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PRESENTATION

Operator

Good day, and welcome to the Flagstar Bank Fourth Quarter 2018 Earnings Call. Today's conference is being recorded.

At this time, I would like to turn the conference over to David Urban, Director of Investor Relations. Please go ahead.

David L. Urban - *Flagstar Bancorp, Inc. - Senior VP & Director of IR*

Thank you, Katie, and good morning. Welcome to Flagstar's fourth quarter 2018 earnings call. Before we begin, I would like to mention that of our fourth quarter earnings release and presentation are available on our website at flagstar.com.

I would also like to remind you that any forward-looking statements made during today's call are subject to risks and uncertainties. Factors that could materially change our current forward-looking assumptions are described on Slide 2 of today's presentation, in our press release and in our 2017 Form 10-K and subsequent reports on file with the SEC.

We are also discussing GAAP and non-GAAP financial measures, which are described in our earnings release and in the presentation we made available for this earnings call. You should refer to these documents as part of this call.

With that, I'd like to now turn the call over to Sandro DiNello, our President and Chief Executive Officer.

Alessandro P. DiNello - *Flagstar Bancorp, Inc. - President, CEO & Director*

Thank you, Dave, and thank you, everyone, for joining us today. In addition to Dave, I am joined this morning by Jim Ciroli, our Chief Financial Officer; Lee Smith, our Chief Operating Officer; Kristy Fercho, our President of Mortgage; Drew Ottaway, our President of Banking; and Steve Figliuolo, our Chief Risk Officer.

As usual, I'm going to start the call by providing a high-level view of our performance for the quarter, then I'll turn the call over to Jim for details on our financial results. Lee will follow with a review of our business segments and strategic initiatives, and I'll conclude with guidance for the first quarter before opening up the line for questions.

On December 31, we closed the books on a good quarter and a good year. For the quarter, we posted adjusted net income of $42 million or $0.72 per diluted share, up 20% from the adjusted results in the same quarter last year. For the full year, we achieved adjusted net income of $176 million or $3.02 per diluted share, topping our adjusted result for the full year 2017 by 23%. The adjustments for the quarter were attributable to 2 items. First, hedging gains; and second, expenses relating to the Wells Fargo branch acquisition.

Take away that noise and we have solid operating earnings where we proved, once again, as we have throughout 2018 that we can grow earnings in a challenging mortgage environment because we have built a stronger, more diversified franchise. In fact, we delivered an adjusted ROA of 0.91% in the quarter, even though, our mortgage rate lock commitments were the lowest of the year and our gain on sale revenue was the lowest since the early days of the financial crisis.

Part of that diversification was apportioned to commercial and industrial, commercial real estate and consumer lending. Quarter-after-quarter, this year, we have registered a solid contribution from these businesses. We have said that we will not compromise on credit to achieve loan growth, and we have backed that up with a track record of no delinquencies in our commercial portfolio. In fact, credit quality has been a standout throughout the year as we saw a downward trend in nonperforming loans in every quarter and a provision benefit in 3 of the 4 quarters.

Should the economy slump, we believe our strong credit discipline will serve us well in the future. Also, in banking, we held the line on deposit cost despite the uptick in short-term rates. And we succeeded in expanding adjusted net interest margin for the third straight quarter. As we have all year, we continue to add accounts to our servicing portfolio. We said last quarter, that we expected to cross that 800,000 account threshold by the end of 2018, and we exceeded that benchmark. Our year-over-year growth in this portfolio was an extraordinary 87%.

I started out saying it was a good quarter, and it was in terms of our performance. But in terms of our positioning for the future, it was a landmark, transformational quarter. We closed on our acquisition of 52 branches from Wells Fargo Bank, which at closing brought in $1.76 billion in deposits, and 170,000 new customers. The transaction reduced our wholesale borrowings and replaced them with much less expensive and less rate-sensitive core deposits, which will boost net interest margin. All that in addition to expanding our market to more people, businesses and geographies. No question, the acquisition was challenging, and it was not the experience we intended for some of our customers. However, I'm immensely proud of the way everyone at Flagstar responded to make things right. Now nearly 2 months after the conversion, although the deposits we purchased at acquisition were lower than expected, post closing attrition is tracking well below the 17% we had modeled, and we are steadily opening new accounts.

That concludes my comments. Now let me turn it over to Jim.

James K. Ciroli - *Flagstar Bancorp, Inc. - Executive VP & CFO*

Thanks, Sandro. Turning to Slide 6. We are pleased with the quarter and our position at the end of 2018. Our adjusted operating net income this quarter was $42 million, $0.72 per share, up 20% from our operating results in the same quarter last year. This growth was consistent with our full year operating earnings growth. These operating results were driven by a stable but stronger level of net interest income adjusted for the outside hedging gain this quarter. Each quarter, as we continue to grow loans and deposits, we stabilize the level of net interest income. This quarter, despite $651 million in lower average balances from loans held for sale and warehouse loans, adjusted net interest income held steady, declining only $1 million. This level of earning assets is supported by a stronger level of deposits from the communities we serve. At year-end, these community deposits, which exclude brokered and custodial deposits, supported 62% of total earning assets, up from 54% at the end of the third quarter.

The result of this balance sheet transformation is that while our mortgage gain on sale revenue came in as low as we've experienced since the fourth quarter of 2008, we were still able to grow net income on a nice pace.

Asset quality continue to be strong as net charge-offs were only 4 basis points, our nonperforming loan ratio improved yet again, and our allowance coverage of the loan portfolio remained at 1.4%, among the strongest in the industry. We're now less than a year away from CECL adoption, and while we're not yet going to discuss its impact on Flagstar, we feel that this coverage level positions us well for whatever that impact might be.

Capital also remained strong after the Wells Fargo branch acquisition. While we await final capital regulations, we find that our total risk-based capital is solidly in our target operating range and our Tier 1 leverage capital is only 7 basis points lower than before the acquisition. I'll take us through a more extensive analysis of our capital later.

So let's turn to Slide 7, and dive deeper into the income statement. Adjusted net interest income was fairly stable as net interest margin expansion largely offset seasonally lower earning assets. The adjusted net interest margin expanded by 6 basis points to 2.99%, reflecting 1 month of the lower cost, Wells Fargo deposits. For the month of December, our adjusted net interest margin was 3.17%, which provides an indication as to where this important metric should be in 2019.

Excluding the impact of the Wells Fargo deposits, our overall cost of deposits rose a modest 7 basis points despite the late third quarter interest rate hike by the Fed for an effective deposit beta of 28%. The impact of the late third quarter increase in short-term rates benefited the yields on interest-earning assets, and we'll discuss earning asset growth on the next slide.

