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Hawaiian Electric Industries, Inc. NYSE:HE

FQ2 2023 Earnings Call Transcripts

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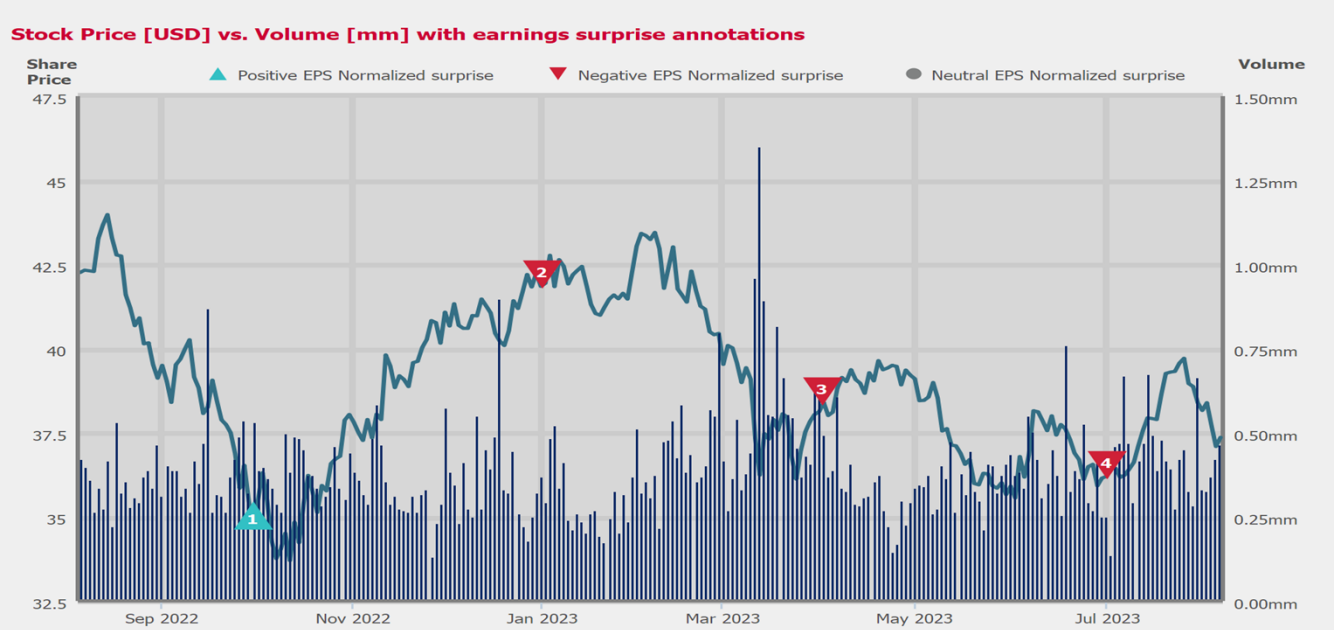
S&P Global Market Intelligence Estimates

	-FQ2 2023-			-FQ3 2023-	-FY 2023-	-FY 2024-
	CONSENSUS	ACTUAL	SURPRISE	CONSENSUS	CONSENSUS	CONSENSUS
EPS Normalized	0.55	0.50	▼ (9.09 %)	0.66	2.20	NA
Revenue (mm)	748.54	895.68	▲ 19.66	790.40	3493.78	NA

Currency: USD
Consensus as of Jul-31-2023 1:45 PM GMT



- EPS NORMALIZED -

	CONSENSUS	ACTUAL	SURPRISE
FQ3 2022	0.54	0.57	▲1 5.56 %
FQ4 2022	0.55	0.52	▼2 (5.45 %)
FQ1 2023	0.53	0.50	▼3 (5.66 %)
FQ2 2023	0.55	0.50	▼4 (9.09 %)

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Presentation

Operator

Good afternoon, and thank you for attending today's second quarter 2023 Hawaiian Industries Inc. Earnings Conference Call. My name is Jason, and I'll be the moderator for today's call. [Operator Instructions]

I would now like to pass the conference over to our host, Mateo Garcia.

Mateo Garcia
Director of Investor Relations

Thank you, Jason. Welcome, everyone, to HEI's Second Quarter 2023 Earnings Call. Joining me today are Scott Seu, HEI President and CEO; Paul Ito, HEI's CFO; and Shelee Kimura, Hawaiian Electric President and CEO; and 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

[Foreign Language] Greetings, everyone. Thank you for joining us today. I'll give an overview of our results, update you on our businesses and the whole economy and then turn the call over to Paul to further discuss our financial results and guidance.

Our combination of businesses continued to work well for us in the second quarter, as it has through many different business cycles and economic environments. Both operating companies delivered solid results in the quarter, and HEI generated net income of $54.6 million and earnings per share of $0.50, compared to $52.5 million and $0.48 in the same quarter last year. Despite the headwinds the bank sector has seen this year, ASB's low-risk community banking model and the utility's execution within our new performance-based regulation, or PBR framework, both contributed to our earnings this quarter.

