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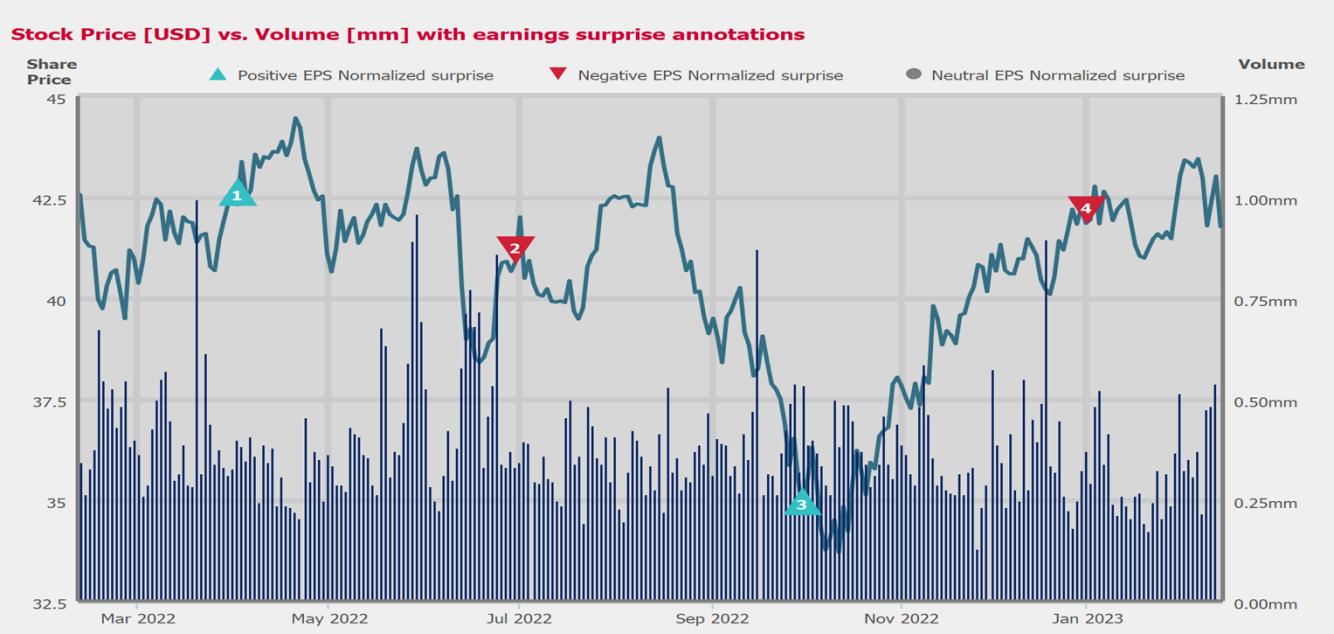
FQ4 2022 Earnings Call Transcripts

Tuesday, February 14, 2023 9:15 PM GMT

S&P Global Market Intelligence Estimates

	-FQ4 2022-			-FQ1 2023-	-FY 2022-			-FY 2023-
	CONSENSUS	ACTUAL	SURPRISE	CONSENSUS	CONSENSUS	ACTUAL	SURPRISE	CONSENSUS
EPS Normalized	0.55	0.52	(5.45 %)	0.39	2.18	2.20	0.92	2.32
Revenue (mm)	1162.70	1019.11	(12.35 %)	712.32	3363.19	3741.98	11.26	3164.67

Currency: USD
Consensus as of Feb-01-2023 11:11 AM GMT



- EPS NORMALIZED -

	CONSENSUS	ACTUAL	SURPRISE
FQ1 2022	0.44	0.63	1 40.00 %
FQ2 2022	0.52	0.48	2 (7.69 %)
FQ3 2022	0.54	0.57	3 5.56 %
FQ4 2022	0.55	0.52	4 (5.45 %)

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Presentation

Operator

Good afternoon, and thank you for attending today's Hawaiian Electric Industries Earnings Conference Call. My name is Danielle, and I will be your moderator for today's call. [Operator Instructions] It is now my pleasure to pass the conference over to our host, Mateo Garcia, Director of Investor Relations. Mateo, the floor is yours.

Mateo Garcia

Thank you, Danielle. Welcome, everyone, to HEI's Full Year and Fourth Quarter 2022 Earnings Call. Joining me today are Scott Seu, HEI President and CEO; Paul Ito, HEI's CFO; Shelee Kimura, Hawaiian Electric President and CEO; Ann Teranishi, American Savings Bank President and CEO; and other members of senior management. Our earnings release and our presentation for this call are available in the Investor Relations section of our website. As a reminder, forward-looking statements will be made on today's call. Factors that could cause actual results to differ materially from expectations can be found in our presentation, our SEC filings and in the Investor Relations section of our website. Now Scott will begin with his remarks.

