REFINITIV STREETEVENTS

EDITED TRANSCRIPT

TBK.OQ - Q3 2022 Triumph Bancorp Inc Earnings Call

EVENT DATE/TIME: OCTOBER 20, 2022 / 12:00PM GMT

CORPORATE PARTICIPANTS

Aaron P. Graft *Triumph Bancorp, Inc. - Founder, Vice Chairman, President & CEO*

Geoffrey P. Brenner *Triumph Bancorp, Inc. - CEO – Triumph Business Capital*

Luke Wyse *Triumph Bancorp, Inc. - SVP of Finance & IR*

Melissa Forman *TBK Bank, SSB - President of TriumphPay*

Todd N. Ritterbusch *TBK Bank, SSB - President*

William Bradley Voss *Triumph Bancorp, Inc. - Executive VP & CFO*

CONFERENCE CALL PARTICIPANTS

Bradley Jason Milsaps *Piper Sandler & Co., Research Division - MD & Senior Research Analyst*

Gary Peter Tenner *D.A. Davidson & Co., Research Division - MD & Senior Research Analyst*

Joseph Peter Yanchunis *Raymond James & Associates, Inc., Research Division - Senior Research Associate*

Matthew Covington Olney *Stephens Inc., Research Division - MD & Analyst*

PRESENTATION

Luke Wyse - *Triumph Bancorp, Inc. - SVP of Finance & IR*

Good morning. I'd like to welcome you to Triumph Bancorp's Third Quarter 2022 Earnings Conference Call. We're so glad you could join us this morning. I'd like to start by thanking all of you for your input following last quarter's call. As you may remember, last quarter, we moved to this new video format. Many of you provided some fantastic feedback for us around this medium. As you can see, we took it to heart, and as a result, we're trying something a little different today as we continue to explore this method of communicating with you, our shareholders.

Today is just another step on that journey, and we'll continue to tweak this around the edges as we go forward. The lights are bright this morning. We're live to the world, and so this is all pretty new to us. Hopefully, it all goes well. On that note, one of the benefits around doing something different like this is it gives us the opportunity to bring you alongside us with us on this adventure. We appreciate your partnership. And thank you again for joining us this morning.

Today, I'm joined by Aaron Graft, our CEO; Brad Voss, our CFO; Melissa Forman, our President of TriumphPay; Geoff Brenner, our CEO of Triumph Business Capital; and Todd Ritterbusch, President of TBK Bank.

Last evening, we published our quarterly shareholder letter. That letter and our quarterly results will form the basis of our call today. However, before we get started, I'd like to remind you that this conversation may include forward-looking statements. Those statements are subject to risks and uncertainties that could cause actual and anticipated results to differ. The company undertakes no obligation to publicly revise any forward-looking statements. For details, please refer to the safe harbor statement in our shareholder letter published last evening. All comments made during today's call are subject to that safe harbor statement.

With that, I'd like to turn the call over to Aaron for a welcome and to kick off our Q&A. Aaron?

Aaron P. Graft - *Triumph Bancorp, Inc. - Founder, Vice Chairman, President & CEO*

Good morning. Thank you for joining us. As you saw in our letter, our earnings this quarter were below expectations. There were a few contributing factors to that. First, we began to see a slowdown in freight. Second, this quarter's results reflect revenue associated with our general factoring and equipment finance portfolios that we sold last quarter. But more importantly, from a long-term perspective, we have made material progress on our payments network, and we've done that despite freight headwinds. Specifically, our invoice volume increased 6.6%. And even more importantly, our network transaction volume increased 21.7%.

Regardless of headwinds in freight or market volatility and whether it last quarters or years, we're committed to our revenue goals and to being EBITDA positive in TriumphPay in 2024. And if you couple that with the profitability of our Banking and Factoring segments, we have a lot to be excited about.

With that introduction, we will turn it over for questions.

QUESTIONS AND ANSWERS

Operator

(Operator Instructions) Our first question comes from Matt Olney from Stephens.

Matthew Covington Olney - *Stephens Inc., Research Division - MD & Analyst*

The TPay payment volumes, Aaron, you mentioned those were pretty flat this quarter, and I appreciate part of this is going to be the lower invoice prices that are out of your control. But I'm curious how you're thinking about the ramp of TPay volume over the next few quarters. Just trying to appreciate where some of the larger customers are in the queue of TPay integration but also TPay adoption.

Aaron P. Graft - *Triumph Bancorp, Inc. - Founder, Vice Chairman, President & CEO*

Matt, it looked like a really great question, but we could not hear it. We're trying to figure out. I'm not sure if you were on mute or if we had you on mute.

Matthew Covington Olney - *Stephens Inc., Research Division - MD & Analyst*

I can hear you guys. Can you guys hear me? Test, test, check, check.

(technical difficulty)

Okay. I think you guys can hear me now. You guys got me?

Aaron P. Graft - *Triumph Bancorp, Inc. - Founder, Vice Chairman, President & CEO*

We hear you. We're ready.

Matthew Covington Olney - *Stephens Inc., Research Division - MD & Analyst*

Okay. All right. Perfect. So my question is on your point, Aaron, about TPay payment volumes. You mentioned they were pretty flat this quarter. I mean the number of invoices was up, but the payment volume was flat. Obviously, that's out of your control to some degree. I'm curious how you're thinking about the ramp of TPay volume over the next few quarters. Just trying to appreciate where some of the larger customers are in the queue of TPay integration and TPay adoption.

