

OFG BANCORP
Form 10-Q
August 10, 2015

UNITED STATES
SECURITIES AND EXCHANGE COMMISSION
Washington, D.C. 20549

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, 2015

or

**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 001-12647

OFG Bancorp

Incorporated in the Commonwealth of Puerto Rico, IRS Employer Identification No. 66-0538893

Principal Executive Offices:

254 Muñoz Rivera Avenue

San Juan, Puerto Rico 00918

Telephone Number: (787) 771-6800

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 x 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 x No

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

| | | | |
|---|--|--|--|
| Large Accelerated Filer <input checked="" type="checkbox"/> | Accelerated Filer <input type="checkbox"/> | Non-Accelerated Filer <input type="checkbox"/> | Smaller Reporting Company <input type="checkbox"/> |
| | | (Do not check if a smaller reporting company) | |

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

Number of shares outstanding of the registrant's common stock, as of the latest practicable date:

43,867,909 common shares (\$1.00 par value per share) outstanding as of July 31, 2015

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FORWARD-LOOKING STATEMENTS

The information included in this quarterly report on Form 10-Q contains certain forward-looking statements within the meaning of the Private Securities Litigation Reform Act of 1995. These forward-looking statements may relate to the financial condition, results of operations, plans, objectives, future performance and business of OFG Bancorp (“we,” “our,” “us” or the “Company”), including, but not limited to, statements with respect to the adequacy of the allowance for loan losses, delinquency trends, market risk and the impact of interest rate changes, capital markets conditions, capital adequacy and liquidity, and the effect of legal proceedings and new accounting standards on the Company’s financial condition and results of operations. All statements contained herein that are not clearly historical in nature are forward-looking, and the words “anticipate,” “believe,” “continues,” “expect,” “estimate,” “intend,” “project” and similar expressions and future or conditional verbs such as “will,” “would,” “should,” “could,” “might,” “can,” “may,” or similar expressions are generally intended to identify forward-looking statements.

These statements are not guarantees of future performance and involve certain risks, uncertainties, estimates and assumptions by management that are difficult to predict. Various factors, some of which by their nature are beyond the Company’s control, could cause actual results to differ materially from those expressed in, or implied by, such forward-looking statements. Factors that might cause such a difference include, but are not limited to:

- the rate of growth in the economy and employment levels, as well as general business and economic conditions;
- changes in interest rates, as well as the magnitude of such changes;
- the fiscal and monetary policies of the federal government and its agencies;
- a credit default or potential restructuring by the Commonwealth of Puerto Rico or any of its agencies, municipalities or instrumentalities;
- changes in federal bank regulatory and supervisory policies, including required levels of capital;
- the impact of the Dodd-Frank Wall Street Reform and Consumer Protection Act (the “Dodd-Frank Act”) on the Company’s businesses, business practices and cost of operations;
- the relative strength or weakness of the consumer and commercial credit sectors and of the real estate market in Puerto Rico;
- the performance of the securities markets;
- competition in the financial services industry;
- additional Federal Deposit Insurance Corporation (“FDIC”) assessments; and

- possible legislative, tax or regulatory changes.

Other possible events or factors that could cause results or performance to differ materially from those expressed in these forward-looking statements include the following: negative economic conditions that adversely affect the general economy, housing prices, the job market, consumer confidence and spending habits which may affect, among other things, the level of non-performing assets, charge-offs and provision expense; changes in interest rates and market liquidity which may reduce interest margins, impact funding sources and affect the ability to originate and distribute financial products in the primary and secondary markets; adverse movements and volatility in debt and equity capital markets; changes in market rates and prices which may adversely impact the value of financial assets and liabilities; liabilities resulting from litigation and regulatory investigations; changes in accounting standards, rules and interpretations; increased competition; the Company's ability to grow its core businesses; decisions to downsize, sell or close units or otherwise change the Company's business mix; and management's ability to identify and manage these and other risks.

All forward-looking statements included in this quarterly report on Form 10-Q are based upon information available to the Company as of the date of this report, and other than as required by law, including the requirements of applicable securities laws, the Company assumes no obligation to update or revise any such forward-looking statements to reflect occurrences or unanticipated events or circumstances after the date of such statements.

