

FIRST BANCORP /PR/  
Form 10-Q  
August 09, 2018

**UNITED STATES  
SECURITIES AND EXCHANGE COMMISSION**

**Washington, DC 20549**

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**FORM 10-Q**

(Mark One)

**QUARTERLY REPORT PURSUANT TO SECTION 13 OR 15(D) OF THE SECURITIES  
EXCHANGE ACT OF 1934**

For the quarterly period ended June 30, 2018

**TRANSITION REPORT PURSUANT TO SECTION 13 OR 15(D) OF THE SECURITIES EXCHANGE  
ACT OF 1934**

For the transition period from \_\_\_\_\_ to \_\_\_\_\_

COMMISSION FILE NUMBER 001-14793

**First BanCorp.**

(EXACT NAME OF REGISTRANT AS SPECIFIED IN ITS CHARTER)

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(State or other jurisdiction of  
incorporation or organization)

(I.R.S. employer

identification number)

1519 Ponce de León Avenue, Stop 23

00908

Santurce, Puerto Rico

(Zip Code)

(Address of principal executive offices)

(787) 729-8200

(Registrant's telephone number, including area code)

Not applicable

(Former name, former address and former fiscal year, if changed since last report)

Indicate by check mark whether the registrant (1) has filed all reports required to be filed by section 13 or 15(d) of the Securities Exchange Act of 1934 during the preceding 12 months (or for such shorter period that the registrant was required to file such reports), and (2) has been subject to such filing requirements for the past 90 days.

Yes No

Indicate by check mark whether the registrant has submitted electronically and posted on its corporate Web site, if any, every Interactive Data File required to be submitted and posted pursuant to Rule 405 of Regulation S-T (§232.405 of this chapter) during the preceding 12 months (or for such shorter period that the registrant was required to submit and post such files).

Yes No

Indicate by check mark whether the registrant is a large accelerated filer, an accelerated filer, a non-accelerated filer, a smaller reporting company, or emerging growth company. See the definitions of "large accelerated filer," "accelerated filer," "smaller reporting company," and "emerging growth company" in Rule 12b-2 of the Exchange Act.

Large accelerated filer

Accelerated filer

Non-accelerated filer  
company

(Do not check if a smaller reporting company)

Smaller reporting

Emerging

growth company

If an emerging growth company, indicate by check mark if the registered has elected not to use the extended transition period for complying with any new or revised financial accounting standards provided pursuant to Section 13 (a) of the Exchange Act.

Indicate by check mark whether the registrant is a shell company (as defined in Rule 12b-2 of the Exchange Act).  
Yes      No

Indicate the number of shares outstanding of each of the issuer's classes of common stock, as of the latest practicable date.

Common stock: 217,183,977 shares outstanding as of July 31, 2018.

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**SIGNATURES**

## Forward Looking Statements

This Form 10-Q contains forward-looking statements within the meaning of Section 27A of the Securities Act of 1933, as amended (the “Securities Act”), and Section 21E of the Securities Exchange Act of 1934, as amended (the “Exchange Act”), which are subject to the safe harbor created by such sections. When used in this Form 10-Q or future filings by First BanCorp. (the “Corporation”) with the U.S. Securities and Exchange Commission (“SEC”), in the Corporation’s press releases or in other public or stockholder communications, or in oral statements made with the approval of an authorized executive officer, the words or phrases “would,” “intends,” “will likely result,” “expect,” “should,” “anticipate,” “look forward,” “believes,” and other terms of similar meaning or import in connection with any discussion of future operating, financial or other performance are meant to identify “forward-looking statements.”

First BanCorp. wishes to caution readers not to place undue reliance on any such “forward-looking statements,” which speak only as of the date made, and to advise readers that these forward-looking statements are not guarantees of future performance and involve certain risks, uncertainties, estimates, and assumptions by us that are difficult to predict. Various factors, some of which are beyond our control, could cause actual results to differ materially from those expressed in, or implied by, such forward-looking statements.

The two hurricanes that affected the Corporation’s service areas in 2017 are discussed below in Note 2 to the financial statements and in various sections of “Management’s Discussion and Analysis of Financial Condition and Results of Operations.” These events caused significant uncertainties, the outcome of which will impact the Corporation’s future results.

Factors that could cause actual results to differ from those expressed in the Corporation’s forward-looking statements include, but are not limited to, risks described or referenced below in Part II, Item 1A. “Risk Factors” and the following:

- the actual pace and magnitude of economic recovery in the Corporation’s service areas that were affected by two hurricanes during 2017 compared to Management’s current views on the economic recovery;
- uncertainties about the effectiveness and the timing of the completion of the rebuilding taking place in the regions affected by the hurricanes, including the rebuilding of the public infrastructure, such as Puerto Rico’s power grid, how and the extent to which government, private or philanthropic funds will be invested in the affected communities, how many displaced individuals will return to their homes in both the short- and long-term, and what other demographic changes will take place, if any;

- uncertainty as to the ultimate outcomes of actions taken, or those that may be taken, by the Puerto Rico government, or the oversight board established by the Puerto Rico Oversight, Management, and Economic Stability Act (“PROMESA”) to address Puerto Rico’s financial problems, including the filing of a form of bankruptcy under Title III of PROMESA, which provides a court debt restructuring process similar to U.S. bankruptcy protection, and the effects of measures included in the Puerto Rico government fiscal plan, or any revisions to it, on our clients and loan portfolios;
- the ability of the Puerto Rico government or any of its public corporations or other instrumentalities to repay its respective debt obligations, including the effect of payment defaults on the Puerto Rico government general obligations, bonds of the Government Development Bank for Puerto Rico (the “GDB”) and certain bonds of government public corporations, and recent and any future downgrades of the long-term and short-term debt ratings of the Puerto Rico government, which could exacerbate Puerto Rico’s adverse economic conditions and, in turn, further adversely impact the Corporation;

- uncertainty about whether the Federal Reserve Bank of New York ( the “New York FED” or “Federal Reserve”) will continue to provide approvals for receiving dividends from the Corporation’s subsidiary, FirstBank Puerto Rico (“FirstBank” or the “Bank”), or making payments of dividends on non-cumulative perpetual preferred stock, or payments on trust preferred securities or subordinated debt, incurring, increasing or guaranteeing debt or repurchasing any capital securities, despite the consents that have enabled the Corporation to receive quarterly dividends from FirstBank since the second quarter of 2016, to pay quarterly interest payments on the Corporation’s subordinated debentures associated with its trust preferred securities since the second quarter of 2016, and to pay monthly dividends on the non-cumulative perpetual preferred stock since December 2016;
- a decrease in demand for the Corporation’s products and services and lower revenues and earnings because of the continued recession in Puerto Rico;
- uncertainty as to the availability of certain funding sources, such as brokered certificates of deposit (“brokered CDs”);
- the Corporation’s reliance on brokered CDs to fund operations and provide liquidity;
- the risk of not being able to fulfill the Corporation’s cash obligations or resume paying dividends to the Corporation’s common stockholders in the future due to the Corporation’s need to receive regulatory approvals to declare or pay any dividends and to take dividends or any other form of payment representing a reduction in capital from FirstBank or FirstBank’s failure to generate sufficient cash flow to make a dividend payment to the Corporation;
- the weakness of the real estate markets and of the consumer and commercial sectors and their impact on the credit quality of the Corporation’s loans and other assets, which have contributed and may continue to contribute to, among other things, high levels of non-performing assets, charge-offs and provisions for loan and lease losses, and may subject the Corporation to further risk from loan defaults and foreclosures;
- the ability of FirstBank to realize the benefits of its net deferred tax assets;
- adverse changes in general economic conditions in Puerto Rico, the United States (“U.S.”), the U.S. Virgin Islands (“USVI”), and the British Virgin Islands (“BVI”), including the interest rate environment, market liquidity, housing absorption rates, real estate prices, and disruptions in the U.S. capital markets, which reduced interest margins and affected funding sources, and have affected demand for all of the Corporation’s products and services and reduced the Corporation’s revenues and earnings and the value of the Corporation’s assets, and may continue to have these effects;

- an adverse change in the Corporation's ability to attract new clients and retain existing ones;
- the risk that additional portions of the unrealized losses in the Corporation's investment portfolio are determined to be other-than-temporary, including additional impairments on the Corporation's remaining \$8.1 million of the Puerto Rico government's debt securities;
- uncertainty about regulatory and legislative changes for financial services companies in Puerto Rico, the U.S., the USVI and the BVI, which could affect the Corporation's financial condition or performance and could cause the Corporation's actual results for future periods to differ materially from prior results and anticipated or projected results;



- changes in the fiscal and monetary policies and regulations of the U.S. federal government and the Puerto Rico and other governments, including those determined by the Board of the Governors of the Federal Reserve System (the “Federal Reserve Board”), the New York FED, the Federal Deposit Insurance Corporation (“FDIC”), government-sponsored housing agencies, and regulators in Puerto Rico, and the USVI and BVI;
- the risk of possible failure or circumvention of controls and procedures and the risk that the Corporation’s risk management policies may not be adequate;
- the risk that the FDIC may increase the deposit insurance premium and/or require special assessments to replenish its insurance fund, causing an additional increase in the Corporation’s non-interest expenses;
- the impact on the Corporation’s results of operations and financial condition of acquisitions and dispositions;
- a need to recognize impairments on the Corporation’s financial instruments, goodwill or other intangible assets relating to acquisitions;
- the risk that downgrades in the credit ratings of the Corporation’s long-term senior debt will adversely affect the Corporation’s ability to access necessary external funds;
- the effect on the Corporation’s businesses, business practices and results of operations of a potential higher interest rate environment;
- uncertainty as to whether FirstBank will be able to satisfy its regulators regarding, among other things, its asset quality, liquidity plans, maintenance of capital levels and compliance with applicable laws, regulations and related requirements; and
- general competitive factors and industry consolidation.

The Corporation does not undertake, and specifically disclaims any obligation, to update any “forward-looking statements” to reflect occurrences or unanticipated events or circumstances after the date of such statements except as required by the federal securities laws.

Investors should refer to the Corporation's Annual Report on Form 10-K for the year ended December 31, 2017, as well as "Part II, Item 1A, Risk Factors," in this Quarterly Report on Form 10-Q, for a discussion of such factors and certain risks and uncertainties to which the Corporation is subject.

**FIRST BANCORP.**  
**CONSOLIDATED STATEMENTS OF FINANCIAL CONDITION**  
**(Unaudited)**

|   | <b>June 30,</b> | <b>December</b> |
|---|-----------------|-----------------|
|   | <b>2018</b>     | <b>31, 2017</b> |
| (In thousands, except for share information)  |                 |                 |
| <b>ASSETS</b>   |                 |                 |
| Cash and due from banks   | \$ 790,809      | \$ 705,980      |
| Money market investments:   |                 |                 |
| Time deposits with other financial institutions   | 300             | 3,126           |
| Other short-term investments  | 97,290          | 7,289           |
| Total money market investments  | 97,590          | 10,415          |
| Investment securities available for sale, at fair value:                                |                 |                 |
| Securities pledged that can be repledged  | 241,378         | 350,123         |
| Other investment securities   | 1,794,632       | 1,540,893       |
| Total investment securities available for sale  | 2,036,010       | 1,891,016       |
| Investment securities held to maturity, at amortized cost:                              |                 |                 |
| Securities pledged that can be repledged  | -               | -               |
| Other investment securities   | 150,486         | 150,627         |
| Total investment securities held to maturity, fair value of \$135,430 (2017- \$131,032) | 150,486         | 150,627         |
| Other investment securities   | 43,400          | 43,119          |
| Loans, net of allowance for loan and lease losses of \$222,035<br>(2017 - \$231,843)    | 8,418,256       | 8,618,633       |
| Loans held for sale, at lower of cost or market   | 80,815          | 32,980          |
| Total loans, net  | 8,499,071       | 8,651,613       |
| Premises and equipment, net   | 144,507         | 141,895         |
| Other real estate owned   | 143,355         | 147,940         |
| Accrued interest receivable on loans and investments                                    | 47,171          | 57,172          |
| Other assets  | 432,463         | 461,491         |
| Total assets  | \$ 12,384,862   | \$ 12,261,268   |
| <b>LIABILITIES</b>  |                 |                 |
| Non-interest-bearing deposits   | \$ 2,317,149    | \$ 1,833,665    |
| Interest-bearing deposits   | 6,900,934       | 7,188,966       |
| Total deposits  | 9,218,083       | 9,022,631       |
| Securities sold under agreements to repurchase  | 200,000         | 300,000         |
| Advances from the Federal Home Loan Bank (FHLB)   | 715,000         | 715,000         |
| Other borrowings  | 184,150         | 208,635         |
| Accounts payable and other liabilities  | 165,950         | 145,905         |
| Total liabilities   | 10,483,183      | 10,392,171      |
| <b>STOCKHOLDERS EQUITY</b>  |                 |                 |

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|  |               |               |
|--|---------------|---------------|
| Preferred stock, authorized, 50,000,000 shares:  |               |               |
| Non-cumulative Perpetual Monthly Income Preferred Stock: issued 22,004,000 shares, outstanding 1,444,146 shares, aggregate liquidation value of \$36,104 | 36,104        | 36,104        |
| Common stock, \$0.10 par value, authorized, 2,000,000,000 shares; issued, 221,724,062 shares (2017 - 220,382,343 shares issued)                          | 22,172        | 22,038        |
| Less: Treasury stock (at par value)  | (453)         | (410)         |
| Common stock outstanding, 217,185,449 shares outstanding (2017 - 216,278,040 shares outstanding)   | 21,719        | 21,628        |
| Additional paid-in capital   | 937,919       | 936,772       |
| Retained earnings, includes legal surplus reserve of \$59,693  | 958,044       | 895,208       |
| Accumulated other comprehensive loss, net of tax of \$7,752  | (52,107)      | (20,615)      |
| Total stockholders equity  | 1,901,679     | 1,869,097     |
| Total liabilities and stockholders equity  | \$ 12,384,862 | \$ 12,261,268 |

The accompanying notes are an integral part of these statements.

**FIRST BANCORP.**  
**CONSOLIDATED STATEMENTS OF INCOME**  
(Unaudited)

|  | <b>Quarter Ended</b> |                | <b>Six-Month Pe</b> |                 |
|--|----------------------|----------------|---------------------|-----------------|
|  | <b>June 30,</b>      |                | <b>Ended</b>        |                 |
|  | <b>2018</b>          | <b>2017</b>    | <b>2018</b>         | <b>2017</b>     |
| (In thousands, except per share information)   |                      |                |                     |                 |
| <b>Interest and dividend income:</b>   |                      |                |                     |                 |
| Loans  | \$ 137,538           | \$ 132,697     | \$ 270,713          | \$ 266,819      |
| Investment securities  | 14,732               | 13,950         | 28,719              | 27,819          |
| Money market investments and interest-bearing cash accounts                            | 3,363                | 727            | 5,619               | 5,619           |
| Total interest income  | 155,633              | 147,374        | 305,051             | 299,257         |
| <b>Interest expense:</b>   |                      |                |                     |                 |
| Deposits   | 16,974               | 16,348         | 33,945              | 33,945          |
| Securities sold under agreements to repurchase   | 2,543                | 2,765          | 4,840               | 4,840           |
| Advances from FHLB   | 3,410                | 2,292          | 6,782               | 6,782           |
| Other borrowings   | 2,235                | 2,065          | 4,320               | 4,320           |
| Total interest expense   | 25,162               | 23,470         | 49,887              | 49,887          |
| Net interest income  | 130,471              | 123,904        | 255,164             | 249,370         |
| <b>Provision for loan and lease losses</b>   |                      |                |                     |                 |
| Net interest income after provision for loan and lease losses                          | 110,935              | 105,808        | 215,084             | 209,483         |
| <b>Non-interest income:</b>  |                      |                |                     |                 |
| Service charges and fees on deposit accounts   | 5,344                | 5,803          | 10,432              | 10,432          |
| Mortgage banking activities  | 4,835                | 4,846          | 9,000               | 9,000           |
| Net gain on sale of investments  | -                    | 371            | -                   | -               |
| Other-than-temporary impairment (“OTTI”) losses on available-for-sale debt securities: |                      |                |                     |                 |
| Total OTTI losses  | -                    | -              | -                   | (12,316)        |
| Portion of OTTI recognized in other comprehensive income (“OCI”)                       | -                    | -              | -                   | -               |
| Net impairment losses on available-for-sale debt securities                            | -                    | -              | -                   | (12,316)        |
| Gain on early extinguishment of debt   | -                    | -              | 2,316               | -               |
| Insurance commission income  | 1,780                | 1,855          | 5,135               | 5,135           |
| Other non-interest income  | 8,513                | 7,674          | 16,373              | 16,373          |
| Total non-interest income  | 20,472               | 20,549         | 43,256              | 43,256          |
| <b>Non-interest expenses:</b>  |                      |                |                     |                 |
| Employees' compensation and benefits   | 39,555               | 38,409         | 80,239              | 78,409          |
| Occupancy and equipment  | 13,746               | 13,759         | 28,851              | 28,851          |
| Business promotion   | 4,016                | 3,192          | 6,592               | 6,592           |
| Professional fees  | 10,193               | 11,800         | 20,253              | 20,253          |
| Taxes, other than income taxes   | 3,637                | 3,745          | 7,493               | 7,493           |
| Insurance and supervisory fees   | 3,701                | 4,855          | 7,556               | 7,556           |
| Net loss on other real estate owned (“OREO”) and OREO operations                       | 5,655                | 3,369          | 5,845               | 5,845           |
| Credit and debit card processing expenses  | 3,766                | 3,566          | 7,303               | 7,303           |
| Communications   | 1,582                | 1,628          | 3,064               | 3,064           |
| Other non-interest expenses  | 4,365                | 4,746          | 9,047               | 9,047           |
| Total non-interest expenses  | 90,216               | 89,069         | 176,243             | 176,243         |
| <b>Income before income taxes</b>  | <b>41,191</b>        | <b>37,288</b>  | <b>82,097</b>       | <b>52,240</b>   |
| <b>Income tax expense</b>  | <b>(10,159)</b>      | <b>(9,290)</b> | <b>(17,917)</b>     | <b>(17,917)</b> |

|   |           |           |           |      |
|---|-----------|-----------|-----------|------|
| <b>Net income</b>                                     | \$ 31,032 | \$ 27,998 | \$ 64,180 | \$ 5 |
| <b>Net income attributable to common stockholders</b> | \$ 30,363 | \$ 27,329 | \$ 62,842 | \$ 5 |
| <b>Net income per common share:</b>                   |           |           |           |      |
| Basic   | \$ 0.14   | \$ 0.13   | \$ 0.29   | \$   |
| Diluted   | \$ 0.14   | \$ 0.13   | \$ 0.29   | \$   |
| <b>Dividends declared per common share</b>            | \$ -      | \$ -      | \$ -      | \$ - |

The accompanying notes are an integral part of these statements.

**FIRST BANCORP.**  
**CONSOLIDATED STATEMENTS OF COMPREHENSIVE INCOME**  
**(Unaudited)**

|   | <b>Quarter Ended</b> |             | <b>Six-Month Period</b> |             |
|---|----------------------|-------------|-------------------------|-------------|
|   | <b>June 30,</b>      |             | <b>Ended</b>            |             |
|   | <b>2018</b>          | <b>2017</b> | <b>2018</b>             | <b>2017</b> |
| (In thousands)  |                      |             |                         |             |
| Net income  | \$ 31,032            | \$ 27,998   | \$ 64,180               | \$ 53,539   |
| Amount reclassified out of accumulated other comprehensive loss per Accounting Standards Update (“ASU”) 2016-01 | -                    | -           | 6                       | -           |
| Other comprehensive (loss) income:  |                      |             |                         |             |
| Unrealized (loss) gain on debt securities on which an OTTI has been recognized                                  | (294)                | 1,127       | 202                     | (1,803)     |
| Reduction of non-credit OTTI component on securities sold   | -                    | 5,678       | -                       | 5,678       |
| Reclassification adjustments for net gain included in net income  | -                    | (371)       | -                       | (371)       |
| Reclassification adjustment for other-than-temporary impairment on debt securities included in net income       | -                    | -           | -                       | 12,231      |
| All other unrealized holding (losses) gains on available-for-sale securities arising during the period          | (7,151)              | 2,631       | (31,700)                | 4,026       |
| Other comprehensive (loss) income for the period  | (7,445)              | 9,065       | (31,492)                | 19,761      |
| Total comprehensive income  | \$ 23,587            | \$ 37,063   | \$ 32,688               | \$ 73,300   |

The accompanying notes are an integral part of these statements.