Melissa Forman - *TBK Bank, SSB - President of TriumphPay*

Yes, that's a great question, Matt. Thank you for that. I'll take that one, Aaron, if you don't mind. So when we look at TPay volume, you're right, there are a lot of contributors that are out of our control like the average invoice price. But one thing I do want to point out is that we have increased transaction volume 6.6% quarter-over-quarter, which is a huge improvement in spite of the headwinds. And so we're excited about that. Our conforming transaction volume has also increased by over 21%, another point that is just an impressive feat by our team considering what we're seeing in the market.

When you think about Tier 1 or the larger freight brokers coming on board, you're right, we don't have one that's in our sights for to go live in Q4, so we wouldn't expect that to happen. But they are lined up in the integration process, and our pipeline is very robust when it comes to those larger customers. They take longer to get onboarded. Right now is peak season for all these freight brokers, so they're focused on getting through the holidays. And in the meantime, we're adding the smaller brokers and getting them in play for the network as well. So we added 18 last quarter, net new freight brokers. We're excited about what we see in our pipeline. The integrations team is quite busy bringing them all on board.

But to your point, Matt, Tier 1s are going to be more of first half of next year.

Aaron P. Graft - *Triumph Bancorp, Inc. - Founder, Vice Chairman, President & CEO*

Yes. That's exactly right. And Matt, specifically, and I know you're thinking about it from a model perspective, and I think any investor would. When we called out the $15 billion in volume, and that's an approximate number, which just like what we saw with TriumphPay this quarter, as the freight market moves, that number is going to move. I mean, ideally, we would be able to express that number to you not as a volume number but as a revenue number. And we have some thoughts around that, but we're early enough in this process that making a revenue projection and the timing of it we're not ready to do.

But to be specific, Schneider does not count in that $15 billion. Schneider was already a client for payments. We just added audit capability which allowed them to do network transactions. The $15 billion we called out, the bulk of that we expect to come on in the first half of next year because, as Melissa said, the fourth quarter for freight brokers is an exceptionally busy season, and most of them go into code freezes as a result of that.

So I can't tell you the exact timing of when it will happen, but I can say we expect the bulk of that volume to come on in the first half of next year. And beyond that, there are a whole lot of smaller brokers and longer-term conversations that are happening. And I go back to what I said in the opening. We're very excited about the pipeline. And frankly, these headwinds in freight have created an opening for us to discuss the value proposition for TriumphPay in an entirely different way than we did before because it's not just about how can I cover these loads in the tightest freight market we've seen in my career. Now people are worried about how do I get more efficient, which has been played right into the TriumphPay story. So I hope that's helpful.

Matthew Covington Olney - *Stephens Inc., Research Division - MD & Analyst*

Yes, that's helpful. And then just as a follow-up, I think you mentioned conforming transactions was one of the highlights in the quarter. I think it was up 22%. Remind us where you think that the level of conforming transactions can ultimately go and what's the path to get there? Or said another way of that, once you achieve that $75 billion of payment volume, what percent of those do you think will be conforming?

Aaron P. Graft - *Triumph Bancorp, Inc. - Founder, Vice Chairman, President & CEO*

Go ahead.

Melissa Forman - *TBK Bank, SSB - President of TriumphPay*

I'll take that, Aaron. So there's a lot of factors that go into play there. And when you look at our brokered freight payments today, we're at over 34% of those payments are network or conforming enabled, which means the payee on the receiving end of those transactions can get access to the data that we provide in the network. That's a huge feat. And our goal is to have all of our payment volume be conforming as we look to integrate -- do deeper integrations with our freight brokers. Our team is working hard to get that done.

Where we think that the biggest point of transition for the network is going to be when we can provide factoring companies and carriers at least 15% of their payment volume that they receive and process as confirming transactions, that's really going to be where it moves the needle and allows them to be able to make meaningful changes to their day-to-day processes and allow them to innovate and create more efficient ways to do business. We're delivering about 5% now, and we can see that with Triumph Business Capital and what they receive from TriumphPay and conforming transactions. And we -- again, we expect that 15%, that's when real development, real process changes can happen within those organizations to create that value that we're talking about that the network will provide.

Aaron P. Graft - *Triumph Bancorp, Inc. - Founder, Vice Chairman, President & CEO*

Yes, exactly. And just to say it, what Melissa exactly got right, but just as you sit and look at a model of $75 billion of payment volume, the first thing I would think about if I were you is 65% of those payments are likely going to factoring companies. And that is the candidate for a network transaction. That's the primary candidate. It could happen outside of that, but it's probably not. So then if you think about that 65%, then it's just a modeling exercise of what's the adoption rate among the factoring community to accept network transactions. And Melissa was exactly right. Right now, and you shouldn't miss this, 1 out of every 6 payments made to Triumph Business Capital or 15% of their payments comes from TriumphPay. And that would be a wonderful proxy for the rest of the industry. We pay more carriers and more factoring companies than anyone active in the market has ever done. But 1 out of 6 is the total payments. If we think about conforming payments, in other words, where the payor has given us both the remittance information and the audit information, that's 1 out of 20 payments or 5%, exactly like Melissa said.

And just to echo what she said, if you think about it from the perspective of a factoring company who's going to bear the primary cost of that network transaction, we believe and we can model it internally that once Triumph Business Capital or any factoring company gets roughly 15% of all of their payment volume coming through as conforming, they can start to reorganize their staffing and enterprise resources models to accept those transactions in an entirely different way and a very profitable way for them. So that's how we think about it. You start at the $75 billion, you work it down to the factory transactions, and then you make some assumptions about market penetration.

And don't lose sight of the fact that we still monetize payments made away from network transactions. We monetize every part of the process. It's just that network transactions deliver the most dimensions of value to the payees, which include factoring companies. And so those are going to be the most profitable for us.

