CIBC Q4 2023 Earnings Conference Call

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Corporate Participants

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Management Discussion Section

Operator

Good morning, and welcome to the CIBC Quarterly Financial Results Call. Please be advised that this call is being recorded.

I would like to turn the meeting over to Geoff Weiss, Senior Vice President, Investor Relations. Please go ahead, Geoff.

Geoff Weiss, Senior Vice-President, Investor Relations & Performance Measurement

Thank you, and good morning. We will begin this morning's presentation with opening remarks from Victor Dodig, our President and Chief Executive Officer; followed by Hratch Panossian, our Chief Financial Officer; and Frank Guse, our Chief Risk Officer. Also on the call today are a number of our group heads, including Shawn Beber, US region; Harry Culham, Capital Markets and Direct Financial Services; and Jon Hountalas, Canadian Banking. They're all available to take questions following the prepared remarks.

We do have a hard stop this morning at 8:30. So, during the Q&A, please limit your questions to one to ensure you all get a chance to participate. We'll make ourselves available after the call for any follow-ups. As noted on slide 2 of our investor presentation, our comments may contain forward looking statements which involve assumptions and have inherent risks and uncertainties. Actual results may differ materially.

With that, I'll now turn the call over to Victor.

Victor G. Dodig, President and Chief Executive Officer

Thank you, Geoff, and good morning, everyone. I realize it's a busy one for all of you. So with that in mind, there are really three key messages I want to leave with you today. The first message is that we made strong progress executing on our strategic growth priorities in 2023, and we delivered solid financial results despite normalizing credit losses. Our solid results are reflected in our healthy net interest margins, our positive operating leverage, and our strong capital and liquidity.

The second message is that we're advancing our competitive advantages by focusing on four key strategic priorities, which I'll elaborate on in a moment. And the third message is that while global economic growth is expected to continue to slow, our client-focused strategy, our disciplined resource allocation, and our experienced leadership team will deliver profitable growth in fiscal 2024 and beyond.

Now, turning to our results, fiscal 2023 demonstrated our bank's strength and resiliency amid a challenging economic backdrop, with high interest rates and elevated inflation, all of which affects our clients to varying degrees. Guided by our purpose, we supported our clients with advice to navigate the challenging environment and to help make their ambitions real. We continued to benefit from our organic investments over the past several years, delivering record revenue of CAD 23.4 billion, which was up 7%; and pre-provision pre-tax earnings of CAD 10.2 billion, which were up 8% from last year.

We achieved revenue growth across all of our businesses where we prudently grew volumes, we remained disciplined on pricing to protect margins, and we generated incremental fee income through deeper relationship with our clients. Adjusted net earnings of CAD 6.5 billion were down 2% as a result of higher provisions for credit losses as credit continues to normalize. Earnings per share of CAD 6.72 were down 5%

from the prior year, impacted by an increased number of shares outstanding, primarily due to the dividend reinvestment plan discount in effect since the first quarter.

Adjusted operating leverage was positive 1.2% in fiscal 2023, in line with our guidance, as we harvested the investments we made to deliver strong revenue growth while prudently managing our expenses. We proactively improved our capital position in every quarter of fiscal 2023 to the end of the year, with a 12.4% CET1 ratio, and have multiple levers available to continue accreting capital.

As we communicated with our second quarter results, we have adopted an annual review of our dividend payment during fourth quarter earnings moving forward. So, today, we've announced a CAD 0.03 dividend increase to our common shareholders. Our adjusted ROE was 13.3% for the year and was impacted by normalizing provisions for credit losses and higher capital levels.

We continue to prioritize investments that support capital-light, fee-based, and deposit-generating businesses that will be accretive to ROE. Our client-focused strategy is working. Our steady execution has enabled us to make good progress, and we have built momentum for our bank on a number of fronts. So as we go forward, our four key strategic priorities will build on our momentum and will advance our real competitive advantage.

These four priorities are, first, we're committed to growing our mass affluent wealth franchise in Canada and the US. In Canada, we're well-positioned with our differentiated mass affluent coverage model through Imperial Service. We have a great private wealth business. And in the US, we have a high quality, scalable private wealth program that we want to grow. Second, we're further enhancing our digital banking offering. We're a leader here today, and we intend to build on our market position.

Third, we'll continue to leverage our connectivity for commercial and capital markets clients. We're uniquely positioned to bring this differentiated approach to the market, and our clients tell us that this sets us apart. Our model creates value by deepening client relationships, it generates recurring revenue, and it enhances our returns. Finally, our efforts to enable, simplify and protect our bank are building the operational excellence and efficiency required to drive higher returns for our stakeholders.