Noninterest income decreased 8% as mortgage revenues fell $12 million. Our gain on sale revenue of $34 million represented a decline of $9 million or 21% in the prior quarter. Return on the mortgage servicing asset also decreased by $3 million. However, loan admin income increased $3 million from last quarter due to significant growth in our sub-servicing business volume, partially offsetting the lower mortgage banking income.

The decrease in gain on sale revenues primarily reflected lower fallout-adjusted locks as a result of seasonal factors. While we've remained fully committed to our multichannel approach to this business, we also remain disciplined in our pricing and have continued to focus on maintaining profitability. As a result, we experienced a higher gain on sales margin, which rose 9 basis points to 60 basis points.

The net return on the mortgage servicing assets decreased $3 million, resulting in a net gain of $10 million this quarter as compared to a net gain of $13 million last quarter. The decrease largely reflected smaller benefit from the collection contingencies related to MSR sales in prior periods.

We remained disciplined on expenses. Operating noninterest expense was $175 million, up $3 million or 2% from the prior quarter and at the low end of our guidance range. This growth reflected the impact of 1 month of operating expenses for the newly-acquired branches. The higher costs were partially offset by lower mortgage expenses.

Finally, now that we're a taxpayer, we've implemented various tax optimization strategies. These strategies are incorporated into this quarter's effective tax rate, which we believe representative of our tax rate going forward. Credit costs were negligible again this quarter. We experienced only 4 basis points in the charge-offs, nonperforming loans were $3 million lower, $22 million or 24 basis points of the portfolio, while the commercial loan portfolio remained clean. As a result of all these positive metrics, we recorded a provision benefit of $5 million.

So let's now turn to Slide 8, which highlights our average balance sheet this quarter. Average loans held for investment grew $44 million even as average warehouse loans seasonally declined by $249 million. All other loan categories experienced modest growth. We continued to portfolio the mortgage loan production that produces nice risk-adjusted returns on equity. Our indirect Marine and RV portfolio averaged $140 million during the quarter, and continue to demonstrate good traction among dealers. And on the commercial side, we continue to grow commercial real estate and C&I loans.

Average deposits increased $606 million or 5% in the quarter driven by the benefit of 1 month of the Wells Fargo branch deposits and higher custodial deposits. Excluding the impact of acquired deposits, average deposits rose $22 million as we experienced a drop in savings deposits yet held this category to only a 16% beta for the quarter, demonstrating the added discipline provided by having the Wells deposits. Average custodial deposits rose $162 million or 8%, driven by a 34% increase in serviced accounts.

At December 31, our capital position remained strong even after the Wells Fargo branch acquisition. The tangible common equity to assets ratio fell only 29 basis points to 7.45%, while our tangible book value per share decreased $1.23 to $23.90. We'll cut the regulatory capital level shortly.

So let's now turn to asset quality on Slide 9. Early-stage delinquencies continue to be negligible. Only $7 million of consumer loans were over 30 days delinquent still accruing at December 31. And we have no commercial loans over 30 days delinquent still accruing and no commercial nonperformers. At December 31, our allowance coverage was 1.4% of the total HFI loans. Coverage remains strong for both consumer and commercial loans.

The commercial loan coverage is even stronger because 29% of that portfolio is in warehouse loans, which are fully secured and we hold the collateral.

Turning to Slide 10. Capital remained robust. Our total risk-based capital ratio was 13.6% at December 31, in the upper half of our target operating range 13%, 14%. Assuming final capital simplification regulations are enacted as proposed, this ratio should be 29 basis points higher. Our Tier 1 leverage ratio is 8.29% at December 31, down just 7 basis points from last quarter and well within its target operating range of 89%. Capital simplification would benefit this ratio by 61 basis points. What these strong capital ratios suggest is that we maintained a robust level of capital even after acquiring Wells Fargo branches. With the lifting of the Supervisory Agreement last year, we now have more levers than we can pull to deploy this capital.

Further, I'll continue to remind you, we have a low level of risk in our business. Stellar asset quality, strong allowance coverage, a neutral rate risk position and strong liquidity levels, combined with a robust risk management function. As such, we would expect to operate at least in the short term, in the lower half of our target operating range of 13% to 14% of the total risk-based capital ratio. We created ample capital support loan growth. With the Wells Fargo acquisition closed, we now have the third component needed for our value creation strategy. We have the sources of well diversified loan growth, the ability to fund loan growth with efficiently priced deposits and the capital necessary to support holding these additional assets. So I'll now turn to Lee for more insight in each of our businesses.

Lee Matthew Smith - *Flagstar Bancorp, Inc. - Executive VP & COO Flagstar Bank*

Thanks, Jim, and good morning, everyone. We're very pleased with our adjusted operating net income of $0.72 per diluted share for the quarter and $3.02 per diluted share for the fiscal year. 2018 was another successful year for Flagstar, as we continue to execute on our strategic plan to deliver value for our shareholders. Some of the key highlights included: we grew average loans held for investment by $1.6 billion or 22% and expanded our net interest margin by 23 basis points year-over-year, after adjusting for the deferred hedging gains associated with the Wells Fargo bank branch acquisition, which enabled us to grow adjusted net interest income by $78 million in 2018 versus 2017. The earning asset growth during the year was spread evenly across multiple commercial and consumer asset classes and included the acquisition of the warehouse lending business, which we closed in the first quarter. Furthermore, during 2018, net interest income accounted for 53% of our total revenues as compared to 45% in 2017.

Average total deposits increased $2.9 billion during the year, and we saw robust growth across all deposit categories. Retail deposits grew $1.1 billion, predominantly because of the acquisitions of the Desert Community Bank branches in March, and the Wells Fargo bank branches, which we acquired in December.

We also saw a healthy increase of $1 billion in company-controlled deposits because of the higher subservicing loan count with the increases in government and wholesale deposits accounting for the difference. Overall, we were very successful in 2018 of creating liquidity to fund our future balance sheet growth.

As of December 31, we were servicing or sub-servicing 827,000 loans, which is an increase of 87% from where we started the year. We are now the sixth largest subservicer of loans in the country, and expect to be servicing or sub-servicing over 900,000 loans by the end of the first quarter. We also saw the lifting of the Federal Reserve supervisory audit during the second half of 2018, which was another major milestone for the bank.

Throughout the year, we've demonstrated our ability to manage expenses in a challenging mortgage environment. Our adjusted noninterest expense run rate has been within a very tight range of $172 million to $177 million every quarter during 2018.