Melissa Forman - *TBK Bank, SSB - President of TriumphPay*

Yes. And Aaron, I add to that, I mean when you think about network transactions and the monetization of that, we can take the same invoice and throughout the participants monetize it multiple times, and that's the network effect for TriumphPay. And we're creating that value to each participant in the transaction, and so it just continues to build on itself, so it's exciting.

Operator

Our next question next question comes from Gary Tenner from D.A. Davidson.

Gary Peter Tenner - *D.A. Davidson & Co., Research Division - MD & Senior Research Analyst*

I wanted to ask about kind of where your expectations are for invoice prices. Obviously, you had in your CEO letter kind of the breakeven spot rate, I think, [$2.22] a mile. Given where spot rates have already fallen and we've seen a little bit of pressure on invoice prices but not really a dramatic level of pressure at this point, where do you think average invoice size heads? I mean, obviously, if volumes are lower and there's a compounding effect of lower invoice prices, it's a little more meaningful to top line revenue.

Aaron P. Graft - *Triumph Bancorp, Inc. - Founder, Vice Chairman, President & CEO*

Geoff, why don't you take that.

Geoffrey P. Brenner - *Triumph Bancorp, Inc. - CEO – Triumph Business Capital*

Happy to. So it's impossible to say with certainty what's going to happen. Average invoice sizes, we project there's going to continue to be a very slow decline. So if you think of a balloon that has a very small hole in it, you just have a very gradual leak, and that's what we've seen.

One thing we're doing to combat that, because we can't control that, is to absolutely grow our presence in the large fleet sector and maximize the number of invoices that we're buying on a daily basis. If you look at our year-over-year numbers, comparing where we are year-to-date right now at the end of Q3 versus where we were a year ago, that's actually a 20% growth in number of invoices. So that's a good indicator that we're winning, that we're growing the number of invoices and whatever that average invoice price size is. For us, the goal line is to have the most number of invoices possible bouncing up against that. That's the part we can control.

Aaron P. Graft - *Triumph Bancorp, Inc. - Founder, Vice Chairman, President & CEO*

Yes, exactly. And Gary, I mean, we've called this out. And I think the reason for your question is because every $100 move in invoice prices is a $10 move -- $10 million move in revenue. But to pile on to what Geoff said and what you saw in the letter, I struggle to see how we will return in the spot market, given current market conditions to $1,500, $1,600 or $1,700 invoices. It's just no matter how soft the market gets, people are not going to haul freight at a rate at which they're losing money. So this is not an economic prediction, but I think you're going to anchor around that $2,000 number. It might be on the -- just under it. It could be slightly over it. I mean one of the things that Geoff and the team have done a great job, we've onboarded over 3,000 clients this year and out of 12,000. And what that means is some of these clients are finding that they can't breakeven, and so they're parking their truck, and they're going to work in another industry or they're signing on to work for a larger fleet.

And without those invoices being around $2,000 an invoice, we struggle to see -- and again, there are shorter hauls, longer hauls, but we sort of aggregated on everything we do. I think we can say we struggle to see how any trucker could hit to be EBITDA breakeven. So that's our best estimate of kind of where the pressure point is of where truckers will continue to accept spot market freight.

Geoffrey P. Brenner - *Triumph Bancorp, Inc. - CEO – Triumph Business Capital*

Gary, if I could just add on, it's an interesting data point. If you look at the interplay between average invoice size and the number of invoices we purchased in Q3, if we had the average invoice size that we had in Q1, with our volume purchased in Q3, it would have been the best quarter in company history. So on the things we can control, we're pressing forward and growing. We just have to wait and see what happens with the market.

Gary Peter Tenner - *D.A. Davidson & Co., Research Division - MD & Senior Research Analyst*

Right. And this is, I guess, a bit of a follow-up to that. But the last, call it, 18 months, you've had the benefit of, call it, a windfall, I think you put it as called Triumph Business Capital of golden goose in your letter. And that's kind of shielded on a consolidated basis, the cost of investing in TriumphPay.

Given kind of the revenue decline, maybe some further decline in invoice prices, et cetera, how do you think about kind of consolidated profitability at the company over this period of time where you're continuing to invest and TriumphPay continues to operate at a pretax loss?

Aaron P. Graft - *Triumph Bancorp, Inc. - Founder, Vice Chairman, President & CEO*

Yes, that's a great question, and I have a lot of thoughts about this. So I will try to, Gary, consolidate them. First of all, by the time we talk to you next quarter, half of our loan book will have turned over 3x. So just the way we're constructed is different because if you think about Triumph Business Capital, it turns every 30 days. So we talked before about we try not to take credit risk, we don't take interest rate risk, and we live with revenue volatility. And if that's true, then how I would characterize the last 18 months is like when you're in the airport and you're on one of those people movers and you're walking and it's pushing you forward, it makes you look faster than you are.

And how I would characterize today is it's neutral. And how it may be in 2023, especially the first quarter, I don't know, but we're -- we think it's possible that it actually could be a treadmill running against us. Okay? So true headwinds, so what does that mean? What does it mean for investment in TriumphPay and for the enterprise itself? Well, the first thing is, assuming TriumphPay were breakeven, our ROA would be over 1.5%, right? That's -- the business is profitable, and that's because Triumph Business Capital and the Community Bank have been constructed to be profitable, whether we have tailwinds or headwinds, whether the treadmill is running against us or for us.