**FIRST BANCORP.**  
**CONSOLIDATED STATEMENTS OF CASH FLOWS**  
**(Unaudited)**

|  | <b>Six-Month Period Ended</b> |                 |
|--|-------------------------------|-----------------|
|  | <b>June 30,</b>               | <b>June 30,</b> |
|  | <b>2018</b>                   | <b>2017</b>     |
| (In thousands)   |                               |                 |
| <b>Cash flows from operating activities:</b>                                       |                               |                 |
| Net income   | \$ 64,180                     | \$ 53,539       |
| Adjustments to reconcile net income to net cash provided by operating activities:  |                               |                 |
| Depreciation and amortization  | 7,686                         | 8,230           |
| Amortization of intangible assets  | 1,868                         | 2,242           |
| Provision for loan and lease losses  | 40,080                        | 43,538          |
| Deferred income tax expense  | 11,479                        | 728             |
| Stock-based compensation   | 3,983                         | 3,599           |
| Gain on sale of investments  | -                             | (371)           |
| OTTI on debt securities  | -                             | 12,231          |
| Unrealized loss (gain) on derivative instruments                                   | 103                           | (307)           |
| Gain on early extinguishment of debt   | (2,316)                       | -               |
| Net gain on sales of premises and equipment and other assets                       | (840)                         | (133)           |
| Net gain on sales of loans   | (2,921)                       | (3,696)         |
| Net amortization/accretion of premiums, discounts and deferred loan fees and costs | (3,937)                       | (4,235)         |
| Originations and purchases of loans held for sale                                  | (160,584)                     | (182,678)       |
| Sales and repayments of loans held for sale  | 173,977                       | 188,890         |
| Loans held for sale valuation adjustments  | 558                           | -               |
| Amortization of broker placement fees  | 676                           | 1,007           |
| Net amortization/accretion of premium and discounts on investment securities       | 1,090                         | 40              |
| Decrease in accrued interest receivable  | 9,948                         | 10              |
| Increase in accrued interest payable   | 115                           | 567             |
| Decrease in other assets   | 11,536                        | 4,225           |
| Increase in other liabilities  | 1,591                         | 4,148           |
| Net cash provided by operating activities  | 158,272                       | 131,574         |
| <b>Cash flows from investing activities:</b>                                       |                               |                 |
| Principal collected on loans   | 1,282,545                     | 1,362,537       |
| Loans originated and purchased   | (1,217,117)                   | (1,498,967)     |
| Proceeds from sales of loans held for investment                                   | 33,709                        | 53,245          |
| Proceeds from sales of repossessed assets  | 24,484                        | 20,999          |
| Proceeds from sales of available-for-sale securities                               | -                             | 23,408          |
| Purchases of available-for-sale securities   | (352,576)                     | (12,440)        |
| Proceeds from principal repayments and maturities of available-for-sale securities | 174,574                       | 119,664         |
| Proceeds from principal repayments of held-to-maturity securities                  | 141                           | 141             |
| Additions to premises and equipment  | (10,305)                      | (5,269)         |
| Proceeds from sale of premises and equipment and other assets                      | 1,857                         | 1,109           |
| Net redemptions/purchase of other investment securities                            | 132                           | (80)            |
| Proceeds from the settlement of insurance claims                                   | 5,118                         | -               |
| Net cash (used in) provided by investing activities                                | (57,438)                      | 64,347          |
| <b>Cash flows from financing activities:</b>                                       |                               |                 |
| Net increase (decrease) in deposits  | 196,687                       | (64,810)        |



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|   |            |            |
|---|------------|------------|
| Repayment of securities sold under agreements to repurchase | (100,000)  | -          |
| Net FHLB advances proceeds                                  | -          | 5,000      |
| Repayment of junior subordinated debentures                 | (21,434)   | -          |
| Repurchase of outstanding common stock                      | (2,745)    | (1,894)    |
| Dividends paid on preferred stock                           | (1,338)    | (1,338)    |
| Net cash provided by (used in) financing activities         | 71,170     | (63,042)   |
| Net increase in cash and cash equivalents                   | 172,004    | 132,879    |
| Cash and cash equivalents at beginning of period            | 716,395    | 299,685    |
| Cash and cash equivalents at end of period                  | \$ 888,399 | \$ 432,564 |
| Cash and cash equivalents include:                          |            |            |
| Cash and due from banks                                     | \$ 790,809 | \$ 422,150 |
| Money market instruments                                    | 97,590     | 10,414     |
|   | \$ 888,399 | \$ 432,564 |

The accompanying notes are an integral part of these statements.

**FIRST BANCORP.**  
**CONSOLIDATED STATEMENTS OF CHANGES IN STOCKHOLDERS' EQUITY**  
**(Unaudited)**

|  | <b>Six-Month Period Ended</b> |                  |
|--|-------------------------------|------------------|
|  | <b>June 30,</b>               | <b>June 30,</b>  |
|  | <b>2018</b>                   | <b>2017</b>      |
| (In thousands)   |                               |                  |
| <b>Preferred Stock</b>   | \$ 36,104                     | \$ 36,104        |
| <b>Common Stock outstanding:</b>   |                               |                  |
| Balance at beginning of period   | 21,628                        | 21,745           |
| Common stock issued as compensation  | 27                            | 27               |
| Common stock issued for exercised warrants                                   | 73                            | -                |
| Common stock withheld for taxes  | (42)                          | (33)             |
| Restricted stock grants  | 34                            | 95               |
| Restricted stock forfeited   | (1)                           | (238)            |
| Balance at end of period   | 21,719                        | 21,596           |
| <b>Additional Paid-In-Capital:</b>   |                               |                  |
| Balance at beginning of period   | 936,772                       | 931,856          |
| Stock-based compensation   | 3,983                         | 3,599            |
| Common stock issued for exercised warrants                                   | (73)                          | -                |
| Common stock withheld for taxes  | (2,703)                       | (1,861)          |
| Restricted stock grants  | (34)                          | (95)             |
| Common stock issued as compensation  | (27)                          | (27)             |
| Restricted stock forfeited   | 1                             | 238              |
| Balance at end of period   | 937,919                       | 933,710          |
| <b>Retained Earnings:</b>  |                               |                  |
| Balance at beginning of period   | 895,208                       | 830,928          |
| Net income   | 64,180                        | 53,539           |
| Dividends on preferred stock   | (1,338)                       | (1,338)          |
| Amount reclassified from accumulated other comprehensive loss per ASU 2016-1 | (6)                           | -                |
| Balance at end of period   | 958,044                       | 883,129          |
| <b>Accumulated Other Comprehensive Income (Loss), net of tax:</b>            |                               |                  |
| Balance at beginning of period   | (20,615)                      | (34,390)         |
| Other comprehensive (loss) income, net of tax                                | (31,492)                      | 19,761           |
| Balance at end of period   | (52,107)                      | (14,629)         |
| <br>Total stockholders' equity   | <br>\$ 1,901,679              | <br>\$ 1,859,910 |

The accompanying notes are an integral part of these statements.

**FIRST BANCORP.  
NOTES TO CONSOLIDATED FINANCIAL STATEMENTS**

**(Unaudited)**

**NOTE 1 – BASIS OF PRESENTATION AND SIGNIFICANT ACCOUNTING POLICIES**

The Consolidated Financial Statements (unaudited) of First BanCorp. (the “Corporation”) have been prepared in conformity with the accounting policies stated in the Corporation’s Audited Consolidated Financial Statements included in the Corporation’s Annual Report on Form 10-K for the year ended December 31, 2017 (the “2017 Annual Report on Form 10-K”). Certain information and note disclosures normally included in the financial statements prepared in accordance with generally accepted accounting principles in the United States of America (“GAAP”) have been condensed or omitted from these statements pursuant to the rules and regulations of the SEC and, accordingly, these financial statements should be read in conjunction with the Audited Consolidated Financial Statements of the Corporation for the year ended December 31, 2017, which are included in the 2017 Annual Report on Form 10-K. All adjustments (consisting only of normal recurring adjustments) that are, in the opinion of management, necessary for a fair presentation of the statement of financial position, results of operations and cash flows for the interim periods have been reflected. All significant intercompany accounts and transactions have been eliminated in consolidation.

The results of operations for the quarter and six-month period ended June 30, 2018 are not necessarily indicative of the results to be expected for the entire year.

## **Adoption of New Accounting Requirements and Recently Issued but Not Yet Effective Accounting Requirements**

The Financial Accounting Standards Board (“FASB”) has issued the following accounting pronouncements and guidance relevant to the Corporation’s operations:

### **Revenue Recognition**

In May 2014, the FASB updated the Accounting Standards Codification (the “Codification” or the “ASC”) to create a new, principles-based revenue recognition framework. This guidance requires entities to recognize revenues when they transfer promised goods or services to customers in an amount that reflects the consideration to which the entity expects to be entitled in exchange for those goods or services. This guidance describes a 5-step process that entities can apply to achieve the core principle of revenue recognition and requires disclosures sufficient to enable users of financial statements to understand the nature, amount, timing, and uncertainty of revenue and cash flows arising from

contracts with customers and the significant judgments used in determining that information.

The Corporation adopted the guidance on January 1, 2018 using a modified retrospective method, in which the guidance applies to existing contracts in effect at January 1, 2018 and new contracts entered into after this date. Most of the Corporation's revenue, including net interest income, gain on sale of loans, and mortgage servicing fees is explicitly out of scope of the new revenue recognition guidance. The Corporation conducted an assessment of the revenue streams that were potentially affected by the new guidance and reviewed contracts in scope to ensure compliance with the new guidance.

The Corporation has identified service charges on deposits and related cash management services, insurance commissions, merchant-related income, and card interchange income as its most significant revenue streams within the scope of the standard. For the revenue streams that were found in scope, management reviewed in detail its most significant contracts with corresponding customers. The adoption of this guidance did not have a material effect on the Corporation's consolidated financial statements. However, additional disclosures required by the standard have been included in Note 23 – Revenue from Contracts with Customers, to the Corporation's consolidated financial statements.

## **Recognition and Measurement of Financial Assets and Liabilities**

In January 2016, the FASB updated the Codification to require an entity to: (i) measure equity investments at fair value through net income, with certain exceptions, thus, eliminating eligibility for the available-for-sale category; (ii) present in OCI the changes in instrument-specific credit risk for financial liabilities measured using the fair value option; (iii) present financial assets and financial liabilities by measurement category and form of financial asset; (iv) calculate the fair value of financial instruments for disclosure purposes based on an exit price; and (v) assess a valuation allowance on deferred tax assets related to unrealized losses of available-for-sale debt securities in combination with other deferred tax assets. The guidance provides an election to subsequently measure certain nonmarketable equity investments at cost less any impairment, adjusted for certain observable price changes. The guidance also requires a qualitative impairment assessment of such equity investments and amends certain fair value disclosure requirements. The adoption of this standard during the first quarter of 2018 did not have a material effect on the Corporation's consolidated financial statements.

## **Statement of Cash Flows Presentation – Restricted Cash**

In August 2016 and November 2016, the FASB updated the Codification to provide specific guidance on the classification and presentation of certain cash payments and cash receipts, including changes in restricted cash, in the statement of cash flows. This guidance is intended to reduce diversity in practice in how certain transactions are classified in the statement of cash flows. The amendments in this update must be applied using a retrospective transition method to each period presented. The Corporation adopted the provisions of this guidance during the first quarter of 2018 without any material effect on the Corporation's consolidated financial statements.

## **Income Tax Effect of Intra-Entity Transfers of Assets**

In October 2016, the FASB updated the Codification to improve the accounting for the income tax consequences of intra-entity transfers of assets other than inventory. With this update, entities are required to recognize the income tax consequences of an intra-entity transfer of an asset other than inventory when the transfer occurs. Under prior GAAP, the recognition of current and deferred income taxes for an intra-entity asset transfer was prohibited until the assets are sold to an outside party. This Update does not include new disclosure requirements; however, existing disclosure requirements might be applicable when accounting for the current and deferred income taxes for an intra-entity transfer of an asset other than inventory. For example, GAAP requires an entity to disclose a comparison of income tax expense (benefit) with statutory expectations (a rate reconciliation for public entities or a description of the nature of each significant reconciling item for nonpublic entities) and also requires an entity to disclose the types of temporary differences and carryforwards that give rise to a significant portion of deferred income taxes. The Corporation adopted the provisions of this guidance during the first quarter of 2018 without any effect on the Corporation's consolidated financial statements.

## Clarifying what Changes Qualify as a Modification of a Share-Based Payment Award

In May 2017, the FASB updated the codification to reduce the cost and complexity when applying ASC Topic 718, “Compensation – Stock Compensation” (“ASC Topic 718”), and standardize the practice of applying ASC Topic 718 to financial reporting. ASC Topic 718 prescribes the accounting treatment of a modification in the terms or conditions of a share-based payment award. The guidance clarifies what changes would qualify as a modification. This was done by better defining what does not constitute a modification. In order for a change to a share-based arrangement to not require ASC Topic 718 modification treatment, all of the following must be met: (i) the fair value (or alternative measurement method used) of the modified award must equal the fair value (or alternative measurement method used) of the original award immediately before the original award is modified; (ii) the vesting conditions of the modified award must be the same as the vesting conditions of the original award immediately before the original award is modified; and (iii) the classification of the modified award as an equity instrument or a liability instrument must be the same as the classification of the original award immediately before the original award is modified. The current disclosure requirements in ASC Topic 718 apply regardless of whether an entity is required to apply modification accounting under this update. The amendments in this update must be applied prospectively to an award modified on or after the adoption date. The Corporation adopted the provisions of this guidance on January 1, 2018 without any effect on the Corporation’s consolidated financial statements. The Corporation’s Omnibus Plan provides for equity-based compensation incentives through the grant of stock options, stock appreciation rights, restricted stock, restricted stock units, performance shares, cash-based awards and other stock-based awards. If any change occurs in the future to awards issued under the Omnibus Plan, the Corporation will evaluate it under this guidance.

## Lease Accounting

In February 2016, the FASB updated the Codification to replace ASC 840, “Leases (Topic 840)” (“ASC Topic 840”), with new guidance for the financial reporting about leasing transactions. Under the new guidance, a lessee will be required to recognize assets and liabilities for leases with lease terms of more than 12 months. Consistent with current GAAP, the recognition, measurement, and presentation of expenses and cash flows arising from a lease by a lessee primarily will depend on its classification as a finance or operating lease. However, unlike current GAAP, which requires the recognition of only capital leases on the balance sheet, the guidance will require both types of leases to be recognized on the balance sheet. The guidance will also require disclosures to help investors and other financial statement users better understand the amount, timing, and uncertainty of cash flows arising from leases. These disclosures include qualitative and quantitative information and additional information about the amounts recorded in the financial statements. The FASB issued an update in January 2018 providing an optional transition practical expedient to not evaluate under new ASC Topic 842, “Leases” (“ASC Topic 842”), land easements that exist or expired before the entity’s adoption of ASC Topic 842 and were not previously accounted for as leases. In addition, the FASB issued an update in July 2018 that makes 16 technical corrections to this guidance that alleviate the potential for unintended consequences from applying the new standard. The guidance on leases will take effect for public companies for fiscal years, and interim periods within those fiscal years, beginning after December 15, 2018. Early adoption is permitted. Entities are required to use a modified retrospective approach for leases that existed prior to, or are entered into after, the beginning of the earliest comparative period presented in the financial statements or they can elect an additional and optional transition method to adopt the new leases. Under the optional transition method, an entity applies the new standard at the adoption date and recognizes a cumulative-effect adjustment to the opening balance of retained earnings in the period of adoption. Also, under the optional transition method, the entity’s reporting for comparative periods presented in the financial statements in which it adopts the new leases standard will continue to be in accordance with ASC Topic 840.

The update is expected to affect the Corporation’s consolidated financial statements since the Corporation has operating and lease arrangements for which it is a lessee. The Corporation has identified the population of its current leases and is in the process of obtaining the data necessary to estimate the amount of right-of-use assets (“ROU”) and lease liabilities that will be recognized upon adoption. Therefore, the Corporation is still evaluating the effect that the adoption of this accounting pronouncement will have on its consolidated financial statements and preliminarily expects that amounts to be recognized as ROU will not be material as a percentage of the Corporation’s total assets.

## Accounting for Financial Instruments – Credit Losses

In June 2016, the FASB updated the Codification to introduce new guidance for the accounting for credit losses. The guidance includes an impairment model (known as the current expected credit loss (“CECL”) model) that is based on expected losses rather than incurred losses. It also modifies the impairment model for available-for-sale debt securities and provides for a simplified accounting model for purchased financial assets with credit deterioration since their origination. The CECL model will apply to: (1) financial assets subject to credit losses and measured at amortized cost and (2) certain off-balance sheet credit exposures. This includes loans, held-to-maturity debt securities, loan commitments, financial guarantees, and net investments in leases, as well as reinsurance and trade receivables. Upon

initial recognition of the exposure, the CECL model requires an entity to estimate the credit losses expected over the life of an exposure (or pool of exposures). The estimate of expected credit losses (“ECL”) should consider historical information, current information, and reasonable and supportable forecasts, including estimates of prepayments. Financial instruments with similar risk characteristics should be grouped together when estimating ECL. The guidance does not prescribe a specific method to make the estimate, so its application will require significant judgment.

Generally, upon initial recognition of a financial asset, the estimate of the ECL will be recorded through an allowance for loan and lease losses with an offset to current earnings. Subsequently, the ECL will need to be reassessed each period, and both negative and positive changes to the estimate will be recognized through an adjustment to the allowance for loan and lease losses and earnings.

The guidance amends the current OTTI model for available-for-sale debt securities. The new available-for-sale debt security model will require an estimate of ECL only when the fair value is below the amortized cost of the asset. The length of time the fair value of an available-for-sale debt security has been below the amortized cost will no longer affect the determination of whether a credit loss exists. As such, the new available-for-sale debt security model is not an OTTI model. In addition, credit losses on available-for-sale debt securities will now be limited to the difference between the security’s amortized cost basis and its fair value. The available-for-sale debt security model will also require the use of an allowance to record estimated credit losses (and subsequent recoveries).



The purchased financial assets with credit deterioration (“PCD”) model applies to purchased financial assets (measured at amortized cost or available-for-sale) that have experienced more than insignificant credit deterioration since origination. This represents a change from the scope of what are considered purchased credit-impaired assets under today’s model. In contrast to the accounting for originated or purchased assets that do not qualify as PCD, the initial estimate of expected credit losses for a PCD would be recognized through an allowance for loan and lease losses with an offset to the cost basis of the related financial asset at acquisition (i.e., there is no effect on net income at initial recognition). Subsequently, the accounting will follow the applicable CECL or available-for-sale debt security impairment model with all adjustments of the allowance for loan and lease losses recognized through earnings. Beneficial interests classified as held-to-maturity or available-for-sale will need to apply the PCD model if the beneficial interest meets the definition of PCD or if there is a significant difference between contractual and expected cash flows at initial recognition.

In general, the new guidance will require modified retrospective application to all outstanding instruments, with a cumulative effect adjustment recorded to opening retained earnings as of the beginning of the first period in which the guidance becomes effective. However, prospective application is required for PCD assets previously accounted for under ASC Topic 310-30, “Receivables,” and for debt securities for which an OTTI was recognized prior to the date of adoption.

This guidance also expands the disclosure requirements regarding an entity’s assumptions, models, and methods for estimating the allowance for loan and lease losses. In addition, public business entities will need to disclose the amortized cost balance for each class of financial asset by credit quality indicator, disaggregated by the year of origination (i.e., by vintage year).

The guidance will be effective for public business entities that are SEC filers in fiscal years beginning after December 15, 2019, including interim periods within those fiscal years. Early adoption of the guidance will be permitted for fiscal years beginning after December 15, 2018, including interim periods within those fiscal years.

The Corporation has developed a transition roadmap in order to comply on a timely basis with the implementation of this new accounting framework. The Corporation has created a working group with members from multiple areas across the organization that is responsible for assessing the effect of the standard, evaluating interpretative issues, and evaluating the current credit loss models against the new guidance to determine any necessary changes and other related implementation activities. The working group provides periodic updates to the Corporation’s CECL Management Committee, which has oversight responsibilities for the implementation efforts. The Corporation continues to evaluate the effect that this guidance, including the method of implementation, will have on its consolidated financial statements.