Finally, we closed on the acquisition of 52 Wells Fargo bank branches at the beginning of December, and we welcome our new colleagues to the Flagstar family. We acquired $1.76 billion in deposits at closing, and have subsequently seen 8.7% of deposit attrition through January '19. This transaction improves the quality of our deposit franchise and gives us the ability to maintain our low deposit beta.

It's been another solid and productive year for Flagstar as we continue to expand our footprint, optimize our balance sheet with high-quality interest-earning assets and low-cost stable liquidity and grow other more predictable sources of noninterest income.

I will now outline some of the key operating metrics from each of our major business segments during the fourth quarter. Please turn to Slide 12. Operating highlights for the community banking segment include average consumer loans held for investment increased $213 million or 6% in the quarter as we added high-quality residential first mortgage loans, non-auto indirect loans and HELOCs to our portfolio. And we expect this rate of growth to continue as we move forward.

Average commercial and industrial and commercial real estate loans increased $80 million or 2% in the quarter, led predominantly by $65 million increase in commercial real estate loans. Average warehouse lending loans decreased $249 million or 16% in the quarter due to the expected seasonal slowdown in the mortgage origination business.

The quality of our loan book is pristine, and we have no nonperforming or delinquent commercial loans on our balance sheet. Given our relationship-based approach and our expanding footprints, we believe we can continue to grow consumer and commercial loans at the same levels you've seen and without taking on any undue credit risk.

Average total deposits increased $606 million or 5% in the quarter led by the benefit of 1 month of acquired deposits from the Wells Fargo bank branch acquisition, which closed at the beginning of December.

Our adjusted net interest margin expanded 6 basis points in the quarter, a result of both expanding yields on interest-earning assets and stable funding cost, following the acquisition of the low-cost Wells Fargo branch deposits. As we look ahead, we believe we can continue to expand our net interest margin, particularly when you factor in a full quarter of the deposits we recently acquired. We feel the ingredients are there for continued earning asset growth coupled with an expanding margin, which should lead to increased net interest income revenues.

We're very encouraged by the performance of the community bank, our expanding footprints and potential for continued future growth.

Please turn to Slide 13. Operating highlights for the mortgage origination business include: fallout-adjusted lock volume decreased 36% to $5.3 billion quarter-over-quarter, while the net gain on loan sale margin rose 9 basis points or 18% to 60 basis points. As a result, gain on sale revenues fell $9 million to $34 million in Q4 versus $43 million in Q3.

The reduction in fallout-adjusted lock volume quarter-over-quarter was due to both the anticipated seasonal slowdown together with the continued excess operating capacity across the industry, which continues to put pressure on our mortgage business.

We think the problem of excess capacity within the industry will eventually correct itself, and believe we can use our market position and scale to succeed in a mortgage market with fewer players. We also remain focused on ensuring we manage cost against revenues in this tougher environment. And believe the benefits of our variable cost model are being seen throughout 2018 given the lower mortgage banking revenues.

Moving to servicing. Quarterly operating highlights for the mortgage servicing segment on Slide 14 include: we service or subservice approximately 827,000 loans, of which over 700,000 are subserviced for others, making us the sixth largest subservicer in the country. We've increased the number of loan service by 385,000 or 87% in 2018. And given our existing onboarding schedule for the first quarter, we estimate we will be above 900,000 loans serviced or subserviced by the end of March.

During 2018, we sold $29 billion in MSRs, and retained the subservicing on 100% of these sales, which is testament to the servicing platform we've created. The custodial deposits these loans generate also help us fund our loan growth. We held $1.7 billion of such deposits at the end of the year. We're thrilled with the progress we've made with our servicing business, and feel confident that you will continue to see this platform go from strength to strength in 2019 given the quality of our offering.

Moving on to expenses on Slide 15. After adjusting for the onetime Wells bank branch integration cost of $14 million in Q4, our noninterest expense increased $3 million to $175 million quarter-over-quarter. While mortgage-related expenses decreased $5 million as a result of actions we took earlier in 2018, and our variable cost model. There was an increase in compensation and benefits, loan processing expenses and other noninterest expenses, reflecting 1 month of. Run rate cost from the Wells Fargo branch acquisition, and more loans being subserviced.

Our adjusted efficiency ratio was 79.2% for the fourth quarter, which was a worsening of 5.1% from the prior quarter. The major reason for this was a reduction in revenues of $10 million quarter-over-quarter, given the reduced mortgage business and an increase in expenses of $3 million for the reasons I just outlined.

We estimate noninterest expense will be between $185 million and $190 million during the first quarter due to a full quarter of operating expenses from Wells Fargo branches and seasonally higher payroll taxes and benefit cost.

We remain focused on improving our efficiency ratio through increasing revenues, while maintaining our cost discipline throughout the organization. We're very pleased with what we've accomplished in 2018. We further diversified and expanded our business model in order for our earnings to be more predictable, and I believe you will continue to see that in our results quarter-over-quarter.

Furthermore, we have the necessary liquidity, capital and asset-generating capabilities to execute on our strategic plan, pursue accretive capital actions and continue to deliver value for our shareholders.

With that, I'll hand it back to Sandro.

Alessandro P. DiNello - *Flagstar Bancorp, Inc. - President, CEO & Director*

Thanks, Lee. Before I get into guidance for Q1, I'd to share some additional comments regarding the Wells Fargo branch acquisition we closed this quarter. Candidly, this wasn't our best moment. We underestimated the conversion cost, we underestimated the ongoing incremental operating cost. We stumbled out of the gate, and the deposits that came to us at closing were less than we anticipated. I could give you a lot of reasons why that happened but it really doesn't matter. What matters is that knowing all that, I continue to believe that this is a very important step in the continuing transformation of our company to a true community bank. Adding 170,000 customers is not easy to do. I've been in these branches. I've seen the strong relationship the bankers have with their customer base. I've witness their high skill level, and the way they performed under pressure was impressive. So knowing everything I know today, I would do this deal again in a heartbeat.

Now let's move to guidance for Q1, and we'll open the call for questions and answers.

Please turn to Slide 17. We expect net interest income will increase slightly on an improved margin, partially offset by a seasonal decrease in interest-earning assets. We anticipate gain on loan sale income will increase 20% to 25% and higher mortgage locks and a modest increase in gain on sale margin. We expect the return on the MSRs to be flat. As Lee noted, we anticipate noninterest expenses to be between $185 million and $190 million, and we expect the effective tax rate to be 18%.

This concludes our prepared remarks, and we'll now open the call for your questions. Katie?

QUESTIONS AND ANSWERS

Operator

(Operator Instructions) We will now take our first question from Scott Siefers of Sandler O'Neill.