The second thing to remember is this. The expense growth in TriumphPay 2 years ago was 200% year-over-year. And between last year and this year, it's 50%. Between this year and next year, it will be less than 20% unless we get far more wins than we can even imagine. So if we're sitting here a year from now and we're telling you expense growth in TriumphPay is 30%, then we're going to be very excited about that because that will be variable expense growth associated with volume that was beyond our expectations. But we've spent 2 years building the foundation to go run this play, and it has required life to date $200 million of investment. And so we're not going to shortchange what we're doing. We are committed to those 2024 goals because you know and I know and I think every investor knows, if we hit those 2024 goals, the valuation from where we sit today to where we will be at that time is materially different.

As you said, we had the benefits of tailwinds while we were building the foundation. That is now done. We are sitting on excess capital. We have a robust pipeline. We have added most of the talent we need. The senior leadership, you've seen the announcement. So if we grow expenses less in TriumphPay in 2023, it's not because we feel this need to manage the overall enterprise to a certain short-term level of profitability, it's just because we've already made the investments.

So we know we have to be profitable. We're not a private equity-backed firm that can for 3 years disappear and go do something and then hope it works out at the end. That's not our story. We have to be profitable between here and there, and we will be profitable between here and there. But we will not hesitate to be opportunistic and to invest in the best talent and technology it takes to deliver on the promise. So that's how we think about it. That gives you some guide rails for how we think about expense growth in TriumphPay which will obviously moderate expense growth for the entire enterprise. And whatever happens in the short term will happen. And we kind of view that as noise as long as we're profitable and we maintain credit quality. We are committed to what we told you our goals are because if we hit those, then everyone wins.

Operator

And our next question comes from Brad Milsaps from Piper Sandler.

Bradley Jason Milsaps - *Piper Sandler & Co., Research Division - MD & Senior Research Analyst*

Just wanted to follow up on the last points you made, Aaron, regarding TPay. I think at one point you mentioned that at $100 million of revenue, you might be at 50% of this duration in that business. But it looks like at the end of the day you're running at about $60 million in annualized expenses. You just said you expect 20% growth there. So that would put you closer to $70 million. Am I thinking about that, that business, you sort of have maybe -- at $100 million of revenue, that would imply maybe 20-ish kind of million of net income? Or am I too low there? Some of those expenses going to fall out. Just really trying to speak about the contribution when you get to that level with maybe a little bit less than I initially thought, but hopefully, you can kind of clear that up for me a little bit.

William Bradley Voss - *Triumph Bancorp, Inc. - Executive VP & CFO*

Brad, thanks for that. I'll take that one. What we're aiming to do with TriumphPay exiting 2024 is 3 key metrics: number one, $100 million in revenue, as you mentioned; number two, EBITDA positive, so we want that number to be a contributor rather than a drag on our earnings; and number three, we think that it takes about $75 billion in payment volume to get there. But the expense load that we have to add between now and then, that provides some guardrails and it's going to force some discipline in order to be EBITDA positive at that point. But the margins are -- at that level are not going to be 50%. That's for another day when we're at bigger scale.

Aaron P. Graft - *Triumph Bancorp, Inc. - Founder, Vice Chairman, President & CEO*

And a couple of things to add on to that, Brad, is as we think about TriumphPay and we think about long-term targets, we think this business will -- should and it will operate at over a 70% gross margin, which is different than how -- bank investors talk about efficiency ratios. Payment investors and fintech investors talk about gross margins. And this is a SaaS or a payments network business. That's our target. So that's number one.

Number two, if you just step back and do unit economics, if you take $75 billion in payments, and you assume you're going to generate $100 million in revenue, and you assume the average invoice size is $1,800, and none of us know what it will be but if you just assume that to be true, that's 42 million invoices. And to get to $100 million, that's $2.40 of revenue per invoice.

Our firm conviction is that the revenue per invoice as the value proposition continues will be far greater than that. And you can see that if you look at the revenue per cohort. The longer we stay with a customer, the more value proposition that is born. And so in year 1, at that volume, could it take $75 billion to generate $100 million in revenue? Yes. Do I think it's plausible that, that same volume of payments generates 1.3x that revenue in the subsequent year? I do. I do because we see fraud mitigation and carrier visibility and some other things we haven't even talked about that are value propositions we deliver back to our payers and our payees.

So the short answer is, in exiting 2024, it will not be a 50% efficiency ratio. And as we said, that's not a terminal goal, that's an interim goal of being EBITDA positive and delivering the brand promise to the market. But over the longer term, every decision we make goes through the grid of can we do this at scale, and can we do this at the profit margins required to get the valuation we think this deserves. And I'm absolutely convinced we will achieve that.

Melissa Forman - *TBK Bank, SSB - President of TriumphPay*

And Aaron, if I can just add on to that, you spoke about the fraud mitigation. When we started the payments network, we knew what our core transaction was going to be to create the transparency and deliver the source of truth to all participants in that transaction. Very clear direction, we knew what we had to go build and what we could do with it.

But what we're learning is the ability that we have and the view that we have on carriers and their transactions, the possibilities are limitless. There is so much activity -- fraudulent activity in the industry today. And as times get tougher in transportation, they're just going to continue to grow. And we see daily opportunities for us to be able to share information with our customers about carriers that have bad behavior or that look like they're doing something wrong. And so we're getting asked every day what else can you do, can you show us this information, can you help us here, can you help us there. And we're taking that to the table and figuring out how can we bring additional value to our existing clients and help them mitigate the fraud and the risk associated with these transactions. So it's exciting.

Aaron P. Graft - *Triumph Bancorp, Inc. - Founder, Vice Chairman, President & CEO*

Exactly.