Scott W. H. Seu
President, CEO & Director

Aloha kakou, greetings, everyone. Thank you for joining us today. I'll give an overview of our results and accomplishments over the past year, update you on the Hawaii economy and then turn the call over to Paul to further discuss our financial results and guidance. 2022 was a year of strong achievement for HEI, highlighting the strategic benefits we continue to see from our combination of companies. We earned $241 million in net income and $2.20 in earnings per share for the full year, reflecting solid performance at both the utility and bank. Despite an unprecedented combination of macroeconomic challenges occurring in the first full year under our new regulatory framework, Hawaiian Electric grew earnings 6% year-over-year to $189 million.

This was consistent with our expectations and in line with the improved guidance we messaged during our third quarter webcast. ASB had a strong year as well with the strongest loan growth in a decade, reflecting continued solid credit quality and a healthy Hawaii economy. Bank earnings of $80 million were in line with the increased earnings guidance we communicated in the third quarter.

As a reminder, the $101 million the bank earned in 2021 reflected benefits from unique pandemic recovery related items that Paul will highlight later. Last week, we raised our annual dividend for the fifth year in a row, reflecting our confidence that our combination of companies will continue to deliver steady results going forward.

Turning to Slide 3. 2022 was our first full year of performance-based regulation, or PBR, given the unusual convergence of macro headwinds during the year, we saw 2022 as a successful stress test of this new regulatory framework.

Our utilities showed an ability to quickly adjust and maintain operational efficiency despite multiple challenges from inflation, interest rates and fuel costs. We executed well and delivered earnings growth even in the stress test conditions. We recognize that 2022 was not an easy year for our customers, historically high inflation and oil prices rising borrowing costs and volatile food and commodity prices challenged Hawaii as they did the rest of the nation, and we responded by finding more ways to care for our customers in need of assistance.

Elevated fuel prices and the resulting customer bill pressures seen in 2020 further highlight the importance of our renewable energy transition. In 2022, we continue to execute on key elements of utilities climate change action plan, which targets reducing carbon emissions in 2018, 70% below 2005 levels and achieving net zero carbon emissions by 2045. In September, we achieved a major milestone in our client interaction plan with the retirement of Hawaii's last coal plants. Despite global supply chain challenges that have impacted renewables projects nationwide, we reached an important milestone last summer when Oahu's first utility-scale solar plus storage project was energized and last month, we brought another of these projects online.

We continue to expand our procurement of renewables. And in 2022, we laid the groundwork for our recently launched Stage 3 RFP. Based on the amount of renewable energy we're seeking, this would be our largest renewables procurement ever. In 2022, we achieved a renewable portfolio standard or RPS level of 39.1%, up from 38% in 2021. I'll note here that there is a new definition of RPS now in effect under Hawaii State law. Going forward, we'll only reference RPS achievement in terms of the new definition which is consistent with the RPS-A performance incentive mechanism.

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Under the new definition, our 2022 RPS was 31.8%, up from 31% in 2021. Even with the new definition, we expect to meet the 40% RPS by 2030 milestone ahead of schedule. Customer owned renewable generation remains key to moving Hawaii towards its 100% renewable energy. Our battery bonus program, which provides a cash incentive and bill credits for customers to add storage to existing or new rooftop solar systems made progress in 2022. This is an innovative program that benefits both the battery bonus customer and other customers on the broader energy system.

As the batteries are programmed to discharge to the grid during the [seasoning] peak period. Our utility is taking additional steps to ensure our renewables transition benefits the communities we serve. In November, the utility selected 7 solar projects across the islands for our community-based renewable energy program for customers who meet low and moderate income loans and are unable to install privately owned rooftop solar. The electrification of transportation is also key to a greener Hawaii and in 2022, the utility launched the charge of commercial pilot program to help nonresidential customers reduce the upfront investment and complexity of installing EV charging stations.

Turning to the bank. American Savings Bank continued to perform very well through 2022. Demonstrating the value of its conservative management approach, good credit quality and low-cost funding base. ASB continues to generate a dividend that provides efficient capital to support both our consolidated investment-grade capital structure and our growing dividends to shareholders. ASB leveraged its strong customer relationships and best-in-class customer service to grow loans by 15% in 2022, the strongest growth in over a decade while maintaining our high standards of loan underwriting.