Robert Scott Siefers - *Sandler O'Neill + Partners, L.P., Research Division - Principal of Equity Research*

I was just wondering if you could spend quick second on sort of the nuance behind the better gain on sale performance expectations in the first quarter. I think only because -- I mean, I can read the guidance, of course, but I think people generally just view the first quarter as likely a seasonally weaker one, so just curious as what gives you confidence that we would see such a pronounced spring back in those revenues in the 1Q?

Alessandro P. DiNello - *Flagstar Bancorp, Inc. - President, CEO & Director*

Well, I'll let Kristy get into some detail. But we saw margins get better as the quarter went on, and we think that given the activity that we see currently and going forward, we're a little more optimistic about where margins might be in the first quarter. Kristy?

Kristy Fercho - *Flagstar Bancorp, Inc. - President of Mortgage*

Yes, what I would add, Scott is, we maintained very strong discipline in Q4 in terms of some of the pricing discipline, which really had some of that kind of follow adjusted lock volume decrease. We're seeing some loosening of that as we enter into Q1. And so we're optimistic that based on some of the things that we're seeing there that we'll be able to really drive that back in Q1.

Robert Scott Siefers - *Sandler O'Neill + Partners, L.P., Research Division - Principal of Equity Research*

Okay, All right. Perfect. And then just -- as I think about the size of the balance sheet, I've kind of become accustomed to you guys generating, call it like a mid-teen year-over-year increase in the base of earning assets. So this might be a little more nuance sort of question, but earning assets were down in the fourth quarter, looks like they'll be down again in the first quarter. So to get back to the typical kind of trajectory, at least the year-over-year basis that you guys have been doing in the couple of last years. It would imply a really, really strong acceleration and balance sheet growth through -- from, call it, second quarter through fourth quarter this quarter. Is that the way -- the right way to think about it? Or just given what happened in the fourth quarter and it's likely to happen to the size of the balance sheet in the 1Q? Is 2019 going to be a bit more muted year-on-year just in terms of overall balance sheet growth?

Alessandro P. DiNello - *Flagstar Bancorp, Inc. - President, CEO & Director*

Well, certainly it could be. I mean, I look at things on a 12-month rolling basis. And I think the last 12 months have been pretty good for us in terms of our growth. And I'm optimistic that, that'll still be the case as we go forward. You have to look for where the opportunities are in the market, Scott, and I can't look too far in the future and understand where that might be. But I think the fact that we've diversified the asset-generating sources that we have over the years, gives us an advantage over others because we can move where the opportunity exists. Now that said, we're not going to grow just for growth's sake, it's got to be profitable, it's got to get the right returns, it's got to have the right credit quality. All those things have to line up. So the most important thing to make sure is that we keep a good, solid, clean balance sheet right now, and from a quality point of view, I think we can do that. I'm happy to let Drew add a comment or 2 about what he'd seen in the commercial space.

Andrew W. Ottaway - *Flagstar Bancorp, Inc. - Executive VP & President of Banking*

Yes, thanks, Sandro. I'd certainly echo your comment. I think if you look at both the commercial and the consumer portfolio, they are far more diversified than they were historically. And so while you may get quarter-to-quarter some lumpier growth in any one of them. If you look at it overall for the year, we've been in very shape. And I think, at the end of the day and especially on the commercial side, it really is a relationship-based model. So it's the lenders that we bring over, it's the relationships that they have, that have allowed us to continually and steadily grow that portfolio in a really meaningful and balanced way.

Lee Matthew Smith - *Flagstar Bancorp, Inc. - Executive VP & COO Flagstar Bank*

Scott, it's Lee. If you -- loans held for investment, we're up $1.6 billion or 22% year-over-year, that's where the commercial and the consumer loans Drew was just talking about sit. When you're looking at overall interest-earning assets, you're including assets held for sale, and given the size of our mortgage business, that number can't fluctuate because if we see opportunities to sell quicker to maximize gain on sale, we'll do that.

Robert Scott Siefers - *Sandler O'Neill + Partners, L.P., Research Division - Principal of Equity Research*

Yes, okay. Good. So it is that held for investment that's probably the one that clue in on as opposed to the...

Lee Matthew Smith - *Flagstar Bancorp, Inc. - Executive VP & COO Flagstar Bank*

Correct.

Robert Scott Siefers - *Sandler O'Neill + Partners, L.P., Research Division - Principal of Equity Research*

Sort of the entirety of the base of earning assets then. Okay, good. And if I can sneak one -- last one in there. Lee, in your prepared remarks, you talked about the margin continuing to expand. So clearly we'll get another boost from the full quarter of having the Wells branches in there. Is your sense that the margin could continue to expand thereafter in 2Q and beyond? Or would we reach sort of a steady state after we get the full quarter benefit in there?

Alessandro P. DiNello - *Flagstar Bancorp, Inc. - President, CEO & Director*

Scott, so you know, we don't go out there farther than a quarter. But I'll say this fundamentally, this is why I believe, the transaction that we just executed on is so fundamentally important. So if rates in the marketplace continue to rise, if the Fed should continue to increase short-term rates, the impact on us will be much less then it would have been had we not done this transaction. So whether it's $2 billion or $1.7 billion or $1.5 billion, that's that much less in funding that we're -- that we have interest sensitively exposure to relative to Fed increases. So we certainly feel much better about the prospects of the margin behaving in a positive way, but we're not going to speculate out farther than Q1.

Operator

We will now take our next question from Bose George of KBW.

Bose Thomas George - *Keefe, Bruyette, & Woods, Inc., Research Division - MD*

Just had a follow-up on the gain on sale margin guidance. Did the gain on sale margin trend sort of improve in the quarter after the rate rally in November? Because it did look like primary, secondary spreads got a little better after that.

Alessandro P. DiNello - *Flagstar Bancorp, Inc. - President, CEO & Director*

Yes, it gradually improved after that point.

Bose Thomas George - *Keefe, Bruyette, & Woods, Inc., Research Division - MD*

Okay, great. And then the -- just on the balance sheet. In the loans held for investment category, the other consumer loans, can you just remind us what's in that bucket?

James K. Ciroli - *Flagstar Bancorp, Inc. - Executive VP & CFO*

Bose, this is Jim. It's largely the indirect Marine/RV that we have.

Lee Matthew Smith - *Flagstar Bancorp, Inc. - Executive VP & COO Flagstar Bank*

And we also, as part of Wells Fargo transaction, we acquired $105 million of unsecured loans, that's also in that bucket.

Bose Thomas George - *Keefe, Bruyette, & Woods, Inc., Research Division - MD*

Okay, great. Then just one last one on the Wells Fargo purchase agreement. I forget, was there any price adjustment based on the attrition prior to the close?