Bradley Jason Milsaps - *Piper Sandler & Co., Research Division - MD & Senior Research Analyst*

Okay. Aaron, you spent some time in your letter talking about how you guys are underwriting equipment suites. You mentioned that some small carriers are choosing to maybe park their trucks at certain invoice prices. Can you maybe add a little more color? Are you worried about maybe, I won't say credit issues, but truckers were into problems where you're having to deal with equipment that could be upside down? Are we far from that? Just curious if you could spend some time in talking about sort of how you guys are approaching that space in your letter.

Todd N. Ritterbusch - *TBK Bank, SSB - President*

I'll take that. Yes, thank you for the question. So in the letter, we talked a lot about the risk mitigation or we talked to some extent about the risk mitigation efforts we're taking. It is important to recognize that as equipment prices have gone up, we haven't always continued to finance the equipment at 100%, so we're requiring down payments now, which gives us some support in the event that equipment prices decline. We also have the benefit of having deep visibility into the financials themselves and long relationships with a lot of the equipment finance borrowers that we serve. And so we feel really comfortable that those players will be able to withstand the cycle. And at the end of the day, the reality is that we see the economics of those businesses looking much better than the industry as a whole. So we do feel comfortable about where we stand and where we're headed.

Bradley Jason Milsaps - *Piper Sandler & Co., Research Division - MD & Senior Research Analyst*

And Aaron, maybe final one for me is also you highlighted in the letter, you pointed out very boldly that you guys have, in your opinion, $200 million of capital that would be above your internal targets. And you highlight maybe M&A as a possibility or share buybacks. Can you kind of talk about your appetite for both and what the stock growth is, where -- if you might be more aggressive with the share buyback?

Aaron P. Graft - *Triumph Bancorp, Inc. - Founder, Vice Chairman, President & CEO*

Yes. And we highlighted it for a purpose because it's something we talk a lot about internally. But there are 2 possible uses for this capital. And I think we have been intentional over the last 3 years about stewarding our capital. And we -- if you remember the HubTran acquisition, we stewarded our capital in order to be able to do that without diluting investors.

So now where we sit today, we have twice that amount of capital. There are really 2 options, and they're not mutually exclusive. Perhaps we will do them side by side. Number one is we will invest to expand the reach and the resiliency of the payments network, and that would specifically be in the shipper space, which includes investing in, thinking about creating freight audit and pay opportunities that we can -- that we think brings value and more redundancy and carriers into our network. And so we continue to look at those opportunities. And the good news about what's happened in the market is revenue multiples for companies in that space don't look like they did a year ago because money is actually worth something now.

The second is, and we've said this before, the ability to buy back our own shares if the market values the intrinsic value of TriumphPay at 0, that's a pretty simple analysis for us. So what's interesting now, and this is where we talked about taking advantage of headwinds, both of those are very real and very actionable. And I can't tell you the exact timing of when and how and what, but you will see activity for us between now and the end of the year on one or possibly both of those fronts because we firmly believe that the enterprise value of TriumphPay alone at that 2024 target is greater than our entire market cap right now. And not to mention we have a very profitable community bank that has really good deposit quality that we've invested in, and we have a factoring company that, notwithstanding headwinds, is going to generate 3% to 6% pretax ROAs at scale. There just aren't a whole lot of other people who can do that.

And so revenue volatility, it's not fun, like none of us enjoy coming in here or talking to you when we miss expectations. But if you were to get us all in a room and say do you believe in the long-term value proposition and do you think you can take advantage of what the market is doing right now to a person, we would all say absolutely. And so I think you'll see us take steps as opportunities are given to us. And right now, I think there's an opportunity in front of us to deploy capital in a way that will create long-term value for our shareholders.

Operator

And our next question, we'll go back to Matt Olney from Stephens.

Matthew Covington Olney - *Stephens Inc., Research Division - MD & Analyst*

Yes. On TPay, I'm thinking more about fees. And I think 1 year ago, you disclosed a framework of various fees that you hope to achieve longer term at TPay, factor subscription fees, network fees, syndication fees. And I guess on this call today, you kind of mentioned this is kind of an evolving topic. It's not something that's set-in stone. But now that TPay volumes are ramping compared to a year ago, curious if you have any updated thoughts on or views of those fees, or does that framework you laid out a year ago, is that still a good framework for us to assume as we think about the next few years in fees from TPay?

Melissa Forman - *TBK Bank, SSB - President of TriumphPay*

Yes, Matt. Yes, so the framework that we laid out is still holding true to our plan. And the subscription fees, network fees, syndication fees and the discounts for QuickPay are all there. So it is playing out pretty close to exactly how we had it modeled. And when you look at the new clients that we're bringing on board, we are using that framework. As we work with our existing clients when they add different services that we have to offer, we're using that framework. So it is lining up exactly where we anticipated it to be, and you'll see more of that revenue come to fruition in 2023 as we had planned out.

Aaron P. Graft - *Triumph Bancorp, Inc. - Founder, Vice Chairman, President & CEO*

Yes, that's exactly right. And Matt, like take this quarter for example. There was a revenue drop at TriumphPay. Now a contributing factor to that is the overall market softened. But another contributing factor is, in addition to everything we talked about, for the largest creditworthy freight brokers, some of them want to use our balance sheet to extend their days to pay. In other words, they're going to pay a carrier on day 30 but collect -- or we would pay the carrier on their behalf, but they would not pay us until day 60. And you saw some of that in this quarter, brokers who we have done that for, who are long-term valuable clients, who appreciated that service but, because of the slowing market and because of capital injections into their business, didn't necessarily need that service.