ITEM 1. FINANCIAL STATEMENTS

OFG BANCORP

UNAUDITED CONSOLIDATED STATEMENTS OF FINANCIAL CONDITION

AS OF JUNE 30, 2015 AND DECEMBER 31, 2014

ASSETS

Cash and cash equivalents:

Cash and due from banks

Money market investments

Total cash and cash equivalents

Restricted cash

Investments:

Trading securities, at fair value, with amortized cost of \$1,327 (December 31, 2014 - \$2,419)

Investment securities available-for-sale, at fair value, with amortized cost of \$1,023,573 (December 31, 2014 - \$1,187,679)

Investment securities held-to-maturity, at amortized cost, with fair value of \$547,776 (December 31, 2014 - \$164,154)

Federal Home Loan Bank (FHLB) stock, at cost

Other investments

Total investments

Loans:

Mortgage loans held-for-sale, at lower of cost or fair value

Non-covered loans, net of allowance for loan and lease losses of \$102,877 (December 31, 2014 - \$69,517)

Covered loans, net of allowance for loan and lease losses of \$71,452 (December 31, 2014 - \$64,245)

Total loans, net

Other assets:

FDIC indemnification asset

Foreclosed real estate covered under shared-loss agreements with the FDIC

Foreclosed real estate not covered under shared-loss agreements with the FDIC

Accrued interest receivable

Deferred tax asset, net

Premises and equipment, net

Customers' liability on acceptances

Servicing assets

Derivative assets

Goodwill

Other assets

Total assets

LIABILITIES AND STOCKHOLDERS' EQUITY

Deposits:

Demand deposits

Savings accounts

Time deposits

Total deposits

Borrowings:

Securities sold under agreements to repurchase

Advances from FHLB

Subordinated capital notes

Other borrowings

Total borrowings

Other liabilities:

Derivative liabilities

Acceptances executed and outstanding

Accrued expenses and other liabilities

Total liabilities

Commitments and contingencies (See Note 20)

Stockholders' equity:

Preferred stock; 10,000,000 shares authorized;

1,340,000 shares of Series A, 1,380,000 shares of Series B, and 960,000 shares of Series D

issued and outstanding, (December 31, 2014 - 1,340,000; 1,380,000; and 960,000) \$25 liquidation value

84,000 shares of Series C issued and outstanding (December 31, 2014 - 84,000); \$1,000 liquidation value

Common stock, \$1 par value; 100,000,000 shares authorized; 52,625,869 shares issued:

44,367,909 shares outstanding (December 31, 2014 - 52,625,869; 44,613,615)

Additional paid-in capital

Legal surplus

Retained earnings

Treasury stock, at cost, 8,257,960 shares (December 31, 2014 - 8,012,254 shares)

Accumulated other comprehensive income, net of tax of -\$185 (December 31, 2014 \$447)

Total stockholders' equity

Total liabilities and stockholders' equity

\$

See notes to unaudited consolidated financial statements.