As Paul will discuss shortly, we expect loan growth to return to more normalized levels in 2023. Excluding the pandemic recovery related items unique to 2021, the bank grew earnings meaningfully in 2022, while continuing to execute on key initiatives such as digital transformation.

For example, ASB implemented Zelle in 2022, providing customers with a secure, fast and convenient way to send money digitally to friends and family. We've continued to see an accelerated pace of digital adoption, first brought on by the pandemic and over half of transactions are now executed through digital channels compared to less than 20% pre-pandemic.

Turning to the economy. Hawaii's economy has continued to show signs of strength and resilience, and we believe it remains well positioned to weather potential economic headwinds. The University of Hawaii Economic Research Organization, UHERO which provides the most frequent forecasts of our state's economy is not expecting a recession in 2023 in part due to continued recovery of Japanese tourism and surging public sector construction.

The strength of Hawaii's economy is all evident in the strong loan growth our bank generated this past year in both residential and commercial real estate. Hawaii's unemployment rate was down to 3.2% in December, continuing the downward trajectory we saw throughout the year. Our state's unemployment has been lower than the national average since October, and this is notable as we had the highest unemployment in the nation during the early days of the pandemic.

Employment here has fared comparatively well during downturns and performed better than the national average during the financial crisis. Hawaii's housing market had a strong year, with housing prices remaining near record levels despite slower sales activity due to higher interest rates. The median Oahu single-family home price was $1.1 million for the full year, up 11.6% versus 2021. Tight supply continues to characterize Hawaii's housing market. Supporting housing prices through downturns and contributing to the strong credit quality of our bank loan portfolio.

Tourism arrivals recovered to over 91% of pre-pandemic levels as of December primarily due to a strong recovery in domestic travel. Visitor spending for the full year was up 9% from 2019 levels. As I hand the call over to Paul, I'm please to say that he is now our CFO after serving as our Interim CFO since July of last year. Many of you likely saw our press release last month announcing Paul's appointment effective January 1. I look forward to continuing to work with him in the capacity, and we're excited to have him in the CFO seat. And with that, I'll turn the call over to Paul.

Paul K. Ito
Executive VP, Controller, Treasurer & CFO

Thank you, Scott. I'll start on Slide 6 with our results for the year. We are pleased with our 2022 performance. We generated consolidated net income of $241 million and EPS of $2.20 compared to $246 million and EPS of $2.25 in 2021. As a reminder, our 2022 results included a $0.06 gain on sale of the EverCharge investment recorded at Pacific Current. Also, as Scott mentioned net income for 2021 reflected bank earnings that were elevated by 2 pandemic recovery related items, a net benefit from the release of reserves and PPP fee income.

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Excluding these items and the EverCharge gain recognized in 2022. Earnings grew meaningfully year-over-year. Our consolidated ROE for 2022 was 10.5%, an increase of 10 basis points from 2021. The utility made progress in narrowing the allowed ROE gap achieving an ROE of 8.2%, which was up from 8.1% in 2021. And bank ROE increased to 14.1% and from 13.8% in 2021.

On Slide 7, we show the major variances across our enterprise compared to last year. Overall, we saw very strong results from the bank in 2022, and results were in line with the increased guidance we provided in the third quarter. As mentioned, the net income variance compared to 2021 was largely due to 2 pandemic related items. First, the bank returned to a more normalized provision for credit losses of $2 million as we provisioned for the strong loan growth seen during the year.

In comparison, in 2021, the bank recorded a negative provision for credit losses that is a net benefit of $25.8 million due to an improved economic outlook and credit quality improvements coming out of the pandemic. Second, net income in 2021 benefited from over $11 million in higher PPP fee income compared to 2022. However, the decrease in PPP fee income was more than offset by higher yields on loans and investment securities and strong loan growth across the entire portfolio in 2022.

Notably, net interest income grew 6.5% as the bank more than made up for the lower PPP fee income. The bank saw lower noninterest income of $57 million compared to $65 million in 2021. The decrease was primarily due to lower mortgage banking income, lower bank-owned life insurance income and lower fees from other financial services, partially offset by higher fee income and deposit liabilities, gains on sales of real estate related to branch closures and fee income on other financial products.

Noninterest expense for 2022 was about 4% higher at $205 million compared to $197 million in 2021. The increase was primarily due to a pension accounting change that resulted in lower pension expense in 2021 and higher occupancy costs in 2020 from the write-off of leases related to branch closures. On the utility side, we saw $25 million more in ARA revenues, $4 million in higher fee revenue, $3 million in higher revenue recovered under our major project interim recovery mechanism, $1 million in higher AFUDC and $1 million due to the reset of heat rate requirements, leading to lower penalties for fuel efficiency at our Hawaii Island facility.