### **Subsequent Measurement of Goodwill**

In January 2017, the FASB updated the Codification to simplify the subsequent measurement of goodwill by eliminating Step 2 from the current two-step goodwill impairment test. This guidance provides that a goodwill impairment test be conducted by comparing the fair value of a reporting unit with its carrying amount. Entities are to recognize an impairment charge for goodwill equal to the excess of the carrying amount over the reporting unit's fair value. Entities have the option to perform the qualitative assessment for a reporting unit to determine if the quantitative impairment test is necessary. This guidance is effective for fiscal years, and interim periods within those fiscal years, beginning after December 15, 2019. The effect of this guidance will depend upon the performance of the reporting units that have goodwill and the market conditions affecting the fair value of each reporting unit going forward.

## **Amortization of Premiums and Discounts of Callable Debt Securities**

In March 2017, the FASB updated the Codification to shorten the amortization period for certain purchased callable debt securities held at a premium. Specifically, the amendments require the premium to be amortized to the earliest call date. With respect to securities held at a discount, the amendments do not require an accounting change; thus, the discount continues to be amortized to maturity. Under current GAAP, premiums and discounts on callable debt securities generally are amortized to the maturity date. An entity must have a large number of similar loans to consider estimates of future principal prepayments when applying the interest method. However, an entity that holds an individual callable debt security at a premium may not amortize that premium to the earliest call date. If that callable debt security is subsequently called, the entity records a loss equal to the unamortized premium. The amendments in this update more closely align the amortization period of premiums and discounts to expectations incorporated in market pricing on the underlying securities. In most cases, market participants price securities to the call date that produces the worst yield when the coupon is above current market rates (that is, the security is trading at a premium) and price securities to maturity when the coupon is below market rates (that is, the security is trading at a discount) in anticipation that the borrower will act in its economic best interest. As a result, the amendments more closely align interest income recorded on bonds held at a premium or a discount with the economics of the underlying instrument. For public business entities, the amendments in this update are effective for fiscal years, and interim periods within those fiscal years, beginning after December 15, 2018. The adoption of this guidance is not expected to have a material effect on the Corporation's consolidated statement of financial condition or results of operations. As of June 30, 2018, the Corporation had \$4.0 million of callable debt securities held at a premium (unamortized premium of \$32 thousand).

## **Derivatives and Hedging**

In August 2017, the FASB updated the Codification to: (i) expand hedge accounting for nonfinancial and financial risk components and amend measurement methodologies to more closely align hedge accounting with a company's risk management activities; (ii) decrease the complexity of preparing and understanding hedge results by eliminating the separate measurement and reporting of hedge ineffectiveness; (iii) enhance transparency, comparability, and understanding of hedge results through enhanced disclosures and a change in the presentation of hedge results to align the effects of the hedging instrument and the hedged item; and (iv) reduce the cost and complexity of applying hedge accounting by simplifying the manner in which assessments of hedge effectiveness may be performed. This update is effective for fiscal years, and interim periods within those fiscal years, beginning after December 15, 2018. Early adoption is permitted. The guidance requires companies to apply requirements to existing hedging relationships on the date of adoption, and the effect of the adoption should be reflected as of the beginning of the fiscal year of adoption. As of June 30, 2018, all of the derivatives held by the Corporation were considered economic undesignated hedges. The adoption of this guidance is not expected to have a material effect on the Corporation's consolidated statement of financial condition or results of operations.

## **Reclassification of Certain Tax Effects From Accumulated Other Comprehensive Income**

In February 2018, the FASB updated the Codification to provide entities with an option to reclassify to retained earnings, tax effects that were stranded in accumulated other comprehensive income, pursuant to the Tax Cuts and Jobs Act of 2017 (the “Tax Act”). This guidance is effective for fiscal years beginning after December 15, 2018, and interim periods within those fiscal years. This guidance may be early adopted in any interim or annual period for which financial statements have not yet been issued and applied either in the period of adoption or retrospectively to each period in which the effect of the change in the corporate tax rate in the Tax Act is recognized. The Corporation is currently evaluating whether it will adopt this guidance. If adopted, the Corporation does not expect a material effect on its consolidated financial statements.

### **Improvements to Nonemployee Share-Based Payment Accounting**

In June 2018, the FASB updated the Codification as part of a simplification initiative to expand the scope of Topic 718 to include share-based payment transactions for acquiring goods and services from non-employees and to address and improve aspects of the accounting for non-employee share-based payment transactions. The amendments will be effective for interim and annual reporting periods beginning after December 15, 2018. The adoption of this guidance is not expected to have an effect on the Corporation’s consolidated financial statements.

## NOTE 2 – UPDATE ON EFFECTS OF NATURAL DISASTERS

Two strong hurricanes affected the Corporation's service areas during September 2017. The following summarizes the more significant continuing financial repercussions of these natural disasters for the Corporation and for its major subsidiary, FirstBank.

### *Credit Quality and Allowance for Loan and Lease Losses*

Relationship officers continued to closely monitor the performance of hurricane-affected commercial loan customers during 2018. Information provided by these commercial loan officers and statistics on the performance of consumer and residential credits were factored into the determination of the allowance for loan and lease losses as of June 30, 2018. Although the identification and evaluation of hurricane-affected credits has been completed, management's assessment of the hurricanes' effect is still subject to uncertainties, both those specific to some individual customers, such as the resolution of insurance claims, and those applicable to the overall economic prospects of the hurricane-affected areas as a whole. During the second quarter and six-month period ended June 30, 2018, the Corporation recorded a net loan loss reserve release of approximately \$2.1 million and \$8.5 million, respectively, in connection with revised estimates associated with the effects of the hurricanes. The revised estimates were primarily attributable to updated assessments of financial performance and repayment prospects of certain individually-assessed commercial credits and, to a lesser extent, lower reserve requirements resulting from payments received during the first six-months of 2018 that reduced the balance of the consumer and residential mortgage loan portfolios outstanding on the dates of the hurricanes.

As of June 30, 2018, the hurricane-related qualitative allowance amounted to \$42.2 million (December 31, 2017 - \$55.6 million). With the future resolution of uncertainties and the ongoing collection of information on individual commercial customers and statistics on the consumer and residential loan portfolios, the loss estimate will be revised as needed. Refer to Note 7 – Loans Held for Investment, to the consolidated financial statements for information about non-performing loans and early delinquency statistics.

### *Disaster Response Plan Costs, Casualty Losses and Related Insurance*

The Corporation has incurred a variety of costs to operate in disaster response mode, and some facilities and their contents, including certain OREO properties, were damaged by the storms. The Corporation maintains insurance for casualty losses, as well as for reasonable and necessary disaster response costs and certain revenue lost through business interruption. Substantially all of the significant disaster response costs had been incurred by the end of the second quarter of 2018. Insurance claim receivables were established for some of the individual costs, when incurred, based on management's understanding of the underlying coverage and when realization of the claim was deemed probable. During the second quarter of 2018, the Corporation reached a final settlement on certain insurance claims arising from the hurricanes. With this settlement, the Corporation received proceeds of approximately \$4.3 million, primarily related to repairs and maintenance costs incurred on certain OREO properties, and \$0.8 million related to a loan receivable fully charged-off in prior periods. The insurance proceeds were recorded against incurred losses, previously-established accounts receivable, or loan recoveries, as applicable. Insurance recoveries are recorded in the same income statement caption as the incurred losses. Recoveries from insurance proceeds in excess of losses incurred, if any, are recognized as a gain from insurance proceeds and reported as part of "other non-interest income" in

the statement of income when the insurance proceeds are received, or when all contingencies related to the insurance claim are resolved. As of June 30, 2018, the Corporation still had an insurance claim receivable of \$6.3 million, included as part of “other assets” in the statement of financial condition. Management also believes that there is a possibility that some gains will be recognized with respect to casualty and lost revenue claims in future periods, but this is contingent on reaching agreement on the Corporation’s claims with the insurance carriers.

*Liquidity Management*

The Corporation experienced rapid accumulation of deposits after the hurricanes in the fourth quarter of 2017 and the first six months of 2018. Total deposits as of June 30, 2018, excluding brokered CDs, increased \$523.3 million from December 31, 2017 and \$884.8 million since September 30, 2017. The most significant increase was in non-interest-bearing demand deposits, which grew 26%, or \$483.5 million from December 31, 2017 and \$731.0 million, or 46%, since September 30, 2017. Hurricane-related factors, such as the effect of disaster relief funds and settlements of insurance claims, continue to contribute to this growth. Although management expects the balances accumulated by deposit customers in the hurricane-affected areas to reduce over time, it is difficult to predict when and to what degree, and there may be further growth as insurance claims are resolved and additional disaster-recovery funds are distributed.

**NOTE 3 – EARNINGS PER COMMON SHARE**

The calculations of earnings per common share for the quarters and six-month periods ended June 30, 2018 and 2017 are as follows:

|   | <b>Quarter Ended<br/>June 30,</b> |             | <b>Six-Month Period Ended<br/>June 30,</b> |             |
|---|-----------------------------------|-------------|--|-------------|
|   | <b>2018</b>                       | <b>2017</b> | <b>2018</b>                                | <b>2017</b> |
| (In thousands, except per share information)          |                                   |             |  |             |
| Net income  | \$ 31,032                         | \$ 27,998   | \$ 64,180                                  | \$ 53,539   |
| Less: Preferred stock dividends                       | (669)                             | (669)       | (1,338)                                    | (1,338)     |
| Net income attributable to common stockholders        | \$ 30,363                         | \$ 27,329   | \$ 62,842                                  | \$ 52,201   |
| <b>Weighted-Average Shares:</b>                       |                                   |             |  |             |
| Average common shares outstanding                     | 215,737                           | 213,900     | 215,194                                    | 213,621     |
| Average potential dilutive common shares              | 929                               | 2,932       | 1,289                                      | 3,482       |
| Average common shares outstanding - assuming dilution | 216,666                           | 216,832     | 216,483                                    | 217,103     |
| <b>Earnings per common share:</b>                     |                                   |             |  |             |
| Basic   | \$ 0.14                           | \$ 0.13     | \$ 0.29                                    | \$ 0.24     |
| Diluted   | \$ 0.14                           | \$ 0.13     | \$ 0.29                                    | \$ 0.24     |

Earnings per common share is computed by dividing net income attributable to common stockholders by the weighted-average number of common shares issued and outstanding. Net income attributable to common stockholders represents net income adjusted for any preferred stock dividends, including any dividends declared, and any cumulative dividends related to the current dividend period that have not been declared as of the end of the period. Basic weighted-average common shares outstanding exclude unvested shares of restricted stock that do not contain non-forfeitable dividend rights.

Potential dilutive common shares consist of unvested shares of restricted stock that do not contain non-forfeitable dividend rights, performance units that do not contain non-forfeitable dividend rights if the performance condition is met as of the end of the reporting period, and warrants outstanding during the period using the treasury stock method. This method assumes that the potential dilutive common shares are issued and outstanding and the proceeds from the exercise, in addition to the amount of compensation cost attributable to future services, are used to purchase common stock at the exercise date. The difference between the numbers of potential dilutive shares issued and the shares purchased is added as incremental shares to the actual number of shares outstanding to compute diluted earnings per share. Unvested shares of restricted stock and performance units that do not contain non-forfeitable dividend rights, and warrants outstanding during the period that result in lower potential dilutive shares issued than shares purchased under the treasury stock method, are not included in the computation of dilutive earnings per share since their

inclusion would have an antidilutive effect on earnings per share.

On May 17, 2018, the U.S. Treasury exercised its warrant to purchase 1,285,899 shares of the Corporation's common stock on a cashless basis, resulting in the issuance of 730,571 shares of common stock.



**NOTE 4 – STOCK-BASED COMPENSATION.**

On May 24, 2016, the Corporation’s stockholders approved the amendment and restatement of the First BanCorp. Omnibus Incentive Plan, as amended (the “Omnibus Plan”), to, among other things, increase the number of shares of common stock reserved for issuance under the Omnibus Plan, extend the term of the Omnibus Plan to May 24, 2026 and re-approve the material terms of the performance goals under the Omnibus Plan for purposes of the then Section 162(m) of the U.S. Internal Revenue Code of 1986, as amended. The Omnibus Plan provides for equity-based compensation incentives (the “awards”) through the grant of stock options, stock appreciation rights, restricted stock, restricted stock units, performance shares, cash-based awards and other stock-based awards. The Omnibus Plan authorizes the issuance of up to 14,169,807 shares of common stock, subject to adjustments for stock splits, reorganizations, and other similar events. As of June 30, 2018, 6,956,802 authorized shares of common stock were available for issuance under the Omnibus Plan. The Corporation’s Board of Directors, based on the recommendation of the Corporation’s Compensation and Benefits Committee, has the power and authority to determine those eligible to receive awards and to establish the terms and conditions of any awards, subject to various limits and vesting restrictions that apply to individual and aggregate awards.

***Restricted Stock***

Under the Omnibus Plan, the Corporation may grant restricted stock to plan participants, subject to forfeiture upon the occurrence of certain events until the dates specified in the participant’s award agreement. While the restricted stock is subject to forfeiture and does not contain non-forfeitable dividend rights, restricted stock participants may exercise full voting rights. The restricted stock granted under the Omnibus Plan is typically subject to a vesting period. During the first six months of 2018, the Corporation awarded 342,439 shares of restricted stock to employees, fifty percent (50%) of those shares vest in two years from the grant date and the remaining (50%) vest in three years of the grant date. Included in those 342,439 shares of restricted stock were 20,447 shares granted to retirement-eligible employees at the grant date. The fair value of the shares of restricted stock granted in the first six months of 2018 was based on the market price of the Corporation’s outstanding common stock on the date of the grant.

The following table summarizes the restricted stock activity in the first six months of 2018 under the Omnibus Plan:

|  | <b>Six-Month Period Ended<br/>June 30, 2018</b>     |           |   |
|--|---|-----------|---|
|  | <b>Number of shares<br/>of restricted<br/>stock</b> | <b>\$</b> | <b>Weighted-Average<br/>Grant Date<br/>Fair Value</b> |
| Non-vested shares at beginning of year | 1,816,968   |           | 2.76  |
| Granted                                | 342,439   |           | 6.30  |
| Forfeited                              | (9,500)   |           | 2.99  |

|                                    |             |    |      |
|------------------------------------|-------------|----|------|
| Vested                             | (1,086,822) |    | 2.09 |
| Non-vested shares at June 30, 2018 | 1,063,085   | \$ | 4.59 |

For the quarter and six-month period ended June 30, 2018, the Corporation recognized \$0.8 million and \$1.9 million, respectively, of stock-based compensation expense related to restricted stock awards, compared to \$1.0 million and \$2.0 million for the same periods in 2017, respectively. As of June 30, 2018, there was \$3.2 million of total unrecognized compensation cost related to non-vested shares of restricted stock. The weighted average period over which the Corporation expects to recognize such cost is 1.5 years. The total expense determined for restricted stock awards granted to retirement-eligible employees was charged against earnings at the grant date.

During the first half of 2017, the Corporation awarded 3,644 shares of restricted stock subject to a one-year vesting period to an independent director appointed in the first quarter of 2017. In addition, during the first half of 2017, the Corporation awarded 951,332 shares of restricted stock to employees subject to a vesting period of two years. Included in those 951,332 shares of restricted stock were 838,332 shares granted in the first quarter of 2017 to certain senior officers consistent with the requirements of the Troubled Asset Relief Program (“TARP”) Interim Final Rule. On May 10, 2017, the United States Department of the Treasury (the “U.S. Treasury”) announced that it had sold all of its remaining 10,291,553 shares of the Corporation’s common stock. As a result of the sale by the U.S. Treasury, the Corporation is no longer subject to the compensation-related restrictions under TARP, which substantially limited the Corporation’s ability to award short-term and long-term incentives to the Corporation’s executives, and the Corporation’s senior officers are no longer subject to the transferability restrictions on their shares of restricted stock. However, since the U.S. Treasury did not recover the full amount of its original investment under TARP, the senior officers forfeited 2,370,571, or 50%, of their outstanding shares of restricted stock, resulting in a reduction in the number of common shares outstanding.

The fair value of the shares of restricted stock granted in the first quarter of 2017 was based on the market price of the Corporation’s outstanding common stock on the date of the grant. For the 838,332 shares of restricted stock granted under the TARP requirements, the market price was discounted assuming that 50% of the shares of restricted stock would become freely transferable and the remaining 50% would be forfeited, resulting in a fair value of \$2.71 for each share of restricted stock granted under TARP requirements.

Stock-based compensation accounting guidance requires the Corporation to reverse compensation expense for any awards that are forfeited due to employee or director turnover. Quarterly changes in the estimated forfeiture rate may have a significant effect on stock-based compensation, as the effect of adjusting the rate for all expense amortization is recognized in the period in which the forfeiture estimate is changed. If the actual forfeiture rate is higher than the estimated forfeiture rate, an adjustment is made to increase the estimated forfeiture rate, which will result in a decrease in the expense recognized in the financial statements. If the actual forfeiture rate is lower than the estimated forfeiture rate, an adjustment is made to decrease the estimated forfeiture rate, which will result in an increase in the expense recognized in the financial statements. The estimated forfeiture rate did not change as a result of the restricted shares forfeited in connection with the aforementioned U.S. Treasury’s sale of the Corporation’s common stock.



***Performance Units***

Under the Omnibus Plan, the Corporation may award performance unit awards to Omnibus Plan participants. During the first six months of 2018, the Corporation granted 304,408 unit awards to executives, with each unit representing the value of one share of the Corporation's common stock. The performance unit awards granted are for the performance period beginning January 1, 2018 and ending on December 31, 2020 and are subject to a three-year requisite service period. These awards do not contain non-forfeitable rights to dividend equivalent amounts and can only be settled in shares of the Corporation's common stock. Included in those 304,408 performance unit awards were 29,171 units granted to retirement-eligible executives at the grant date. The performance unit will vest based on the achievement of a pre-established tangible book value per share target as of December 31, 2020. All of the performance units will vest if performance is at the pre-established performance target level or above. However, the participants may vest on 50% of the awards to the extent that performance is below the target but at 80% of the pre-established performance target level (the 80% minimum threshold) which is measured based upon the growth in the tangible book value during the performance cycle. If performance is between the 80% minimum threshold and the pre-established performance target level, the participants will vest on a proportional amount. No performance units will vest if performance is below the 80% minimum threshold.

The fair value of the performance unit awards granted during the first six months of 2018 was based on the market price of the Corporation's outstanding common stock on the date of the grant. For the quarter and the first six months of 2018, the Corporation recognized \$0.1 million and \$0.3 million, respectively, of stock-based compensation related to performance unit awards. As of June 30, 2018, there was \$1.6 million of total unrecognized compensation cost related to unvested performance units that the Corporation expects to recognize over the three-year requisite service period. The total expense determined for the performance unit awards granted to retirement-eligible executives was charged against earnings at the grant date. The total amount of compensation expense recognized reflects management's assessment of the probability that the pre-established performance goal will be achieved. A cumulative adjustment to compensation expense is recognized in the current period to reflect any changes in the probability of achievement of the performance goals.

***Salary stock***

Also, effective April 1, 2013, the Corporation's Board of Directors determined to increase the salary amounts paid to certain executive officers, primarily by paying the increased salary amounts in the form of shares of the Corporation's common stock issued under the Omnibus Plan, instead of cash. During the first six months of 2018, the Corporation issued 268,709 shares of common stock (first six months of 2017 – 272,959 shares) with a weighted average market value of \$6.51 (first six months of 2017 – \$5.94) as salary stock compensation. This resulted in a compensation expense of \$1.7 million recorded in the first six months of 2018 (first six months of 2017 – \$1.6 million). Effective July 1, 2018, the payment of additional salary amounts in the form of stock was eliminated in accordance to the previously reported executive compensation program.

For the first six months of 2018, the Corporation withheld 96,377 shares (first six months of 2017 – 90,973 shares) from the common stock paid to certain senior officers as additional compensation and 328,433 shares of restricted stock that vested during the first six months of 2018 (first six months of 2017 – 235,680) to cover employees' payroll and income tax withholding liabilities; these shares are held as treasury shares. The Corporation paid in cash any fractional share of salary stock to which the officer was entitled. In the consolidated financial statements, the Corporation treats shares withheld for tax purposes as common stock repurchases.