With that, let's get into the segment results. In Canadian Personal and Business Banking, we have been a leader in growing our client retail client base. On a trailing 12-month basis, we grew over 650,000 net new clients across our CIBC and Simplii brands, including successfully attracting many newcomers and students to our bank. We're leveraging our highly differentiated Imperial Service offering to serve clients in the mass affluent segment. This year, we introduced a dedicated leadership structure to sharpen our focus on growing this business.

Our success in client growth and franchising has been a product of a relentless focus on enhancing our client relationship experience. CIBC continued to maintain a leadership position with our digital offering. For the third time since 2020, we ranked number one in the 2023. J.D. Power Canada Banking Mobile App Satisfaction Study.

In Canadian Commercial Banking, the effect of rapidly rising interest rates and inflationary pressures slowed growth across the Canadian commercial market. Against the backdrop of moderating economic growth, we achieved our third consecutive year of increasing client Net Promoter Scores; and, in fact, hit a record this year. We continue to improve the client experience and deliver our whole bank to each client, as evidenced by the CAD 17 billion of referrals since fiscal 2019 across commercial banking and private wealth management. And in our CIBC Wood Gundy franchise, we ranked among the leaders for Big Six banks in the Investment Executive Brokerage Report Card survey of advisors.

In the US, higher interest rates also cooled lending demand. However, our highly connected franchise and the investments we've made to scale our footprint have enabled us to attract new clients in a tempered economic environment. Deposit volumes in the US have stabilized, and we're focused on strengthening and diversifying our deposit base.

Our efforts to build the best-in-class US private wealth franchise was recognized again by Barron's, who ranked us in the top 10 of RIA firms in the United States for the fourth consecutive year. Now, looking ahead, we'll continue to grow our US commercial banking franchise organically with a focus on industries that value high-touch service and specialized expertise. We'll also be expanding our US private wealth platform by leveraging our talent and technology investments and expanding into fast growing, affluent markets like southern Florida.

In Capital Markets and Direct Financial Services, our differentiated platform continued to generate consistently strong performance. Our double-digit revenue growth was enabled by our strong client focus and increased activity in global markets as we helped clients address their short and long-term needs in a rising rate environment.

In line with our strategy, more than 20% of total capital markets revenue was originating from the US region where we've almost tripled our capital markets revenues since 2017. We also further expanded our DFS business to generate growing recurring revenue and to attract new clients seeking convenient digital banking and investing solutions. Through continued growth of Simplii Financial and our leading edge FX and remittance capabilities, DFS revenues of CAD 1.2 billion increased 26% year-over-year. Collectively, the strength of our diversified platform and strategic connectivity positions us well for more fluid market conditions in the year ahead.

We closed out 2023 in a position of strength as a result of strategic investments in all of our core businesses. Looking ahead to 2024, we expect slowing consumer spending and continued softness in global economic growth in response to monetary policy tightening. Amid this backdrop, we'll continue to prioritize financial strength and risk discipline while advancing our purpose-driven culture and our growth strategy. We're confident that this approach, combined with our client-focused strategy and strong execution, will deliver relative outperformance and top tier shareholder returns over the years to come.

And with that, I'll turn it over to my colleague, Hratch, for a detailed review of our financial results.

Hratch Panossian, Senior Executive Vice-President and Chief Financial Officer

Thanks, Victor, and good morning to you all. We delivered a solid fourth quarter to cap off 2023 as laid out on slide 10. Echoing the themes we demonstrated throughout fiscal 2023, our fourth quarter results reflect the resilience of our business, our ability to proactively manage through a dynamic environment, and the strength of our balance sheet. Supported by revenue momentum across all of our business units and a continued focus on productivity, we generated robust operating leverage, strong pre-tax pre-provision earnings growth, and diluted earnings per share of CAD 1.53, which was up 22% over the prior year. Excluding items of note, adjusted EPS was CAD 1.57 and ROE was 12.1%.

Our capitalization and liquidity continued to improve during the quarter, coming in ahead of our in-year guidance on both fronts with a period-end CET1 ratio of 12.4% and average LCR of 135%. The balance of my presentation will refer to adjusted results which exclude items of note starting with slide 11.

Adjusted net income of CAD 1.5 billion increased 16% from the same quarter last year. Revenue of CAD 5.8 billion was up 9%, supported broadly by higher NII, trading revenue, and fee income. And we grew pre-provision pre-tax earnings 18% by containing expense growth to 3% and generating over 6% operating leverage. Credit provisions of CAD 541 million were up 24% from a year ago, which Frank will discuss in more detail.

Slides 12 and 13 highlight key trends and drivers of net interest income. While trading income was 26% higher year-over-year in aggregate, we continue to see a shift in trading revenues from interest to non-interest income due to higher rates. Excluding trading, NII was up 8% over the year, driven by continued balance sheet growth and solid margins. Total bank NIM, excluding trading, was up 6 basis points from the prior year or down 1 basis point sequentially. Last quarter's margin included a couple of basis points from non-recurring interest as we disclosed at the time. And underlying these quarterly fluctuations, we continue to see gradual margin expansion.