And so along the journey, there will be plug and play. I mean that's what we -- that's the value proposition. When you insert yourself into the supply chain and you are a bank and you have access to the ability to deliver financing solutions invisibly at the point of sale to whomever needs it, whether it's a payer or a payee, your ability to monetize the same transaction and to deliver value on the same transaction goes both ways.

So we think it works very much like we said. I mean if you think about just a specific invoice and just the wide disparity of what the revenue we generate on a specific invoice might be, if we're just doing audit on an invoice, it might be $0.10, $0.20, $0.30, $0.40. If however we're facilitating a QuickPay on that same invoice that sits on the balance sheet of our freight broker client, the value to try and pay more might be closer to $10. And so you're looking at aggregate numbers and you're distilling it down to some median number but understand that underneath that there's a wide disparity based upon what people need us to do. Do you need us to audit? Do you need us to pay? Do you want us to create the network transaction, and do you need our balance sheet? Or do you need us to facilitate the QuickPay to sit on your balance sheet? We're good with any of those because we know at scale, we have a certain fixed cost to do what we do to make sure the invoice is real, to maintain the integrations we need on both sides of the network.

And so the more things you ask us to do, we are glad to do them because the incremental profitability goes up substantially. So we've laid it out for you the best we can. You just need to know that different constituents use our network differently just like, I think, different constituents use the Visa network for different things. The core of it, the core of the transaction is using structured data to have absolute visibility between a payer and a payee about what's due and to whom it's due and getting out of the business of making educated guesses. There will always be the need for that. The factoring industry is going to continue, it's going to persist, and it will probably continue to grow not just because of what TriumphPay is doing for it but because we know there are always going to be transactions that don't flow through TriumphPay. Not every payer is going to be on the network as hard as we may try to do that.

So I think what the guidance we've given you, you can depend on. But don't miss the fact that the longer we go, the more value there is on the same transaction as people become more accustomed to the set of tools we give them for how they can accelerate the payment, how they can recognize the payment, how they can create supply chain finance opportunities for themselves if they're on the payer side of the transaction. All of that comes together in the ether of this overall revenue per invoice. And as we go, we'll continue to give you disclosure on what we're seeing. But what we are currently seeing is the ability to monetize an individual invoice continues to go up because there's more value we can deliver back to the market on that individual invoice.

Matthew Covington Olney - *Stephens Inc., Research Division - MD & Analyst*

Yes. Okay. I appreciate that, Aaron. Then I guess on TPay, going back to the expense discussion, I appreciate kind of the commentary that you've already given us for the puts and takes for expense growth for next year. I appreciate there are some fixed costs in the TPay model, but it also seems like there's some variable costs through sales commissions. And I assume those sales commissions are still ramping as you bring on more Tier 1s. But at some point, it feels like there's going to be some relief there, and there could be an inflection. Any color on when that inflection could be as far as the sales commissions through the TPay expense line?

Melissa Forman - *TBK Bank, SSB - President of TriumphPay*

I'll take that, Aaron. So Matt, the way we have structured our sales commissions is we are front-loading that. So as we bring on Tier 1s, you'll see that commission hit the expense lines in the first 12 to 18 months of the life of that account, and then it goes away. And so as we keep bringing on new Tier 1s, Tier 2s, every broker accounts and is meaningful to the network, you'll see those commissions happen. But for the existing clients, it will start to fall off as you won't see any reoccurring expenses to that effect.

Aaron P. Graft - *Triumph Bancorp, Inc. - Founder, Vice Chairman, President & CEO*

Yes. Melissa is exactly right, Matt. I mean, I think, think about it in 2 dimensions. At some point, it won't be Q4 of 2024. But at some point in the year or 2 thereafter, we will have touched brokers who control 90% of all freight. Okay? There's a long tail of 8,000, 9,000 freight brokers who control 10% of all freight, but the top 1,000 control 90%. And you can know that all of them know our name. We probably bought dinner for most of them. And so that day is coming when you've touched the majority of that network, and it's not 10 years out in the future, right? It's 3, 4 years in the future.

Where I hope you see commissions, beyond that is in our growth in the shipper market. I mean we have Fortune 100 companies who use us to pay their carriers. We believe that, that $250 billion shipper market is not just ancillary to the payments network but the other side of it. And so if we see commissions shift from largely the brokerage community, the shipper community, then we win because that just drives network market penetration. So we'll do our best to explain to you, hey, this commission is tied to these brokers. And look, in the first half of next year, you're going to see commissions go up. And I'm celebrating that because to date, we haven't lost a customer. This is an incredibly sticky value proposition, and you have to invest to get there.

Had I known when we started, how much we were going to have to invest to get here, I probably would have coughed a little. But now that we're in it and we're seeing it and we're winning, those are dollars I'm happy to spend because you've got to go live on the end of it. And you have a customer who the longer they're with you the more value you create.

Matthew Covington Olney - *Stephens Inc., Research Division - MD & Analyst*

Yes. Okay. Aaron. And then just lastly, in the shareholder letter, you disclosed the credit loss in the third quarter. And it sounds like that loss was from the liquid credit portfolio. And as you guys are aware that investors are hyper focused on credit quality in the banking industry. Any color you can give us as far as the industry or the borrower, anything that would be interesting to us as far as potential credit weakness?

William Bradley Voss - *Triumph Bancorp, Inc. - Executive VP & CFO*

Matt, that was -- that $2.7 million provision was related to a single borrower that had issued debt about 6 weeks before cutting their guidance in half and firing their CEO. So there were some of the various things going on at that borrower. They caught us and a lot of other institutional lenders off guard. We, as a result of that, did a pretty deep dive into the rest of that liquid credit portfolio. It's about $225 million in exposure across 40 different obligors. And there's nothing else in that portfolio that gives us pause that we may have issues like we did with this particular one. We really do view it as a one-off situation.