OFG BANCORP

UNAUDITED CONSOLIDATED STATEMENTS OF OPERATIONS

FOR THE QUARTERS AND SIX-MONTH PERIODS ENDED JUNE 30, 2015 AND 2014

| | Quarter Ended June 30, | | Six-Month Period Ended June 30, | |
|--|--|----------------|--|----------------|
| | 2015 | 2014 | 2015 | 2014 |
| | (In thousands, except per share data) | | (In thousands, except per share data) | |
| Interest income: | | | | |
| Non-covered loans | \$ 77,746 | \$ 88,064 | \$ 159,725 | \$ 173,307 |
| Covered loans | 12,758 | 24,879 | 28,262 | 48,267 |
| Total interest income from loans | 90,504 | 112,943 | 187,987 | 221,574 |
| Mortgage-backed securities | 7,998 | 11,984 | 16,587 | 24,400 |
| Investment securities and other | 911 | 973 | 1,840 | 3,000 |
| Total interest income | 99,413 | 125,900 | 206,414 | 248,974 |
| Interest expense: | | | | |
| Deposits | 6,604 | 9,165 | 13,708 | 18,143 |
| Securities sold under agreements to repurchase | 7,394 | 7,372 | 14,558 | 14,784 |
| Advances from FHLB and other borrowings | 2,248 | 2,289 | 4,483 | 4,583 |
| Subordinated capital notes | 875 | 996 | 1,738 | 1,988 |
| Total interest expense | 17,121 | 19,822 | 34,487 | 39,498 |
| Net interest income | 82,292 | 106,078 | 171,927 | 209,476 |
| Provision for non-covered loan and lease losses | 15,644 | 13,220 | 53,027 | 23,282 |
| (Recovery) Provision for covered loan and lease losses | (105) | 1,595 | 4,705 | 3,224 |
| Total provision for loan and lease losses | 15,539 | 14,815 | 57,732 | 26,506 |
| Net interest income after provision for loan and lease losses | 66,753 | 91,263 | 114,195 | 182,970 |
| Non-interest income: | | | | |
| Banking service revenue | 10,212 | 9,995 | 20,417 | 20,552 |
| Wealth management revenue | 7,285 | 7,336 | 14,440 | 14,203 |
| Mortgage banking activities | 1,862 | 1,554 | 3,725 | 3,249 |
| Total banking and financial service revenues | 19,359 | 18,885 | 38,582 | 38,004 |
| FDIC shared-loss expense, net: | | | | |
| FDIC indemnification asset expense | (22,512) | (17,499) | (34,733) | (35,121) |
| Change in true-up payment obligation | (733) | (856) | (1,596) | (1,721) |
| | (23,245) | (18,355) | (36,329) | (36,842) |
| Net gain (loss) on: | | | | |
| Sale of securities | - | - | 2,572 | 4,366 |
| Derivatives | 77 | (247) | (13) | (470) |
| Other non-interest (loss) income | (847) | 224 | (2,587) | 678 |
| Total non-interest (loss) income, net | (4,656) | 507 | 2,225 | 5,736 |
| Non-interest expense: | | | | |
| Compensation and employee benefits | 19,260 | 20,707 | 39,440 | 42,494 |
| Professional and service fees | 4,143 | 3,512 | 8,324 | 7,719 |
| Occupancy and equipment | 8,883 | 8,605 | 17,519 | 16,914 |
| Insurance | 2,251 | 2,333 | 4,204 | 4,407 |
| Electronic banking charges | 5,851 | 4,796 | 11,218 | 9,449 |
| Information technology expenses | 1,543 | 1,485 | 2,997 | 3,300 |

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| | | | | |
|--|-------------------|------------------|--------------------|------------------|
| Advertising, business promotion, and strategic initiatives | 1,558 | 1,669 | 3,186 | 3,450 |
| Foreclosure, repossession and other real estate expenses | 10,337 | 6,656 | 15,783 | 13,043 |
| Loan servicing and clearing expenses | 2,594 | 1,669 | 4,947 | 3,728 |
| Taxes, other than payroll and income taxes | 2,703 | 3,776 | 4,182 | 7,511 |
| Communication | 770 | 813 | 1,460 | 1,770 |
| Printing, postage, stationary and supplies | 582 | 645 | 1,219 | 1,200 |
| Director and investor relations | 289 | 293 | 583 | 544 |
| Other | 3,673 | 2,889 | 5,707 | 5,723 |
| Total non-interest expense | 64,437 | 59,848 | 120,769 | 121,252 |
| (Loss) income before income taxes | (2,340) | 31,922 | (4,349) | 67,454 |
| Income tax expense | 769 | 10,613 | 1,748 | 22,398 |
| Net (loss) income | (3,109) | 21,309 | (6,097) | 45,056 |
| Less: dividends on preferred stock | (3,466) | (3,466) | (6,931) | (6,931) |
| Net (loss) income available to common shareholders | \$ (6,575) | \$ 17,843 | \$ (13,028) | \$ 38,125 |
| (Loss) earnings per common share: | | | | |
| Basic | \$ (0.15) | \$ 0.40 | \$ (0.29) | \$ 0.84 |
| Diluted | \$ (0.15) | \$ 0.38 | \$ (0.29) | \$ 0.80 |
| Average common shares outstanding and equivalents | 51,774 | 52,352 | 51,876 | 52,476 |
| Cash dividends per share of common stock | \$ 0.10 | \$ 0.08 | \$ 0.20 | \$ 0.16 |

See notes to unaudited consolidated financial statements.