Our utility grew net income to $45.3 million. And although there were elevated operations and maintenance expenses during the quarter, we expect this to moderate in the second half of the year, with full year expenses expected to be within annual revenue adjustment or ARA allowed levels. The utility has executed well on its capital plan this year, ensuring the reliability and resilience of our system as we continue to aggressively pursue our clean energy transition.

The PBR framework continues to work well for us and we've been pleased with the improved visibility and predictability the framework provides. Our bank grew net income to $20.2 million this quarter, despite industry-wide funding cost pressures impacting banking sector profitability. ASB's net interest margin compression in the quarter was relatively small, compared to peers and are primarily insured and mostly retail deposit base remained stable. Credit quality remains excellent, supported by the continued stability of Hawaii's economy.

Overall, our bank remains very well positioned to continue delivering value to our enterprise. I'm proud to say that ASB was recently named to Forbes, America's best in-state banks list, the only bank in Hawaii to receive this prestigious recognition this year.

In addition, we recently received credit ratings upgrades at both the utility and HEI from Fitch. The upgrades were based on our utilities more predictable regulatory construct under PBR, management's ability to manage near-term renewable targets and the bank's role as a low-risk, well-run institution providing stable dividends over time. Fitch also reaffirmed ASB's BBB rating with an outlook of stable. While ASB has been successful in maintaining deposit levels, we've seen a continuing shift to higher cost funding sources that is expected to persist for the remainder of the year.

Last quarter, we mentioned that we'd revisit bank guidance this quarter given some of the trends we thought were likely to play out. And as a result of continued funding cost pressures, we're revising guidance for the bank, which Paul will cover in more detail.

Turning to the utility. We continue to advance our decarbonization initiatives, while improving reliability, resilience and affordability for our customers. Affordability has improved significantly since last year with the average residential customer bill on Oahu down

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17% from last year's peak in September. In late May, we filed our final Integrated Grid Plan, or IGP, which proposes a clear path forward to meeting our state's clean energy goals, while prioritizing reliability and affordability.

The proposed plan would require significant investment in our transmission and distribution systems as well as new firm and variable renewable generation. Our IGP is the result of industry-leading planning and analysis for renewables powered and highly distributed energy-reliant grid.

The plan is the culmination of a robust stakeholder engagement effort over 5 years, and includes a stakeholder-driven governance structure focused on technical, market and social aspects. Our IGP is crucial to achieving our state's clean energy goals of net-zero carbon emissions and 100% renewables by 2045.

The utility is on track with milestones for the Stage 3 renewable energy request for proposals, or RFP. For the Oahu, Hawaii Island and variable generation portion of Maui RFPs, the utility is currently evaluating best in final offers from the selected priority list and will announce the selection of the final award group in late October. Proposals for the firm generation portion of the Maui RFP are due on August 17, 2023. The utility is bidding into the RFP, consistent with the reliability requirements under the competitive bid framework.

The utility has submitted its best and final offer to provide firm renewable generation by repowering the Waiau power plant on Oahu. The proposed project would replace 6 aging fossil fuel-powered steam generators with smaller, more efficient and fuel flexible units. The proposed new units can provide firm renewable generation to back up the expanding portfolio of variable resources on Oahu's grid. The project has advanced to the selected priority list.

My last highlight is that we're ahead of schedule on our system-wide smart meter deployment. We now have 285,000 smart meters deployed, serving about 60% of our customers. Advanced meters provide data and tools that help us operate our grid more efficiently, reliably and affordably. They'll help us get distributed energy resources, or DER, connected to our system faster, contribute to our efforts to achieve the DER interconnection performance incentive mechanism or PIM and enable time-of-use rates, which are currently in a pilot phase and will further contribute to customer affordability.

Turning to the bank on Slide 4. ASB continues to be well positioned compared to peers, despite the headwinds the sector has seen this year. We're performing well in a local banking market characterized by stability and customer loyalty. Our depositor base remained strong and stable, and 86% of deposits are FDIC insured or fully collateralized. Total deposits at the end of the second quarter were essentially flat, compared to deposits at year-end, down a modest 8 basis points. ASB remains a consistent contributor to earnings and cash flow. And during the quarter paid HEI $11 million of dividends.

We continue to see positive trends in credit quality, evidence of the stability of our economy and financial health of our borrowers. Our high-quality loan book, most of which is Hawaii real estate secured, saw a continuation of low delinquency rates and net charge-offs this quarter. ASB's capital position remains very strong with excess liquidity of approximately 3x the amount of uninsured or uncollateralized deposits.

Turning to Slide 5. Key indicators continue to point to a healthy Hawaii economy. The University of Hawaii Economic Research Organization, which provides regular forecasts of our state's economy, is projecting growth in Hawaii in 2023, driven by continued strength in tourism despite the delayed Japanese market recovery and strong public sector construction spending. Hawaii's labor market has continued to strengthen throughout the year. Our state's unemployment rate was 3.0% in June, an improvement from 3.1% in May and lower than the national average of 3.6%.