The team that manages that portfolio for us, it's a 4-person team that's been with us for about 3 years and has brought a ton of value to the organization. If you recall, during the early COVID period in the spring of [2000], we were able to leverage that team to invest in hundreds of millions of dollars of securities and loans at just fire sale prices. That accrued value to our shareholders pretty quickly. And we've been very happy with what that team has done for us. We continue to like the flexibility and the opportunistic nature that we can deploy in that business. So to answer your question succinctly, no, we don't see any broader credit concerns that were a result of that, and we do really feel like it was an isolated event.

Aaron P. Graft - *Triumph Bancorp, Inc. - Founder, Vice Chairman, President & CEO*

Yes. Matt, exactly what Brad said, for a loan to go underwritten by 2 of the largest banks in the world, to go bad in 60 days, I mean, that is a one-off event. Like that's not we were out there taking undue risk. That was in this instance, the management team was able to convince some very large investors and institutions to issue debt on their behalf. I mean that, look, we have a $4.3 billion loan book. There's going to be things that surprise you. This is not systemic. This is an isolated event. I'm sure there's going to be litigation against the underwriters of this. But if I look at that whole portfolio or our entire portfolio, I mean, we -- you see this. We've got to be one of the few banks in your coverage universe whose loan portfolio has shrunk over the last few years. And that's not because we don't see lending opportunities and not because we don't know how to lend, it's because we're being very intentional in what we do. And so we can be intentional, and we can be right 99% of the time. This is the 1%, where we thought we knew all the facts, so did a lot of other people smarter than us. We didn't, we get it, we'll move on but ...

Todd N. Ritterbusch - *TBK Bank, SSB - President*

But I'd just like to add that, yes, we took a reserve here, but we're a long way from thinking that we would necessarily take a loss here. There's a lot of information that's yet to come forward on this, and there's a lot of strength in the company that's behind this deal as well. So I think that this is definitely an anomaly. This is not a loss. This is a reserve for the purpose of being conservative right now, and we'll work through the situation.

Aaron P. Graft - *Triumph Bancorp, Inc. - Founder, Vice Chairman, President & CEO*

Yes, exactly.

Unidentified Company Representative

There are no further questions on this line at this time. We'll now move over to the phone line for further Q&A. Thank you.

Operator

(Operator Instructions) We will take our first question from Joe Yanchunis with Raymond James.

Joseph Peter Yanchunis - *Raymond James & Associates, Inc., Research Division - Senior Research Associate*

I apologize for not being on video. I haven't put my face on yet.

Aaron P. Graft - *Triumph Bancorp, Inc. - Founder, Vice Chairman, President & CEO*

So we get it.

Joseph Peter Yanchunis - *Raymond James & Associates, Inc., Research Division - Senior Research Associate*

So with Schneider now fully integrated with audit capabilities, how large of a contribution do you expect them to have in boosting the level of number -- the number of conforming transactions?

Melissa Forman - *TBK Bank, SSB - President of TriumphPay*

Yes, good question. So Schneider is a very large organization with multiple divisions. And so what I want to make sure that we're very clear about is that Schneider has been added to the payments network for one portion of their logistics division. And what we see that happen in every implementation that we do where we start in one section and begin to grow that throughout the enterprise.

So in terms of Schneider's total volume, you won't see 100% of that be conforming out of the gate. But as we continue to add that functionality and those features to the rest of their divisions, you'll see it start to grow.

Aaron P. Graft - *Triumph Bancorp, Inc. - Founder, Vice Chairman, President & CEO*

Exactly.

Joseph Peter Yanchunis - *Raymond James & Associates, Inc., Research Division - Senior Research Associate*

Got it. And I was hoping to get a better understanding of TPay's capacity to onboard additional clients. I mean, based on your comments from earlier, it sounds like it's going to take a year to bring on that $15 billion in annualized payment volume you outlined last quarter. And so in order to reach your $75 billion target by year-end '24 would apply a pretty meaningful volume ramp in 3Q '23 and beyond. Can you help me better understand how you'll be able to accelerate the onboarding process?

Melissa Forman - *TBK Bank, SSB - President of TriumphPay*

Yes. What I would say is that we have a team ready and waiting to onboard all of the brokers. And so as we build our pipeline, we'll have the smaller Tier 2, Tier 3 brokers that come into the network. We're actively onboarding them each and every day. Our team is deployed all over the country working with customers to get that process done.

What we're saying on the Tier 1s, those are more lumpy, and you're going to see those happen in the first half, second half of next year. It's not a matter of what we have to onboard all at once. There will be continuous onboarding throughout the year. It's just those larger ones tend to add $3 billion, $4 billion, $5 billion all at once when they come on to the network. And so the team is actively deployed. We have the capacity to add more brokers to the network. But what we have to understand is that the capacity of our customers also has to be kept in mind. So we have to --

we can only work as fast as they're available to do so. And so we stack up all of our implementations to ensure that our team is fully deployed and busy all the time but also account for when our large Tier 1s are ready to go, we have the team available to jump right on it.

Todd N. Ritterbusch - *TBK Bank, SSB - President*

Yes, Melissa, in our conversations, it seems like a lot more of the conversation is around the clients' ability to handle the integration, not ours. So yes.

Melissa Forman - *TBK Bank, SSB - President of TriumphPay*

Yes, you're absolutely right.

