn of National Bank Financial.

Jaeme Gloyn - *National Bank Financial, Inc., Research Division - Analyst*

Yes. I just want to spend some time digging into the payment deferrals. So first off, the significant decline that you've reported here since the peak levels to where we are today. Can you just describe what's driving that decline? Is it just a roll-off and these borrowers are continuing -- are now paying their mortgages? Is there any was there any other reasons why it would decline so fast?

Andrew R. G. Moor - *Equitable Group Inc. - President, CEO & Director*

Look, we're trying to, as we expressed in the prepared remarks, turn -- some describe it as a shift into a slope. So when we first gave deferrals, we had a lot of calls coming in on the retail book, which is where most of it sits. And we were generally giving 1-, 2- or 3-month deferral. So clearly, we're sort of past the point of those 3 month deferrals, we're just trying to get past that point. And our general feeling is that many of our customers called looking for a deferral just out of an abundance of caution in an uncertain economic scenario. And so they -- many of those have rolled off. And it's clear, I think that if there are people in financial trouble that they'll start to emerge now. Ron's team has done a lot of work in this area. Ron, I wonder if you can give some other color there and I believe that the analysis you've done supports the view that our credit reserving is pretty damn good as well.

Ron Tratch - *Equitable Group Inc. - Senior VP & Chief Risk Officer*

Yes. What I could add there, Jaeme, is -- well, Andrew's referenced it, it is early with respect to these what we've called expired deferrals as they're now no longer under a contractual deferral. The early results, and we use that term again in terms of the number transitioning back to regular payment has been extremely encouraging. There are still a significant portion to go, obviously. So we don't want to push too far ahead and looking forward. But the research that Andrew is referencing that my team has done is, we try to reference everything, not just in the context of these deferrals, but also going back and triangulating back to what we have set aside in stage 1 and stage 2 expected credit loss. And given how encouraging the early results are, all indications are that we are very, very well reserved from an ECL perspective, barring any major shift in economic forecasts, et cetera, et cetera. So it actually gives us a lot of comfort going forward when you triangulate these COVID deferral, the actual experience and then what we have forecasted going forward.

Jaeme Gloyn - *National Bank Financial, Inc., Research Division - Analyst*

Okay. Great. And so it sounds like the expired deferrals are now current and not on some other form of forbearance measure. In terms of the -- those that are active, have you dug into the characteristics of those borrowers? Are they still active because of -- are they passing a certain criteria that you're looking at in terms of income impairment or job loss? Or is the threshold to qualify for a deferral still fairly loose?

Ron Tratch - *Equitable Group Inc. - Senior VP & Chief Risk Officer*

Well, a good portion of them are deferrals that are still under the original deferral request that came in originally. The balance of -- another good portion would be the deferral that are under their subsequent deferral request. So the individual characteristics really obviously boils down to the individual loans. But the experience with those is, as we come to that second deferral, we do get additional information. We make sure that the information that is there to support that subsequent deferral, and so we don't expect them to perform any differently than the ones that have transitioned to expire. If there were issues when it came to a request for subsequent deferral, we would have moved it to a normal proceeding through our typical impaired loan and enforcement process. So there isn't any reason for us to believe at this stage, that remaining balance should perform any differently than what we've seen with the expired deferrals.

Andrew R. G. Moor - *Equitable Group Inc. - President, CEO & Director*

And what we're trying to do is, we're trying to create a bit of attention to get these loans coming back into normal payment cadence which we think would be constructive for our customers, while at the same time, recognizing there's going to be people still on temporary employment and job loss. Serving other things, even on the commercial side, the CDIC, are providing some (inaudible) are providing some relief to borrowers. The government programs are still being helpful to allow people to migrate back to regular then.

Jaeme Gloyn - *National Bank Financial, Inc., Research Division - Analyst*

Yes. So you actually raised another point that I wanted to just clarify. In terms of the serve, it's obviously been very beneficial to borrowers, do you have any sense as to the uptake in the serve from your underlying borrowers and how that is impacting the payment deferral numbers?