**NOTE 5 – INVESTMENT SECURITIES*****Investment Securities Available for Sale***

The amortized cost, non-credit loss component of OTTI recorded in OCI, gross unrealized gains and losses recorded in OCI, estimated fair value, and weighted-average yield of investment securities available for sale by contractual maturities as of June 30, 2018 and December 31, 2017 were as follows:

|  | Amortized<br>cost | Noncredit<br>Loss<br>Component<br>of OTTI<br>Recorded<br>in OCI | June 30, 2018             |        | Fair value | Weighted-<br>average yield% |
|--|-------------------|---|---------------------------|--------|------------|-----------------------------|
|  |                   |   | Gross Unrealized<br>gains | losses |            |                             |
| (Dollars in thousands)                                     |                   |   |                           |        |            |                             |
| U.S. Treasury securities:                                  |                   |   |                           |        |            |                             |
| Due within one year  | \$ 57,464         | \$ -  | \$ 2                      | \$ 67  | \$ 57,399  | 1.52                        |
| U.S.<br>government-sponsored<br>agencies obligations:      |                   |   |                           |        |            |                             |
| Due within one year  | 74,962            | -   | -                         | 326    | 74,636     | 1.18                        |
| After 1 to 5 years   | 311,675           | -   | -                         | 5,481  | 306,194    | 1.51                        |
| After 5 to 10 years  | 186,269           | -   | 87                        | 3,675  | 182,681    | 2.94                        |
| After 10 years   | 36,702            | -   | -                         | 211    | 36,491     | 2.28                        |
| Puerto Rico government<br>obligations:                     |                   |   |                           |        |            |                             |
| After 5 to 10 years  | 4,032             | -   | 43                        | -      | 4,075      | 3.14                        |
| After 10 years   | 4,054             | -   | -                         | 1,286  | 2,768      | 6.97                        |
| United States and Puerto<br>Rico<br>government obligations | 675,158           | -   | 132                       | 11,046 | 664,244    | 1.95                        |
| Mortgage-backed<br>securities:                             |                   |   |                           |        |            |                             |
| Freddie Mac (“FHLMC”) certificates:                        |                   |   |                           |        |            |                             |
| After 5 to 10 years  | 89,235            | -   | 23                        | 3,378  | 85,880     | 2.01                        |
| After 10 years   | 265,350           | -   | 295                       | 8,379  | 257,266    | 2.49                        |

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|   |              |          |          |           |              |      |
|---|--------------|----------|----------|-----------|--------------|------|
|   | 354,585      | -        | 318      | 11,757    | 343,146      | 2.37 |
| Ginnie Mae (“GNMA”) certificates:                                     |              |          |          |           |              |      |
| After 1 to 5 years  | 142          | -        | 2        | -         | 144          | 3.10 |
| After 5 to 10 years   | 61,136       | -        | 540      | 25        | 61,651       | 3.03 |
| After 10 years  | 135,599      | -        | 3,746    | 1,102     | 138,243      | 3.81 |
|   | 196,877      | -        | 4,288    | 1,127     | 200,038      | 3.57 |
| Fannie Mae (“FNMA”) certificates:                                     |              |          |          |           |              |      |
| Due within one year   | 801          | -        | 11       | -         | 812          | 1.90 |
| After 1 to 5 years  | 11,606       | -        | -        | 260       | 11,346       | 2.38 |
| After 5 to 10 years   | 148,799      | -        | 63       | 5,335     | 143,527      | 2.10 |
| After 10 years  | 618,975      | -        | 1,965    | 16,416    | 604,524      | 2.65 |
|   | 780,181      | -        | 2,039    | 22,011    | 760,209      | 2.54 |
| Collateralized mortgage obligations guaranteed by the FHLMC and GNMA: |              |          |          |           |              |      |
| After 1 to 5 years  | 7,588        | -        | 5        | 11        | 7,582        | 2.74 |
| After 10 years  | 45,385       | -        | 367      | 22        | 45,730       | 2.57 |
|   | 52,973       | -        | 372      | 33        | 53,312       | 2.59 |
| Other mortgage pass-through trust certificates:                       |              |          |          |           |              |      |
| After 10 years  | 20,590       | 5,529    | -        | -         | 15,061       | 4.51 |
| Total mortgage-backed securities                                      | 1,405,206    | 5,529    | 7,017    | 34,928    | 1,371,766    | 2.67 |
| Total investment securities available for sale                        | \$ 2,080,364 | \$ 5,529 | \$ 7,149 | \$ 45,974 | \$ 2,036,010 | 2.44 |



|  | Amortized cost | Noncredit<br>Loss<br>Component<br>of OTTI<br>Recorded<br>in OCI | December 31, 2017         |        | Fair value | Weighted-<br>average yield% |
|--|----------------|---|---------------------------|--------|------------|-----------------------------|
|  |                |   | Gross Unrealized<br>gains | losses |            |                             |
| (Dollars in thousands)                               |                |   |                           |        |            |                             |
| U.S. Treasury securities:                            |                |   |                           |        |            |                             |
| After 1 to 5 years                                   | \$ 7,458       | \$ -  | \$ -                      | \$ 57  | \$ 7,401   | 1.29                        |
| U.S. government-sponsored agencies obligations:      |                |   |                           |        |            |                             |
| Due within one year                                  | 122,471        | -   | -                         | 319    | 122,152    | 1.06                        |
| After 1 to 5 years                                   | 309,472        | -   | 28                        | 3,735  | 305,765    | 1.42                        |
| After 5 to 10 years                                  | 133,451        | -   | 117                       | 319    | 133,249    | 2.72                        |
| After 10 years                                       | 40,769         | -   | 1                         | 149    | 40,621     | 1.84                        |
| Puerto Rico government obligations:                  |                |   |                           |        |            |                             |
| After 5 to 10 years                                  | 4,071          | -   | 47                        | -      | 4,118      | 3.14                        |
| After 10 years                                       | 3,972          | -   | -                         | 1,277  | 2,695      | 6.97                        |
| United States and Puerto Rico government obligations | 621,664        | -   | 193                       | 5,856  | 616,001    | 1.70                        |
| Mortgage-backed securities:                          |                |   |                           |        |            |                             |
| FHLMC certificates:                                  |                |   |                           |        |            |                             |
| After 5 to 10 years                                  | 18,658         | -   | 14                        | 63     | 18,609     | 2.14                        |
| After 10 years                                       | 297,733        | -   | 217                       | 4,853  | 293,097    | 2.23                        |
|  | 316,391        | -   | 231                       | 4,916  | 311,706    | 2.23                        |

|   |              |          |           |           |              |      |
|---|--------------|----------|-----------|-----------|--------------|------|
| GNMA  |              |          |           |           |              |      |
| certificates:   |              |          |           |           |              |      |
| After 1 to 5 years  | 81           | -        | 1         | -         | 82           | 3.23 |
| After 5 to 10 years   | 69,661       | -        | 1,244     | -         | 70,905       | 3.05 |
| After 10 years  | 145,067      | -        | 5,910     | 334       | 150,643      | 3.81 |
|   | 214,809      | -        | 7,155     | 334       | 221,630      | 3.56 |
| FNMA certificates:  |              |          |           |           |              |      |
| After 1 to 5 years  | 20,831       | -        | 294       | 109       | 21,016       | 2.69 |
| After 5 to 10 years   | 49,934       | -        | -         | 818       | 49,116       | 1.83 |
| After 10 years  | 613,129      | -        | 3,180     | 6,401     | 609,908      | 2.43 |
|   | 683,894      | -        | 3,474     | 7,328     | 680,040      | 2.39 |
| Collateralized mortgage obligations issued or guaranteed by the FHLMC and GNMA: |              |          |           |           |              |      |
| After 1 to 5 years  | 5,918        | -        | 14        | -         | 5,932        | 2.21 |
| After 5 to 10 years   | 2,556        | -        | 11        | -         | 2,567        | 2.23 |
| After 10 years  | 35,331       | -        | 231       | -         | 35,562       | 2.22 |
|   | 43,805       | -        | 256       | -         | 44,061       | 2.22 |
| Other mortgage pass-through trust certificates:                                 |              |          |           |           |              |      |
| After 10 years  | 22,791       | 5,731    | -         | -         | 17,060       | 2.44 |
| Total mortgage-backed securities  | 1,281,690    | 5,731    | 11,116    | 12,578    | 1,274,497    | 2.54 |
| Other   |              |          |           |           |              |      |
| Due within one year   | 100          | -        | -         | -         | 100          | 1.48 |
| Equity securities (1)   | 424          | -        | -         | 6         | 418          | 2.11 |
| Total investment securities   |              |          |           |           |              |      |
| available for sale  | \$ 1,903,878 | \$ 5,731 | \$ 11,309 | \$ 18,440 | \$ 1,891,016 | 2.27 |

- (1) As of January 1, 2018, the Corporation adopted ASU 2016-01, resulting in the reclassification of equity securities from available-for-sale investment securities to other investment securities.

Maturities of mortgage-backed securities (“MBS”) are based on the period of final contractual maturity. Expected maturities of investments might differ from contractual maturities because they may be subject to prepayments and/or call options. The weighted-average yield on investment securities available for sale is based on amortized cost and, therefore, does not give effect to changes in fair value. The net unrealized gain or loss on securities available for sale and the noncredit loss component of OTTI are presented as part of OCI.

The following tables show the Corporation’s available-for-sale investments’ fair value and gross unrealized losses, aggregated by investment category and length of time that individual securities have been in a continuous unrealized loss position, as of June 30, 2018 and December 31, 2017. The tables also include debt securities for which an OTTI was recognized and only the amount related to a credit loss was recognized in earnings. For unrealized losses for which OTTI was recognized, the related credit loss was charged against the amortized cost basis of the debt security.

|  | Less than 12 months |           | As of June 30, 2018<br>12 months or more |           | Total        |           |
|--|---------------------|-----------|--|-----------|--------------|-----------|
|  | Unrealized          |           | Unrealized                               |           | Unrealized   |           |
|  | Fair Value          | Losses    | Fair Value                               | Losses    | Fair Value   | Losses    |
| (In thousands)   |                     |           |  |           |              |           |
| <b>Debt securities:</b>  |                     |           |  |           |              |           |
| Puerto Rico-government obligations   | \$ -                | \$ -      | \$ 2,768                                 | \$ 1,286  | \$ 2,768     | \$ 1,286  |
| U.S. Treasury and U.S. government agencies obligations                     | 237,349             | 4,448     | 355,093                                  | 5,312     | 592,442      | 9,760     |
| <b>Mortgage-backed securities:</b>   |                     |           |  |           |              |           |
| FNMA   | 343,390             | 9,315     | 262,712                                  | 12,696    | 606,102      | 22,011    |
| FHLMC  | 155,213             | 4,011     | 150,268                                  | 7,746     | 305,481      | 11,757    |
| GNMA   | 65,966              | 1,109     | 601                                      | 18        | 66,567       | 1,127     |
| Collateralized mortgage obligations issued or guaranteed by FHLMC and GNMA | 17,196              | 33        | -  | -         | 17,196       | 33        |
| Other mortgage pass-through trust certificates                             | -                   | -         | 15,061                                   | 5,529     | 15,061       | 5,529     |
|  | \$ 819,114          | \$ 18,916 | \$ 786,503                               | \$ 32,587 | \$ 1,605,617 | \$ 51,503 |

|  | Less than 12 months |        | As of December 31, 2017<br>12 months or more |          | Total      |          |
|--|---------------------|--------|--|----------|------------|----------|
|  | Unrealized          |        | Unrealized                                   |          | Unrealized |          |
|  | Fair Value          | Losses | Fair Value                                   | Losses   | Fair Value | Losses   |
| (In thousands)   |                     |        |  |          |            |          |
| <b>Debt securities:</b>                                |                     |        |  |          |            |          |
| Puerto Rico-government obligations                     | \$ -                | \$ -   | \$ 2,695                                     | \$ 1,277 | \$ 2,695   | \$ 1,277 |
| U.S. Treasury and U.S. government agencies obligations | 136,459             | 494    | 362,050                                      | 4,085    | 498,509    | 4,579    |
| <b>Mortgage-backed securities:</b>                     |                     |        |  |          |            |          |

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|   |            |          |            |           |              |           |
|---|------------|----------|------------|-----------|--------------|-----------|
| FNMA  | 189,699    | 1,705    | 274,963    | 5,623     | 464,662      | 7,328     |
| FHLMC   | 91,174     | 590      | 166,331    | 4,326     | 257,505      | 4,916     |
| GNMA  | 39,145     | 334      | -          | -         | 39,145       | 334       |
| Other mortgage pass-through<br>trust certificates | -          | -        | 17,060     | 5,731     | 17,060       | 5,731     |
| <b>Equity securities (1)</b>                      | -          | -        | 407        | 6         | 407          | 6         |
|   | \$ 456,477 | \$ 3,123 | \$ 823,506 | \$ 21,048 | \$ 1,279,983 | \$ 24,171 |

(1) As of January 1, 2018, the Corporation adopted ASU 2016-01, resulting in the reclassification of equity securities from available-for-sale investment securities to other investment securities.

**Assessment for OTTI**

Debt securities issued by U.S. government agencies, U.S. government-sponsored entities, and the U.S. Treasury accounted for approximately 99% of the total available-for-sale portfolio as of June 30, 2018, and no credit losses are expected, given the explicit and implicit guarantees provided by the U.S. federal government. The Corporation's OTTI assessment was concentrated mainly on private label MBS, and on Puerto Rico government debt securities, for which credit losses are evaluated on a quarterly basis. The Corporation considered the following factors in determining whether a credit loss exists and the period over which the debt security is expected to recover:

- The length of time and the extent to which the fair value has been less than the amortized cost basis;
- Any adverse change to the credit conditions and liquidity of the issuer, taking into consideration the latest information available about the financial condition of the issuer, credit ratings, the failure of the issuer to make scheduled principal or interest payments, recent legislation and government actions affecting the issuer's industry, and actions taken by the issuer to deal with the present economic climate;
- Changes in the near term prospects of the underlying collateral for a security, if any, such as changes in default rates, loss severity given default, and significant changes in prepayment assumptions; and
- The level of cash flows generated from the underlying collateral, if any, supporting the principal and interest payments of the debt securities.

The Corporation recorded OTTI losses on available-for-sale debt securities as follows:

|  | Quarter Ended |      | Six-Month Period Ended |             |
|--|---------------|------|------------------------|-------------|
|  | June 30,      |      | June 30,               |             |
|  | 2018          | 2017 | 2018                   | 2017        |
| (In thousands)                                   |               |      |                        |             |
| Total OTTI losses                                | \$ -          | \$ - | \$ -                   | \$ (12,231) |
| Portion of OTTI recognized in OCI                | -             | -    | -                      | -           |
| Net impairment losses recognized in earnings (1) | \$ -          | \$ - | \$ -                   | \$ (12,231) |

(1) Credit losses on Puerto Rico government debt securities, recorded in the first quarter of 2017.

The following tables summarize the roll-forward of credit losses on debt securities held by the Corporation for which a portion of an OTTI is recognized in OCI:

|                               | <b>Cumulative OTTI credit losses recognized in earnings on securities still held</b> |                             |                        |                 |
|-------------------------------|--|-----------------------------|------------------------|-----------------|
|                               | <b>March 31,</b>   | <b>Credit impairments</b>   | <b>Credit loss</b>     | <b>June 30,</b> |
|                               | <b>2018</b>  | <b>recognized in</b>        | <b>reductions for</b>  | <b>2018</b>     |
|                               | <b>Balance</b>   | <b>earnings on</b>          | <b>securities sold</b> | <b>Balance</b>  |
|                               |  | <b>securities that have</b> | <b>during the</b>      |                 |
|                               |  | <b>been</b>                 | <b>period</b>          |                 |
|                               |  | <b>previously impaired</b>  |                        |                 |
| (In thousands)                |  |                             |                        |                 |
| Available-for-sale securities |  |                             |                        |                 |
| Private label MBS             | \$ 6,792   | \$ -                        | \$ -                   | \$ 6,792        |

|                               | <b>Cumulative OTTI credit losses recognized in earnings on securities still held</b> |                        |                          |                 |
|-------------------------------|--|------------------------|--------------------------|-----------------|
|                               | <b>December 31,</b>  | <b>Credit</b>          | <b>Credit loss</b>       | <b>June 30,</b> |
|                               | <b>2017</b>  | <b>impairments</b>     | <b>reductions for</b>    | <b>2018</b>     |
|                               | <b>Balance</b>   | <b>recognized in</b>   | <b>securities sold</b>   | <b>Balance</b>  |
|                               |  | <b>earnings on</b>     | <b>during the period</b> |                 |
|                               |  | <b>securities that</b> |                          |                 |
|                               |  | <b>have been</b>       |                          |                 |
|                               |  | <b>previously</b>      |                          |                 |
|                               |  | <b>impaired</b>        |                          |                 |
| (In thousands)                |  |                        |                          |                 |
| Available-for-sale securities |  |                        |                          |                 |
| Private label MBS             | \$ 6,792   | \$ -                   | \$ -                     | \$ 6,792        |

|                                    | <b>Cumulative OTTI credit losses recognized in earnings on securities still held</b> |                                |                            |                 |
|------------------------------------|--|--------------------------------|----------------------------|-----------------|
|                                    | <b>March 31,</b>   | <b>Credit impairments</b>      | <b>Credit loss</b>         | <b>June 30,</b> |
|                                    | <b>2017</b>  | <b>recognized in</b>           | <b>reductions</b>          | <b>2017</b>     |
|                                    | <b>Balance</b>   | <b>earnings</b>                | <b>for securities sold</b> | <b>Balance</b>  |
|                                    |  | <b>on securities that have</b> | <b>during the period</b>   |                 |
|                                    |  | <b>been</b>                    |                            |                 |
|                                    |  | <b>previously</b>              |                            |                 |
|                                    |  | <b>impaired</b>                |                            |                 |
| (In thousands)                     |  |                                |                            |                 |
| Available-for-sale securities      |  |                                |                            |                 |
| Puerto Rico government obligations | \$ 34,420  | \$ -                           | \$ (34,420)                | \$ -            |
| Private label MBS                  | 6,792  | -                              | -                          | 6,792           |

|   |    |        |    |   |    |          |    |       |
|---|----|--------|----|---|----|----------|----|-------|
| Total OTTI credit losses<br>for available-for-sale<br>debt securities | \$ | 41,212 | \$ | - | \$ | (34,420) | \$ | 6,792 |
|---|----|--------|----|---|----|----------|----|-------|

**Cumulative OTTI credit losses recognized in earnings on securities still held**

|   | <b>December 31,</b>     |        | <b>Credit impairments<br/>recognized in<br/>earnings<br/>on securities that<br/>have been<br/>previously impaired</b> |        | <b>Credit loss<br/>reductions<br/>for securities sold<br/>during the period</b> |          | <b>June 30,</b>         |       |
|---|-------------------------|--------|---|--------|---|----------|-------------------------|-------|
|   | <b>2016<br/>Balance</b> |        |   |        |   |          | <b>2017<br/>Balance</b> |       |
| (In thousands)  |                         |        |   |        |   |          |                         |       |
| Available-for-sale<br>securities                                      |                         |        |   |        |   |          |                         |       |
| Puerto Rico<br>government obligations                                 | \$                      | 22,189 | \$  | 12,231 | \$  | (34,420) | \$                      | -     |
| Private label MBS   |                         | 6,792  |   | -      |   | -        |                         | 6,792 |
| Total OTTI credit losses<br>for available-for-sale<br>debt securities | \$                      | 28,981 | \$  | 12,231 | \$  | (34,420) | \$                      | 6,792 |



During the second quarter of 2017, the Corporation sold for an aggregate of \$23.4 million three Puerto Rico government available-for-sale debt securities, specifically bonds of the Government Development Bank for Puerto Rico (the "GDB") and the Puerto Rico Public Buildings Authority, carried on its book at an amortized cost at the time of sale of \$23.0 million (net of \$34.4 million in cumulative OTTI impairment charges). Approximately \$12.2 million of the cumulative OTTI charges on these securities was recorded in the first quarter of 2017.