Visitor arrivals have been hovering near pre-pandemic levels throughout 2023. In June, over 889,000 visitors arrived in Hawaii, an increase of 5.5% from last year and reaching 94% of June 2019 levels. International arrivals were up over 60%, compared to June of last year and have nearly doubled year-to-date. Visitor spending remains robust and year-to-date June expenditures were up 17% compared to last year.

Hawaii's supply-constrained housing market continues to see prices near record levels. And while sales volumes have been lower this year, given high mortgage rates, Oahu's median prices are still over $1 million. Hawaii's housing market is a key focus of our state's policymakers. And in July, Governor Green signed an emergency proclamation on housing. The proclamation aims to streamline the development process and empower developers and stakeholders to contribute to the creation of more housing opportunities across our state.

I'll now hand the call over to Paul to further discuss our financial results and outlook.

Paul K. Ito

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Executive VP, Treasurer & CFO

Thank you, Scott. I'll start with our results for the quarter on Slide 6. We Consolidated net income of $54.6 million and EPS of $0.50, were up from $52.5 million and EPS of $0.48 last year. The utility grew net income despite elevated O&M expenses during the quarter, some of which were due to timing. The bank grew net income amid a challenging interest rate environment that has pressured net interest margins across the industry.

Our consolidated last 12 months ROE remains healthy at 10.2%, which is down slightly from 10.4% last year due primarily to higher last 12-month earnings in the prior year due to a gain on sale recognized in the first quarter of 2022. Utility ROE remained stable at 8.2% and bank ROE on an annualized basis was up 400 basis points compared to the same quarter last year.

On Slide 7, we show major variances across the enterprise, compared to the second quarter of last year. Higher bank net income was primarily due to higher noninterest income from higher bank-owned life insurance income, a gain on sale of real estate and higher fee income as well as a lower provision for credit losses and higher net interest income, primarily due to higher interest and fees on loans. These impacts were partially offset by higher noninterest expense, primarily due to higher compensation and benefits expenses and FDIC insurance premiums.

On the utility side, we saw higher ARA and MPIR revenues, higher fossil fuel cost risk-sharing revenues, higher AFUDC from increased CapEx and higher revenues from a onetime true-up of billable costs related to our poll infrastructure. These are partially offset by higher O&M, primarily due to higher transmission and distribution expenses, higher outside services costs, increased labor and employee benefit costs, higher facilities expenses and higher legal and other fees associated with environmental matters, partially offset by fewer overhauls performed in the quarter. The higher holding company and other segment net loss was primarily due to higher interest expense.

Turning to Slide 8. Year-to-date, Utility CapEx was $225 million, about $100 million higher than at the same time last year. The utility is on track with the execution of their capital plan with steps taken to mitigate supply chain challenges, including advanced planning for the availability of labor and material resources. For the full year, we expect to be in the top half of our $370 million to $410 million CapEx guidance range.

On Slide 9, we show utility earnings drivers for the remainder of the year. The utility saw elevated O&M expenses in the second quarter. However, there were approximately $2 million of elevated expenses due to timing, and we expect O&M to moderate in the second half of the year. The timing-related expenses included vegetation management and generating station maintenance work that was accelerated into the first half of the year in preparation for hurricane season and the fall generation peak. Efficient execution will remain a key area of focus for us for the remainder of the year, and we still expect to manage O&M increases within the 3.68% inflationary adjustment allowed under the ARA.

Performance incentive mechanisms, or PIMs, will also be a key driver of our full year earnings. We still expect total net sales of approximately $4 million, although a different mix of PIMs are contributing to this total than originally forecast. Fuel prices have decreased since the beginning of the year. And during the second quarter, we recognized approximately $1 million of net income from fuel cost risk-sharing mechanism due to our fuel costs being lower than the benchmark, which was set based on our January fuel costs. Lower fuel prices have also contributed to lower customer bills across our items.

We are also expecting a higher interconnection approval award as we improve interconnection times for our DER customers and increased renewable generation. We no longer expect to recognize any rewards from our RPS-A PIM this year as we've seen delays in one of our third-party-owned generators on Hawaii Island in ramping up to full capacity after undergoing repair work as well as delays in ramping up at 2 other renewable projects. However, we expect the higher fuel cost risk-sharing reward and rewards from our interconnection approval PIM to offset the RPS-A PIM reduction.

Turning to the bank. ASB's loyal and long tenure deposit base, along with our conservative approach to lending, underpin our low-risk community banking business model. This model has continued to serve us well this year as we navigated challenges arising from the bank failures and sector liquidity fears that occurred earlier this year. And as we work to manage the industry-wide funding cost pressures caused by the rapid interest rate increases of the last 1.5 years.

As a reminder, the vast majority of our deposits or 85% are from our retail customers. Nearly 50% of our retail customers have been with us for 10 years or longer. We also have strong commercial customer relationships with nearly 40% of our commercial accounts, having a tenure of more than 10 years. The long-term nature of our customer base contributes to our funding stability.