These items were partially offset by $13 million in higher O&M expenses, which were driven by increased generating station maintenance, higher bad debt expense and increased transmission and distribution, preventative and corrective maintenance, $4 million from higher depreciation expense, $3 million higher interest expense and $2 million in net tax adjustments due to tax credit benefits recognized in 2021.

I would note that the utility managed cost well in 2022. On a GAAP basis, the utility had a net increase of about 4.6%. However, adjusted O&M, which is a non-GAAP measure and excludes retirement service costs and expenses covered by surcharges and activities billed to third parties was up 3.7% and reflecting our proactive measures to offset the inflationary pressures we experienced during the year.

For perspective, 2022 GDPPI was 7%. We remain well within that level. As always, continuing to manage costs efficiently will remain a central focus under the PBR framework.

On Slide 8, utility CapEx for the year was approximately $357 million, in line with the guidance range of $350 million to $375 million we communicated during our third quarter earnings call. CapEx in 2022 was lower than originally anticipated due to supply chain disruptions, customer work delays, project rescoping, resource availability and permitting delays.

Looking ahead to 2023, we are expecting CapEx to increase to $370 million to $410 million. Under PBR, our ARA revenues cover baseline CapEx and O&M and we expect baseline CapEx of $300 million to $330 million annually. The remainder of our CapEx is recovered under separate mechanisms, such as our exceptional project recovery mechanism, which provide incremental earnings opportunities. We already have about $60 million in approved separately CapEx in our forecast for 2023 with another $12 million awaiting approval.

As you can see on the slide, there is some lumpiness in the forecast. But with projects awaiting PUC approval or applications to be filed with the PUC, CapEx could increase to $540 million by 2025. As of December 31, 2022, we had about [$472] million of EPRM project applications filed awaiting PUC approval. Of this total, 40% of the capital is forecasted in the 2023 to 2025 time frame, but weighted toward the back end with the balance following 2025. Not shown is this slide are potential investments for several utility-owned generation projects. Over the next few years, we may be filing applications for these projects, including for critical contingency generation and firm renewable generation facilities under the Stage 3 RFP that are needed for reliability and resilience.

The estimated capital cost for projects are in the process of being developed and any material advancements would begin after this forecast period.

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Turning to the next slide, recall that there are 3 key earnings drivers for the utility under our PBR framework. First, the annual revenue adjustment or ARA, covering baseline O&M and baseline CapEx through an inflationary adjustment minus the customer dividend. For 2023, this inflationary adjustment was set in October of last year according to the Blue Chip GDPPI forecast for 2023 and is 3.68% net of the customer dividend. Second, the separate recovery mechanisms for eligible capital and O&M projects, providing recovery above the baseline levels covered by the ARA.

And third, performance incentive mechanisms or PIMs, which provide opportunity for additional rewards if we achieve preset goals. I'll now cover what we expect from each of these mechanisms in 2023. The ARA minus the customer dividend provides a net $33.5 million in revenues for 2023. The accrual for the ARA started January 1. To the extent we are able to manage O&M and capital efficiently, we would benefit in the form of additional earnings. Our current forecast assumes we've managed adjusted O&M and capital within the ARA inflationary adjustment.

With respect to separate recovery, we'll be accruing over $26 million in revenues for projects that have been approved by the PUC. This is under the EPRM and the major project interim recovery mechanism. Additional revenues of about $1 million are possible for separate recovery projects that are expected to be placed in service in 2023 and thus received a partial year of revenues. Lastly, we expect about $4 million in pretax income from net PIM rewards in 2023, primarily coming from the achievement of RPS-A and interconnection experience incentives. With respect to the fuel cost risk-sharing mechanism, we have assumed no penalty or reward.

Turning to the bank on Slide 10. Net interest income grew in 2022 with earning asset growth and higher yields. ASB's net interest margin remained relatively stable in 2022 at 2.89%. Compared to 2.91% in 2021. Higher yields on loans and investment securities, strong loan growth and higher balances of investment securities benefited the bank's NIM although these items were offset by lower PPP fee income and our cost of funds. The average of funds was 16 basis points for the full year 2022, 10 basis points higher than the prior year.

We saw a larger increase in the fourth quarter as the bank utilized wholesale borrowings to support our strong loan growth. As a result, we saw an increase in our funding costs in the fourth quarter to 38 basis points up 25 basis points from the prior quarter. We do expect higher funding costs to continue throughout 2023, as market interest rates continue to increase and to the extent our level of wholesale funding remains elevated. However, we believe the strength of our core deposit base will allow us to maintain our funding cost advantage in comparison to our peers throughout 2023.