For the OTTI charge recorded on the Puerto Rico government debt securities in the first quarter of 2017, the Corporation considered the latest available information about the Puerto Rico government's financial condition, including but not limited to credit ratings downgrades, revised estimates of recovery rates, and other relevant developments such as government actions, including debt exchange proposals and the fiscal plan published by the Puerto Rico government in March 2017, as applicable. The Corporation applied a discounted cash flow analysis to its Puerto Rico government debt securities in order to calculate the cash flows expected to be collected and to determine if any portion of the decline in market value of these securities was considered a credit-related OTTI. The analysis derived an estimate of value based on the present value of risk-adjusted cash flows of the underlying securities and included of the following components:

- The contractual future cash flows of the bonds were projected based on the key terms as set forth in the official statements for each security. Such key terms included, among others, the interest rate, amortization schedule, if any, and maturity date.
- The risk-adjusted cash flows were calculated based on a probability of default analysis and recovery rate assumptions, including the weighting of different scenarios of ultimate recovery, considering the credit rating of each security. Constant monthly default rates were assumed throughout the life of the bonds, which considered the respective security's credit rating as of the date of the analysis.
- The adjusted future cash flows were then discounted at the original effective yield of each investment based on the purchase price and expected risk-adjusted future cash flows as of the purchase date of each investment.

The discounted risk-adjusted cash flow analysis for the three Puerto Rico government bonds mentioned above assumed a default probability of 100%, as these three non-performing bonds had been in default since the third quarter of 2016. Based on this analysis, the Corporation recorded in the first quarter of 2017 credit-related OTTI amounting to \$12.2 million, assuming recovery rates ranging from 15% to 80% (with a weighted average of 41%).

In addition, the Corporation performed an OTTI assessment on its private label MBS, which are collateralized by fixed-rate mortgages on single-family residential properties in the United States. The interest rate on these private-label MBS is variable, tied to 3-month LIBOR and limited to the weighted-average coupon on the underlying collateral. The underlying mortgages are fixed-rate, single-family loans with original high FICO scores (over 700) and

moderate loan-to-value ratios (under 80%), as well as moderate delinquency levels.

Based on the expected cash flows, and since the Corporation does not have the intention to sell the securities and has sufficient capital and liquidity to hold these securities until a recovery of the fair value occurs, only the credit loss component, if any, is reflected in earnings. Significant assumptions in the valuation of the private label MBS were as follows:

|                                | <b>As of<br/>June 30, 2018</b> |              | <b>As of<br/>December 31, 2017</b> |               |
|--------------------------------|--------------------------------|--------------|------------------------------------|---------------|
|                                | <b>Weighted<br/>Average</b>    | <b>Range</b> | <b>Weighted<br/>Average</b>        | <b>Range</b>  |
| Discount rate                  | 14.6%                          | 14.6%        | 14.0%                              | 14.0%         |
| Prepayment rate                | 12.6%                          | 5.0% - 23.0% | 16.4%                              | 12.0% - 29.0% |
| Projected Cumulative Loss Rate | 4%                             | 0% - 8.7%    | 3%                                 | 0% - 6.8%     |

No OTTI charges on private label MBS were recorded in either the first half of 2018 or the first half of 2017.

**Investments Held to Maturity**

The amortized cost, gross unrecognized gains and losses, estimated fair value, weighted-average yield and contractual maturities of investment securities held to maturity as of June 30, 2018 and December 31, 2017 were as follows:

**June 30, 2018****Gross Unrecognized**

|  | <b>Amortized cost</b> | <b>gains</b> | <b>losses</b> | <b>Fair value</b> | <b>Weighted-average yield %</b> |
|--|-----------------------|--------------|---------------|-------------------|---------------------------------|
| Puerto Rico Municipal Bonds:                 |                       |              |               |                   |                                 |
| After 1 to 5 years                           | \$ 3,712              | \$ -         | \$ 151        | \$ 3,561          | 5.68                            |
| After 5 to 10 years                          | 39,523                | -            | 2,705         | 36,818            | 5.63                            |
| After 10 years                               | 107,251               | -            | 12,200        | 95,051            | 5.78                            |
| Total investment securities held to maturity | \$ 150,486            | \$ -         | \$ 15,056     | \$ 135,430        | 5.74                            |

**December 31, 2017****Gross Unrecognized**

|  | <b>Amortized cost</b> | <b>gains</b> | <b>losses</b> | <b>Fair value</b> | <b>Weighted-average yield %</b> |
|--|-----------------------|--------------|---------------|-------------------|---------------------------------|
| Puerto Rico Municipal Bonds:                 |                       |              |               |                   |                                 |
| After 1 to 5 years                           | \$ 3,853              | \$ -         | \$ 173        | \$ 3,680          | 5.38                            |
| After 5 to 10 years                          | 39,523                | -            | 3,048         | 36,475            | 5.28                            |
| After 10 years                               | 107,251               | -            | 16,374        | 90,877            | 4.93                            |
| Total investment securities held to maturity | \$ 150,627            | \$ -         | \$ 19,595     | \$ 131,032        | 5.03                            |

The following tables show the Corporation's held-to-maturity investments' fair value and gross unrecognized losses, aggregated by investment category and length of time that individual securities have been in a continuous unrecognized loss position, as of June 30, 2018 and December 31, 2017:

|                             | As of June 30, 2018     |        |                   |           |              |                |
|-----------------------------|-------------------------|--------|-------------------|-----------|--------------|----------------|
|                             | Less than 12 months     |        | 12 months or more |           | Total        |                |
|                             | Unrecognized            |        | Unrecognized      |           | Unrecognized |                |
|                             | Fair Value              | Losses | Fair Value        | Losses    | Fair Value   | Losses         |
|                             |                         |        |                   |           |              | (In thousands) |
| <b>Debt securities:</b>     |                         |        |                   |           |              |                |
| Puerto Rico Municipal Bonds | \$ -                    | \$ -   | \$ 135,430        | \$ 15,056 | \$ 135,430   | \$ 15,056      |
|                             |                         |        |                   |           |              |                |
|                             | As of December 31, 2017 |        |                   |           |              |                |
|                             | Less than 12 months     |        | 12 months or more |           | Total        |                |
|                             | Unrecognized            |        | Unrecognized      |           | Unrecognized |                |
|                             | Fair Value              | Losses | Fair Value        | Losses    | Fair Value   | Losses         |
|                             |                         |        |                   |           |              | (In thousands) |
| <b>Debt securities:</b>     |                         |        |                   |           |              |                |
| Puerto Rico Municipal Bonds | \$ -                    | \$ -   | \$ 131,032        | \$ 19,595 | \$ 131,032   | \$ 19,595      |

The Corporation determines the fair market value of Puerto Rico Municipal Bonds based on a discounted cash flow analysis using risk-adjusted discount rates. A security with similar characteristics traded in the open market is used as a proxy for each municipal bond. Then the cash flow is discounted at the average spread over the discount curve exhibited by the proxy security at the end of each quarter.

All of the Puerto Rico Municipal Bonds are performing and current as to scheduled contractual payments as of June 30, 2018. Approximately 70% of the held-to-maturity municipal bonds were issued by three of the largest municipalities in Puerto Rico. The vast majority of revenues of these three municipalities is independent of the Puerto Rico central government. These obligations typically are not issued in bearer form, nor are they registered with the SEC, and they are not rated by external credit agencies. In most cases, these bonds have priority over the payment of operating costs and expenses of the municipality, which are required by law to levy special property taxes in such amounts as are required for the payment of all of their respective general obligation bonds and loans. The Corporation performs periodic credit quality reviews on these issuers. Based on the quarterly analysis performed, management concluded that no individual debt security held to maturity was other-than-temporarily impaired as of June 30, 2018.

The PROMESA oversight board has not designated any of Puerto Rico's 78 municipalities as covered entities under PROMESA. However, while the fiscal plan recently certified by the PROMESA oversight board did not contemplate a restructuring of the debt of Puerto Rico's municipalities, the plan did call for the gradual elimination of budgetary subsidies provided to municipalities by the central government. Furthermore, municipalities are also likely

to be affected by the negative economic and other effects resulting from the 2017 hurricanes and from expense, revenue or cash management measures taken by the Puerto Rico government to address its fiscal and liquidity shortfalls, or measures included in fiscal plans of other government entities, such as the fiscal plans of the GDB and the Puerto Rico Electric Power Authority (“PREPA”). Given the uncertain effect that the negative fiscal situation of the Puerto Rico central government and the measures taken, or to be taken, by other government entities may have on municipalities, the Corporation cannot be certain if future impairment charges will be required relating to these securities.

From time to time, the Corporation has securities held to maturity with an original maturity of three months or less that are considered cash and cash equivalents and classified as money market investments in the consolidated statements of financial condition. As of June 30, 2018 and December 31, 2017, the Corporation had no outstanding securities held to maturity that were classified as cash and cash equivalents.

## **NOTE 6 – OTHER INVESTMENT SECURITIES**

Institutions that are members of the FHLB system are required to maintain a minimum investment in FHLB stock. Such minimum investment is calculated as a percentage of aggregate outstanding mortgages, and the FHLB requires an additional investment that is calculated as a percentage of total FHLB advances, letters of credit, and the collateralized portion of outstanding interest-rate swaps. The stock is capital stock issued at \$100 par value. Both stock and cash dividends may be received on FHLB stock.

As of June 30, 2018 and December 31, 2017, the Corporation had investments in FHLB stock with a book value of \$40.8 million and \$40.9 million, respectively. Dividend income from FHLB stock for the quarters ended June 30, 2018 and 2017 was \$0.7 million and \$0.5 million, respectively, and for the six-month periods ended June 30, 2018 and 2017 was \$1.3 million and \$0.9 million, respectively.

The FHLB of New York issued the shares of FHLB stock owned by the Corporation. The FHLB of New York is part of the Federal Home Loan Bank System, a national wholesale banking network of 11 regional, stockholder-owned congressionally chartered banks. The FHLBs are all privately capitalized and operated by their member stockholders. The system is supervised by the Federal Housing Finance Agency, which ensures that the FHLBs operate in a financially safe and sound manner, remain adequately capitalized and able to raise funds in the capital markets, and carry out their housing finance mission.

On January 1, 2018, the Corporation adopted ASU 2016-01, resulting in the reclassification of equity securities with a readily determinable fair value of approximately \$0.4 million from available-for-sale investment securities to other investment securities. During the second quarter and six-month period ended June 30, 2018, the Corporation measured these equity securities at fair value through earnings resulting in the recognition of market-to-market losses of \$3 thousand and \$10 thousand, respectively, recorded as part of other non-interest income in the statement of income.

The Corporation has other equity securities that do not have readily available fair values. The aggregate carrying value of such securities as of June 30, 2018 and December 31, 2017 was \$2.2 million.

## **NOTE 7 – LOANS HELD FOR INVESTMENT**

The following provides information about the loan portfolio held for investment:

|   | <b>As of</b>    |    | <b>As of</b>        |
|---|-----------------|----|---------------------|
|   | <b>June 30,</b> |    | <b>December 31,</b> |
|   | <b>2018</b>     |    | <b>2017</b>         |
| (In thousands)  |                 |    |                     |
| Residential mortgage loans, mainly secured by first mortgages | \$ 3,238,001    | \$ | 3,290,957           |
| Commercial loans:   |                 |    |                     |
| Construction loans (1)  | 84,683          |    | 111,397             |
| Commercial mortgage loans (1)(2)                              | 1,533,308       |    | 1,614,972           |
| Commercial and Industrial loans (3)                           | 2,009,049       |    | 2,083,253           |
| Total commercial loans  | 3,627,040       |    | 3,809,622           |
| Finance leases  | 283,274         |    | 257,462             |
| Consumer loans  | 1,491,976       |    | 1,492,435           |
| Loans held for investment                                     | 8,640,291       |    | 8,850,476           |
| Allowance for loan and lease losses                           | (222,035)       |    | (231,843)           |
| Loans held for investment, net                                | \$ 8,418,256    | \$ | 8,618,633           |

- (1) During the first quarter of 2018, the Corporation transferred \$57.2 million (net of fair value write-downs of \$9.7 million) in non-performing loans to held for sale. Loans transferred to held for sale consisted of a \$30.0 million non-performing construction loan (net of a \$5.1 million fair value write-down) and two non-performing commercial mortgage loans totaling \$27.2 million (net of fair value write-downs of \$4.6 million).
- (2) During the second quarter of 2018, the Corporation completed the sale of a \$10.4 million non-performing commercial mortgage loan that was among the loans transferred to held for sale in the first quarter of 2018.
- (3) As of June 30, 2018 and December 31, 2017, includes \$792.0 million and \$833.5 million, respectively, of commercial loans that are secured by real estate but are not dependent upon the real estate for repayment.

Loans held for investment on which accrual of interest income had been discontinued were as follows:

| (In thousands)   | <b>As of<br/>June 30,<br/>2018</b> | <b>As of<br/>December 31,<br/>2017</b> |
|--|------------------------------------|--|
| Non-performing loans:                                    |                                    |  |
| Residential mortgage                                     | \$ 162,539                         | \$ 178,291                             |
| Commercial mortgage (1)                                  | 142,614                            | 156,493                                |
| Commercial and Industrial                                | 76,887                             | 85,839                                 |
| Construction:  |                                    |  |
| Land   | 12,926                             | 15,026                                 |
| Construction-commercial (1)                              | -                                  | 35,100                                 |
| Construction-residential                                 | 1,222                              | 1,987                                  |
| Consumer:  |                                    |  |
| Auto loans   | 12,299                             | 10,211                                 |
| Finance leases   | 2,032                              | 1,237                                  |
| Other consumer loans                                     | 8,622                              | 5,370                                  |
| Total non-performing loans held for investment (2)(3)(4) | \$ 419,141                         | \$ 489,554                             |

- (1) During the first quarter of 2018, the Corporation transferred \$57.2 million (net of fair value write-downs of \$9.7 million) in non-performing loans to held for sale. Loans transferred to held for sale consisted of a \$30.0 million non-performing construction loan (net of a \$5.1 million fair value write-down) and two non-performing commercial mortgage loans totaling \$27.2 million (net of fair value write-downs of \$4.6 million).
- (2) Excludes \$54.5 million and \$8.3 million of non-performing loans held for sale as of June 30, 2018 and December 31, 2017, respectively.
- (3) Amount excludes purchased-credit impaired (“PCI”) loans with a carrying value of approximately \$152.2 million and \$158.2 million as of June 30, 2018 and December 31, 2017, respectively, primarily mortgage loans acquired from Doral Bank in the first quarter of 2015 and from Doral Financial in the second quarter of 2014, as further discussed below. These loans are not considered non-performing due to the application of the accretion method, under which these loans will accrete interest income over the remaining life of the loans using an estimated cash flow analysis.
- (4) Non-performing loans exclude \$393.3 million and \$374.7 million of Troubled Debt Restructuring (“TDR”) loans that are in compliance with modified terms and in accrual status as of June 30, 2018 and December 31, 2017, respectively.

During the first quarter of 2018, the Corporation transferred to held for sale three non-performing commercial and construction loans. The aggregate recorded investment in these loans was written down to \$57.2 million, which resulted in charge-offs of \$9.7 million, of which \$4.1 million was taken against previously-established reserves for loan losses, resulting in a charge to the provision for loan and lease losses of \$5.6 million in the first quarter of 2018. Loans transferred to held for sale consisted of a \$30.0 million non-performing construction loan (net of a \$5.1 million fair value write-down) and two non-performing commercial mortgage loans totaling \$27.2 million (net of fair value write-downs of \$4.6 million).



During the second quarter of 2018, the Corporation completed the sale of a \$10.4 million non-performing commercial mortgage loan that was among the loans transferred to held for sale during the first quarter.

***Loans in Process of Foreclosure***

As of June 30, 2018, the recorded investment of residential mortgage loans collateralized by residential real estate property that are in the process of foreclosure amounted to \$142.6 million, including \$21.8 million of loans insured by the FHA or guaranteed by the VA, and \$12.4 million of PCI loans. The Corporation commences the foreclosure process on residential real estate loans when a borrower becomes 120 days delinquent in accordance with the guidelines of the Consumer Financial Protection Bureau (“CFPB”). Foreclosure procedures and timelines vary depending on whether the property is located in a judicial or non-judicial state. Judicial states (i.e., Puerto Rico, Florida and USVI) require the foreclosure to be processed through the state’s court while foreclosure in non-judicial states (i.e., BVI) is processed without court intervention. Foreclosure timelines vary according to state law and investor guidelines. Occasionally, foreclosures may be delayed due to, among other reasons, mandatory mediations, bankruptcy, court delays and title issues.

The Corporation's aging of the loans held for investment portfolio is as follows:

| As of June<br>30, 2018<br>(In thousands)  | 30-59<br>Days<br>Past Due | 60-89<br>Days<br>Past Due | 90 days<br>or more<br>Past Due<br>(1)(2)(3) | Total<br>Past Due | Purchased<br>Credit-Impaired<br>Loans | Current      | Total loans<br>held for<br>investment | 90 days<br>past due<br>and still<br>accruing<br>(1)(2)(3) |
|---|---------------------------|---------------------------|---|-------------------|---------------------------------------|--------------|---------------------------------------|---|
| Residential<br>mortgage:<br>FHA/VA<br>government-guaranteed<br>loans<br>(2)(3)(4) | \$ -                      | \$ 3,810                  | \$ 109,995                                  | \$ 113,805        | \$ -                                  | \$ 37,698    | \$ 151,503                            | \$ 109,995  |
| Other<br>residential<br>mortgage<br>loans (4)                                     | -                         | 55,861                    | 177,340                                     | 233,201           | 148,025                               | 2,705,272    | 3,086,498                             | 14,801  |
| Commercial:<br>Commercial<br>and Industrial<br>loans                              | 2,768                     | 10,261                    | 77,456                                      | 90,485            | -                                     | 1,918,564    | 2,009,049                             | 569   |
| Commercial<br>mortgage<br>loans (4)   | -                         | 2,401                     | 145,760                                     | 148,161           | 4,217                                 | 1,380,930    | 1,533,308                             | 3,146   |
| Construction:<br>Land (4)   | -                         | 68                        | 18,836                                      | 18,904            | -                                     | 6,135        | 25,039                                | 5,910   |
| Construction-commercial   | -                         | -                         | 1,013                                       | 1,013             | -                                     | 52,806       | 53,819                                | 1,013   |
| Construction-residential-<br>(4)  | -                         | -                         | 1,222                                       | 1,222             | -                                     | 4,603        | 5,825                                 | -   |
| Consumer:<br>Auto loans   | 32,527                    | 6,906                     | 12,299                                      | 51,732            | -                                     | 804,224      | 855,956                               | -   |
| Finance<br>leases   | 5,777                     | 1,404                     | 2,032                                       | 9,213             | -                                     | 274,061      | 283,274                               | -   |
| Other<br>consumer<br>loans  | 8,112                     | 5,039                     | 14,649                                      | 27,800            | -                                     | 608,220      | 636,020                               | 6,027   |
| Total<br>loans held for<br>investment   | \$ 49,184                 | \$ 85,750                 | \$ 560,602                                  | \$ 695,536        | \$ 152,242                            | \$ 7,792,513 | \$ 8,640,291                          | \$ 141,461  |

(1) Includes non-performing loans and accruing loans that are contractually delinquent 90 days or more (i.e., FHA/VA guaranteed loans and credit cards). Credit card loans continue to accrue finance charges and fees until charged-off at 180 days.

(2) It is the Corporation's policy to report delinquent residential mortgage loans insured by the FHA or guaranteed by the VA as past-due loans 90 days and still accruing as opposed to non-performing loans since the principal repayment is insured. These balances include \$30.1 million of residential mortgage loans insured by the FHA or

guaranteed by the VA that are over 15 months delinquent, and are no longer accruing interest as of June 30, 2018.

- (3) As of June 30, 2018, includes \$78.7 million of defaulted loans collateralizing GNMA securities for which the Corporation has an unconditional option (but not an obligation) to repurchase the defaulted loans.
- (4) According to the Corporation's delinquency policy and consistent with the instructions for the preparation of the Consolidated Financial Statements for Bank Holding Companies (FR Y-9C) required by the Federal Reserve Board, residential mortgage, commercial mortgage, and construction loans are considered past due when the borrower is in arrears on two or more monthly payments. FHA/VA government-guaranteed loans, other residential mortgage loans, commercial mortgage loans, land loans, construction-residential loans and construction-commercial loans past due 30-59 days as of June 30, 2018 amounted to \$6.8 million, \$112.0 million, \$3.0 million, \$0.4 million, \$0.3 million and \$0.6 million, respectively.