Alessandro P. DiNello - *Flagstar Bancorp, Inc. - President, CEO & Director*

Well, the premium paid was based on the deposits at close. So there is kind of an automatic price adjustment based on that.

Operator

We will now take our next question from Steve Moss of B. Riley.

Stephen M. Moss - *B. Riley FBR, Inc., Research Division - Analyst*

Tallying up on the Wells Fargo deposits, just wondering do you think we've hit bottom here in terms of the attrition? And that they'll stabilize going forward? Or could we see a bit more to go?

Alessandro P. DiNello - *Flagstar Bancorp, Inc. - President, CEO & Director*

Well, I don't know, Steve, I mean we're working real hard on keeping the attrition at well below the 17% number that we had anticipated or modeled. And at this point, what do we say, 8%? 8.5%?

Lee Matthew Smith - *Flagstar Bancorp, Inc. - Executive VP & COO Flagstar Bank*

8.7%, Yes.

Alessandro P. DiNello - *Flagstar Bancorp, Inc. - President, CEO & Director*

Somewhere in there right now. We feel pretty good about where it's at today. So to the extent we can keep it at that or better, it obviously makes the transaction more accretive to us. But the important point, I think, more important point is that, once we settle in and whatever attrition takes place -- happens, then it's about moving forward and growing the relationships with these customers, and that's the other benefit of this. I already talked about the interest rate sensitivity benefit, but the other benefit is, now we have 150,000, 160,000, 170,000 customers, whatever is it that we didn't have a couple of months ago that we can sell products to and so -- and grow deposits from. So what's more important to me than whether the attrition ends up being 8%, 9% or 12% is what we do after things settle down and how we grow that business going forward.

Lee Matthew Smith - *Flagstar Bancorp, Inc. - Executive VP & COO Flagstar Bank*

Can I just jump on what Sandro said and just give you 1 fact, which, I think, is important if you're looking at the attrition. So when you look at the deposits and what we announced originally. Some of these deposits, what we term out of footprint. So the primary addresses were not within the 4 states where we -- where these branches were located. When you look at the attrition that's occurred preclose and postclose, 82% of those out of footprint deposits have gone. So you're only left with a very small amount of those added footprint deposits. That's where we've seen the majority of the attrition.

Stephen M. Moss - *B. Riley FBR, Inc., Research Division - Analyst*

Okay, that's helpful. In terms of -- I'm going on to mortgage warehouse lending here. Commitments have declined again this quarter. Just wondering what trends you're seeing there. Looking from the deck, it seems spreads are holding up, but are you seeing pressure from competition?

Alessandro P. DiNello - *Flagstar Bancorp, Inc. - President, CEO & Director*

It's not so much pressure from competition, I'm not saying -- I wouldn't say if there isn't any pressure from competition, there certainly is. But I think that commitments go down not because necessarily customers leave you but if their business levels are lower than they had been in the past and they don't need the level of line they've had in the past, there's no reason for us to keep a large commitment out there. So we would like the line to be used, so we've adjusted commitments to be more aligned with the actual level of business that our customers are at these days. More important number, really, to look at is the outstandings, and we're in a difficult time right now. Not only as -- are we at a seasonal point where balances are going to be lower but originations are lower. And prospects for 2019 are probably for a further decline in originations. So I think there's going to be pressure on the warehouse business. But we're a big player in that market, and I'm confident that we'll hold up.

Stephen M. Moss - *B. Riley FBR, Inc., Research Division - Analyst*

Okay. And if I could -- one more in -- on the homebuilder finance business. Commitments are up nicely again quarter-over-quarter. Spreads have -- to come in a bit, but just wondering what are your expectations for the business going forward, especially given what seems to be slowing home sales?

Andrew W. Ottaway - *Flagstar Bancorp, Inc. - Executive VP & President of Banking*

Yes, thanks. This is Drew. I'd say this. We still think there is a lot of room with that team. I think as you probably heard in prior calls, that group that came over just a few short years ago, it's been in the business a long time, has very established relationships. And so even though you have seen pressure in the home building -- homebuilder industry overall. They really continue to make good progress based on those relationships that they have. You still get a little bit of seasonality at year-end with some of their larger borrowers. But generally speaking, the pipeline that's been in place and continues to be in place is a strong signal to me in terms of the continued growth that we hope to have there.

Alessandro P. DiNello - *Flagstar Bancorp, Inc. - President, CEO & Director*

Yes, we've kind of kept a lid on this business because we want to maintain safe concentration levels. And so as the company has grown growing, as capital has grown, we've allocated more capital to the line of business. And we're continuing to see opportunities to bring new customers, strong new customers into the company because of the strong relationships that our team has and Drew and the team under Joe Hardy have been able to add a couple of people here. So that's an area where we're very bullish on our ability to continue to grow that in a very smart way.

Andrew W. Ottaway - *Flagstar Bancorp, Inc. - Executive VP & President of Banking*

Yes. And I'd just, Sandro. I mean, if you look at that portfolio, we now have direct relationships with 6 of the top 10 builders and over 40% of the top 100 builders. So these are large well-capitalized companies. They perform very well during the downturn. And needless to say I think that helps us as we continue to grow that portfolio.

Operator

We will now take our next question from Kevin Barker of Piper Jaffray.

Kevin James Barker - *Piper Jaffray Companies, Research Division - Principal & Senior Research Analyst*

In regards to the -- just a follow-up on the attrition rates. Could you give us an idea of how much attrition you saw the first couple of weeks after the deal closed? And then what the attrition rates were like through January?

Alessandro P. DiNello - *Flagstar Bancorp, Inc. - President, CEO & Director*

It's been pretty steady. It wasn't like -- it was 8% coming out of the gate, and then it's been flat, it's been pretty steady. Lee or Jim, you want to add to that?

Lee Matthew Smith - *Flagstar Bancorp, Inc. - Executive VP & COO Flagstar Bank*

Guess, what I would say though is, we've definitely seen it slowing down as we moved into January versus December. So I would -- it was higher in December than it has been in January. So we have seen it begin to drop off a little bit.

Alessandro P. DiNello - *Flagstar Bancorp, Inc. - President, CEO & Director*

I don't know how to read that, Kevin, because we have the holidays in the middle there. It's really difficult with weird number of business days that we had. So if you got a conclusion you want to share with us, I'm happy to hear your opinion on what that means because I don't know what it mean.

James K. Ciroli - *Flagstar Bancorp, Inc. - Executive VP & CFO*

I would also observe balances normally kind of go lower around the end of the year. So we're at 8.7% right now, and we're going to work hard to maintain that as low as we can.