OFG BANCORP

UNAUDITED CONSOLIDATED STATEMENTS OF COMPREHENSIVE (LOSS) INCOME
FOR THE QUARTERS AND SIX-MONTH PERIODS ENDED JUNE 30, 2015 AND 2014

| | Quarter Ended June 30, | | Six-Month Period Ended June 30, | |
|---|------------------------|------------------|------------------------------------|------------------|
| | 2015 | 2014 | 2015 | 2014 |
| | (In thousands) | | (In thousands) | |
| Net (loss) income | \$ (3,109) | \$ 21,309 | \$ (6,097) | \$ 45,056 |
| Other comprehensive (loss) income before tax: | | | | |
| Unrealized (loss) gain on securities available-for-sale | (12,916) | 14,941 | (5,541) | 24,504 |
| Realized (loss) gain on investment securities included in net income | - | - | (2,572) | (4,366) |
| Unrealized (loss) gain on cash flow hedges | 2,016 | 14 | 2,071 | 391 |
| Other comprehensive (loss) income before taxes | (10,900) | 14,955 | (6,042) | 20,529 |
| Income tax effect | 877 | (1,221) | 632 | (1,965) |
| Other comprehensive (loss) income after taxes | (10,023) | 13,734 | (5,410) | 18,564 |
| Comprehensive (loss) income | \$ (13,132) | \$ 35,043 | \$ (11,507) | \$ 63,620 |

See notes to unaudited consolidated financial statements.

OFG BANCORP

UNAUDITED CONSOLIDATED STATEMENTS OF CHANGES IN STOCKHOLDERS' EQUITY

FOR THE SIX-MONTH PERIODS ENDED JUNE 30, 2015 AND 2014

| | Six-Month Period Ended June 30, | |
|--|---------------------------------|-------------------|
| | 2015 | 2014 |
| | (In thousands) | |
| Preferred stock: | | |
| Balance at beginning of period | \$ 176,000 | \$ 176,000 |
| Balance at end of period | 176,000 | 176,000 |
| Common stock: | | |
| Balance at beginning of period | 52,626 | 52,707 |
| Exercised stock options | - | 23 |
| Balance at end of period | 52,626 | 52,730 |
| Additional paid-in capital: | | |
| Balance at beginning of period | 539,311 | 538,071 |
| Stock-based compensation expense | 794 | 946 |
| Exercised stock options | - | 242 |
| Lapsed restricted stock units | (436) | (323) |
| Balance at end of period | 539,669 | 538,936 |
| Legal surplus: | | |
| Balance at beginning of period | 70,467 | 61,957 |
| Transfer (to) from retained earnings | (533) | 4,481 |
| Balance at end of period | 69,934 | 66,438 |
| Retained earnings: | | |
| Balance at beginning of period | 181,152 | 133,629 |
| Net (loss) income | (6,097) | 45,056 |
| Cash dividends declared on common stock | (8,920) | (7,218) |
| Cash dividends declared on preferred stock | (6,931) | (6,931) |
| Transfer from (to) legal surplus | 533 | (4,481) |
| Balance at end of period | 159,737 | 160,055 |
| Treasury stock: | | |
| Balance at beginning of period | (97,070) | (80,642) |
| Stock repurchased | (4,238) | (10,393) |
| Lapsed restricted stock units | 640 | 323 |
| Balance at end of period | (100,668) | (90,712) |
| Accumulated other comprehensive income, net of tax: | | |
| Balance at beginning of period | 19,711 | 3,191 |
| Other comprehensive (loss) income, net of tax | (5,410) | 18,564 |
| Balance at end of period | 14,301 | 21,755 |
| Total stockholders' equity | \$ 911,599 | \$ 925,202 |

See notes to unaudited consolidated financial statements.