Andrew R. G. Moor - *Equitable Group Inc. - President, CEO & Director*

I certainly don't have -- I mean we hear other stories and it's a complicated picture out there, right, because you often -- you might have 2 people in a partnership and 1 person is on serve and the other one is working, when both were working. So you're seeing that kind of scenario out there or perhaps even multigenerational families living in one household, where you've got some serve income. So it's a bit of a complicated story to understand at this point. It would be certainly confidently. We hear that qualitatively, but we can't put any quantitative numbers around that.

Jaeme Gloyn - *National Bank Financial, Inc., Research Division - Analyst*

Okay. And just lastly on this topic. The -- you mentioned that there was a good chunk that were extended, I guess, their payment deferral time was extended. Can you share the percentage of the portfolio that would have received an extension? And how do you think about extensions generally? Is this something where you can roll a 2-month deferral 3 times and stay onside here or is it sort of one deferral and that's it?

Ron Tratch - *Equitable Group Inc. - Senior VP & Chief Risk Officer*

So the overall percentage that is in a second or third request is actually quite low given the grand scheme of the entire facility of the -- roughly in the retail book, the $5 billion roughly that we've showed as our peak level. The actual portion that has gone on for subsequent request is actually quite low. It's a good portion of the $1.4 billion of remaining ones. But on balance, it's quite low. So with the approach that we've taken is simply -- when some institutions in the industry offered 6 months right out of the gate, we chose to offer 3. We could have chosen to offer 6. And today, virtually have no line of sight into payment history or performance, and we would still be in a holding pattern waiting to see. We elected to do things differently from a management perspective. We've seen very good results with a lot of those transitioning. But we've always been prepared to work with our customers if, for example, they needed another month to 2 months or even 3 months, depending on the customers' individual circumstance and working that through with them to make sure that we were offering them the maximum that we could under the industry allowed 6 months to work with them on an individual basis. So while I can paint the picture in broad strokes, we've really tailored it to the individual and asking some pointed questions at the time those deferrals come up and if it's supported for 1, 2 or 3 months up to what the industry is allowing.

Andrew R. G. Moor - *Equitable Group Inc. - President, CEO & Director*

Yes. So it's very -- it's becoming a very manageable process in terms of being able to have good dialogue with our customers about what the individual situation is at this point. I think CMHC actually came out with some good kind of flow chart log and the flow charts, but decisions around how you would treat individual loans. And it may well be that the industry evolves over the next 2 to 3 months to things like making interest-only payments rather than the full deferral and that kind of thing, but we have not made any of those moves yet to be clear. But generally speaking, today, if there's somebody that's been on deferral and is coming back asking for a second one, which as Ron mentioned, has actually been pleasingly small proportion of our loans coming off deferral. We're generally giving them -- having a conversation with them if it makes sense, giving a 1-month deferral and still keeping that nice tension where we're helping them kind of get through the next month or 2, but understanding that we need to actually figure out how to get back onto a regular payment mode.

Jaeme Gloyn - *National Bank Financial, Inc., Research Division - Analyst*

Okay. Great. That's really great color on that topic. Shifting to the outlook somewhat. I think, Andrew, you've sort of mentioned that just recently, you've seen some good application volumes and the quality of those applications. Can you just talk about the environment today? Obviously, the housing market looks pretty strong like we're having a delayed spring market here. Is that something you're also seeing in terms of the application volumes? And that if you can just focus those comments more on the alternative book as opposed to the prime book?

Andrew R. G. Moor - *Equitable Group Inc. - President, CEO & Director*

Yes. I'll start with (inaudible). Clearly, we're seeing a lot of demand in the prime book, and so that's indicative of that strong housing market, as you say. I think sort of as your commentary so set out, we're seeing less demand in that Alt book. So we haven't seen that get to that level of strength yet. I don't know whether there's some delay between that and the housing market. But clearly, there's a good cadence of business there, but it's not what I would have expected yet, but our teams are out there trying to beat the bushes to find the business. So we'll see how that goes. But clearly, we have a strong franchise. We're the leader in this marketplace. We'll find the business if it's there. But so far, we've seen less demand in that Alt book.