On Slide 11, we provide further detail on our expectations for ASP this year. We are expecting the provision for credit losses for the year ranging from $0 to $10 million. This range reflects our expectations for credit quality, loan growth and economic conditions. We continue to maintain our conservative lending practices with a loan book that is over 80% real estate secured at a conservative weighted average loan to value of around 50%. As a result, we're confident about the strong credit quality of our loan portfolio.

As Scott mentioned, loan growth in 2022 was at a historically strong level, but we do expect loan growth to return to a more normalized level in 2023. We currently expect loan growth to be in the low single-digit range this year. In order to fund the strong loan growth in 2022, given flat deposit growth we increased our wholesale borrowings and CD balances, which reduced our balance sheet asset sensitivity to be essentially neutral. As a result, although additional Fed rate increases will continue to benefit us, we'll also have to manage our funding cost to see the improved net interest margin. We are already taking measures to manage our funding costs, including focusing on paying down higher cost wholesale borrowings as those costs have come up considerably as short-term rates have risen.

Similar to the utility, the bank is very focused on efficiency, and that is expected to help keep bank operating expense increase as moderate even while investing in the bank's digital transformation. We expect to see an improvement in the bank's efficiency ratio in 2023. I've discussed the drivers behind our expectations for utility and bank performance in 2023 and on Slide 12, we bring this all together for our 2023 guidance. We are initiating our 2023 consolidated earnings guidance of $2.15 to $2.35 per share.

Our midpoint of $2.25 represents 5% growth over our 2022 EPS excluding the onetime $0.06 gain on sale for EverCharge we recorded in the first quarter of 2022. Our utility EPS guidance of $1.75 to $1.85 assumes recovery of COVID-19 related deferred expenses, the vast majority of which was related to bad debt. The amount to be recovered has been reduced significantly to approximately $11 million due to payments received and we expect a PUC decision in the second half of 2023.

We expect adjusted O&M excluding pension, to increase at a rate that is below the ARA inflation adjustment. This reflects the utility's continued focus on cost efficiency. I've already covered our expectations for 2023 regarding CapEx and contributions from PIM, but I'll add that beyond 2023, we expect a long-term utility earnings compound annual growth rate of 5% through 2025 of a 2022 base, including an average of $4 million to $5 million pretax annually from PIM.

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Last year, we projected long-term utility earnings growth guidance of 5% through 2024 with upside from PIMs. Our current guidance reflects continued higher generating station maintenance moderating in the coming years as we bring new generation and storage resources online and as units are retired. Higher O&M expenses due to inflationary environment and higher bad debt expense. Updated time lines for placing EPRM-recovered projects in service; and finally, higher interest expense related to higher rates.

Our bank guidance of $0.75 to $0.85 per share reflects continued solid profitability and earnings growth. It accounts for inflationary impacts to expenses, which we continue to manage through cost efficiencies including our branch optimization strategy. We expect low single-digit loan growth and net interest margin of 3% to 3.15%. We expect holding company expenses to be higher than in 2022 levels due to higher interest rates and debt balances, leading to increased holding company interest expense and we expect a holding company net loss of $0.34 to $0.36 in 2023.

We do not anticipate any equity issuances for '23. I'll now turn the call back to Scott, who will provide closing remarks.

Scott W. H. Seu
President, CEO & Director

Mahalo Paul and mahalo to all of you for joining us today. In summary, we had a great year characterized by strong performance from both the utility and bank, and our investors benefited from our unique combination of operating companies during a challenging macroeconomic period.

There were no surprises in our results, and we executed well to the higher revised guidance given in the third quarter. Our new regulatory framework at the utility is showing that it provides us with stability and predictability. And as macroeconomic and operational headwinds ease up, we expect to see growing performance as we execute our strategies of investing in our system and running the business efficiently for our customers.
Our bank will continue to be run conservatively and is well situated to respond to changes in the economy and interest rate environment. We are confident that we will again deliver solid results in 2023. With that, let's open up the call for questions.

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Question and Answer

Operator

[Operator Instructions] The first question comes from the line of Shahriar Pourreza of Guggenheim Partners.

Unknown Analyst

It's actually [indiscernible] for Shar. Congrats on a great quarter and to Paul on the new position.

Paul K. Ito
Executive VP, Controller, Treasurer & CFO

Thanks, Shar. Appreciate it.

Unknown Analyst

Maybe starting off on the utility. Can you help elaborate on the O&M targets that you're setting prospectively and conditions that you're seeing across the business? Any constraints on labor, materials and any path normalize? Just to get a sense of kind of percentage of O&M that's subject to external factors? And maybe what will cause you to rethink kind of any level of regulatory release?