Canadian P&C NIM of 267 basis points was up 20 basis points from the prior year and was stable sequentially, as modest expansion in core margins offset the one-time interest last quarter. We have once again provided incremental disclosure on P&C margin drivers in the appendix. NIM of 344 basis points in our US segment was down 5 basis points year-over-year and 2 basis points from the prior quarter. The sequential decrease was largely due to interest on a significant loan recovery in the prior quarter.

As shown on slide 13, average client loans and deposits continued to grow over the prior year despite the market-wide slowdown experienced this year. Deposit mix has largely stabilized and aggregate balance growth in deposits picked up late in the quarter, resulting in 4% growth sequentially on a spot basis. We remain focused on growing our balance sheet prudently and with strong returns, and we anticipate this to drive continued momentum in non-trading NII based on current market interest rate expectations.

Turning to slide 14, non-interest income of CAD 2.6 billion was up 20% from the prior year due to growth in trading revenues, as well as higher market-related and transactional fees. Excluding trading, market-related fees increased 8% year-over-year, driven by higher investment management and custodial revenues, as well as recovery from lower treasury income in the same quarter last year.

Transaction-related fees were up 6% year-over-year, driven by growth in credit as well as deposit and payment fees. While market factors can significantly impact these revenues, our strategic focus on deep relationships, as well as advice and differentiated solutions for key client segments will continue supporting ongoing growth in non-interest income.

Slide 15 highlights our continued success in maintaining robust investment in our bank while also containing overall expense growth. In Q4, year-over-year expense growth moderated to 3% as investments were partly offset by the benefits of prior initiatives to improve efficiency and deliver a better experience for our clients and our team. We've also demonstrated the impact of this approach over the longer term. For the full year, this approach allowed us to meet our targets, containing expense growth to 6% and generating operating leverage of positive 1.2%.

And despite the significant increase in strategic investment over the last few years, we've delivered neutral operating leverage in aggregate while positioning ourselves to improve on that going forward by leveraging these foundational investments. We intend to manage expense growth to around or below mid-single digits for fiscal 2024, and we continue to target positive operating leverage over the medium-term.

Slide 16 is focused on our balance sheet, which continues to benefit from our focus on disciplined resource allocation and an emphasis on returns over balance sheet growth. We improved our CET1 ratio to 12.4% over the quarter, driven by organic capital generation and share issuance, partly offset by higher RWA, driven in part by credit migration and model changes.

Late in the quarter, we also received regulatory approval to apply the internal rating-based approach to the majority of our US bank portfolio, which we intend to implement in Q1 2024. On a pro forma basis, we estimate this implementation, net of the other regulatory changes coming into effect in Q1, results in us starting fiscal 2024 with a CET1 ratio over 12.5%.

Our already strong liquidity position improved further throughout the quarter as loan growth slowed and deposits rebounded, resulting in a sequentially higher average LCR of 135%. Despite an evolving environment and regulatory landscape, throughout 2023, we demonstrated our ability to absorb unexpected headwinds and strengthened our balance sheet while maintaining support for our clients and deploying capital to generate solid top line growth. This positions us well as the environment continues to be fluid.

Starting on slide 17, we highlight our strategic business unit results. Net income in Canadian Personal and Business Banking was CAD 639 million, up 32% from the same quarter last year. We grew pre-provision pre-tax earnings 19% from the prior year by driving 9% revenue growth through the strategic priorities Victor outlined earlier. Revenue was supported by a 19-basis-point increase in margins and volume growth on both sides of the balance sheet. And we delivered operating leverage of 8% by containing expense growth to 1% from the same period despite continued investment against our strategic priorities.

Turning to slide 18, net income in Canadian Commercial Banking and Wealth Management was CAD 490 million. Revenue of CAD 1.4 billion was up 4% from a year ago, benefiting from mid-single-digit loan and deposit growth in commercial banking, as well as higher fee-based revenues from market appreciation and net flows in wealth management.

We also delivered positive operating leverage as we manage expenses to 3% increase year-over-year. Our strategy continues to create momentum across our combined Canadian P&C Banking franchise, where net income was up 22%; while pre-provision pre-tax earnings were up 15%, fueled by 8% revenue growth and over 6% operating leverage. And we expect this momentum to continue. We've included more details on this segment in the appendix of our presentation.

Turning to U.S. Commercial Banking and Wealth Management. Net income of $39 million USD was down 69% from the prior year due to higher credit provisions, predominantly in the office portfolio. Revenues were up 2% over the same period, driven by 5% increase in fee income and a 1% increase in net interest income. Expenses were up 11% year-over-year, including higher severance in the quarter.