86% of ASP's deposits were FDIC insured or collateralized as of the end of the second quarter, up slightly from 85% at the end of the first quarter. 79% of deposits were FDIC insured equivalent to last quarter. This is a very high level of deposit security for

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our customers and contributes to deposit stability. Total deposits as of quarter end of $8.2 billion were roughly flat, compared to December 31, 2022. Time deposits were up, while core deposits saw a modest decline of 2.8% as we've continued to see a slight uptick in customer spending due to the inflationary environment.

We have not seen any unusual customer behavior as a result of the mainland bank issues experienced earlier this year. However, in addition to higher customer spending, we continue to see some depositors seeking higher-yielding alternatives and we'll continue to mitigate these pressures through cost efficiencies as well as prioritizing bringing in new deposits.

On the asset side of the balance sheet, the very high quality of ASB's loan book is the result of our conservative approach to lending. This has served the bank well as we've started to see a focus on the quality of commercial real estate credits for mainland banks. The quality of our CRE loan portfolio and the quality of our broader loan book remain very strong. Delinquencies, net charge-offs and nonaccrual loan percentages are at low levels. The vast majority of our loan book is backed by real estate, all located within Hawaii, where real estate values are supported by the real estate supply-constrained nature of our Island markets.

Turning to Slide 11. Although higher interest rates have continued to benefit our yield on earning assets, which was up 7 basis points in the second quarter, the higher rates and a shift in funding mix have increased funding costs, which are similarly pressuring net interest margins industry-wide. Our cost of funds still remains relatively low, compared to similarly sized peers but was up 17 basis points to 83 basis points in the second quarter. The increase was due to higher rates and a shift in funding mix to include higher amounts of certificates of deposits and wholesale borrowings as you can see at the bottom left of the slide.

During the quarter, our net interest margin was down 10 basis points to 2.75%. Our NIM compression compares favorably to similarly sized peers and places us in the top quartile of the KRX constituents.

Turning to drivers of bank performance for the rest of the year on Slide 12. Due to the shift in funding mix and higher funding costs we've seen across the industry, we are expecting net interest margin to be lower for the full year than previously anticipated. We are expecting relative stability, compared to our peers, and we've seen this play out so far this year. Our net interest margin guidance, which I'll cover in more detail on the next slide reflects the continued composition shift in our funding mix. Further Fed fund rate increases this year are expected to be immaterial to our guidance due to our balance sheet being interest-sensitive neutral and the limited period left in 2023 that a rate increase would affect.

Our credit outlook remains very positive, and we now expect a lower provision for credit losses than previously anticipated. We are seeing strong credit quality with low net charge-offs and delinquencies. Our credit outlook and our expectations of continued stability in the Hawaii economy have contributed to our expectations of a lower provision now in the 0 to $6 million range for the year. Expense management remains a key focus for ASB as we continue to make critical investments in digital transformation while prudently controlling costs.

Turning to Slide 13. I'll provide a recap of our updated guidance expectations for the remainder of the year. We are reaffirming our utility guidance of $1.75 to $1.85 per share, achieving performance incentive mechanism rewards and controlling O&M expenses remain key areas of focus for management. As mentioned, we expect other PIMs, such as fuel cost risk-sharing and interconnection approval, to offset our lower expectations for RPS-A rewards. The utility's liquidity remains strong, having proactively addressed all near-term financing needs early in the year.

Turning to the bank's outlook for the remainder of the year. Higher short-term interest rates and a challenging deposit environment continued to create margin pressures across the sector. Although our net interest margin has fared well relative to peers in the current environment, we now expect net interest margin for the year to be 2.7% to 2.8%, versus our previous expectation of 2.8% to 2.9%. Given continuing stable credit trends, we are forecasting a lower provision for credit losses at 0 to $6 million versus $0 to $10 million previously. Still assume low single-digit loan growth for the year.

Last quarter, we indicated that we would revisit bank EPS guidance this quarter given uncertainty and macro trends. Due to continued funding cost pressures and the resulting impact on net interest margin, we now expect bank EPS to be $0.62 to $0.66 down from our previous expectation of $0.75 to $0.85. Our guidance assumes a continued gradual funding mix share for the balance of the year. The bank has managed noninterest expense increases within our guidance this year, and we expect this to continue as we proceed through the second half of the year.

Due to the lower-than-anticipated Pacific Current performance, we expect holding company and other segment net losses of $0.37 to $0.39 per share, compared to our previous expectation of $0.34 to $0.36 per share. We still do not anticipate any equity issuances for 2023. Based on the combined forecast for the segments, consolidated EPS is expected to be in the range of $2 and $2.10, down from $2.15 to $2.35 previously. Although our updated forecast reflects some near-term bank headwinds resulting from an unusually rapid rise in interest rates and its related impacts, the bank performed well overall in the second quarter.

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I'll now turn it back over to Scott, who will provide closing remarks.