Scott W. H. Seu
President, CEO & Director

Yes. Well, maybe I can start. What we have baked into our forecast, there are still some elevated O&M expenses, especially with respect to our power plant generation station maintenance. We are expecting that to continue into 2023, but albeit it will start to taper off as we start to get more new generation resources online. And later on, of course, as we're able to retire some of our older power plant units.

So we've taken that into account in our look ahead. Like we experienced in 2022, I think the utility was able to respond fairly well to managing overall expenses in other areas of the company. So we're going to continue to be able to do that in 2023 and beyond. Maybe, Paul, if you have any further comment specifically about our management or our expenses within the ARA.

Paul K. Ito
Executive VP, Controller, Treasurer & CFO

Yes. So we are committed to managing O&M and looking at efficiencies to further ensure that our O&M stays within the ARA recovery levels. I'll just provide a data point in terms of how successful the utility has been over the past few years in managing O&M efficiently. So if you look at O&M and I'm referencing adjusted O&M, which strips out some of the pension and other costs that are recovered from other parties from 2019 through 2022, if you look at the compounded annual growth rate of O&M, it's been less than 0.5%. So utility has done very well in managing those costs. Obviously, the low-hanging fruit has probably been harvested. So it does get a little bit harder over time.

But I think the utility has shown that it has the ability to manage O&M well within this PBR framework, which again we feel is a good framework because we know what -- it adds stability and predictability. We know what revenues we're getting. And so our task as a management team is to ensure that we conduct a business such that our expenses come in within that area allowance.

Unknown Analyst

Excellent. I think that's very helpful. And you kind of mentioned a part of my second question which was on the revenue side kind of since the -- kind of ARA portion of the revenue formulas for '23 is fairly well defined by the GDPPI. Just a question on what level of visibility do you have on the other PBR elements, namely the non-RPS related ones, like AMI energy efficiency as those could kind of impact earnings? And how is the most recent fuel cost trajectory impacting your risk-sharing calculations?

Scott W. H. Seu
President, CEO & Director

Yes, I'll start. I think with respect to the full slate of performance incentive mechanisms or PIMS, we now have a track record of a full year of operating under the PBR and experiencing how those PIMs perform. So the utility is able to put their focus on the PIMs

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that they have pretty good line of sight on controlling. Perhaps a good example is the interconnection PIM which the utility performed fairly well last year, earning a reward there. Those are the types of PIMs that provide the utility with the ability to manage their work how they plan and execute the work.

And ultimately achieve on the PIM rules. That's going to continue to be the focus of our utility team. There are admittedly some other PIMs that are a little bit more challenging to just have direct control over. And one example of that is probably the fuel cost risk sharing PIM where we did receive a penalty based on overall fuel prices last year. As best we can, we're going to continue to focus on the PIMs that we do have control over. And meanwhile, on the other PIMs, we'll just as we see how they play out during the course of the year, that will just be a signal on how we need to adjust in other areas of the business.

Paul K. Ito
Executive VP, Controller, Treasurer & CFO

And I'll just add, there are good number of PIMs. But what we focus on, at least in terms of providing guidance that we initiated here on the PIMs is really the RPS-A and some of the DER related PIMs because those are the ones that are more meaningful. A lot of the other ones, one is more difficult to predict, but of smaller amounts. And so those tend to have puts and takes that generally offset in our -- we're at least -- what we're forecasting here. So again, the most important ones that we focus on would be the RPS-A PIM, which we see overtime growing as additional projects come online.

Unknown Analyst

Okay. That makes sense. And the last one, if I may, really quick. Just on what's embedded in guidance on the bank side for repricing of earnings assets, and that's been kind of tracking, I believe since June until that's raised from roughly $175 million to $475 million. But just beyond that, kind of what are you embedding in terms of repricing kind of as we look at the guidance today?

Paul K. Ito
Executive VP, Controller, Treasurer & CFO

Yes. So if you're referring to our NIM, we are expecting that to increase in 2023 to 3% to 3.15%. That increase is in a large part, based on managing the funding side, so paying down higher cost wholesale borrowings. That at the margin has -- those costs have increased quite significantly, as the Fed has increased rates. So we see an opportunity as our investment portfolio pays down. Those proceeds are used to pay off some of those higher cost borrowings. And that will help us increase our net interest margin.

Unknown Analyst

And the revenue side of the adjustable rate assets, those are kind of in plan marked as of the last Fed date, any assumptions around increases for '23 or just holding flat?