Excluding one-time charges, expenses were up 6%, reflecting investments across our business and infrastructure, which we expect to continue into 2024 as we expand our US platform. We remain focused on prudent and profitable growth to scale this business across both commercial banking and wealth management.

Turning to slide 20 and our Capital Markets and DFS business. Net income of CAD 383 million was up 1% year-over-year. Revenues of CAD 1.3 billion were up 9% over the prior year, driven by 20% growth in global markets and 12% growth in Direct Financial Services. Expenses of CAD 734 million were up 12% year-over-year, partly driven by charges in the quarter, including higher severance. Excluding these charges, expenses grew 8% and we anticipate them to moderate.

Slide 21 reflects the results of the corporate and other business unit. Net loss of CAD 48 million compared with a net loss of CAD 197 million in the prior year, largely due to higher revenues from treasury and international banking, as well as lower corporate expenses. Going forward, we now anticipate a quarterly loss of CAD 50 million to CAD 100 million in this segment.

In summary, notwithstanding a more challenging environment, throughout 2023 we took proactive steps to make meaningful progress against our strategy while staying on track relative to our medium-term objectives. Extending the momentum we demonstrated in 2022, we grew revenue by 7% and pre-provision pre-tax earnings by 8.5% in line with our in-year guidance and medium-term targets.

We delivered positive operating leverage through cost discipline and efficiency improvements to balance continued investment in our bank. And we overcame significant headwinds to enter the new year with a strong CET1 ratio of over 12.5% on a pro forma basis. EPS growth and ROE were below our medium-term targets this year, largely due to the impact of higher credit provisions and increase in capitalization. But we remain focused on working towards these targets despite external headwinds.

We expect credit provisions and capital ratios to start stabilizing in 2024 and we will drive further EPS and ROE improvements through our strategic focus, by emphasizing growth in key client segments with strong returns, maintaining discipline in resource allocation with a focus on returns over balance sheet growth, and leveraging our capabilities to drive simplification and efficiency to generate ongoing operating leverage.

With that, let me turn the call over to Frank.

Frank Guse, Senior Executive Vice-President and Chief Risk Officer

Thank you, Hratch, and good morning, everyone. During 2023, as we navigated economic uncertainties, we saw our loan loss performance generally in line with our expectations, with retail credit normalizing and sectoral-specific issues materializing in the business and government portfolio.

Over the past few quarters, the headwinds in the US office sector have translated into higher impairments in our US commercial real estate portfolio. While the Canadian consumer remains resilient to higher interest cost, we are seeing excess savings accumulated during the pandemic decline, so clients adjust to a variety of inflationary pressures. Notwithstanding, our allowance steadily increased throughout fiscal 2023 positions us well and will ensure we are prepared for uncertainty in the year ahead.

Turning to slide 25, our total provision for credit losses was CAD 541 million in Q4 compared to CAD 736 million last quarter. Total allowance coverage increased to 76 basis points this quarter, up from 73 basis points in Q3. Our performing provision was CAD 63 million in Q4, mainly attributable to changes to our forward-looking indicators, some model parameter updates, portfolio growth, and some credit migration.

Provision on impaired loans was CAD 478 million, which was flat quarter-over-quarter. And this was largely due to higher impairments in the US commercial and Canadian retail portfolios and was partially offset by lower impairments in the Canadian commercial portfolio and CIBC FirstCaribbean. While our impaired losses over the full year continue to perform in line with our expectations, we have seen elevated losses in the back of the fiscal year.

Slide 26 summarizes our gross impaired loans and formations. Balances were up this quarter, mainly driven by business and government loans in the US and was specifically attributable to the office sector. Overall, new formations remained relatively stable with the increase in retail, mostly offset by a reduction in business and government loans.

On slide 27, we show the trends in our Canadian consumer portfolios. Net write-offs and 90-day-plus delinquency rates for personal lending have moved higher over the past year, reflecting the impact of higher rates. This was expected given the interest rate sensitivity of this portfolio. Our residential mortgage and credit card portfolios continue to perform well and remain below pre-pandemic levels.

Slide 28 provides an overview of our Canadian real estate secured personal lending portfolio, which makes up 55% of our total loan balances. Late-stage delinquency rates of residential mortgages continue to trend higher, as expected, as they return closer to what we experienced prior to the pandemic. Variable rate mortgages account for one-third of our mortgage book, and the portfolio quality remains strong.

The portion of non-amortizing variable rate mortgages was down quarter-over-quarter from CAD 50 billion in Q3 to CAD 43 billion in Q4. Clients are choosing to increase their payments, converting to fixed rates, making one-time prepayment, and all of which bring the loan back to amortizing status.