Kevin James Barker - *Piper Jaffray Companies, Research Division - Principal & Senior Research Analyst*

Right. I would think attrition rates would be the fastest in the beginning and then slow down from there. Just trying to get an idea like the run rate that you're at right now. And then also your expectations for how that's going to play out, I guess, over the next 2 to 3 months because it's such an important period in the transition from Wells on to Flagstar?

Lee Matthew Smith - *Flagstar Bancorp, Inc. - Executive VP & COO Flagstar Bank*

Yes, no, Kevin, we get it. We are working hard to give the customers as good of experience as possible to minimize that attrition. And as you can tell based on the deposits we acquired at closing, there was a lot of attrition prior to closing.

Alessandro P. DiNello - *Flagstar Bancorp, Inc. - President, CEO & Director*

One thing I can tell you, Kevin. As I said in my prepared remarks, I've been to a few of the branches and I've seen the relationships, they're tight. These are customers that have banked with these bankers for a long time, and the tenure of the bankers that came over to us from Wells Fargo on average is very long. So there is a history, there is loyalty. And so I think, once the sort of more mobile type of customers find their way, whatever that is, I think, the far, far, far majority are going to stick with the bankers, and they're going to give Flagstar a chance. And -- so I'm very optimistic on where we we'll end up here, but I don't have enough information to give you an estimate of what I think might happen.

Kevin James Barker - *Piper Jaffray Companies, Research Division - Principal & Senior Research Analyst*

Okay. And then follow-up on some of the mortgage banking comments. It seems like the fallout-adjusted locks on a quarter-over-quarter basis declined in a much faster pace than maybe estimates for industry volumes? And then also the decline in your held-for-sale portfolio and the warehouse lines. So it seems that you might be more sensitive to price right now as opposed to holding market share. Are you being a little bit more resilient there? Or just a little more discipled around pricing?

Alessandro P. DiNello - *Flagstar Bancorp, Inc. - President, CEO & Director*

So look, if you're -- if you want to compete on price, I can get you big increase in locks real easily. But you won't like the margin that it takes to do that. So we're trying to make sure that this business is profitable. So you can't have your cake and eat it too. If you're going to cut expenses so that you protect yourself on a downside then you've got to make sure that the business you bring in is profitable. That's what we've been doing, that's why you saw our margin expand in Q4. I think that's consistent with what our history has been. We are not going to go out there and try to buy the business. Kristy, anything you want to add there?

Kristy Fercho - *Flagstar Bancorp, Inc. - President of Mortgage*

Yes, the only other thing I would add, Kevin is, we're seeing some crazy pricing in the market. And it's -- we made a conscious decision to not chase that irrationality and to be really smart about where we were going to price. And in fact, in some cases, which is why I think, you saw the gain on sale margin go up. We just remained disciplined around our pricing and didn't chase. But another thing that we did is, we're getting really a lot smarter about our analytics in terms of these different markets and really understanding where the competition is and where we can compete. And this is where I think our long-term customer relationships and understanding those customers and what their needs are, are really paying off for us. But as we're getting more analytical about different markets, different products and different customers and where we can price, it's really allowing us to figure out where to get sensitive on price and then where we can actually take margin. And so we were really strategical in Q4, as Sandro said, we didn't chase the irrational pricing, and so that's why you saw the fallout-adjusted locks go down but margin hold. And we're going to continue that discipline as we go into Q1. But some of the strategies that we put in place in Q4 are going to come to fruition in Q1, which is why we feel strongly that you'll see both net gain on loan sales and the locks increase quarter-over-quarter.

Operator

We will now take our next question from Chris Gamaitoni.

Edward Christopher Gamaitoni - *Compass Point Research & Trading, LLC, Research Division - MD & Assistant Director of Research*

I wanted to follow-up on the corresponding competition commentary. Is there any -- do you have a sense of who are the most aggressive players, I'm not looking for names, but is the large national banks that are always in the business or is it more on the nonbank sector? Just trying to understand the competitive dynamics.

Alessandro P. DiNello - *Flagstar Bancorp, Inc. - President, CEO & Director*

And you're specifically asking about corresponding business, Chris, versus retail?

Edward Christopher Gamaitoni - *Compass Point Research & Trading, LLC, Research Division - MD & Assistant Director of Research*

Yes, correspondence.

Alessandro P. DiNello - *Flagstar Bancorp, Inc. - President, CEO & Director*

Yes, I think it's mostly nonbanks, but I'll let Kristy answer.

Kristy Fercho - *Flagstar Bancorp, Inc. - President of Mortgage*

Yes, we know the names. So yes, we are very clear about who it is and it is absolutely the nonbanks that we're seeing in the corresponding channel as well as the brokered channel.

Edward Christopher Gamaitoni - *Compass Point Research & Trading, LLC, Research Division - MD & Assistant Director of Research*

Okay. Definitely makes sense. On your subservicing growth, if you could just give a sense of where this amazing growth is coming from? Do not want any specific names, but kind of what your value proposition is that's leading to a lot of placements?

Lee Matthew Smith - *Flagstar Bancorp, Inc. - Executive VP & COO Flagstar Bank*

Yes, so well -- Chris, it's Lee. The value proposition is: one, we have a quality platform, and as you know, we've won the Fannie Mae STAR award in the category of General Servicing for 3 years running. We also have this one-stop shop. So not only can we subservice the loans we offer MSR lending, servicing advanced lending, recapture services. We're very well capitalized. We have a robust risk and compliance infrastructure in place. So we're seen as just being a very strong counter party, and people can also buy MSRs from us. And because we're producing so much given the scale of our mortgage business, and they just leave them on our platform, which is appealing for the big financial funds that are MSR buyers. What has happened over these last 12 months in particular is those financial funds that are buying MSRs from multiple parties, they just like the service they get into. So they are moving those big portfolios to Flagstar, and that's really why you've seen the 87% growth or 385,000 additional loans added to the platform in 2018.

Alessandro P. DiNello - *Flagstar Bancorp, Inc. - President, CEO & Director*

Don't underestimate the regularly comforts that these MSR owners get from Flagstar, because it really earns very, many regulated banks that are in this space. And so if you can show that you can do the business, and it's -- took a while to prove it out, but we did. Now there is an advantage there that it's not financial, but you know that the regulatory world has -- can change on a dime. And you don't want to be in a bad place if that should happen. And so I think the comfort that we provide is -- there is some real hidden value there.

Edward Christopher Gamaitoni - *Compass Point Research & Trading, LLC, Research Division - MD & Assistant Director of Research*

Okay. That makes sense. And one nitpicky. Your year-end deposits looked like they were down about 8.4% quarter-over-quarter at the acquisition. Is that's the seasonality of custodial deposits or is there something else going on?