OFG BANCORP

UNAUDITED CONSOLIDATED STATEMENTS OF CASH FLOWS
FOR THE SIX-MONTH PERIODS ENDED JUNE 30, 2015 AND 2014

| | Six-Month Period | |
|---|-------------------------|---------------|
| | Ended June 30, | |
| | 2015 | 2014 |
| | (In thousands) | |
| Cash flows from operating activities: | | |
| Net (loss) income | \$ (6,097) | \$ 45,056 |
| Adjustments to reconcile net (loss) income to net cash provided by operating activities: | | |
| Amortization of deferred loan origination fees, net of costs | 1,813 | 1,330 |
| Amortization of fair value premiums, net of discounts, on acquired loans | 2,766 | 6,884 |
| Amortization of investment securities premiums, net of accretion of discounts | 5,931 | 203 |
| Amortization of core deposit and customer relationship intangibles | 953 | 1,085 |
| Amortization of fair value premiums on acquired deposits | 478 | 2,908 |
| FDIC shared-loss expense, net | 36,329 | 36,842 |
| Depreciation and amortization of premises and equipment | 5,930 | 4,826 |
| Deferred income tax (benefit) expense, net | (1,316) | 13,211 |
| Provision for covered and non-covered loan and lease losses, net | 57,732 | 26,506 |
| Stock-based compensation | 794 | 946 |
| (Gain) loss on: | | |
| Sale of securities | (2,572) | (4,366) |
| Sale of mortgage loans held-for-sale | (2,010) | (2,447) |
| Derivatives | (113) | 646 |
| Foreclosed real estate | (706) | 5,052 |
| Sale of other repossessed assets | 3,427 | 3,305 |
| Sale of premises and equipment | 10 | (10) |
| Originations of loans held-for-sale | (111,433) | (86,058) |
| Proceeds from sale of loans held-for-sale | 46,678 | 47,834 |
| Net (increase) decrease in: | | |
| Trading securities | 808 | 256 |
| Accrued interest receivable | 2,091 | (3,774) |
| Servicing assets | 1,216 | 146 |
| Other assets | (19,813) | 11,651 |
| Net increase (decrease) in: | | |
| Accrued interest on deposits and borrowings | (608) | (932) |
| Accrued expenses and other liabilities | 24,219 | (16,247) |
| Net cash provided by operating activities | 46,507 | 94,853 |
| Cash flows from investing activities: | | |
| Purchases of: | | |
| Investment securities available-for-sale | (1,671) | (217,974) |
| Investment securities held-to-maturity | (399,206) | (26,707) |
| FHLB stock | - | (76,725) |
| Maturities and redemptions of: | | |
| Investment securities available-for-sale | 121,121 | 295,013 |

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| | | |
|--|-----------------|----------------|
| Investment securities held-to-maturity | 10,725 | - |
| FHLB stock | 343 | 76,794 |
| Proceeds from sales of: | | |
| Investment securities available-for-sale | 103,831 | 163,235 |
| Foreclosed real estate and other repossessed assets | 34,136 | 22,991 |
| Premises and equipment | 10 | 20 |
| Mortgage servicing rights | 5,927 | - |
| Origination and purchase of loans, excluding loans held-for-sale | (414,725) | (347,691) |
| Principal repayment of loans, including covered loans | 491,330 | 339,102 |
| Reimbursements from the FDIC on shared-loss agreements | 31,657 | 18,700 |
| Additions to premises and equipment | (1,838) | (4,100) |
| Net change in securities purchased under agreements to resell | - | 60,000 |
| Net change in restricted cash | 2,321 | 67,029 |
| Net cash (used) provided by investing activities | (16,039) | 369,687 |

OFG BANCORP

UNAUDITED CONSOLIDATED STATEMENTS OF CASH FLOWS

FOR THE SIX-MONTH PERIODS ENDED JUNE 30, 2015 AND 2014 – (CONTINUED)