This quarter, we're also providing a scenario highlighting the credit quality and payment increases for our mortgages coming up for renewal in the coming years. Overall, these cohorts show very low LTVs of between 40% and 60% in the next five years. The average monthly payment increase is roughly between CAD 350 and CAD 700 for these cohorts, which represents an increase of about 3% to 5% based on the origination income.

I also want to note that in this scenario we assumed an interest rate of 6% across the next five years, and the analysis also assumes income remains where it was at origination. I want to acknowledge that this high rate environment, paired with cost of living pressures, puts pressure on our clients. We are actively working with clients experiencing financial hardship to help drive to the best possible outcome. But overall, we feel comfortable with the resilience and reserve levels of our mortgage portfolio.

Turning to slide 30, as we previously guided, our US office portfolio continues to see elevated losses. In 2023, we had CAD 2.1 billion maturing, which is slightly more than 50% of the portfolio. Out of these maturities, around 54% qualified for extension or negotiated a renewal, around 15% was repaid, and the remaining 31% went into nonaccrual. Our allowance coverage continue to increase this quarter and now stands at 9.1%, reflective of the headwinds that persist in the office sector.

In closing, despite the headwinds in the US office sector, our credit performance remained within our expectations and guidance for fiscal 2023. As we head into the new fiscal year, we expect uncertainties to persist in certain areas, and we will see impaired losses trend above our previous guidance of 25 to 30 basis points, more in the mid-30s range.

We will continue to proactively manage portfolio exposures and we will work with our clients to mitigate risks. The additional allowances we saw throughout 2023 will provide prudent reserves for headwinds in the new year.

And I will now turn back the call to the operator.

Question and Answer Section

Operator

Thank you. We will now take questions from the telephone lines. [Operator Instructions] Our first question is from Doug Young from Desjardins Capital Markets. Please go ahead.

Doug Young, Analyst, Desjardins Securities, Inc.

Hi. Good morning. Maybe, Hratch, just if we can talk a bit about expenses. It sounded like you had some restructuring charges in the US and in Capital Markets. Can you quantify what those were? Can you confirm that was not backed out of cash EPS? And I do understand your position about looking to drive positive operating leverage over the medium-term. I'm trying to get a sense of is that something you think you can achieve – you did obviously very well this quarter. Is that something you think you can achieve through fiscal 2024 and 2025? Thank you.

Hratch Panossian, Senior Executive Vice-President and Chief Financial Officer

Good morning, Doug. Thank you for the question. Happy to take that. So let me start with your immediate question. And we did disclose that, right. So we had about CAD 114 million in severance. There was a few other things this quarter that I referred to in terms of onetime charges that were in those businesses relating to some matters, some real estate, some software, et cetera, across the bank. But that severance number that we disclosed was the majority of it.

In terms of how it breaks down, I'm not going to get into a lot of detail, but the predominant pieces of it were in the corporate and other segment and in Capital Markets. And there was a piece of it in the US, the one time in the US. And given what I said in terms of that growth, excluding the one-time you can back into it, it's sort of about in the 10% of that number range that you had this quarter.

And all of that is part of our journey, and it ties to the second part of your question. As we've said, we want to continue optimizing the bank as we go, making continuous improvements, investing, having the ability to move the team around and our resources around. So that's how we've delivered not just this quarter for the full year, 1.2% operating leverage as we've shown over three years and five years around neutral despite significantly increasing investment levels over that period of time.

And with that foundational capability now built, we have the ability to take out 1% to 2% of our expenses every year. This year it was more around the 1% range. Going forward, we've got now visibility into the pipeline of efficiency savings we're getting that's getting to that 2% number a year in 2024 and beyond.

So that's what allows us to manage our expenses to around mid-single digits, plus or minus, as we said we will do. And the plus or minus depends on the top line environment. So next year, we think it might be a tougher environment around the top line. And so, as I said in my guidance, we're now managing to the minus side of mid-single-digit on the expenses, but we can do that while actually investing and growth, having expenses grow above mid-single through those investments, funding everything we've laid out in those four priorities that Victor spoke about, including further efficiency improvements through enabling and simplifying our bank. And so, that's what allows us to continue generating that operating leverage on an ongoing basis.

Doug Young, Analyst, Desjardins Securities, Inc.

I'll adhere to my one question limit. So, thank you very much.

Operator

Thank you. A following question is from Ebrahim Poonawala from Bank of America. Please go ahead.

Ebrahim H. Poonawala, Analyst, BofA Securities, Inc.

Hey. Good morning. I guess maybe on the macro and credit for maybe Victor and Frank. I mean, just talk to us going back to your comment on the impaired PCL outlook in the mid-30s for next year. One, assuming that the Bank of Canada and rates are done going higher for this cycle, just give us a sense of your expectations on weakness in the economy and the consumer that you expect over the coming quarters and where the downside risk – like, what should – what are you paying attention to ensure that impaired PCLs are not meaningfully above, Frank, the guidance that you provided? Thanks.