As of  
December 31,  
2017

| (In thousands)  | 30-59<br>Days<br>Past Due | 60-89<br>Days Past<br>Due | 90 days<br>or more<br>Past Due<br>(1)(2)(3) | Total<br>Past<br>Due | Purchased<br>Credit-<br>Impaired<br>Loans | Current   | Total loans<br>held for<br>investment | 90 days<br>past due<br>and still<br>accruing<br>(1)(2)(3) |
|---|---------------------------|---------------------------|---|----------------------|---|-----------|---------------------------------------|---|
| Residential<br>mortgage:                                |                           |                           |   |                      |   |           |                                       |   |
| FHA/VA<br>government-guaranteed<br>loans (2) (3)<br>(4) | \$ -                      | \$ 6,792                  | \$102,815                                   | \$109,607            | \$ -                                      | \$ 29,332 | \$ 138,939                            | \$102,815   |
| Other<br>residential<br>mortgage loans<br>(4)           | -                         | 92,502                    | 193,750                                     | 286,252              | 153,991                                   | 2,711,775 | 3,152,018                             | 15,459  |
| Commercial:   |                           |                           |   |                      |   |           |                                       |   |
| Commercial<br>and Industrial<br>loans                   | 8,971                     | 576                       | 88,156                                      | 97,703               | -   | 1,985,550 | 2,083,253                             | 2,317   |
| Commercial<br>mortgage loans<br>(4)                     | -                         | 7,525                     | 163,180                                     | 170,705              | 4,183                                     | 1,440,084 | 1,614,972                             | 6,687   |
| Construction:   |                           |                           |   |                      |   |           |                                       |   |
| Land (4)  | -                         | 124                       | 15,177                                      | 15,301               | -   | 11,630    | 26,931                                | 151   |
| Construction-commercial                                 | -                         | -                         | 35,100                                      | 35,100               | -   | 41,456    | 76,556                                | -   |
| Construction-residential                                | -                         | 95                        | 1,987                                       | 2,082                | -   | 5,828     | 7,910                                 | -   |
| Consumer:   |                           |                           |   |                      |   |           |                                       |   |
| Auto loans  | 57,560                    | 23,783                    | 10,211                                      | 91,554               | -   | 752,777   | 844,331                               | -   |
| Finance<br>leases                                       | 10,549                    | 3,484                     | 1,237                                       | 15,270               | -   | 242,192   | 257,462                               | -   |
|   | 10,776                    | 5,052                     | 9,361                                       | 25,189               | -   | 622,915   | 648,104                               | 3,991   |

|                     |           |            |            |            |            |              |              |            |  |
|---------------------|-----------|------------|------------|------------|------------|--------------|--------------|------------|--|
| Other               |           |            |            |            |            |              |              |            |  |
| consumer loans      |           |            |            |            |            |              |              |            |  |
| Total loans         |           |            |            |            |            |              |              |            |  |
| held for investment | \$ 87,856 | \$ 139,933 | \$ 620,974 | \$ 848,763 | \$ 158,174 | \$ 7,843,539 | \$ 8,850,476 | \$ 131,420 |  |

- (1) Includes non-performing loans and accruing loans that are contractually delinquent 90 days or more (i.e. FHA/VA guaranteed loans and credit cards). Credit card loans continue to accrue finance charges and fees until charged-off at 180 days.
- (2) It is the Corporation's policy to report delinquent residential mortgage loans insured by the FHA or guaranteed by the VA as past-due loans 90 days and still accruing as opposed to non-performing loans since the principal repayment is insured. These balances include \$29.9 million of residential mortgage loans insured by the FHA or guaranteed by the VA that are over 15 months delinquent, and are no longer accruing interest as of December 31, 2017.
- (3) As of December 31, 2017, includes \$62.1 million of defaulted loans collateralizing GNMA securities for which the Corporation has an unconditional option (but not an obligation) to repurchase the defaulted loans.
- (4) According to the Corporation's delinquency policy and consistent with the instructions for the preparation of the Consolidated Financial Statements for Bank Holding Companies (FR Y-9C) required by the Federal Reserve Board, residential mortgage, commercial mortgage, and construction loans are considered past due when the borrower is in arrears on two or more monthly payments. FHA/VA government-guaranteed loans, other residential mortgage loans, commercial mortgage loans, and land loans past due 30-59 days as of December 31, 2017 amounted to \$6.0 million, \$224.0 million, \$9.0 million, and \$2.5 million, respectively.

The Corporation's credit quality indicators by loan type as of June 30, 2018 and December 31, 2017 are summarized below:

**Commercial Credit Exposure - Credit Risk Profile Based on Creditworthiness  
Category:**

| June 30, 2018<br>(In thousands) | Substandard | Doubtful | Loss | Total<br>Adversely<br>Classified (1) | Total Portfolio |
|---------------------------------|-------------|----------|------|--------------------------------------|-----------------|
| Commercial mortgage             | \$ 291,045  | \$ -     | \$ - | \$ 291,045                           | \$ 1,533,308    |
| Construction:                   |             |          |      |                                      |                 |
| Land                            | 14,350      | -        | -    | 14,350                               | 25,039          |
| Construction - commercial       | -           | -        | -    | -                                    | 53,819          |
| Construction - residential      | 1,222       | -        | -    | 1,222                                | 5,825           |
| Commercial and Industrial       | 123,855     | 5,072    | 341  | 129,268                              | 2,009,049       |

**Commercial Credit Exposure - Credit Risk Profile Based on Creditworthiness  
Category:**

| December 31, 2017<br>(In thousands) | Substandard | Doubtful | Loss | Total<br>Adversely<br>Classified (1) | Total Portfolio |
|-------------------------------------|-------------|----------|------|--------------------------------------|-----------------|
| Commercial mortgage                 | \$ 257,503  | \$ 4,166 | \$ - | \$ 261,669                           | \$ 1,614,972    |

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|                            |         |       |     |         |           |
|----------------------------|---------|-------|-----|---------|-----------|
| Construction:              |         |       |     |         |           |
| Land                       | 15,971  | 490   | -   | 16,461  | 26,931    |
| Construction - commercial  | 35,100  | -     | -   | 35,100  | 76,556    |
| Construction - residential | 1,987   | -     | -   | 1,987   | 7,910     |
| Commercial and Industrial  | 154,416 | 3,854 | 676 | 158,946 | 2,083,253 |

(1) Excludes non-performing loans held for sale of \$54.5 million (\$16.8 million commercial mortgage, \$30.0 million construction-commercial, and \$7.7 million construction-land) and \$8.3 million (construction-land) as of June 30, 2018 and December 31, 2017, respectively.



| <b>June 30, 2018</b><br>(In thousands) | <b>FHA/VA/<br/>Guaranteed</b> | <b>Other<br/>residential<br/>loans</b> | <b>Auto</b> | <b>Finance<br/>Leases</b> | <b>Other<br/>Consumer</b> |
|--|-------------------------------|--|-------------|---------------------------|---------------------------|
|  | (1)                           |  |             |                           |                           |
| Performing                             | \$ 151,503                    | \$ 2,775,934                           | \$ 843,657  | \$ 281,242                | \$ 627,398                |
| Purchased                              | -                             | 148,025                                | -           | -                         | -                         |
| Credit-Impaired (2)                    | -                             | 162,539                                | 12,299      | 2,032                     | 8,622                     |
| Non-performing                         | -                             | 162,539                                | 12,299      | 2,032                     | 8,622                     |
| Total                                  | \$ 151,503                    | \$ 3,086,498                           | \$ 855,956  | \$ 283,274                | \$ 636,020                |

- (1) It is the Corporation's policy to report delinquent residential mortgage loans insured by the FHA or guaranteed by the VA as 90 days past-due loans and still accruing as opposed to non-performing loans since the principal repayment is insured. This balance includes \$30.1 million of residential mortgage loans insured by the FHA or guaranteed by the VA, which are over 15 months delinquent, and are no longer accruing interest as of June 30, 2018.
- (2) PCI loans are excluded from non-performing statistics due to the application of the accretion method, under which these loans will accrete interest income over the remaining life of the loans using estimated cash flow analyses.

**Consumer Credit Exposure - Credit Risk Profile Based on Payment Activity**

| <b>December 31, 2017</b><br>(In thousands) | <b>Residential Real Estate</b> |  | <b>Consumer</b> |                           |                           |
|--|--------------------------------|--|-----------------|---------------------------|---------------------------|
|  | <b>FHA/VA/<br/>Guaranteed</b>  | <b>Other<br/>residential<br/>loans</b> | <b>Auto</b>     | <b>Finance<br/>Leases</b> | <b>Other<br/>Consumer</b> |
|  | (1)                            |  |                 |                           |                           |
| Performing                                 | \$ 138,939                     | \$ 2,819,736                           | \$ 834,120      | \$ 256,225                | \$ 642,734                |
| Purchased                                  | -                              | 153,991                                | -               | -                         | -                         |
| Credit-Impaired (2)                        | -                              | 178,291                                | 10,211          | 1,237                     | 5,370                     |
| Non-performing                             | -                              | 178,291                                | 10,211          | 1,237                     | 5,370                     |
| Total                                      | \$ 138,939                     | \$ 3,152,018                           | \$ 844,331      | \$ 257,462                | \$ 648,104                |

- (1) It is the Corporation's policy to report delinquent residential mortgage loans insured by the FHA or guaranteed by the VA as 90 days past-due loans and still accruing as opposed to non-performing loans since the principal repayment is insured. This balance includes \$29.9 million of residential mortgage loans insured by the FHA or guaranteed by the VA, which are over 15 months delinquent, and are no longer accruing interest as of December 31, 2017.
- (2) PCI loans are excluded from non-performing statistics due to the application of the accretion method, under which these loans will accrete interest income over the remaining life of the loans using estimated cash flow analyses.

The following tables present information about impaired loans held for investment, excluding PCI loans, which are reported separately as discussed below:

### Impaired Loans

|   |            |            |           |            | Quarter Ended               |          | Six-Month Period Ended |          |     |     |
|---|------------|------------|-----------|------------|-----------------------------|----------|------------------------|----------|-----|-----|
|   |            |            |           |            |                             |          | June 30, 2018          |          |     |     |
|   |            |            |           |            | Interest Income             |          | Interest Income        |          |     |     |
|   |            |            |           |            | Year-To-Date Recognized     |          | Recognized             |          |     |     |
|   |            |            |           |            | Unpaid Recorded Investment  |          | on Cash Accrual Basis  |          |     |     |
|   |            |            |           |            | Average Recorded Investment |          | on Cash Accrual Basis  |          |     |     |
|   |            |            |           |            | on Investment Basis         |          | on Cash Accrual Basis  |          |     |     |
|   |            |            |           |            | on Investment Basis         |          | on Cash Accrual Basis  |          |     |     |
|   |            |            |           |            | on Investment Basis         |          | on Cash Accrual Basis  |          |     |     |
|   |            |            |           |            | on Investment Basis         |          | on Cash Accrual Basis  |          |     |     |
| (In thousands)                                      |            |            |           |            |                             |          |                        |          |     |     |
| <b>As of June 30, 2018</b>                          |            |            |           |            |                             |          |                        |          |     |     |
| <b>With no related specific allowance recorded:</b> |            |            |           |            |                             |          |                        |          |     |     |
| FHA/VA-Guaranteed loans                             | \$         | -          | \$        | -          | \$                          | -        | \$                     | -        | \$  | -   |
| Other residential mortgage loans                    | 121,396    | 163,583    | -         | 123,058    | 788                         | 193      | 1,529                  | 351      |     |     |
| Commercial:   |            |            |           |            |                             |          |                        |          |     |     |
| Commercial mortgage loans                           | 58,992     | 100,247    | -         | 62,892     | 119                         | 41       | 201                    | 78       |     |     |
| Commercial and Industrial loans                     | 43,566     | 60,380     | -         | 45,086     | 496                         | 8        | 920                    | 20       |     |     |
| Consumer:   |            |            |           |            |                             |          |                        |          |     |     |
| Auto loans  | 326        | 326        | -         | 342        | 4                           | -        | 5                      | -        |     |     |
| Other consumer loans                                | 2,454      | 2,801      | -         | 2,639      | 35                          | 9        | 72                     | 21       |     |     |
|   | \$ 226,734 | \$ 327,337 | \$        | -          | \$ 234,017                  | \$ 1,442 | \$ 251                 | \$ 2,727 | \$  | 470 |
| <b>With a related specific allowance recorded:</b>  |            |            |           |            |                             |          |                        |          |     |     |
| FHA/VA-Guaranteed loans                             | \$         | -          | \$        | -          | \$                          | -        | \$                     | -        | \$  | -   |
| Other residential mortgage loans                    | 287,689    | 312,868    | 19,804    | 290,079    | 3,570                       | 178      | 7,089                  | 473      |     |     |
| Commercial:   |            |            |           |            |                             |          |                        |          |     |     |
| Commercial mortgage loans                           | 116,583    | 127,995    | 12,204    | 119,058    | 737                         | 307      | 1,397                  | 354      |     |     |
| Commercial and Industrial loans                     | 67,805     | 80,850     | 10,592    | 69,293     | 128                         | 8        | 253                    | 24       |     |     |
| Construction:                                       |            |            |           |            |                             |          |                        |          |     |     |
| Land  | 11,009     | 19,868     | 1,022     | 11,522     | 23                          | 7        | 47                     | 15       |     |     |
| Construction-residential                            | 252        | 355        | 39        | 252        | -                           | -        | -                      | -        |     |     |
| Consumer:   |            |            |           |            |                             |          |                        |          |     |     |
| Auto loans  | 19,367     | 19,367     | 3,697     | 20,484     | 385                         | -        | 779                    | -        |     |     |
| Finance leases                                      | 1,594      | 1,594      | 162       | 1,754      | 28                          | -        | 59                     | -        |     |     |
| Other consumer loans                                | 9,101      | 9,584      | 1,994     | 9,434      | 241                         | 25       | 489                    | 53       |     |     |
|   | \$ 513,400 | \$ 572,481 | \$ 49,514 | \$ 521,876 | \$ 5,112                    | \$ 525   | \$ 10,113              | \$       | 919 |     |
| <b>Total:</b>                                       |            |            |           |            |                             |          |                        |          |     |     |
| FHA/VA-Guaranteed loans                             | \$         | -          | \$        | -          | \$                          | -        | \$                     | -        | \$  | -   |
| Other residential mortgage loans                    | 409,085    | 476,451    | 19,804    | 413,137    | 4,358                       | 371      | 8,618                  | 824      |     |     |
| Commercial:   |            |            |           |            |                             |          |                        |          |     |     |



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|                                 |            |            |           |            |          |        |           |          |
|---------------------------------|------------|------------|-----------|------------|----------|--------|-----------|----------|
| Commercial mortgage loans       | 175,575    | 228,242    | 12,204    | 181,950    | 856      | 348    | 1,598     | 432      |
| Commercial and Industrial loans | 111,371    | 141,230    | 10,592    | 114,379    | 624      | 16     | 1,173     | 44       |
| Construction:                   |            |            |           |            |          |        |           |          |
| Land                            | 11,009     | 19,868     | 1,022     | 11,522     | 23       | 7      | 47        | 15       |
| Construction-commercial         | -          | -          | -         | -          | -        | -      | -         | -        |
| Construction-residential        | 252        | 355        | 39        | 252        | -        | -      | -         | -        |
| Consumer:                       |            |            |           |            |          |        |           |          |
| Auto loans                      | 19,693     | 19,693     | 3,697     | 20,826     | 389      | -      | 784       | -        |
| Finance leases                  | 1,594      | 1,594      | 162       | 1,754      | 28       | -      | 59        | -        |
| Other consumer loans            | 11,555     | 12,385     | 1,994     | 12,073     | 276      | 34     | 561       | 74       |
|                                 | \$ 740,134 | \$ 899,818 | \$ 49,514 | \$ 755,893 | \$ 6,554 | \$ 776 | \$ 12,840 | \$ 1,389 |

**Impaired Loans**

|   | <b>Recorded<br/>Investment</b> | <b>Unpaid<br/>Principal<br/>Balance</b> | <b>Related<br/>Specific<br/>Allowance</b> | <b>Year-To-Date<br/>Average<br/>Recorded<br/>Investment</b> |
|---|--------------------------------|---|---|---|
| (In thousands)                                      |                                |   |   |   |
| <b>As of December 31, 2017</b>                      |                                |   |   |   |
| <b>With no related specific allowance recorded:</b> |                                |   |   |   |
| FHA/VA-Guaranteed loans                             | \$ -                           | \$ -                                    | \$ -                                      | \$ -  |
| Other residential mortgage loans                    | 116,818                        | 154,048                                 | -   | 120,241   |
| Commercial:   |                                |   |   |   |
| Commercial mortgage loans                           | 65,100                         | 100,612                                 | -   | 86,563  |
| Commercial and Industrial loans                     | 28,292                         | 31,254                                  | -   | 28,567  |
| Construction:                                       |                                |   |   |   |
| Land  | 48                             | 49                                      | -   | 48  |
| Consumer:   |                                |   |   |   |
| Auto loans  | 267                            | 267                                     | -   | 290   |
| Other consumer loans                                | 2,521                          | 3,688                                   | -   | 2,745   |
|   | \$ 213,046                     | \$ 289,918                              | \$ -                                      | \$ 238,454  |
| <b>With a related specific allowance recorded:</b>  |                                |   |   |   |
| FHA/VA-Guaranteed loans                             | \$ -                           | \$ -                                    | \$ -                                      | \$ -  |
| Other residential mortgage loans                    | 316,616                        | 349,284                                 | 22,086                                    | 318,606   |
| Commercial:   |                                |   |   |   |
| Commercial mortgage loans                           | 87,814                         | 124,084                                 | 9,783                                     | 93,720  |
| Commercial and Industrial loans                     | 90,008                         | 112,005                                 | 12,359                                    | 92,666  |
| Construction:                                       |                                |   |   |   |
| Land  | 11,865                         | 19,973                                  | 1,402                                     | 14,126  |
| Construction-commercial                             | 35,101                         | 38,595                                  | 560                                       | 35,996  |
| Construction-residential                            | 252                            | 355                                     | 55  | 252   |
| Consumer:   |                                |   |   |   |
| Auto loans  | 22,338                         | 22,338                                  | 3,665                                     | 24,328  |
| Finance leases                                      | 2,184                          | 2,184                                   | 104                                       | 2,428   |
| Other consumer loans                                | 11,084                         | 11,830                                  | 1,396                                     | 11,579  |
|   | \$ 577,262                     | \$ 680,648                              | \$ 51,410                                 | \$ 593,701  |
| <b>Total:</b>                                       |                                |   |   |   |
| FHA/VA-Guaranteed loans                             | \$ -                           | \$ -                                    | \$ -                                      | \$ -  |
| Other residential mortgage loans                    | 433,434                        | 503,332                                 | 22,086                                    | 438,847   |
| Commercial:   |                                |   |   |   |
| Commercial mortgage loans                           | 152,914                        | 224,696                                 | 9,783                                     | 180,283   |
| Commercial and Industrial loans                     | 118,300                        | 143,259                                 | 12,359                                    | 121,233   |
| Construction:                                       |                                |   |   |   |
| Land  | 11,913                         | 20,022                                  | 1,402                                     | 14,174  |
| Construction-commercial                             | 35,101                         | 38,595                                  | 560                                       | 35,996  |
| Construction-residential                            | 252                            | 355                                     | 55  | 252   |
| Consumer:   |                                |   |   |   |
| Auto loans  | 22,605                         | 22,605                                  | 3,665                                     | 24,618  |

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|                      |            |            |           |            |
|----------------------|------------|------------|-----------|------------|
| Finance leases       | 2,184      | 2,184      | 104       | 2,428      |
| Other consumer loans | 13,605     | 15,518     | 1,396     | 14,324     |
|                      | \$ 790,308 | \$ 970,566 | \$ 51,410 | \$ 832,155 |

Interest income of approximately \$6.8 million (\$6.3 million on an accrual basis and \$0.5 million on a cash basis) and \$13.6 million (\$12.4 million on an accrual basis and \$1.2 million on a cash basis) was recognized on impaired loans for the second quarter and six-month period ended June 30, 2017, respectively.