Scott W. H. Seu
President, CEO & Director

[Foreign Language] Paul and [Foreign Language] to all of you for joining us today. In summary, HEI delivered solid performance in the second quarter, growing net income at both the utility and bank, despite the macro challenges that face the broader banking sector. The utility is executing well under performance-based regulation, and we continue to make progress on our clean energy transition.

ASB's conservative business model, with our mostly retail and largely insured deposit base, has proven its stability through different business and interest rate cycles, consistently contributing earnings and dividends that reduce HEI's need to issue equity. Our management team is laser-focused on execution and efficiency, and our combination of businesses continues to serve HEI's shareholders well.
With that, let's open up the call for questions.

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Question and Answer

Operator

[Operator Instructions] Our first question is from Julien Dumoulin-Smith with Bank of America.

Julien Patrick Dumoulin-Smith
BofA Securities, Research Division

Can you guys hear me, okay?

Scott W. H. Seu
President, CEO & Director

Absolutely.

Julien Patrick Dumoulin-Smith
BofA Securities, Research Division

Just picking up on the bank side here real quickly here. I mean, obviously, you saw the revisions that you just mentioned in the remarks,how do you think about growth here year-over-year into '24? What are going to be the puts and takes? Do you think that we sort of rebaseline at this point? Or how do you think about the moving pieces here within the guidance and the sort of incremental trends from here as you annualize at this level?

Paul K. Ito
Executive VP, Treasurer & CFO

Yes, Julien, thanks for the question. So in terms of year-over-year growth, I think we're starting our planning process, and we won't have sort of the outlook for '24 until later in the year. And then, of course, we'll give our guidance in the first quarter of next year. But the factors that would drive what happens next year are some of the things that we're seeing now, right?

So in terms of interest rates, where they head from here and when the Fed starts to reduce those rates, loan growth, of course, would be a factor for next year as well. As we messaged for this -- for the balance of the year, we do expect loan growth to be in the single -- mid-single digits, low single digits. As higher interest rates have sort of reduced borrow interest in taking out loans. And of course, on the mortgage side, it's also -- has led to lower activity.

The other thing is deposit mix shift is an important factor in terms of driving our margin as we've messaged right, for the balance of this year, we are seeing sort of a gradual mix shift continuing and we've built that into our guidance. To the extent those trends change, that obviously will affect our earnings. So I would say, and then, of course, noninterest expense is the other factor for drivers. And over the long term, we expect to manage our expenses sort of low mid-single digits.

So those are various factors that would drive next year. But in terms of talking about this year, I think we've given our guidance. So we feel like, although we can't call any certain we can't -- we're not seeing in terms of the trends in terms of deposit growth -- I'm sorry, deposit mix. We built that into our 2.70% to 2.80% NIM guidance there.

Scott W. H. Seu
President, CEO & Director

Julien, this is Scott. Yes, I'm just going to add to what Paul said. Of course, I'm thinking about this from an enterprise-wide perspective, and of course, the whole banking sector this year has been under some -- has seen some challenges as we said in some of our remarks. What we expect to see through the remainder of the year for the bank is impacts those challenges, moderating performance starting to get better.

And then, of course, the rest of the enterprise, the utility will continue to see pretty stable growth as we projected there. So overall, working through 2023. I think the utility and the bank combination continues to serve us pretty well sort of points to the value of having the combination.

Julien Patrick Dumoulin-Smith
BofA Securities, Research Division

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Right. But you're comfortable that you would annualize still at this level of the reduced NIM here, the 2.7% to 2.8%? I know that obviously, that's what you incrementally brought down here quarter-over-quarter. But I just want to get some degree of confidence in that new level here, if you will?

Scott W. H. Seu
President, CEO & Director

Yes, we are -- yes, Julien, we're confident that that's the range that we're putting out there. That takes into effect -- it takes into account what we see in terms of the market here in Hawaii and the trends.

Julien Patrick Dumoulin-Smith
BofA Securities, Research Division

All right. Fair enough. And then I want to come back to the procurement avenues. I know that there's 2 separate avenues there. And you also alluded to in your comments that there are some wires investments potentially as well. Can you give us a sense of the scale of opportunity represented here? I mean, obviously, there's megawatts released here as well. But as you think about -- especially the T&D side of that, right, whether or not you're awarded some of these projects, how do you think about that wire side in both Maui and Oahu, if you can speak to it? And presumably, those announcements will be made simultaneously for the wires and the generation in late October?

Scott W. H. Seu
President, CEO & Director

Well, just to clarify a bit, Julien, the announcement will be for the final award group for the generation. I mean this is a renewable generation RFP. The investment -- the added investment down the road in the transmission and distribution system would come about partly to support these new renewable generation projects that would be brought online, but then also just continued investment in modernization as we see more distributed energy resources and the like.

I think in our -- I referenced our IGP plan and that's where I made reference to this additional T&D investment. Most of that would probably come in post 2025, because that would be aligned with the timing of a lot of these new resources coming online.