| | Six-Month Period Ended June 30, | |
|--|---------------------------------|-------------------|
| | 2015 | 2014 |
| | (In thousands) | |
| Cash flows from financing activities: | | |
| Net increase (decrease) in: | | |
| Deposits | (209,272) | (235,062) |
| Securities sold under agreements to repurchase | 181,129 | (255,000) |
| FHLB advances, federal funds purchased, and other borrowings | (2,845) | 24,279 |
| Subordinated capital notes | 525 | 787 |
| Exercise of stock options and restricted units lapsed, net | 204 | 265 |
| Purchase of treasury stock | (4,238) | (10,393) |
| Dividends paid on preferred stock | (6,931) | (6,931) |
| Dividends paid on common stock | (8,932) | (7,269) |
| Net cash used in financing activities | (50,360) | (489,324) |
| Net change in cash and cash equivalents | (19,892) | (24,784) |
| Cash and cash equivalents at beginning of period | 573,427 | 621,269 |
| Cash and cash equivalents at end of period | \$ 553,535 | \$ 596,485 |
| Supplemental Cash Flow Disclosure and Schedule of Non-cash Activities: | | |
| Interest paid | \$ 34,403 | \$ 42,667 |
| Income taxes paid | 6,730 | \$ 319 |
| Mortgage loans securitized into mortgage-backed securities | \$ 61,854 | \$ 46,505 |
| Transfer from loans to foreclosed real estate and other repossessed assets | \$ 15,390 | \$ 47,852 |
| Reclassification of loans held-for-investment portfolio to held-for-sale portfolio | \$ 1,473 | \$ 473 |
| Reclassification of loans held-for-sale portfolio to held-for-investment portfolio | \$ 156 | \$ 26,376 |

See notes to unaudited consolidated financial statements.

OFG BANCORP

NOTES TO UNAUDITED CONSOLIDATED FINANCIAL STATEMENTS

NOTE 1 – ORGANIZATION, CONSOLIDATION AND BASIS OF PRESENTATION

Nature of Operations

OFG Bancorp (the “Company”) is a publicly-owned financial holding company incorporated under the laws of the Commonwealth of Puerto Rico. The Company operates through various subsidiaries including, a commercial bank, Oriental Bank (the “Bank”), a securities broker-dealer, Oriental Financial Services Corp. (“Oriental Financial Services”), an insurance agency, Oriental Insurance, Inc. (“Oriental Insurance”) and a retirement plan administrator, Oriental Pension Consultants, Inc. (“OPC”), formerly known as Caribbean Pension Consultants, Inc. Through these subsidiaries and their respective divisions, the Company provides a wide range of banking and financial services such as commercial, consumer and mortgage lending, auto loans, financial planning, insurance sales, money management and investment banking and brokerage services, as well as corporate and individual trust services.

On April 30, 2010, the Bank acquired certain assets and assumed certain deposits and other liabilities of Eurobank, a Puerto Rico commercial bank, in an FDIC-assisted acquisition. On December 18, 2012, the Company acquired a group of Puerto Rico-based entities that included Banco Bilbao Vizcaya Argentaria Puerto Rico (“BBVAPR”), a Puerto Rico commercial bank, as well as a securities broker-dealer and an insurance agency, which is referred to herein as the “BBVAPR Acquisition.” The businesses acquired in these acquisitions have been integrated with the Company’s existing business.

Recent Accounting Developments

In April 2015, the Financial Accounting Standards Board (“FASB”) issued Accounting Standards Update (“ASU”) No. 2015-03, *Simplifying the Presentation of Debt Issuance Costs* (“ASU 2015-03”). ASU 2015-03 requires that all costs incurred to issue debt be presented in the balance sheet as a direct deduction from the carrying value of the associated debt liability rather than as an asset. The standard does not affect the recognition and measurement of debt issuance costs; therefore, the amortization of such costs shall continue to be reported as interest expense. ASU 2015-03 will be effective for fiscal years, and interim periods within those fiscal years, beginning after December 15, 2015, with early adoption permissible for financial statements that have not been previously issued. The new guidance is to be applied on a retrospective basis to all prior periods. The Company does not expect the adoption of ASU 2015-03 to have a material impact on its consolidated financial statements.

Other than the accounting pronouncement disclosed above, there were no other new accounting pronouncements issued during the second quarter of 2015 that could have a material impact on the Company's financial position, operating results or financials statement disclosures.