Frank Guse, Senior Executive Vice President and Chief Risk Officer

Sure. And in that guidance, I mean, if you can imagine, there is a couple of moving parts. As I said, we continue to expect some further normalization in our consumer portfolios. Something we have seen and something we expect to continue to see. And then there is some others where we expect office to moderate in the next year, in line with our maturity profile. And then, give and take, that should lead us to that mid-30s range that we feel very confident with.

I mean, if asking about downsides, and again, we have increases in unemployment factored in, in our forward-looking information. If there is a more rapid shock to unemployment, that of course would change our outlook on impaired loan losses. But otherwise, given that we have started the fiscal year already and as such have a fairly good line of sight into the next few quarters, we feel very confident with our base case outlook even though there is, as you said, risks to the downside. And in particular any sharp shocks to the economy, a sharp increase in unemployment, a sharp drop in GDP, would certainly bring us closer to the downside.

And Victor will jump in.

Victor G. Dodig, President and Chief Executive Officer

Just really quick because I know there are a lot of questions and we're on tight time. So, we've architected CIBC to deal with the economic environment that might come in 2024. If things go slow, we'll manage accordingly. If things turn better, and there's a very good chance that we have this "soft landing," we will capitalize on that as well. Thanks, Ebrahim.

Operator

Thank you. A following question is from Gabriel Dechaine from National Bank Financial. Please go ahead.

Gabriel Dechaine, Analyst, National Bank Financial

Good morning. Just a question on capital here. And you converted the US loan book to IRB. That's going to add 20 basis points next quarter. That's great. I'm just wondering how does that affect the proximity of your risk- weighted assets to triggering the output floor because the IRB deflates RWA. So, I would think that might sort of bring it closer to that floor.

Hratch Panossian, Senior Executive Vice-President and Chief Financial Officer

Yeah. Thanks for that question, Gabe. I'll take that. So, first let me clarify that the 20 basis points approximate number that we disclosed is pro forma net of everything. So, that is – we have more than that in benefit from the transition to IRB. It's netted off by some fairly modest negatives from the combination of FRTB implementation and CVA changes, as well as negative amortization mortgages, as well as taking into account any floor impact. And we don't see at this point even post the IRB floor being an impact in the foreseeable future. And so net, we would have that 20 basis points this quarter and don't anticipate any other impacts because of that in the short-term.

Gabriel Dechaine, Analyst, National Bank Financial

Okay. So not a 2024 issue.

Hratch Panossian, Senior Executive Vice-President and Chief Financial Officer

Not a material issue, 2024 or 2025. I'm not going to comment beyond that.

Gabriel Dechaine, Analyst, National Bank Financial

Okay. All right. Thanks a lot.

Operator

Thank you. A following question is from Meny Grauman from Scotiabank. Please go ahead.

Meny Grauman, Analyst, Scotiabank

Hi. Good morning. Frank, I found slide 29 very helpful. Just a question in terms of the LTVs that you're showing. What are you assuming in terms of home prices to calculate those? Is there any sort of change in home prices that's being reflected?

Frank Guse, Senior Executive Vice President and Chief Risk Officer

Yeah. So those are – our current LTV calculations were based on externally published indices. We adjust house prices to our best predictor of current LTVs. So that would include the more recent moderation we have seen in house prices. It does not include any forward-looking further moderation or a recovery in the house prices. It's our current LTV calculation that's shown on the slide.

Meny Grauman, Analyst, Scotiabank

Got it. And then just in terms of some of the dynamics impacting the performing PCL line, especially in Canada. Just wondering the role of expert credit judgment this quarter in determining that number. And is anything notable from a modeling perspective as well that inputs into that?

Frank Guse, Senior Executive Vice President and Chief Risk Officer

Yeah. A lot smaller number this quarter. As we discussed last quarter, we adjusted our forward-looking indicators and our expectations to a more conservative scenario last quarter. This quarter, I wouldn't call out anything specific. It's a smaller number – or a number of smaller items impacting that number. It's our model results. It's our expert credit judgment. And it's going through our processes that we go through every quarter to land in the right spot for our allowances. So nothing to call out specifically, I would say.

Meny Grauman, Analyst, Scotiabank

Okay. Great. Thank you.

Operator

Thank you. A following question is from Darko Mihelic from RBC Capital Markets. Please go ahead.

Darko Mihelic, Analyst, RBC Capital Markets

Hi. Thank you very much. I'll be brief, Frank. I probably have a lot of follow-ups later. And I do appreciate the extra disclosure. I had a question on the negatively amortizing variable mortgages coming down from CAD 50 billion to CAD 43 billion. You're showing some success there in getting people out of negatively amortizing. But what I'm interested in is the opposite effect which is, of the CAD 50 billion, how many have you contacted? And clearly we could see 14% reduction, but how many people are electing not to increase their payments or reduce? And what would be the main reason for them not to move into a positively amortizing situation? Thanks.