Paul K. Ito
Executive VP, Controller, Treasurer & CFO

Yes. So in terms of our adjustable rate assets, as we mentioned, because of the strong loan growth that we had in 2022, we did have to supplement on the funding side, some of these higher-cost sources of funds, FHLB and some CDs. And so our balance sheet is a little bit more asset neutral, meaning additional fund rate increases doesn't -- is not accretive to NIM, it does -- it's accretive to net interest income. So in terms of further Fed rate increases, we wouldn't expect a significant impact to our NIM. But again, as I mentioned, if we are able to manage the funding side and pay down those higher cost borrowings, our balance sheet will become more asset sensitive in which case for the Fed fund rate increases would be accretive to NIM.

So that's the plan currently is, again, to focus on paying down some of those higher-cost funding sources.

Scott W. H. Seu
President, CEO & Director

Yes. And we expect to have more capacity to do that as we see the loan activity sort of get back more towards normal levels.

Paul K. Ito
Executive VP, Controller, Treasurer & CFO

Yes. We just saw a very unusually high probably more than a decade of high loan growth in which we had to tap some of these other sources of funding.

Scott W. H. Seu

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President, CEO & Director

Yes. Let me ask Ann Teranishi, our Bank President, if she has any other comment.

Ann C. Teranishi
CEO, President & Director of American Savings Bank

Yes. Maybe just specific to the question about our adjustable rate portfolio, about $1 billion of our loan book is in the adjustable rate category. So that does change as the rates go up. Also, all of our new origination, all the new loans coming on are at a higher rate than what's on our books. So the rate environment in that sense helps us. But I think what Paul and Scott are referencing is what all banks are experiencing is just increasing funding costs.

The one thing I would add to that, though, is Hawaii traditionally has a fairly sticky deposit base. So our betas are low. Our deposit betas are low and our funding costs, while they are increasing. They are lower relative to our mainland peers. So that's something that should help us whether that's particular portion of the rate cycle.

Operator

The next question comes from the line of Paul Patterson of Glenrock Associates.

Paul Patterson
Glenrock Associates LLC

So just -- I apologize. I just want to follow up on [indiscernible] question, I guess, from a different angle. When looking at the NIM, I just -- I guess, it sounds like you're -- could you just walk through a little bit for me. I guess I'm a little slow on what's driving your expected lower costs.

You're saying you're paying down wholesale cost -- wholesale funding, are you going to be increasing deposits? Or is this -- just walk me through in terms of what's leading to because it seems that your costs are going up. And I just did not clear on the NIM, what you're projecting to decrease that exactly? I mean you're going to be using less wholesale. Where is that coming from now? Where is the source of funding coming form, is it coming from deposits?

Paul K. Ito
Executive VP, Controller, Treasurer & CFO

So in terms of the funding, right? So we expect the loan growth to normalize from the high growth rates that we had in 2022. So in 2022, we had to find additional funding beyond sort of the investment portfolio runoff. And because deposit growth was relatively flat in 2022, we had to take on these higher cost wholesale borrowings. Looking forward to 2023, we expect loan growth to moderate. And so we expect the runoff from the investment portfolio as well as retained earnings to provide the funding to pay down some of these wholesale borrowings. And so that's what allows us to shift the kind of the funding mix on the balance sheet.

Paul Patterson
Glenrock Associates LLC

I got you. I understand. So and the loan growth you see going down to what level?

Paul K. Ito
Executive VP, Controller, Treasurer & CFO

Loan growth of low to mid-single digits,which is the normal sort of rate in the Hawaii market.

Paul Patterson
Glenrock Associates LLC

Okay. And there's no pressure at all in the -- on deposits in terms of -- in terms of increased cost there at all. The market just doesn't -- if there is any competition from online banking or anything like that? Or you're not seeing any, I guess, is what you're expecting, at least or what you've been seeing?

Paul K. Ito
Executive VP, Controller, Treasurer & CFO

Well, as rates rise, I mean, we are seeing some pressures more on the commercial side versus our core deposit base. But over time, we do expect rates to follow kind of the Fed fund rate increases. I would say we still believe we have a low deposit beta relative to the

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Mainland, much lower. We're -- to date, our deposit beta is in sort of the single-digit range. So we expect that to kind of remain as we go through this rate cycle. But again, it is a faster increase in rates versus in prior rate cycles.

So we could be a little bit higher than that. But again in the context of betas across the nation. I think we're in a pretty good position here in the Hawaii market.

Scott W. H. Seu
President, CEO & Director

And just to add to what you just said, Paul, in terms of most of the pressure coming from the commercial side, of our deposits, our core deposits, 75% are retail, 25% are commercial. So a large part of our base is retail with a little bit less pressure.