OFG BANCORP**NOTES TO UNAUDITED CONSOLIDATED FINANCIAL STATEMENTS – (Continued)****NOTE 2 – RESTRICTED CASH**

The following table includes the composition of the Company's restricted cash:

| | June 30, 2015 | | December 31, 2014 |
|---|--------------------------|-----------|------------------------------|
| | (In thousands) | | |
| Cash pledged as collateral to other financial institutions to secure: | | | |
| Derivatives | \$ 2,980 | \$ | 2,980 |
| Obligations under agreement of loans sold with recourse | 3,106 | | 5,427 |
| | \$ 6,086 | \$ | 8,407 |

At June 30, 2015 and December 31, 2014, the Bank's international banking entities, Oriental International Bank Inc. ("OIB") and Oriental Overseas, each held unencumbered certificates of deposit in the amount of \$300 thousand as the legal reserve required for international banking entities under Puerto Rico law. Each certificate of deposit cannot be withdrawn by OIB or Oriental Overseas without prior written approval of the Office of the Commissioner of Financial Institutions ("OCFI").

As part of its derivative activities, the Company has entered into collateral agreements with certain financial counterparties. At June 30, 2015 and December 31, 2014, the Company had delivered \$3.0 million of cash as collateral for such derivatives activities.

As part of the BBVA Acquisition, the Company assumed a contract with FNMA which required collateral to guarantee the repurchase, if necessary, of loans sold with recourse. At June 30, 2015 and December 31, 2014, the Company delivered as collateral cash amounting to \$3.1 million and \$5.4 million, respectively.

The Bank is required by Puerto Rico law to maintain average weekly reserve balances to cover government demand deposits. The amount of those minimum average reserve balances for the week that covered June 30, 2015 was \$152.7 million (December 31, 2014 - \$141.5 million). At June 30, 2015 and December 31, 2014, the Bank complied with the requirement. Cash and due from bank as well as other short-term, highly liquid securities are used to cover the required average reserve balances.

NOTE 3 – INVESTMENT SECURITIES

Money Market Investments

The Company considers as cash equivalents all money market instruments that are not pledged and that have maturities of three months or less at the date of acquisition. At June 30, 2015 and December 31, 2014, money market instruments included as part of cash and cash equivalents amounted to \$5.8 million and \$4.7 million, respectively.

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NOTES TO UNAUDITED CONSOLIDATED FINANCIAL STATEMENTS – (Continued)

Investment Securities

The amortized cost, gross unrealized gains and losses, fair value, and weighted average yield of the securities owned by the Company at June 30, 2015 and December 31, 2014 were as follows:

| | June 30, 2015 | | | | Weighted Average Yield |
|---|---------------------|------------------------------|-------------------------------|---------------------|------------------------------|
| | Amortized Cost | Gross Unrealized Gains | Gross Unrealized Losses | Fair Value | |
| (In thousands) | | | | | |
| Available-for-sale | | | | | |
| Mortgage-backed securities | | | | | |
| FNMA and FHLMC certificates | \$ 832,127 | \$ 30,638 | \$ 1,192 | \$ 861,573 | 3.01% |
| GNMA certificates | 3,625 | 249 | - | 3,874 | 5.03% |
| CMOs issued by US government-sponsored agencies | 157,884 | 83 | 2,921 | 155,046 | 1.83% |
| Total mortgage-backed securities | 993,636 | 30,970 | 4,113 | 1,020,493 | 2.83% |
| Investment securities | | | | | |
| Obligations of US government-sponsored agencies | 6,114 | 14 | - | 6,128 | 1.36% |
| Obligations of Puerto Rico government and political subdivisions | 20,988 | - | 6,259 | 14,729 | 5.41% |
| Other debt securities | 2,835 | 134 | - | 2,969 | 2.99% |
| Total investment securities | 29,937 | 148 | 6,259 | 23,826 | 4.35% |
| Total securities available for sale | \$ 1,023,573 | \$ 31,118 | \$ 10,372 | \$ 1,044,319 | 2.87% |
| Held-to-maturity | | | | | |
| Mortgage-backed securities | | | | | |
| FNMA and FHLMC certificates | 525,504 | 978 | 3,757 | 522,725 | 2.28% |
| Investment securities | | | | | |
| US Treasury securities | 25,049 | 6 | 4 | 25,051 | 0.49% |
| Total securities held to maturity | 550,553 | 984 | 3,761 | 547,776 | 2.20% |
| Total | \$ 1,574,126 | \$ 32,102 | \$ 14,133 | \$ 1,592,095 | 2.64% |