Julien Patrick Dumoulin-Smith
BofA Securities, Research Division

Got it. Any indications on scale? I mean, obviously, you said you'd be in the top half here of the overall CapEx range for the current year and maybe call it $410 million, but any sense of what that could do as you think about scaling into that post '25 period? And then obviously, difficult to say necessarily early on in the RFP process -- but any commentary about what that's kind of the range of opportunities that could emerge?

Paul K. Ito
Executive VP, Treasurer & CFO

So Julien, in terms of the IGP plan, we do have the final draft of filed. And in that plan, we do put out some forecast of what that investment could be. And obviously, a lot could change until those plans are finalized. But in terms of building out the renewable energy zone infrastructure, it is a pretty significant investment. I think we do have -- post 2025, as Scott mentioned, some numbers in the IGP. There's a portion of about $60 million, and then there's a larger portion that's very, very significant, over $1 billion, but that's over a long period of time.

So those are the sort of the numbers, again, very preliminary until we have these plans developed in more detail. That's the guidance that we can give. It's a long-term investment opportunity for us going forward.

Shelee M. T. Kimura
President, CEO & Director

And I'll just add, Julien. This is Shelee Kimura. I'll just add that those numbers that Paul provided of $60 million and over $1 billion, that would happen after 2025 through 2035. And on the generation side, because we're in a competitive procurement process right now, we're not going to be discussing any more details on the scale or amount of the bids that we either already put in for the or the bid that we will be putting in for the Maui RFP.

Julien Patrick Dumoulin-Smith
BofA Securities, Research Division

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Yes. No, I understand. It's difficult to speak to you exactly today. Is it fair to assume that next quarter, we'll get a formal update post the awards here on what that would translate to in dollars and timing?

Shelee M. T. Kimura
President, CEO & Director

Yes. So for the Oahu RFP, the results will come out in October. So we would be able to talk about that at that time. For the Maui RFP, we won't have the results at that point.

Operator

Our next question is from Paul Patterson with Glenrock Associates.

Paul Patterson
Glenrock Associates LLC

So just a couple of items on the bank here. The -- It sounds to me that, if I heard it correctly, and I apologize if I did it, that you guys are seeing more competition from customers looking for higher interest rates than you were previously in the last quarter. Is that correct?

Paul K. Ito
Executive VP, Treasurer & CFO

No, Paul. I think what we're seeing is compared to our previous forecast. So obviously, the interest rate forecast is higher than we had previously anticipated. So that's one driver. We are seeing a mix shift and we actually did a little bit or we dug down in terms of deposit changes and what we're seeing there for the first half of the year. And what we saw was probably a majority, what we're seeing is a lot more deposits coming in, but also a lot more deposits going out. So there's a net-net outflow related to consumer spending. So in other words, depositors spending more on sort of daily living expenses because of the higher inflationary environment.

Now we did -- we are seeing some migration to higher-yielding alternatives in the data, and we expect that to continue if the rate environment stays elevated. But in terms of your question on competition, I think in the local Hawaii banking market, what we're seeing is all banks are competing on CDs. And as we've mentioned before, right, this is new money that in order to take advantage of the higher rates, it requires a certain level of new money coming into the bank. And so that's where we are seeing a little bit more competition.

Scott W. H. Seu
President, CEO & Director

Yes. And Paul, the other thing I'd say is that I don't think this was unexpected given the higher interest rate environment, right? I mean all the banks are competing. We are starting to see a little bit of shift from core deposits to the time-based CDs. And that's -- I think that was anticipated. Our overall total cost of funds still remains very attractive compared to our peers.

Paul Patterson
Glenrock Associates LLC

And I apologize for not speaking more clearly. I guess when I was talking about competition, I meant from all sources, from Treasury Direct to online banking, what have you, not just the Hawaiian market. And I guess what I'm wondering, I guess, in this context is, I guess, back to Julian's question, this net interest margin, I'm wondering whether or not there's a risk of further deterioration given the interest rate environment. And just the rollover as we go into quarter after quarter going into 2024, if you follow what I'm saying?

Scott W. H. Seu
President, CEO & Director

Yes, Paul, I'm going to ask Ann Teranishi our Bank President, to comment a little bit on that. I think in general, though, what we're starting to see is a moderation of impacts on NIM, but maybe, Ann, you can expand.

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

Yes. I think, Paul, to answer your initial question about are we seeing increased competition? I think the competition has been there and hasn't changed quarter-over-quarter. And we have been quite successful in the second quarter with some of our CD campaigns and had great success in bringing in new retail deposit money, some from existing customers, some from new customers as well as being

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able to expand our commercial deposit base as well. So we're feeling that the revised NIM is appropriate and tracking to what we're seeing -- what we've seen in the first 6 months as well as what we're preliminarily seeing in the second half as well.

Paul Patterson
Glenrock Associates LLC

I guess. But what Julien was asking but I believe was the annualized rate, and I think he was suggesting from the annualized rate starting now and the new net interest margin. And I guess to be clear about this, how do you see the net interest margin for the next 12 months, I guess, is what I'm saying. Or for the next 6 months, how about that? Would it just be the -- if we average it out, we could be reverse engineered, I guess, basically looking at what you guys had 4 months ago and what it is now? Or how should we think about that?