Operator

The next question comes from Julien Dumoulin-Smith from Bank of America.

Julien Patrick Dumoulin-Smith
BofA Securities, Research Division

Maybe just coming back to the questions on cost for a moment ago and just talk about the earnings trajectory. I see the 5% figure rolled forward here. Can you talk a little bit about the utility earnings growth and sort of the cadence of that inflation playing itself out? I mean, effectively, let me ask this directly, given the fact that inflation, at least from near-term perspective, seems acute, are we expecting for them to be a linear trajectory to this 5% growth? Or do you think actually the '24 to '25 time frame to see something of an uptick as you deal with and effectively absorb some of these inflationary items as well as some of the commentary you made on CapEx in the remarks as well.

Paul K. Ito
Executive VP, Controller, Treasurer & CFO

Yes, I can start, and then I can ask Dane to kind of jump in here. But in terms of the inflationary question, we do expect that to moderate over time. So that has been built into our forecast. I would say that because of the inflationary adjustment we received in 2022 versus what actually happened, there is a little bit of a leakage, if you will, where we do have some catch-up. So that's part of kind of our forecast, right?

Because the ARA was at 2.78%, I believe, in the inflation that we actually realized was higher than that. And so again, going forward, though, we expect to manage within the ARA, and we expect to catch up over time. With respect to your question on linear growth, I do believe we're expecting a relatively consistent growth as opposed to variations between the years. Again, because under the PBR framework, right, it provides more predictability and stability. And so we're forecasting kind of the ARA inflationary adjustment to sort of normalize as we go out here. And then it's just matter of then planning our work and our O&M to be within that level. So the growth would be a little bit more in the linear.

Now having said that, I think where there could be earnings that may not as be as linear would be EPRM because that's really based on when we file the applications when we start work, et cetera. Dane, do you have any to add to that?

Dane A. Teruya
Executive VP & Chief Financial Officer

No, I would echo what Paul said because if you look at our CapEx trajectories there, we do have some projects that are awaiting PUC approval under the EPRM mechanism. And the timing of those projects are slowly coming in, in the 2023 and 2024 period. So I mean, there is a slight opportunity there. But as Paul mentioned in his prepared comments, for those projects that are awaiting EPRM recovery, 40% of those projects -- 40% of those costs are within this '23 to '25 forecast period. But a large part of those expenses and the completion of those projects are expected in the sort of back-ended part of this forecast.

Julien Patrick Dumoulin-Smith
BofA Securities, Research Division

Got it. So if I'm hearing you, there's maybe some degree of upside as you see these programs play themselves out. But perhaps just as you look at the outlook for as much as this, perhaps a near-term impact or a pressure point on O&M, you're managing this to have a more linear trajectory?

Scott W. H. Seu

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President, CEO & Director

Yes, that's right, Julien.

Julien Patrick Dumoulin-Smith
BofA Securities, Research Division

All right. Fair enough. Excellent. And actually, how does that fit with just a regulatory recovery timeline? If you can speak to that just quickly through the '25 timeline in terms of managing these pressures.

Scott W. H. Seu
President, CEO & Director

Sorry, Julien, you're asking for how is our outlook in terms of regulatory lags or is there anything you...

Julien Patrick Dumoulin-Smith
BofA Securities, Research Division

Yes. Just how do you think about this aligning against your regulatory lag expectations? Obviously, there's some degree of under earning there and not obviously it [generates] by the year. Can you talk a little bit about how that fits against this inflation narrative in terms of managing the pain points and keeping it linear through the forecast?

Scott W. H. Seu
President, CEO & Director

Well, I'll speak generally, just to begin with and Paul, if you want to jump in or Dane. But I think one of the nice things about the PBR regulatory framework is that it actually has removed a lot of the regulatory lag because effective January 1, that's when the new ARA, the adjustment kicked in for us. So we are seeing higher revenues provided by that ARA adjustment, the net 3.68%. So what, at least on our core CapEx and core O&M spend, that gives us the line of sight so that we can manage within that going forward. And then with respect to the larger projects, whether they're MPIR or EPRM projects. Again, those are large -- typically large projects that we plan accordingly, and we will reduce the risk by not making major commitments until we actually have the commission's approval.

Operator

Thank you. There are currently no additional questions registered at this time. So I would like to pass the conference back over to the management team for closing remarks.

Mateo Garcia

Thank you for joining us, everyone. Have a good rest of your day.

Scott W. H. Seu
President, CEO & Director

Thank you, everyone.

Operator
That concludes the conference call. Thank you for your participation. You may now disconnect your line.

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