Aaron P. Graft - *Triumph Bancorp, Inc. - Founder, Vice Chairman, President & CEO*

And just what Melissa has done such a great job of laying the foundation of, and again, you see this in the expense ramp, it's not -- we don't integrate them one at a time. It's a multifront war. So it's not like, oh, this one has to go, then this one and this one. There are multiple teams of systems engineers working alongside the client. So it may be in a given week, multiple ones go live or multiple divisions of a Tier 1 go live. Don't think of it as linear. Like it's a thread of multiple work streams happening at the same time, which is why there had to be so much investment that Melissa led us through and the team we built to get here.

So we can't tell you exactly when that wave will crest. All we can tell you is a tremendous amount of work has been done to prepare us for it, and we expect to start harvesting some -- the fruit of some of that work in 2023 and really, I think, in the first half.

Joseph Peter Yanchunis - *Raymond James & Associates, Inc., Research Division - Senior Research Associate*

Great. I appreciate it. And then kind of going back to the expenses, it looks like TPay expenses declined a little bit in the quarter. What drove that?

William Bradley Voss - *Triumph Bancorp, Inc. - Executive VP & CFO*

So the primary thing that drove that, and we didn't call this out in the letter but there was about $1.2 million in expenses in the second quarter that were borne by the TPay organization that would be -- that have been more appropriately borne by the bank. So we unwound that in the third quarter. So that accounts for the drop that you saw in Q3.

Joseph Peter Yanchunis - *Raymond James & Associates, Inc., Research Division - Senior Research Associate*

I appreciate it. And I know you previously guided to TBC being able to generate $240 million in revenue in 2022. I was wondering if you might be able to provide an update on that outlook and then as well discuss your ability to purchase more invoice prices to offset potential decline in spot rates. I'm just trying to understand the process and purchasing more invoices to help support TBC.

Geoffrey P. Brenner - *Triumph Bancorp, Inc. - CEO – Triumph Business Capital*

Yes, I'll take that one. So there's no material change in our revenue forecast. So that's unchanged, and we're on track. I think in terms of growing the number of invoices we purchased, it relates to the strategy of where you want to grow, and this was outlined in our letter. We serve all of the segments, but there are interesting differences between those segments. So as you saw in the letter, we have 8,000 clients that pay us less than $1,000 a month in revenue. They generate fewer invoices, and per client revenue is just very low. We've been very successful going upstream, and we're one of only a few transportation factors who can even do that.

And going to the larger fleets, the medium-sized fleets, discussing a value proposition that's just different than factoring, you're also talking about how they finance their trucks, how they fuel their trucks, how they ensure their trucks and integrating all of that into a platform that's intuitive and digitally backed and makes sense with the banking of a bank is just a competitive advantage. And we have great headway with that larger fleet. That's what's explaining, I think, when you look at our data, we have headwinds, average invoice prices are down, our client count took a dip. But if you look at the total number of invoices being purchased is going up, that's indicative of winning out that larger fleet segment.

So that's the strategy. And the revenue per client in that larger segment is 10x what we have in the small segment. So that's the game. That's how we'll win.

Joseph Peter Yanchunis - *Raymond James & Associates, Inc., Research Division - Senior Research Associate*

Okay. I appreciate it. Sorry for jumping around here. I just have one more question, so let me sneak in. Kind of going back to the M&A discussion, I guess how many potential acquisition targets are out there that you think check all the boxes for you guys?

Aaron P. Graft - *Triumph Bancorp, Inc. - Founder, Vice Chairman, President & CEO*

Yes, good question. So if we think about -- I've been specific about the shipper market as an area of interest for the reasons I laid out. There are 5 freight audit and pay providers that are upsized. We're an investor in one of them, Intelligent audit, which is having a great year, and we're very proud of what they're doing. So there's not 100 that matter. It's somewhat consolidated.

The other places you might invest is in -- and if you think about all the technology companies that have been formed for -- to do virtual wallets and payments and all this freight tech, as long as it's in post load because we don't do preload, we don't do on-load, that's what our clients do. Our view is when the trailer is dropped and the proof of delivery is signed, that's when we take over.

And so what does that include? Well, that includes audit, payment and then how does the carrier spend the payment. There's a virtual wallet, whether it's bank accounts, there's things we're working on organically, and there are players out there that could complement that. And so those would be another opportunity set.

But I think if you were to consolidate all of it, people who try to compete with what we're doing in the network, to people who have a customer experience for the carrier on the back end, to the people who provide legacy freight audit and pay services, if you looked at that whole universe, you're talking about 10 names. And we're not going to do 10 deals. We might do 0 deals. But it's not a huge universe of opportunities, and we want to pick our spots. Things that we can't build ourselves or haven't built ourselves, that's great. A lot of it is being built. There's stuff that we're working on in Triumph Business Capital that take the customer experience for all carriers and make it incredibly intuitive, as Geoff said, and change the dynamics. Well, we kind of think we should deliver that to the market rather than go buy something that's not as good.

So it's less than 10 names. And the 11th name is our own stock, right, which is a pretty easy M&A discussion because we know where the skeletons are in our closet. Everybody does, right? You go read our 10-K. And so that's just a valuation exercise of is this the appropriate time to step in meaningfully to start buying shares back from people who are thinking short term? It may be.

Operator

(Operator Instructions) There are no further questions on the phone lines. We can head back to the studio now.

Aaron P. Graft - *Triumph Bancorp, Inc. - Founder, Vice Chairman, President & CEO*

I just want to conclude by saying thank you all for joining us, and we look forward to speaking to you again soon. Have a great day.