Alessandro P. DiNello - *Flagstar Bancorp, Inc. - President, CEO & Director*

I didn't catch the first part of your question, so...

Andrew W. Ottaway - *Flagstar Bancorp, Inc. - Executive VP & President of Banking*

Period-end deposits have been...

Alessandro P. DiNello - *Flagstar Bancorp, Inc. - President, CEO & Director*

Period-end deposits.

James K. Ciroli - *Flagstar Bancorp, Inc. - Executive VP & CFO*

We'll take a look at that. We don't focus too much, it's likely the custodials, Chris. That we -- yes, as I mentioned earlier, just seasonally, all deposit categories typically go down at around the end of the year.

Alessandro P. DiNello - *Flagstar Bancorp, Inc. - President, CEO & Director*

Yes, we'll get back to you on that, Chris. But I do think it was a fairly significant custodial deposit drop in Q4 quarter-end to quarter-end.

Operator

We will now take our next question from Henry Coffey of Wedbush.

Henry Joseph Coffey - *Wedbush Securities Inc., Research Division - MD of Equity Research*

Interesting quarter. Just a bunch of small things, but I want to ask a really stupid question with -- and I know...

Alessandro P. DiNello - *Flagstar Bancorp, Inc. - President, CEO & Director*

I'm good at those.

Jade Joseph Rahmani - *Keefe, Bruyette, & Woods, Inc., Research Division - Director*

Yes, I mean -- no, I know some of my colleagues have done an excellent job on tracking this issue. But with deposit attrition, is it the issue that you've got, what I'll call, either commercial deposits or price-sensitive money just waking up and saying, okay, my bank is changing, I'm now open to a price bid and they walk out the door? Or is it angry, dissatisfied customers because you, I don't know, made them mad over something? What is the mechanism by which people decide to leave their bank?

Alessandro P. DiNello - *Flagstar Bancorp, Inc. - President, CEO & Director*

Well, I'll speculate a little bit here. Lee already mentioned that 82% of the attrition was people that are no longer domiciled in the area where the branches are located. So that's part of it, obviously, they want a branch that they can go to, if they can go to the branch. Number two, I think that they're -- competitors always come out with very interesting offers. If you move your account when a new bank comes to town. We'll buy your checks, all that sort of thing. So there you have some of the price-sensitive people that move. And there's people that just don't like change. Maybe they didn't like how it all happened. And so it's a combination of things. And my experience is, you got to let things settle down and not get too excited over what happens right away. Establish yourself, give your people a chance to get comfort -- comfortable themselves with the new company and then get back on your feet and go forward. And that's why I'm focusing more on that than I am on whether we end up at 8%, 10% or 12% attrition. In on the long run, that's not going to matter. What's going to matter is, how we grow this business.

Henry Joseph Coffey - *Wedbush Securities Inc., Research Division - MD of Equity Research*

The -- you've also done sort of smaller, less visible deals on the West Coast. Can you compare and contrast your experience there versus this? And what would your thoughts be on taking on a major West Coast deal?

Alessandro P. DiNello - *Flagstar Bancorp, Inc. - President, CEO & Director*

Yes, I mean, very different what we saw with DCB just because it's such a -- the franchise is so much smaller. And so as you may recall, we didn't experience any attrition in the DCB acquisition. So it definitely makes a difference who the customer -- where they're coming from, they're coming from a very large bank or if they are used to kind of community bank type experience. Where do we take on something else? I mean, we're not ready right now, we've got a lot of work to do to prove this one out. But sure, at some point, we'll take a look at what makes the most sense for our future, and if the right situation presented itself, we would consider it.

Lee Matthew Smith - *Flagstar Bancorp, Inc. - Executive VP & COO Flagstar Bank*

Certainly a whole bank acquisition would be a challenge, given our trust-preferred situation.

Henry Joseph Coffey - *Wedbush Securities Inc., Research Division - MD of Equity Research*

So that's helpful to hear also. Given -- the MBA mortgage index, frankly, went nuts in last 3 weeks, up a lot. And the -- and primary, secondary spreads as well. And a lot of it is just market factors not real business factors. What is -- what are your thoughts about what we've seen in January? I mean, is that volume sustainable? Is that profitability sustainable? Or is it -- or when we get back into February or in March, we're going to be up against all those headwinds that have plagued the industry for the last year or so?

Alessandro P. DiNello - *Flagstar Bancorp, Inc. - President, CEO & Director*

I mean, I think it's going to be tough year, right? If you look at the experts, the estimates are to be $100 billion smaller than last year, I think, in terms of overall originations. So I think what we saw in 2018 is likely to continue in 2019. As capacity adjusts we'll have more of an opportunity to look at expanding spreads. But I wouldn't take anything you've seen in early January as some sort of trend. It's -- we haven't seen anything for long enough. And again, I think, when you get around the holidays, there's a lot of weird things that happen. And I just wouldn't take much from what's happened thus far in January.

Operator

We will now take our next question from Daniel Tamayo of Raymond James.

Daniel Tamayo - *Raymond James & Associates, Inc., Research Division - Senior Research Associate*

Just a couple of modeling questions here on the expense side. First, the lower tax rate in fourth quarter and lower tax rate guidance going forward. Is any of that -- is there -- you mentioned the tax strategy, is there any kind of offset in expenses there that we've seen or going forward that you're expecting?

James K. Ciroli - *Flagstar Bancorp, Inc. - Executive VP & CFO*

No. No. No, we're not -- typically, you'd see a historical tax credits that tax good guy and expense bad guy. And that's not what's driving the expense -- effective tax rate lower.

Daniel Tamayo - *Raymond James & Associates, Inc., Research Division - Senior Research Associate*

All right. And specifically looking at the first quarter, you mentioned the seasonal impact of the higher payroll tax and benefit costs with Wells Fargo branches now in the run rate. What are the -- in terms of a dollar amount, do you have a ballpark for what that would be?

James K. Ciroli - *Flagstar Bancorp, Inc. - Executive VP & CFO*

The dollar amount on the Wells branch operating expenses?

Daniel Tamayo - *Raymond James & Associates, Inc., Research Division - Senior Research Associate*

Just on the total seasonal impact.

James K. Ciroli - *Flagstar Bancorp, Inc. - Executive VP & CFO*

No, I don't think we've given that in the past.

Lee Matthew Smith - *Flagstar Bancorp, Inc. - Executive VP & COO Flagstar Bank*

No, here's what I would say, though, just high level, because we don't get that specific. You can see the adjusted noninterest expense was $175 million in Q4. We've guided to $185 million, $190 million in Q1. You've got an extra 2 months of the Wells Fargo branches, because we only had 1 month in Q4. You've got this seasonal adjustment for higher comp and benefits. And then as you know, we've guided to higher gain on sales, so there's an incremental piece for just the higher mortgage business as well. That's basically a bridge without sort of giving you numbers for each of those categories.