Jaeme Gloyn - *National Bank Financial, Inc., Research Division - Analyst*

Okay. And can you refresh for me the new Canadian segment of the portfolio? I just want to get a sense as to if immigration and the closing of borders, what kind of an impact that could have on acquiring new customers as they enter Canada.

Andrew R. G. Moor - *Equitable Group Inc. - President, CEO & Director*

I mean the way we think about that is about 40% of our Alt originations are new Canadians, so relative recent immigration history. But I would say is, when we talk about new Canadians, when does the new Canadian become an established Canadian. And I think really, we're talking about people that have arrived in Canada over the last 5 years or so. So it's a fairly significant backlog there of people that -- people didn't particularly come move into the country and then buy a house right away, they would be again establishing some kind of credit and job track record and tenure. And it might be 2 to 3 years before they actually buying a house. We would consider that to be still kind of in our new to Canada type book. So the immediate softening of immigration probably won't have that much impact on the business. And there are some nice things to think about, particularly the (inaudible) are nice things, but the situation in Hong Kong where over 300,000 Canadians might choose to exercise the rights for their passport to come to Canada, for example. My -- we're hearing anecdotally it's causing some sort of upward demand for housing and that's certainly a market that we play in quite successfully. But if, Jaeme, to your point, for long term, immigration clearly will be down significantly this year, but it doesn't have an impact in the short term, but over next 3 to 4 years, maybe.

Jaeme Gloyn - *National Bank Financial, Inc., Research Division - Analyst*

Okay. Great. And last one, and maybe this is more for Tim. Just want to get a sense as to how the net interest margin in the alternative single-family space is looking here in recent months as we're seeing lower GIC rates, likely you'll lower the EQ bank rates eventually. How is the asset side of the equation performing recently given let's say, less volumes on the alternative single-family side that you've just described. Are you seeing increased competition driving those asset yields significantly lower that could impair margins? Or does it look like it's going to hold fairly steady?

Andrew R. G. Moor - *Equitable Group Inc. - President, CEO & Director*

Yes. I mean, we actually use the ROE calculator. We've described before, I think basically takes up what's a slice of that marginal loan. And so our spreads when using that methodology are actually pretty attractive now, above the level they would have been at 6 months ago. So sort of no problem on the NIM side.

Operator

Your next question comes from Geoff Kwan of RBC Capital Markets.

Geoffrey Kwan - *RBC Capital Markets, Research Division - Analyst*

Just had one question. Just going back on the deferral side. When you're getting the requests for extensions, I think you kind of mentioned you're getting a little bit more information on the income side. Are you actually getting kind of more formalized income verification of some sort of impairment or are you doing just some sort of declaration? And then the other part of my question on that is, are you doing these assessments differently for your prime customers relative to your Alt-A customers?

Andrew R. G. Moor - *Equitable Group Inc. - President, CEO & Director*

Yes. It's more of a conversation, Geoff, about what is the situation rather than going back and we would in the mortgage origination, looking for source documents, certainly with the challenges around COVID, one of the challenges have been kind of getting -- heading to HR departments and getting proof of income in any event. So it's more about a conversation about the situation with the customer maybe looking at bank statements as a source document, but not going back in the same level as we would for an original transaction.

And yes, we are taking a position that's more aligned with the larger banks on the prime side. So we'd be more relaxed about providing deferrals on the prime side of the business.

Operator

(Operator Instructions) Your next question comes from Cihan Tuncay of Stifel.

Cihan Tuncay - *Stifel Nicolaus Canada Inc., Research Division - Analyst*

I just had a follow-up question on the NIM, but it looks like that's been answered already.

Operator

There are no further questions at this time. I will now return the call to Mr. Andrew Moor for closing comments.

Andrew R. G. Moor - *Equitable Group Inc. - President, CEO & Director*

Thanks, Chris. We look forward to reporting Q3 in early November. In the meantime, please enjoy the rest of your summer, and goodbye for now.

Operator

This concludes today's conference call. Thank you for your participation. You may now disconnect.