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

Yes. So the NIM guidance is for the full 2023, and we're not really able to comment as to 2024. The cost of funds is creating some pressure on the NIM, and we're just managing that, being very surgical in how we apply pricing as well we originate new loans, how we're structuring and how we're pricing loans. So that's all being very carefully managed.

Scott W. H. Seu
President, CEO & Director

Yes. And Paul, I think I'm trying to be clear on my answer here. So the 2.70% to 2.80% range is for the full year 2023, right? Our Q1 was 2.85%. Q2 was 2.75%. And as we project them throughout the remainder of the year, that's where we are estimating the full 2.70% to 2.80%. And that is our range. That's our -- we're fairly confident in that.

Operator

Our next question is from Jonathan Reeder with Wells Fargo.

Jonathan Garrett Reeder
Wells Fargo Securities, LLC, Research Division

Can you guys hear me okay?

Scott W. H. Seu
President, CEO & Director

Yes, Jonathan.

Jonathan Garrett Reeder
Wells Fargo Securities, LLC, Research Division

Good. I guess I might as well continue with a bank question. But I guess, for us, utility dedicated folks like what can you do to limit or even eliminate the higher wholesale funding? Like it seems like that's something that's more controllable on your end to some degree.

Paul K. Ito
Executive VP, Treasurer & CFO

Yes, Jonathan, in terms of the wholesale funding, what drives whether we can pay that down is really deposit trends or deposit growth. In this current environment, right, we're seeing deposits relatively flat. And so being able to pay down those -- that wholesale fund is we're not expecting that for the balance of the year. The other thing that drives that is sort of pay down off of the investment portfolio and our loan portfolio, the cash flow from that. But the other offsetting factor is loan growth, right?

So we have to sort of balance all those 3 things in terms of loan growth, deposit growth and then determine is there excess cash flow? And if there's excess cash flow, we would pay down the highest cost funding sources first. But specific to wholesale funding, we're not expecting a significant -- or we're not expecting to pay that higher cost of funding down any meaningful amount for this year.

Jonathan Garrett Reeder
Wells Fargo Securities, LLC, Research Division

So I mean, in your opinion, it's still worth having, I guess, that wholesale funding balance out there if that -- in order to, I guess, grow your loan book still like that's a trade-off that still is worth it versus just saying let's keep the loans flat versus low single-digit growth?

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Paul K. Ito
Executive VP, Treasurer & CFO

Yes. I think -- I mean, yes, just given the current interest rate environment that we're in, the fact that loans are pricing or being issued at higher rates, but our funding is also at a higher rate. So it is a little bit not accretive to NIM, but accretive to NII.

Scott W. H. Seu
President, CEO & Director

Yes. And the other thing, Jonathan, is we are being very careful in terms of the loans that we're issuing. We recognize that there is still a need by our customers for funding. But at the same time, we're being fairly selective in the loan book in terms of how we're growing it because again, balancing all these different factors.

Jonathan Garrett Reeder
Wells Fargo Securities, LLC, Research Division

Sure. Okay. That makes sense. I kind of missed it, but what was driving the revision in the Hold Co. drag, was that just higher interest expense at parent?

Paul K. Ito
Executive VP, Treasurer & CFO

No, this was related to Pacific Current. We're expecting a little bit lower performance this year at one of their projects, there were some equipment issues that continued resulting in the plant being down for a little bit of time. That's largely been resolved. So -- but in effect for the full year, we're expecting a little bit lower or higher net loss related to that.

Jonathan Garrett Reeder
Wells Fargo Securities, LLC, Research Division

Okay. So that should hopefully be something that, I guess, bounces back in '24, not having that outage?

Paul K. Ito
Executive VP, Treasurer & CFO

Yes, correct.

Jonathan Garrett Reeder
Wells Fargo Securities, LLC, Research Division

And then last for me, following up on Julian's question on the IGP. Is that something that like the commission actually approves and like sets a definitive road map for you to follow an approval process to move forward with the Capex? And then if so, what's the HPUC's time line for approving that IGP?

Shelee M. T. Kimura
President, CEO & Director

This is Shelee. So the IGP was filed or waiting for PUC approval, our next steps are to file the RFP that builds off of the IGP, we plan to file a draft in September. And our hope is that we can issue the final RFP in March of 2024.

With respect to your question about the T&D investments longer term, that would require a separate filing to request approval for that kind of program, but it would be based in the broader master plan of the IGP.

Jonathan Garrett Reeder
Wells Fargo Securities, LLC, Research Division

So the commission does give their blessing to the IGP, but you just have these other ways of actually, I guess, definitively moving forward projects and maybe setting costs?

Shelee M. T. Kimura
President, CEO & Director

Yes, that's right. And I'd also like to add that just a reminder, under PBR, we have our cost recovery. So there is some level of CapEx that's already built into the PBR and we get the inflationary increases each year.