Frank Guse, Senior Executive Vice President and Chief Risk Officer

Yeah. Thank you. Thank you, Darko, for the question. So, we have had a proactive outreach program to our clients for quite some while. We started that early. We have now reached out or contacted most of our clients in their portfolio and we do see strong results and we've seen those results quarter-over-quarter. In this quarter alone, 13,000 clients took action to remove themselves from negative amortizing status for the most part by increasing their monthly payments on a voluntary basis to remove their accounts off of negative amortization.

Why are clients not electing? There's a couple of reasons for that. Some are just saying, well, I'm aware of the status. I do not have to take action right now. I expect interest rates to come down and I just want to wait for that. There may be other reasons for that. But in general, we are very pleased with the outcomes that we are seeing so far. We continue to expect seeing those outcomes, and we continue to expect that number coming down as we keep up our outreach efforts and having conversations with our clients.

Darko Mihelic, Analyst, RBC Capital Markets

Okay. Thank you.

Operator

Thank you. A following question is from Lemar Persaud from Cormark Securities. Please go ahead.

Lemar Persaud, Analyst, Cormark Securities, Inc.

Hi. Thanks for taking my question. A question for Frank. Can you talk about what gives you the confidence in your PCL outlook despite the continued increase in delinquencies in Canadian consumer? Like, does that assume normalization of delinquencies to the Q1 2020 rate you're showing here so the 34 basis points; or are you assuming something above that 34 basis points you're showing in your slide 27? Thanks.

Frank Guse, Senior Executive Vice President and Chief Risk Officer

Yeah. Well, I would say, as I said before, there's a couple of moving parts. So we do expect some further normalization and it's probably a little bit more product specific. We talked a little bit about mortgages in our prepared remarks where we expect normalization, but we are very confident with the quality of those books and that those renewals will remain very manageable for us.

Cards performance continues to be very good. There is, in part, our co-brand portfolio that is supporting strong credit quality, but there is underlying investments in risk management that we did in the cards book that is helping drive real change in credit quality as well. And then in personal lending, again, that is a little bit a mix of different things, but we are seeing strong credit quality there. But there's also certain pockets like our unsecured lines book where we see normalization and we should expect to see normalization.

So that gives us confidence with our base outlook because it's based on a bottoms-up assessment of all of those moving parts.

Lemar Persaud, Analyst, Cormark Securities, Inc.

Thanks. I'll adhere to the one question.

Operator

Thank you. A following question is from Sohrab Movahedi from BMO Capital Markets. Please go ahead.

Sohrab Movahedi, Analyst, BMO Capital Markets

Okay. Thank you. Capital ratio is going to look pretty strong. Maybe a question for Victor and/or Hratch. Can I get a sense of what are the priorities and at what sort of levels are you comfortable running the capital ratios for the bank given the type of outlook that you've kind of presented to us? And I guess implicit in that, Hratch and Victor, is whether or not you intend to continue to keep the DRIP on? Thank you.

Victor G. Dodig, President and Chief Executive Officer

Good morning, Sohrab. Thanks for that question. We've been, as a leadership team, very focused on accreting capital over the course of the year. And as I said in my opening remarks, we've done that every quarter through organic capital generation, through our DRIP, as well as through a strategic risk transaction.

We continue to focus on a strong capital level. We look at it through three lenses. What is the regulatory stance today vis-à-vis the buffer that OSFI has put in place? How do we compare against our peer group? And, three, is how do we view the macroeconomic environment? Our goal is to continue to maintain a strong level of capital and liquidity.

I'll hand it over to Hratch to take you through the numbers, how we think about the buffer, how we think about the DRIP. But you can rest assured that, that focus of ours as a leadership team on capital is paramount.

Hratch Panossian, Senior Executive Vice-President and Chief Financial Officer

Thanks for the question, Sohrab. Let me just add a little bit to what Victor said. First of all, we have very strong capital generation on an ongoing basis, and we do not need the DRIP on in order to continue growing our business and delivering on the EPS targets that we've laid out. If you look at any given quarter, we generate 25 to 30 basis points of capital net of our dividend payments. And our ROE is such that, that allows us to grow our risk-weighted assets in the high single-digits and continue growing our business alongside with that.

And so what that means is the DRIP program over this year has been to absorb the headwinds and to drive our capital ratio up. And we talk about how much we've driven the capital ratio up year-over-year at 70 basis points. But that is after having absorbed a significant amount of headwinds through some of the legal charges, some of the regulatory changes and so forth that have happened. So that's what the DRIP has allowed us to do.