Daniel Tamayo - *Raymond James & Associates, Inc., Research Division - Senior Research Associate*

That's helpful. And then finally just in terms of the $14 million in the fourth quarter, what was the breakout of where that came out of in the line items and the merger costs?

Alessandro P. DiNello - *Flagstar Bancorp, Inc. - President, CEO & Director*

The $14 million of merger costs. Jim you know what line items are?

James K. Ciroli - *Flagstar Bancorp, Inc. - Executive VP & CFO*

It was largely other in salary and benefits.

Operator

We will now take our next question from Scott Beury.

James Prescott Beury - *Boenning and Scattergood, Inc., Research Division - Analyst of Banks and Thrifts*

I just had one quick follow-up question. Regarding the Wells Fargo branch acquisition, was there any concentration, if you will, in the deposit attrition by market or just generally the regions? I mean, obviously, there was much less of the franchise in the northern part. But I was just curious if there was any specific area where that really was more prevalent?

Alessandro P. DiNello - *Flagstar Bancorp, Inc. - President, CEO & Director*

Well, just in the out of market, Scott, that's where the bid concentration was. Within the footprint, while the percentages by area varied some, there wasn't dramatic difference between say, Northern Michigan and South Bend. It was within a fairly tight range across.

James Prescott Beury - *Boenning and Scattergood, Inc., Research Division - Analyst of Banks and Thrifts*

Okay, that's helpful . And then I guess similarly if you look forward to more growth opportunities in -- with the expanded footprint in Indiana and in the North. Do you have any general color on areas that you're looking to that would potentially be attractive to expand? Are there any specific business lines that you think would be good fits?

Alessandro P. DiNello - *Flagstar Bancorp, Inc. - President, CEO & Director*

Well, I think there's going to be opportunity for our middle market, commercial, both in the C&I as well as the CRE space. I mean, in terms of dollars there is opportunity there. There's always opportunity with business banking, but the dollar impact is less there. So I think, all of those sort of core commercial offerings, not to mention consumer loans are all opportunities. So whether there is more opportunity for one type of business in one market versus another, I can't speak to that. I don't know if Drew -- if you have any thoughts about that.

Andrew W. Ottaway - *Flagstar Bancorp, Inc. - Executive VP & President of Banking*

No, I think you're exactly right. I mean, in addition to bringing over those branches, the deposits and the small-amount loans that we brought over, there really is a great opportunity to leverage that footprint with respect to consumer lending, business banking, insurance and investment and mortgage because those aren't things that came over with that it. So we really do believe that to be a big opportunity going forward.

Operator

We will now take our next question from Kevin Barker.

Kevin James Barker - *Piper Jaffray Companies, Research Division - Principal & Senior Research Analyst*

So in regards to the first quarter, what should we expect as far as the FHLB advances on a, like, period-end basis and at average basis given the deposits that we've seen? There was a big drop in the long-term FHLB advances, but do you still see somewhat of a decline? And then can you just give us some near-term view on deposit growth in the first quarter?

Alessandro P. DiNello - *Flagstar Bancorp, Inc. - President, CEO & Director*

Okay, so I'll let Jim take the advanced question. In terms of deposit growth. So this is a tough one because that the betas that a lot of others have experienced have been much higher than ours have. And we've been able to be conservative in the way we've approached deposit pricing because we knew that the Wells Fargo acquisition was coming and we were going to have those lower cost deposits coming on to the balance sheet. So now that we're past that, now we've got to look across the whole organization, and we've got to make some decisions on how aggressive we want to be with that with pricing of deposits, and how that compares to alternative funding sources. So this is kind of like game-time decisions, you got to see what's going on in the market and you got to see what the opportunities are. There's a lot of people on the deposit side that are pricing irrationally just like they are on the mortgage side. So this is a fine line and it could be different in one market versus another. But I think our history shows that we're pretty good. We've been pretty good at understanding where the opportunity is and keeping the betas at reasonable level. So we know that's what we'll work -- to continue to do.

Lee Matthew Smith - *Flagstar Bancorp, Inc. - Executive VP & COO Flagstar Bank*

I would -- Kevin, in my prepared remarks, I made a remark that not only does the Wells Fargo give us that direct benefit of lower cost deposits -- and yes, we always message that we would pay off FHLB borrowings and that's what you saw, that what you saw us do, and paid that off near the end of the year with the FHLB borrowings. But what I made -- the remark I made is that the deposits not only give us that primary benefit but the secondary benefit is exactly what Sandro said. We can be more disciplined because we have ample liquidity at this point. So we don't have to go out and get that extra deposit dollar, our success doesn't hinge upon getting that. So we'll be rather disciplined on the entire deposit franchise, not just the Wells deposit franchise and how we manage the deposit costs.

Kevin James Barker - *Piper Jaffray Companies, Research Division - Principal & Senior Research Analyst*

So in the first quarter, would you -- would we expect a further decline if FHLB advances on a period-end basis given the Wells Fargo deposits understands that?

Alessandro P. DiNello - *Flagstar Bancorp, Inc. - President, CEO & Director*

Yes, I don't think we're going to be that specific with you on where we see the funding numbers at the end of the quarter. It depends, it depends on how much more attrition there is, and how much we're able to grow in other markets. So I don't know, but I would tell you this that the -- if we grow deposits, it'll be at a cost that's less than what the alternative funding cost for FHLB or anything else would be.

Operator

It appears there are no further questions at this time. I would now like to hand the call back over to the Sandro DiNello.

Alessandro P. DiNello - *Flagstar Bancorp, Inc. - President, CEO & Director*

Thanks, Katie, and thanks to everyone for your interest in Flagstar. From a high-level perspective, the fourth quarter was about fundamentals and the future. Fundamentals because we have remained focused on expense discipline, strong credit quality and abundant capital. Additionally, we have embraced revenue diversification, which has delivered consistent earnings despite the continued challenge from mortgage originations. The future, because we changed the face of our funding, grew our core customer base in a big way and significantly expanded our branch footprint.

We're moving to 2019 with a strong business model and a level of core funding that we have never experienced before. Going forward, our strong capital gives us flexibility and durability. We will use these strengths to maximize returns and grow shareholder value. We look forward to the future with confidence and optimism.

A very special thank you, this quarter, to the Flagstar team for the way you successfully overcame some very difficult challenges. To everyone else, thank you for your attention this morning. I look forward to reporting Q1 results in April.

Operator

This concludes today's conference call. You may now disconnect.