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Operator

Our next question is from Ashar Khan with Verition Fund.

Ashar Khan
Verition Fund Management LLC

Can I just ask a question? So the bank earnings are now expected to be down $0.14 from quarter 1 guidance. Can you break it down? How much is it NIM related? How much of it is ROE related? Or what are the factors? Could you help us to -- then to break down the drop in guidance? What are the factors, which lead to the $0.14?

Paul K. Ito
Executive VP, Treasurer & CFO

Yes. Really, the driver is essentially the NIM, right? So because of the mix shift and higher interest rate environment, that significantly increased our interest expense that we were previously forecasting. And so that resulted in a large compression in our NII. Again, given our first quarter forecast, we weren't expecting as much of a mix shift and were expecting deposit -- total deposits to be flat to modestly up, whereas now our guidance incorporates continued mix shift for the balance of the year.

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

Yes. And I'd just like to add, too. So I think banks are all experiencing the similar cost of fund pressure. And I just want to highlight, though, with the change in our NIM guidance. We've been managing it while our NIM compression quarter-over-quarter was just 10 basis, the average for peers is more like [20]. So I think we're trying to be pretty upfront in what we think the impact will be on cost of funds for the remainder of the year. But just know that we're managing it very closely with our deposit pricing and managing that shift in deposits.

Ashar Khan
Verition Fund Management LLC

So can I just assume that like if I'm right, right, the NIM went down by about 10 basis points assumption between the 2 quarters. So the 10 basis points is equivalent to $0.14. Is that the right sensitivity?

Paul K. Ito
Executive VP, Treasurer & CFO

Yes. So in terms of -- so I'm thinking about total funding costs, right? There are different sometimes banks talk about their core funding costs. We generally refer to our total funding cost and our total funding costs for the quarter was a 17 basis point change.

In terms of the full year, we haven't, I guess, given the guidance of what that change will be. But I think you can maybe take it from our NIM guidance in the first quarter versus our new guidance. So essentially moving down from 2.80% to 2.90% down to 2.70% to 2.80%. But -- I mean, that would be the -- in terms of the drivers is really the NIM. So if your question is whether you can assume that, I mean, I think what you have to do is look at our earning assets and then take the change in the NIM, and that would be sort of what you could expect.

Ashar Khan
Verition Fund Management LLC

Okay, fair enough. Yes. I'm just trying to see if there is further NIM pressure, what would be the impact on earnings and whether this 10 basis points equals to $0.14 is a good benchmark to use the -- if one is to go up or down as things play out this year or next year.

Paul K. Ito
Executive VP, Treasurer & CFO

Again, I think you -- go ahead.

Ashar Khan
Verition Fund Management LLC

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And my final question is, so I see your cash flow slides have not changed. So can I ask you -- so we are losing about $14 million or $15 million in earnings after tax. So where is that -- how is that being absorbed as the cash flow is exactly the same as in quarter 1. So what is coming in to replace that lost earnings in your cash flow projections for the year?

Paul K. Ito
Executive VP, Treasurer & CFO

Yes, Ashar. I assume you're talking about the cash flow dividends from the bank to the holding company. And that -- the way we size the dividend to the holding company is based on the bank's Tier 1 leverage ratio and the Tier 1 leverage ratio is affected by earnings to some extent, but also balance sheet size growth or contraction of the balance sheet also has an impact. So based on our outlook, even though earnings have come down, but based on our outlook for Tier 1 leverage, we're still able to manage the dividend that we set earlier in the year.

Ashar Khan
Verition Fund Management LLC

Okay. So can I just follow up to that is what is the maximum that you can dividend out of the bank to manage that Tier 1? What is -- can I just have that information? What is -- what -- at the tier that you are, what is the maximum dividend that you can get out from the bank?

Paul K. Ito
Executive VP, Treasurer & CFO

So we manage our Tier 1 leverage ratio to be between 7.5% to 8%. In terms of the maximum weaker dividend, I don't have that exact number in front of me. I think in our 10-K, we sort of touch on the amount of dividends that our subsidiaries are restricted from not able to be dividend up to the holding company. But at the end of the quarter, we were at 7.79% for our Tier 1 leverage ratio.

Ashar Khan
Verition Fund Management LLC

And you can go down to 7.5%, you said the range was to 7.5% to 8%, right? -- correct? Am I right?

Paul K. Ito
Executive VP, Treasurer & CFO

Technically, but I think we like to manage our Tier 1 leverage ratio conservatively. So we wouldn't necessarily make a decision to dividend the maximum amount to get down to 7.5%. But we generally try to stay within that 7.5% to 8% range.

Operator

There are no more questions. So I'll pass the call back over to Scott Seu for closing remarks.

Scott W. H. Seu
President, CEO & Director

So I just want to thank everybody again for joining us today. We look forward to another quarter of solid results, supported by our stability of the efficiency and reliable performance at our companies. So thank you, everybody.

Operator

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

Scott W. H. Seu
President, CEO & Director
So thank you, everybody.

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