The following tables show the activity for impaired loans and the related specific reserve for the quarters and six-month periods ended June 30, 2018 and 2017:

|   | Quarter Ended<br>June 30, |            | Six-Month Period Ended<br>June 30, |            |
|---|---------------------------|------------|------------------------------------|------------|
|   | 2018                      | 2017       | 2018                               | 2017       |
| (In thousands)                              |                           |            |                                    |            |
| <b>Impaired Loans:</b>                      |                           |            |                                    |            |
| Balance at beginning of period              | \$ 746,280                | \$ 807,198 | \$ 790,308                         | \$ 887,905 |
| Loans determined impaired during the period | 34,273                    | 18,976     | 95,681                             | 38,604     |
| Charge-offs (1)(2)                          | (13,207)                  | (43,083)   | (30,420)                           | (60,487)   |
| Loans sold, net of charge-offs              | -                         | -          | (4,121)                            | (53,245)   |
| Increases to existing impaired loans        | 77                        | 698        | 7,075                              | 1,239      |
| Foreclosures                                | (7,777)                   | (21,233)   | (19,452)                           | (30,690)   |
| Loans no longer considered impaired         | (2,433)                   | (1,890)    | (3,940)                            | (2,782)    |
| Loans transferred to held for sale          | -                         | -          | (57,213)                           | -          |
| Paid in full or partial payments            | (17,079)                  | (25,041)   | (37,784)                           | (44,919)   |
| Balance at end of period                    | \$ 740,134                | \$ 735,625 | \$ 740,134                         | \$ 735,625 |

- (1) For the six-month period ended June 30, 2018 includes charge-offs totaling \$9.7 million associated with the \$57.2 million in non-performing loans transferred to held for sale.
- (2) For the six-month period ended June 30, 2017 includes a charge-off of \$10.7 million related to the sale of the PREPA credit line as further discussed below.

|                                | Quarter Ended<br>June 30, |           | Six-Month Period Ended<br>June 30, |           |
|--------------------------------|---------------------------|-----------|------------------------------------|-----------|
|                                | 2018                      | 2017      | 2018                               | 2017      |
| (In thousands)                 |                           |           |                                    |           |
| <b>Specific Reserve:</b>       |                           |           |                                    |           |
| Balance at beginning of period | \$ 56,930                 | \$ 66,311 | \$ 51,410                          | 64,421    |
| Provision for loan losses      | 5,753                     | 17,563    | 28,456                             | 36,195    |
| Net charge-offs                | (13,169)                  | (43,080)  | (30,352)                           | (59,822)  |
| Balance at end of period       | \$ 49,514                 | \$ 40,794 | \$ 49,514                          | \$ 40,794 |

**Purchased Credit Impaired Loans (PCI)**

The Corporation acquired PCI loans accounted for under ASC 310-30, “Receivables – Loans and Debt Securities Acquired with Deteriorated Credit Quality” (“ASC Topic 310-30”) as part of a transaction that closed on February 27, 2015 in which FirstBank acquired 10 Puerto Rico branches of Doral Bank, and acquired certain assets, including PCI loans, and assumed deposits, through an alliance with Banco Popular of Puerto Rico, that was the successful lead bidder with the FDIC on the failed Doral Bank, as well as other co-bidders. The Corporation also acquired PCI loans in previously completed asset acquisitions that are accounted for under ASC Topic 310-30. These previous transactions include the acquisition from Doral Financial in the second quarter of 2014 of all its rights, title and interest in first and second residential mortgages loans in full satisfaction of secured borrowings owed by such entity to FirstBank.

Under ASC Topic 310-30, the acquired PCI loans were aggregated into pools based on similar characteristics (i.e. delinquency status and loan terms). Each loan pool is accounted for as a single asset with a single composite interest rate and an aggregate expectation of cash flows. Since the loans are accounted for under ASC Topic 310-30, they are not considered non-performing and will continue to have an accretable yield as long as there is a reasonable expectation about the timing and amount of cash flows expected to be collected. The Corporation recognizes additional losses on this portfolio when it is probable that the Corporation will be unable to collect all cash flows expected as of the acquisition date plus additional cash flows expected to be collected arising from changes in estimates after the acquisition date.

The carrying amounts of PCI loans were as follows:

|   |    | <b>June 30,<br/>2018</b> | <b>As of</b> | <b>December 31,<br/>2017</b> |
|---|----|--------------------------|--------------|------------------------------|
| (In thousands)                                    |    |                          |              |                              |
| Residential mortgage loans                        | \$ | 148,025                  | \$           | 153,991                      |
| Commercial mortgage loans                         |    | 4,217                    |              | 4,183                        |
| Total PCI loans                                   | \$ | 152,242                  | \$           | 158,174                      |
| Allowance for loan losses                         |    | (11,354)                 |              | (11,251)                     |
| Total PCI loans, net of allowance for loan losses | \$ | 140,888                  | \$           | 146,923                      |

The following tables present PCI loans by past due status as of June 30, 2018 and December 31, 2017:

| <b>As of June 30, 2018</b> |    | <b>30-59<br/>Days</b> | <b>60-89<br/>Days</b> | <b>90 days or<br/>more</b> | <b>Total Past<br/>Due</b> | <b>Current</b> | <b>Total PCI<br/>loans</b> |
|----------------------------|----|-----------------------|-----------------------|----------------------------|---------------------------|----------------|----------------------------|
| (In thousands)             |    |                       |                       |                            |                           |                |                            |
| Residential mortgage loans | \$ | -                     | \$ 8,588              | \$ 27,024                  | \$ 35,612                 | \$ 112,413     | \$ 148,025                 |
| Commercial mortgage loans  |    | -                     | -                     | 3,252                      | 3,252                     | 965            | 4,217                      |

|           |    |   |          |           |           |            |            |
|-----------|----|---|----------|-----------|-----------|------------|------------|
| Total (1) | \$ | - | \$ 8,588 | \$ 30,276 | \$ 38,864 | \$ 113,378 | \$ 152,242 |
|-----------|----|---|----------|-----------|-----------|------------|------------|

(1) According to the Corporation's delinquency policy and consistent with the instructions for the preparation of the Consolidated Financial Statements for Bank Holding Companies (FR Y-9C) required by the Federal Reserve Board, residential mortgage and commercial mortgage loans are considered past due when the borrower is in arrears two or more monthly payments. PCI residential mortgage loans past due 30-59 days as of June 30, 2018 amounted to \$11.7 million. No PCI commercial mortgage loan was 30-59 days past due as of June 30, 2018.

| As of December 31, 2017    | 30-59 Days | 60-89 Days | 90 days or more | Total Past Due | Current    | Total PCI loans |
|----------------------------|------------|------------|-----------------|----------------|------------|-----------------|
| (In thousands)             |            |            |                 |                |            |                 |
| Residential mortgage loans | \$ -       | \$ 16,600  | \$ 26,471       | \$ 43,071      | \$ 110,920 | \$ 153,991      |
| Commercial mortgage loans  | -          | 355        | 2,834           | 3,189          | 994        | 4,183           |
| Total (1)                  | \$ -       | \$ 16,955  | \$ 29,305       | \$ 46,260      | \$ 111,914 | \$ 158,174      |

(1) According to the Corporation's delinquency policy and consistent with the instructions for the preparation of the Consolidated Financial Statements for Bank Holding Companies (FR Y-9C) required by the Federal Reserve Board, residential mortgage and commercial mortgage loans are considered past due when the borrower is in arrears two or more monthly payments. PCI residential mortgage loans and commercial mortgage loans past due 30-59 days as of December 31, 2017 amounted to \$28.1 million and \$0.2 million, respectively.

*Initial Fair Value and Accretable Yield of PCI Loans*

At acquisition of PCI loans, the Corporation estimated the cash flows the Corporation expected to collect on the loans. Under the accounting guidance for PCI loans, the difference between the contractually required payments and the cash flows expected to be collected at acquisition is referred to as the non-accretable difference. This difference is neither accreted into income nor recorded on the Corporation's consolidated statements of financial condition. The excess of cash flows expected to be collected over the estimated fair value is referred to as the accretable yield and is recognized in interest income over the remaining life of the loans, using the effective-yield method.

*Changes in Accretable Yield of Acquired Loans*

Subsequent to the acquisition of loans, the Corporation is required to periodically evaluate its estimate of cash flows expected to be collected. These evaluations, performed quarterly, require the continued use of key assumptions and estimates, similar to the initial estimate of fair value. Subsequent changes in the estimated cash flows expected to be collected may result in changes in the accretable yield and non-accretable difference or reclassifications from non-accretable yield to accretable yield. Increases in the cash flows expected to be collected will generally result in an increase in interest income over the remaining life of the loan or pool of loans. Decreases in expected cash flows due to further credit deterioration will generally result in an impairment charge recognized in the Corporation's provision for loan and lease losses, resulting in an increase to the allowance for loan and lease losses. As of June 30, 2018, the reserve related to PCI loans acquired from Doral Financial in 2014 and from Doral Bank in 2015 amounted to \$11.4 million.

Changes in the accretable yield of PCI loans for the quarters and six-month periods ended June 30, 2018 and 2017 were as follows:

|   | <b>Quarter Ended</b>     |                          | <b>Six-Month Period Ended</b> |                          |
|---|--------------------------|--------------------------|-------------------------------|--------------------------|
|   | <b>June 30,<br/>2018</b> | <b>June 30,<br/>2017</b> | <b>June 30,<br/>2018</b>      | <b>June 30,<br/>2017</b> |
| (In thousands)                            |                          |                          |                               |                          |
| Balance at beginning of period            | \$ 101,059               | \$ 113,665               | \$ 103,682                    | \$ 116,462               |
| Accretion recognized in earnings          | (2,570)                  | (2,724)                  | (5,193)                       | (5,521)                  |
| Reclassification (to) from non-accretable | -                        | (1,970)                  | -                             | (1,970)                  |
| Balance at end of period                  | \$ 98,489                | \$ 108,971               | \$ 98,489                     | \$ 108,971               |

Changes in the carrying amount of loans accounted for pursuant to ASC 310-30 were as follows:

|  | <b>Quarter Ended</b> |                      | <b>Six-Month Period Ended</b> |                      |
|--|----------------------|----------------------|-------------------------------|----------------------|
|  | <b>June 30, 2018</b> | <b>June 30, 2017</b> | <b>June 30, 2018</b>          | <b>June 30, 2017</b> |
| (In thousands)                                   |                      |                      |                               |                      |
| Balance at beginning of period                   | \$ 155,281           | \$ 163,100           | \$ 158,174                    | \$ 165,818           |
| Accretion  | 2,570                | 2,724                | 5,193                         | 5,521                |
| Collections                                      | (4,359)              | (4,509)              | (7,755)                       | (9,102)              |
| Foreclosures                                     | (1,250)              | (947)                | (3,370)                       | (1,869)              |
| Ending balance                                   | \$ 152,242           | \$ 160,368           | \$ 152,242                    | \$ 160,368           |
| Allowance for loan losses                        | (11,354)             | (9,446)              | (11,354)                      | (9,446)              |
| Ending balance, net of allowance for loan losses | \$ 140,888           | \$ 150,922           | \$ 140,888                    | \$ 150,922           |

Changes in the allowance for loan losses related to PCI loans were as follows:

|                                | <b>Quarter Ended</b> |                      | <b>Six-Month Period Ended</b> |                      |
|--------------------------------|----------------------|----------------------|-------------------------------|----------------------|
|                                | <b>June 30, 2018</b> | <b>June 30, 2017</b> | <b>June 30, 2018</b>          | <b>June 30, 2017</b> |
| (In thousands)                 |                      |                      |                               |                      |
| Balance at beginning of period | \$ 11,251            | \$ 6,857             | \$ 11,251                     | \$ 6,857             |
| Provision for loan losses      | 103                  | 2,589                | 103                           | 2,589                |
| Balance at the end of period   | \$ 11,354            | \$ 9,446             | \$ 11,354                     | \$ 9,446             |

The outstanding principal balance of PCI loans, including amounts charged off by the Corporation, amounted to \$188.0 million as of June 30, 2018 (December 2017 - \$196.6 million).



## Purchases and Sales of Loans

During the first six months of 2018, the Corporation purchased \$29.7 million of residential mortgage loans consistent with a strategic program to purchase ongoing residential mortgage loan production from mortgage bankers in Puerto Rico. In general, the loans purchased from mortgage bankers were conforming residential mortgage loans. Purchases of conforming residential mortgage loans provide the Corporation the flexibility to retain or sell the loans, including through securitization transactions, depending upon the Corporation's interest rate risk management strategies. When the Corporation sells such loans, it generally keeps the servicing of the loans.

In the ordinary course of business, the Corporation sells residential mortgage loans (originated or purchased) to GNMA and government-sponsored entities ("GSEs"), such as FNMA and FHLMC, which generally securitize the transferred loans into mortgage-backed securities for sale into the secondary market. During the first six months of 2018, the Corporation sold \$119.8 million of FHA/VA mortgage loans to GNMA, which packaged them into mortgage-backed securities. Also, during the first six months of 2018, the Corporation sold approximately \$51.1 million of performing residential mortgage loans to FNMA and FHLMC. The Corporation's continuing involvement in these sold loans consists primarily of servicing the loans. In addition, the Corporation agreed to repurchase loans when it breaches any of the representations and warranties included in the sale agreement. These representations and warranties are consistent with the GSEs' selling and servicing guidelines (i.e., ensuring that the mortgage was properly underwritten according to established guidelines). The total amount of loans sold in the secondary market included \$9.8 million of seasoned residential mortgage loans sold to FNMA in the second quarter of 2018.

For loans sold to GNMA, the Corporation holds an option to repurchase individual delinquent loans issued on or after January 1, 2003 when the borrower fails to make any payment for three consecutive months. This option gives the Corporation the ability, but not the obligation, to repurchase the delinquent loans at par without prior authorization from GNMA.

Under ASC Topic 860, *Transfer and Servicing*, once the Corporation has the unilateral ability to repurchase the delinquent loan, it is considered to have regained effective control over the loan and is required to recognize the loan and a corresponding repurchase liability on the balance sheet regardless of the Corporation's intent to repurchase the loan. As of June 30, 2018 and December 31, 2017, rebooked GNMA delinquent loans included in the residential mortgage loan portfolio amounted to \$78.7 million and \$62.1 million, respectively.

During the first six months of 2018 and 2017, the Corporation repurchased, pursuant to its repurchase option with GNMA, \$2.0 million and \$17.5 million, respectively, of loans previously sold to GNMA. The principal balance of these loans is fully guaranteed and the risk of loss related to the repurchased loans is generally limited to the difference between the delinquent interest payment advanced to GNMA, which is computed at the loan's interest rate, and the interest payments reimbursed by FHA, which are computed at a pre-determined debenture rate. Repurchases of GNMA loans allow the Corporation, among other things, to maintain acceptable delinquency rates on outstanding GNMA pools and remain as a seller and servicer in good standing with GNMA. During the fourth quarter of 2017, the

Corporation requested and received approval from GNMA for the exclusion of loans in the areas affected by Hurricanes Irma and Maria from calculations of delinquency and default ratios established in the GNMA Mortgage-Backed Securities Guide. The Corporation generally remediates any breach of representations and warranties related to the underwriting of such loans according to established GNMA guidelines without incurring losses. The Corporation's estimate of losses related to breaches in representations and warranties is zero as of June 30, 2018.

Loan sales to FNMA and FHLMC are without recourse in relation to the future performance of the loans. The Corporation repurchased at par loans previously sold to FNMA and FHLMC in the amount of \$3 thousand and \$16 thousand during the first half of 2018 and 2017, respectively. The Corporation's risk of loss with respect to these loans is also minimal as these repurchased loans are generally performing loans with documentation deficiencies.

In addition, during the first six months of 2018, the Corporation purchased a \$21.4 million commercial and industrial loan participation. Also, during the first six months of 2018, the Corporation sold a \$5.6 million commercial and industrial adversely-classified loan in Puerto Rico (recording a charge-off of \$1.3 million), a \$10.4 million non-performing commercial mortgage loan held for sale in Puerto Rico, and a \$9.2 million commercial and industrial loan participation in the Florida region.

#### **Sale of the Puerto Rico Electric Power Authority ("PREPA") Loan**

During the first quarter of 2017, the Corporation received an unsolicited offer and sold its outstanding participation in the PREPA line of credit with a book value of \$64 million at the time of sale (principal balance of \$75 million), thereby reducing its direct exposure to the Puerto Rico government. A specific reserve of approximately \$10.2 million had been allocated to this loan. Gross proceeds of \$53.2 million from the sale resulted in an incremental loss of \$0.6 million recorded as a charge to the provision for loan and lease losses in the first quarter of 2017.

## Loan Portfolio Concentration

The Corporation's primary lending area is Puerto Rico. The Corporation's banking subsidiary, FirstBank, also lends in the USVI and BVI markets and in the United States (principally in the state of Florida). Of the total gross loans held for investment of \$8.6 billion as of June 30, 2018, credit risk concentration was approximately 75% in Puerto Rico, 19% in the United States, and 6% in the USVI and BVI.

As of June 30, 2018, the Corporation had \$54.6 million outstanding in loans extended to the Puerto Rico government, its municipalities and public corporations, compared to \$55.9 million as of December 31, 2017. Approximately \$33.1 million of the outstanding loans as of June 30, 2018 consisted of loans extended to municipalities in Puerto Rico, which in most cases are supported by assigned property tax revenues. The vast majority of revenues of the municipalities included in the Corporation's loan portfolio are independent of the Puerto Rico central government. These municipalities are required by law to levy special property taxes in such amounts as are required for the payment of all of their respective general obligation bonds and notes. Late in 2015, the GDB and the Municipal Revenue Collection Center ("CRIM") signed and perfected a deed of trust. Through this deed, the GDB, as fiduciary, is bound to keep the CRIM funds separate from any other deposits and must distribute the funds pursuant to applicable law. The CRIM funds are deposited at another commercial depository financial institution in Puerto Rico. In addition to loans extended to municipalities, the Corporation's exposure to the Puerto Rico government as of June 30, 2018 includes a \$6.7 million loan extended to a unit of the central government, and a \$14.8 million loan granted to an affiliate of PREPA.

In addition, the Corporation had \$114.7 million in exposure to residential mortgage loans that are guaranteed by the Puerto Rico Housing Finance Authority. Residential mortgage loans guaranteed by the Puerto Rico Housing Finance Authority are secured by the underlying properties and the guarantees serve to cover shortfalls in collateral in the event of a borrower default. The Puerto Rico government guarantees up to \$75 million of the principal under the mortgage loan insurance program. According to the most recently-released audited financial statements of the Puerto Rico Housing Finance Authority, as of June 30, 2016, the Puerto Rico Housing Finance Authority's mortgage loans insurance program covered loans in an aggregate of approximately \$576 million. The regulations adopted by the Puerto Rico Housing Finance Authority require the establishment of adequate reserves to guarantee the solvency of the mortgage loan insurance fund. As of June 30, 2016, the most recent date as to which information is available, the Puerto Rico Housing Finance Authority had a restricted net position for such purposes of approximately \$77.4 million.

The Corporation also has credit exposure to USVI government entities. As of June 30, 2018, the Corporation had \$72.5 million in loans to USVI government instrumentalities and public corporations, compared to \$70.4 million as of December 31, 2017. Of the amount outstanding as of June 30, 2018, public corporations of the USVI owed approximately \$49.2 million and an independent instrumentality of the USVI government owed approximately \$23.2 million. As of June 30, 2018, all loans were currently performing and up to date on principal and interest payments.

The Corporation cannot predict at this time the ultimate effect that the current fiscal situation of the Commonwealth of Puerto Rico, the uncertainty about the debt restructuring process, the various legislative and other measures adopted and to be adopted by the Puerto Rico government and the PROMESA oversight board in response to such fiscal situation, and the effect of Hurricane Maria will have on the Puerto Rico economy, the Corporation's clients, and the Corporation's financial condition and results of operations.

## Troubled Debt Restructurings

The Corporation provides homeownership preservation assistance to its customers through a loss mitigation program in Puerto Rico that is similar to the U.S. government's Home Affordable Modification Program guidelines. Depending upon the nature of borrowers' financial condition, restructurings or loan modifications through this program, as well as other restructurings of individual commercial, commercial mortgage, construction, and residential mortgage loans, fit the definition of a TDR. A restructuring of a debt constitutes a TDR if the creditor, for economic or legal reasons related to the debtor's financial difficulties grants a concession to the debtor that it would not otherwise consider. Modifications involve changes in one or more of the loan terms that bring a defaulted loan current and provide sustainable affordability. Changes may include, among others, the extension of the maturity of the loan and modifications of the loan rate. As of June 30, 2018, the Corporation's total TDR loans held for investment of \$557.2 million consisted of \$342.9 million of residential mortgage loans, \$91.7 million of commercial and industrial loans, \$84.3 million of commercial mortgage loans, \$6.4 million of construction loans, and \$31.9 million of consumer loans. Outstanding unfunded commitments on TDR loans amounted to \$1.4 million as of June 30, 2018. In addition, the loans held for sale portfolio includes a \$30.0 million TDR construction loan.