We're in a good place now. If you look at those three factors Victor spoke about, there's still a little bit of uncertainty around regulatory requirements where they stabilize around the peer group and where it stabilizes. We're in a very good place entering north of 12.5% and accreting from there in 2024. And we'll look at as we get more certainty on those factors, once we're satisfied that we're stabilizing around these levels on a relative and absolute basis, we're able to shut down the DRIP and able to continue growing our business through our strong organic generation.

Sohrab Movahedi, Analyst, BMO Capital Markets

Thank you.

Operator

Thank you. A following question is from Nigel D'Souza from Veritas Investment Research. Please go ahead.

Nigel D'Souza, Analyst, Veritas Investment Research Corp.

Thank you. Good morning. This is another question for Frank. On performing credit losses this quarter, a couple of factors here. First, it doesn't look like your FLIs fully reflect the recent softening macroeconomic outlook and specifically on home prices. From what I understand, your economic team has negatively revised outlook for house prices for 2024. So just wondering how sensitive your performing PCLs would be to that downward revision in home prices. And maybe some comments on why you elected not to apply management overlays to build more provisions given the challenging macroeconomic backdrop.

Frank Guse, Senior Executive Vice President and Chief Risk Officer

Yeah. So thanks for the question, Nigel. Overall, as I said, we feel very comfortable with our allowances. We reflected some of those adjustments last quarter and didn't feel like there was anything that we had to add materially this quarter for those outlooks. Generally and across all products, I would say it's probably debt service ratios, unemployment, GDP that is more sensitive to actual PCLs.

House prices, of course, would play a role in the mortgage allowances, but that is an area where we actually have built quite a lot of reserves. And then again, we are reflecting a variety of outcomes and have adequately reflected that in our allowance.

Nigel D'Souza, Analyst, Veritas Investment Research Corp.

Okay, that's my one question. Thank you.

Operator

Thank you. A following question is from Mario Mendonca with TD Securities. Please go ahead.

Mario Mendonca, Analyst, TD Securities

Good morning. On this new Canadian Mortgage Charter, I've gone through it and I am having a little difficulty finding stuff that's brand new. Just high level from your perspective, is there anything in there that's new that affects CIBC that could affect earnings or capital? That's my first question.

Frank Guse, Senior Executive Vice President and Chief Risk Officer

You're right. It's very well aligned with previous guidance and expectations. It's something that we do. We work with clients in financial hardship and we try to get to the best possible outcomes with our clients wherever possible. So, there's nothing new that I would say that sticks out and would impact us as we already have established practices of how we work with clients in financial hardship.

Mario Mendonca, Analyst, TD Securities

Two quick follow-ups on that then. So the notion that banks can't charge interest on interest. Presumably that only applies to mortgages that fall under that relief category under the charter. It doesn't apply to existing mortgages that are negative. Is that appropriate? Is that fair?

Frank Guse, Senior Executive Vice President and Chief Risk Officer

That is our understanding.

Mario Mendonca, Analyst, TD Securities

And then finally on the hardship. When mortgages fall into hardship, does that necessarily increase the capital requirements and is that meaningful?

Frank Guse, Senior Executive Vice President and Chief Risk Officer

Well, it does increase capital requirements, but it is a very small part that would actually be captured under the financial hardship rule. So overall, it is not material or meaningful, but it would impact capital requirement, for sure.

Mario Mendonca, Analyst, TD Securities

Thank you.

Operator

Thank you. We have no further questions registered at this time. I would now like to turn the meeting back over to Victor.

Victor G. Dodig, President and Chief Executive Officer

Thank you, operator. And thank you for the questions today. We're going to give you back some time. I know you got another call at 8:30 and another call today. I want to thank you all for your engagement with us throughout the fiscal year this past year, on our quarterly calls and in the other forums where we get to engage with you.

I said at the outset of my remarks that we have the right strategy at CIBC. We also know how to operate in a fluid and uncertain environment. Our proactive management in a more challenging environment this past year is an example of that, a year in which we generated positive operating leverage, a year in which we protected net interest margin, and a year in which we strengthened our balance sheet throughout the year, while continuing to make strategic investments to ensure our bank is well-positioned for the future.

I have full confidence and our leadership team has full confidence in the deep bench of talent within our businesses, and our experienced leadership team is there to deliver on our strategic priorities that we've laid out here in all of our businesses in the upcoming year.

Before we close the call, I'd also like to recognize our entire CIBC team for their contributions as they delivered on our purpose for our clients, our communities, and for one another, and of course, for our shareholders. This purpose comes to life each year at CIBC Miracle Day taking place next week, next Wednesday, to raise funds for children's charities. I'm looking forward to the event. It's a big deal for us. It's a big deal for the community. It's something we started over three decades ago and I hope you all participate. Wishing you all the best for the holiday season. Thank you.

Operator

Thank you. The conference has now ended. Please disconnect your lines at this time. And we thank you for your participation.