The Corporation's loss mitigation programs for residential mortgage and consumer loans can provide for one or a combination of the following: movement of interest past due to the end of the loan, extension of the loan term, deferral of principal payments and reduction of interest rates either permanently or for a period of up to six years (increasing back in step-up rates). Additionally, in certain cases, the restructuring may provide for the forgiveness of contractually-due principal or interest. Uncollected interest is added to the end of the loan term at the time of the restructuring and not recognized as income until collected or when the loan is paid off. These programs are available only to those borrowers who have defaulted, or are likely to default, permanently on their loan and would lose their homes in a foreclosure action absent some lender concession. Nevertheless, if the Corporation is not reasonably assured that the borrower will comply with its contractual commitment, properties are foreclosed.

Prior to permanently modifying a loan, the Corporation may enter into trial modifications with certain borrowers. Trial modifications generally represent a six-month period during which the borrower makes monthly payments under the anticipated modified payment terms prior to a formal modification. Upon successful completion of a trial modification, the Corporation and the borrower enter into a permanent modification. TDR loans that are participating in or that have been offered a binding trial modification are classified as TDRs when the trial offer is made and continue to be classified as TDRs regardless of whether the borrower enters into a permanent modification. As of June 30, 2018, the Corporation classified an additional \$1.1 million of residential mortgage loans as TDRs that were participating in or had been offered a trial modification.

For the commercial real estate, commercial and industrial, and construction loan portfolios, at the time of a restructuring, the Corporation determines, on a loan-by-loan basis, whether a concession was granted for economic or legal reasons related to the borrower's financial difficulty. Concessions granted for loans in these portfolios could include: reductions in interest rates to rates that are considered below market; extension of repayment schedules and maturity dates beyond original contractual terms; waivers of borrower covenants; forgiveness of principal or interest; or other contractual changes that are considered to be concessions. The Corporation mitigates loan defaults for these

loan portfolios through its collection function. The function's objective is to minimize both early stage delinquencies and losses upon default of loans in these portfolios. In the case of the commercial and industrial, commercial mortgage, and construction loan portfolios, the Corporation's Special Asset Group ("SAG") focuses on strategies for the accelerated reduction of non-performing assets through note sales, short sales, loss mitigation programs, and sales of OREO.

In addition, the Corporation extends, renews, and restructures loans with satisfactory credit profiles. Many commercial loan facilities are structured as lines of credit, which generally have one-year terms and, therefore, are required to be renewed annually. Other facilities may be restructured or extended from time to time based upon changes in the borrower's business needs, use of funds, timing of completion of projects, and other factors. If the borrower is not deemed to have financial difficulties, extensions, renewals, and restructurings are done in the normal course of business and not considered concessions, and the loans continue to be recorded as performing.

Selected information on TDR loans held for investment that includes the recorded investment by loan class and modification type is summarized in the following tables. This information reflects all TDRs held for investment:

|  | <b>June 30, 2018</b>                      |   |  |   |                                  |                             |              |
|--|---|---|--|---|----------------------------------|-----------------------------|--------------|
|  | <b>Interest<br/>rate below<br/>market</b> | <b>Maturity<br/>or term<br/>extension</b> | <b>Combination<br/>of<br/>reduction<br/>in interest<br/>rate and<br/>extension of<br/>maturity</b> | <b>Forgiveness<br/>of<br/>principal<br/>and/or<br/>interest</b> | <b>Forbearance<br/>Agreement</b> | <b>Other <sup>(1)</sup></b> | <b>Total</b> |
| (In thousands)                         |   |   |  |   |                                  |                             |              |
| Troubled Debt Restructurings:          |   |   |  |   |                                  |                             |              |
| Non-FHA/VA                             |   |   |  |   |                                  |                             |              |
| Residential Mortgage loans             | \$ 23,972                                 | \$ 8,481                                  | \$ 249,820   | \$ -  | \$ 158                           | \$ 60,423                   | \$ 342,854   |
| Commercial Mortgage loans              | 5,594                                     | 31,646                                    | 35,499   | -   | 1,970                            | 9,572                       | 84,281       |
| Commercial and Industrial loans        | 1,239                                     | 20,221                                    | 14,562   | -   | 4,534                            | 51,113                      | 91,669       |
| Construction loans:                    |   |   |  |   |                                  |                             | -            |
| Land                                   | 17  | 3,697                                     | 2,149  | -   | -                                | 381                         | 6,244        |
| Construction-commercial <sup>(2)</sup> | -   | -   | -  | -   | -                                | -                           | -            |
| Construction-residential               | -   | -   | -  | -   | -                                | 217                         | 217          |
| Consumer loans                         |   |   |  |   |                                  |                             |              |
| - Auto                                 | -   | 1,746                                     | 11,666   | -   | -                                | 6,280                       | 19,692       |
| Finance leases                         | -   | 158                                       | 1,436  | -   | -                                | -                           | 1,594        |
| Consumer loans - Other                 | 1,178                                     | 1,612                                     | 5,932  | 216   | -                                | 1,707                       | 10,645       |
| Total Troubled Debt Restructurings     | \$ 32,000                                 | \$ 67,561                                 | \$ 321,064   | \$ 216  | \$ 6,662                         | \$ 129,693                  | \$ 557,196   |

(1) Other concessions granted by the Corporation included deferral of principal and/or interest payments for a period longer than what would be considered insignificant, payment plans under judicial stipulation, or a combination of the concessions listed in the table.

(2) Excludes TDRs held for sale amounting to \$30.0 million as of June 30, 2018.

|  | <b>December 31, 2017</b>                  |   |  |   |                                  |                             | <b>Total</b> |
|--|---|---|--|---|----------------------------------|-----------------------------|--------------|
|  | <b>Interest<br/>rate below<br/>market</b> | <b>Maturity<br/>or term<br/>extension</b> | <b>Combination<br/>of<br/>reduction<br/>in interest<br/>rate and<br/>extension of<br/>maturity</b> | <b>Forgiveness<br/>of<br/>principal<br/>and/or<br/>interest</b> | <b>Forbearance<br/>Agreement</b> | <b>Other <sup>(1)</sup></b> | <b>Total</b> |

|                                    | <b>market</b> | <b>extension</b> | <b>reduction<br/>in interest<br/>rate and<br/>extension of<br/>maturity</b> | <b>principal<br/>and/or<br/>interest</b> |          |            |            |  |
|------------------------------------|---------------|------------------|---|--|----------|------------|------------|--|
| (In thousands)                     |               |                  |   |  |          |            |            |  |
| Troubled Debt Restructurings:      |               |                  |   |  |          |            |            |  |
| Non-FHA/VA                         |               |                  |   |  |          |            |            |  |
| Residential Mortgage loans         | \$ 25,964     | \$ 8,318         | \$ 267,578  | \$ -                                     | \$ -     | \$ 62,070  | \$ 363,930 |  |
| Commercial Mortgage loans          | 6,563         | 2,094            | 31,870  | -  | -        | 10,285     | 50,812     |  |
| Commercial and Industrial loans    | 2,510         | 20,648           | 16,049  | -  | 6,623    | 48,282     | 94,112     |  |
| Construction loans:                |               |                  |   |  |          |            |            |  |
| Land                               | 18            | 3,941            | 2,186   | -  | -        | 331        | 6,476      |  |
| Construction-commercial            | -             | -                | -   | 35,100                                   | -        | -          | 35,100     |  |
| Construction-residential           | -             | -                | -   | -  | -        | 217        | 217        |  |
| Consumer loans - Auto              | -             | 1,347            | 14,233  | -  | -        | 7,025      | 22,605     |  |
| Finance leases                     | -             | 238              | 1,946   | -  | -        | -          | 2,184      |  |
| Consumer loans - Other             | 892           | 2,097            | 6,891   | 217                                      | -        | 1,686      | 11,783     |  |
| Total Troubled Debt Restructurings | \$ 35,947     | \$ 38,683        | \$ 340,753  | \$ 35,317                                | \$ 6,623 | \$ 129,896 | \$ 587,219 |  |

(1) Other concessions granted by the Corporation included deferral of principal and/or interest payments for a period longer than what would be considered insignificant, payment plans under judicial stipulation or a combination of the concessions listed in the table.



The following table presents the Corporation's TDR loans held for investment activity:

|  | Quarter Ended<br>June 30, |            | Six-Month Period Ended<br>June 30, |            |
|--|---------------------------|------------|------------------------------------|------------|
|  | 2018                      | 2017       | 2018                               | 2017       |
| (In thousands)   |                           |            |                                    |            |
| Beginning balance of TDRs                              | \$ 572,376                | \$ 602,364 | \$ 587,219                         | \$ 647,048 |
| New TDRs   | 13,228                    | 13,368     | 56,647                             | 54,267     |
| Increases to existing TDRs                             | 75                        | 330        | 6,846                              | 754        |
| Charge-offs post modification<br>(1)(2)                | (8,616)                   | (9,365)    | (17,787)                           | (24,027)   |
| Sales, net of charge-offs                              | -                         | -          | -                                  | (53,245)   |
| Foreclosures   | (3,759)                   | (16,150)   | (10,802)                           | (20,521)   |
| TDR transferred to held for sale,<br>net of charge-off | -                         | -          | (30,000)                           | -          |
| Paid-off and partial payments                          | (16,108)                  | (22,004)   | (34,927)                           | (35,733)   |
| Ending balance of TDRs                                 | \$ 557,196                | \$ 568,543 | \$ 557,196                         | \$ 568,543 |

- (1) The six-month period ended June 30, 2018 includes a charge-off of \$5.1 million associated with a \$30.0 million construction loan transferred to held for sale.
- (2) The six-month period ended June 30, 2017 includes a charge-off of \$10.7 million related to the sale of the PREPA credit line.

TDR loans are classified as either accrual or nonaccrual loans. Loans in accrual status may remain in accrual status when their contractual terms have been modified in a TDR if the loans had demonstrated performance prior to the restructuring and payment in full under the restructured terms is expected. Otherwise, loans on nonaccrual and restructured as a TDR will remain on nonaccrual status until the borrower has proven the ability to perform under the modified structure, generally for a minimum of six months, and there is evidence that such payments can, and are likely to, continue as agreed. Performance prior to the restructuring, or significant events that coincide with the restructuring, are included in assessing whether the borrower can meet the new terms and may result in the loan being returned to accrual status at the time of the restructuring or after a shorter performance period. If the borrower's ability to meet the revised payment schedule is uncertain, the loan remains classified as a nonaccrual loan. Loan modifications increase the Corporation's interest income by returning a non-performing loan to performing status, if applicable, increase cash flows by providing for payments to be made by the borrower, and limit increases in foreclosure and OREO costs. A TDR loan that specifies an interest rate that at the time of the restructuring is greater than or equal to the rate the Corporation is willing to accept for a new loan with comparable risk may not be reported as a TDR, or an impaired loan in the calendar years subsequent to the restructuring, if it is in compliance with its modified terms. The Corporation did not remove any loans from the TDR classification during the first six months of 2018 and 2017.

The following table provides a breakdown of the TDR loans held for investment by those in accrual and nonaccrual status:

**As of June 30, 2018**

| (In thousands)                        | Accrual    | Nonaccrual (1) | Total TDRs |
|---------------------------------------|------------|----------------|------------|
| Non-FHA/VA Residential Mortgage loans | \$ 270,358 | \$ 72,496      | \$ 342,854 |
| Commercial Mortgage loans             | 54,354     | 29,927         | 84,281     |
| Commercial and Industrial loans       | 43,478     | 48,191         | 91,669     |
| Construction loans:                   |            |                |            |
| Land                                  | 1,091      | 5,153          | 6,244      |
| Construction-commercial (2)           | -          | -              | -          |
| Construction-residential              | -          | 217            | 217        |
| Consumer loans - Auto                 | 13,345     | 6,347          | 19,692     |
| Finance leases                        | 1,334      | 260            | 1,594      |
| Consumer loans - Other                | 9,321      | 1,324          | 10,645     |
| Total Troubled Debt Restructurings    | \$ 393,281 | \$ 163,915     | \$ 557,196 |

- (1) Included in non-accrual loans are \$51.7 million in loans that are performing under the terms of the restructuring agreement but are reported in nonaccrual status until the restructured loans meet the criteria of sustained payment performance under the revised terms for reinstatement to accrual status and are deemed fully collectible.
- (2) Excludes a \$30.0 million non-performing construction loans transferred to held for sale during the first quarter of 2018.

**As of December 31, 2017**

| (In thousands)                         | Accrual    | Nonaccrual (1) | Total TDRs |
|--|------------|----------------|------------|
| Non- FHA/VA Residential Mortgage loans | \$ 280,729 | \$ 83,201      | \$ 363,930 |
| Commercial Mortgage loans              | 23,329     | 27,483         | 50,812     |
| Commercial and Industrial loans        | 41,536     | 52,576         | 94,112     |
| Construction loans:                    |            |                |            |
| Land                                   | 1,291      | 5,185          | 6,476      |
| Construction-commercial                | -          | 35,100         | 35,100     |
| Construction-residential               | -          | 217            | 217        |
| Consumer loans - Auto                  | 15,548     | 7,057          | 22,605     |
| Finance leases                         | 1,968      | 216            | 2,184      |
| Consumer loans - Other                 | 10,294     | 1,489          | 11,783     |
| Total Troubled Debt Restructurings     | \$ 374,695 | \$ 212,524     | \$ 587,219 |

- (1) Included in non-accrual loans are \$88.6 million in loans that are performing under the terms of the restructuring agreement but are reported in non-accrual status until the restructured loans meet the criteria of sustained payment performance under the revised terms for reinstatement to accrual status and are deemed fully collectible.



TDR loans exclude restructured residential mortgage loans that are guaranteed by the U.S. federal government (e.g., FHA/VA loans) totaling \$62.2 million as of June 30, 2018 (December 31, 2017 - \$62.1 million). The Corporation excludes FHA/VA guaranteed loans from TDR loan statistics given that, in the event that the borrower defaults on the loan, the principal and interest (at the specified debenture rate) are guaranteed by the U.S. government; therefore, the risk of loss on these types of loans is very low. The Corporation does not consider loans with U.S. federal government guarantees to be impaired loans for the purpose of calculating the allowance for loan and lease losses.

Loan modifications that are considered TDR loans completed during the quarters and six-month periods ended June 30, 2018 and 2017, were as follows:

|                                       | Number of contracts | Quarter Ended June 30, 2018                      |   |
|---------------------------------------|---------------------|--|---|
|                                       |                     | Pre-modification Outstanding Recorded Investment | Post-Modification Outstanding Recorded Investment |
| (Dollars in thousands)                |                     |  |   |
| Troubled Debt Restructurings:         |                     |  |   |
| Non-FHA/VA Residential Mortgage loans | 19                  | \$ 2,034   | \$ 1,934  |
| Commercial Mortgage loans             | 2                   | 5,765  | 5,765   |
| Commercial and Industrial loans       | 3                   | 3,453  | 3,128   |
| Construction loans:                   |                     |  |   |
| Land                                  | 1                   | 97   | 97  |
| Consumer loans - Auto                 | 76                  | 1,245  | 1,239   |
| Consumer loans - Other                | 231                 | 1,034  | 1,065   |
| Total Troubled Debt Restructurings    | 332                 | \$ 13,628  | \$ 13,228   |
|                                       |                     | Six-Month Period Ended June 30, 2018             |   |
|                                       | Number of contracts | Pre-modification Outstanding Recorded Investment | Post-Modification Outstanding Recorded Investment |
| (Dollars in thousands)                |                     |  |   |
| Troubled Debt Restructurings:         |                     |  |   |
| Non-FHA/VA Residential Mortgage loans | 43                  | \$ 4,642   | \$ 4,548  |
| Commercial Mortgage loans             | 5                   | 42,511   | 42,523  |
| Commercial and Industrial loans       | 6                   | 6,050  | 5,710   |
| Construction loans:                   |                     |  |   |
| Land                                  | 1                   | 97   | 97  |
| Consumer loans - Auto                 | 121                 | 1,925  | 1,919   |
| Consumer loans - Other                | 367                 | 1,819  | 1,850   |
| Total Troubled Debt Restructurings    | 543                 | \$ 57,044  | \$ 56,647   |

## Quarter Ended June 30, 2017

|                                       |                                | <b>Pre-Modification<br/>Outstanding<br/>Recorded<br/>Investment</b> | <b>Post-Modification<br/>Outstanding<br/>Recorded<br/>Investment</b> |
|---------------------------------------|--------------------------------|---|--|
|                                       | <b>Number of<br/>contracts</b> |   |  |
| (Dollars in thousands)                |                                |   |  |
| Troubled Debt Restructurings:         |                                |   |  |
| Non-FHA/VA Residential Mortgage loans | 48                             | \$ 9,577  | \$ 9,483   |
| Commercial Mortgage loans             | 2                              | 267   | 267  |
| Commercial and Industrial loans       | 2                              | 326   | 326  |
| Consumer loans - Auto                 | 122                            | 1,926   | 1,926  |
| Finance leases                        | 14                             | 362   | 362  |
| Consumer loans - Other                | 193                            | 991   | 1,004  |
| Total Troubled Debt Restructurings    | 381                            | \$ 13,449   | \$ 13,368  |

## Six-Month Period Ended June 30, 2017

|                                       |                                | <b>Pre-Modification<br/>Outstanding<br/>Recorded<br/>Investment</b> | <b>Post-Modification<br/>Outstanding<br/>Recorded<br/>Investment</b> |
|---------------------------------------|--------------------------------|---|--|
|                                       | <b>Number of<br/>contracts</b> |   |  |
| (Dollars in thousands)                |                                |   |  |
| Troubled Debt Restructurings:         |                                |   |  |
| Non-FHA/VA Residential Mortgage loans | 88                             | \$ 14,227   | \$ 13,991  |
| Commercial Mortgage loans             | 8                              | 22,705  | 22,465   |
| Commercial and Industrial loans       | 5                              | 11,074  | 11,074   |
| Construction loans:                   |                                |   |  |
| Land                                  | 1                              | 25  | 28   |
| Consumer loans - Auto                 | 274                            | 4,173   | 4,173  |
| Finance leases                        | 22                             | 548   | 548  |
| Consumer loans - Other                | 403                            | 1,960   | 1,988  |
| Total Troubled Debt Restructurings    | 801                            | \$ 54,712   | \$ 54,267  |

Recidivism, or the borrower defaulting on its obligation pursuant to a modified loan, results in the loan once again becoming a non-performing loan. Recidivism on a modified loan occurs at a notably higher rate than do defaults on new origination loans, so modified loans present a higher risk of loss than do new origination loans. The Corporation considers a loan to have defaulted if the borrower has failed to make payments of either principal, interest, or both for a period of 90 days or more.

Loan modifications considered TDR loans that defaulted during the quarters and six-month periods ended June 30, 2018 and 2017, and had become TDR during the 12-months preceding the default date, were as follows:

|                                       | <b>Quarter Ended June 30,</b>      |                                |                                    |                                |
|---------------------------------------|------------------------------------|--------------------------------|------------------------------------|--------------------------------|
|                                       | <b>2018</b>                        |                                | <b>2017</b>                        |                                |
|                                       | <b>Number<br/>of<br/>contracts</b> | <b>Recorded<br/>Investment</b> | <b>Number<br/>of<br/>contracts</b> | <b>Recorded<br/>Investment</b> |
| (Dollars in thousands)                |                                    |                                |                                    |                                |
| Non-FHA/VA Residential Mortgage loans | 6                                  | \$ 681                         | 19                                 | \$ 2,614                       |
| Consumer loans - Auto                 | 31                                 | 514                            | 5                                  | 69                             |
| Consumer loans - Other                | 28                                 | 100                            | 29                                 | 103                            |
| Total                                 | 65                                 | \$ 1,295                       | 53                                 | \$ 2,786                       |

**Six-Month Period Ended June 30,  
2018**