| | December 31, 2014 | | | | Weighted Average Yield |
|-----------------------------------|-------------------|------------------------------|-------------------------------|---------------|------------------------------|
| | Amortized Cost | Gross Unrealized Gains | Gross Unrealized Losses | Fair Value | |
| (In thousands) | | | | | |
| Available-for-sale | | | | | |
| Mortgage-backed securities | | | | | |
| FNMA and FHLMC certificates | \$ 972,836 | \$ 37,876 | \$ 1,203 | \$ 1,009,509 | 3.12% |
| GNMA certificates | 4,473 | 288 | 8 | 4,753 | 4.94% |

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| | | | | | |
|---|---------------------|------------------|-----------------|---------------------|--------------|
| CMOs issued by US government-sponsored agencies | 179,146 | 136 | 3,153 | 176,129 | 1.81% |
| Total mortgage-backed securities | 1,156,455 | 38,300 | 4,364 | 1,190,391 | 2.92% |
| Investment securities | | | | | |
| Obligations of US government-sponsored agencies | 7,148 | 33 | - | 7,181 | 1.34% |
| Obligations of Puerto Rico government and public instrumentalities | 20,939 | - | 5,267 | 15,672 | 5.41% |
| Other debt securities | 3,137 | 157 | - | 3,294 | 2.95% |
| Total investment securities | 31,224 | 190 | 5,267 | 26,147 | 4.23% |
| Total securities available-for-sale | \$ 1,187,679 | \$ 38,490 | \$ 9,631 | \$ 1,216,538 | 2.96% |
| Held-to-maturity | | | | | |
| Mortgage-backed securities FNMA and FHLMC certificates | 162,752 | 1,402 | - | 164,154 | 2.48% |
| Total | \$ 1,350,431 | \$ 39,892 | \$ 9,631 | \$ 1,380,692 | 2.90% |

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NOTES TO UNAUDITED CONSOLIDATED FINANCIAL STATEMENTS – (Continued)

The amortized cost and fair value of the Company's investment securities at June 30, 2015, by contractual maturity, are shown in the next table. Securities not due on a single contractual maturity date, such as collateralized mortgage obligations, are classified in the period of final contractual maturity. Expected maturities may differ from contractual maturities because issuers may have the right to call or prepay obligations with or without call or prepayment penalties.

| | June 30, 2015 | | | |
|--|---------------------|---------------------|-------------------|-------------------|
| | Available-for-sale | | Held-to-maturity | |
| | Amortized Cost | Fair Value | Amortized Cost | Fair Value |
| | (In thousands) | | (In thousands) | |
| Mortgage-backed securities | | | | |
| Due after 5 to 10 years | | | | |
| FNMA and FHLMC certificates | \$ 18,125 | \$ 18,401 | \$ - | \$ - |
| Total due after 5 to 10 years | 18,125 | 18,401 | - | - |
| Due after 10 years | | | | |
| FNMA and FHLMC certificates | 814,002 | 843,172 | 525,504 | 522,725 |
| GNMA certificates | 3,625 | 3,874 | - | - |
| CMOs issued by US government-sponsored agencies | 157,884 | 155,046 | - | - |
| Total due after 10 years | 975,511 | 1,002,092 | 525,504 | 522,725 |
| Total mortgage-backed securities | 993,636 | 1,020,493 | 525,504 | 522,725 |
| Investment securities | | | | |
| Due from 1 to 5 years | | | | |
| US Treasury securities | - | - | 25,049 | 25,051 |
| Obligations of Puerto Rico government and political subdivisions | 10,521 | 8,444 | - | - |
| Total due from 1 to 5 years | 10,521 | 8,444 | 25,049 | 25,051 |
| Due after 5 to 10 years | | | | |
| Obligations of US government and sponsored agencies | 6,114 | 6,128 | - | - |
| Total due after 5 to 10 years | 6,114 | 6,128 | - | - |
| Due after 10 years | | | | |
| Obligations of Puerto Rico government and political subdivisions | 10,467 | 6,285 | - | - |
| Other debt securities | 2,835 | 2,969 | - | - |
| Total due after 10 years | 13,302 | 9,254 | - | - |
| Total investment securities | 29,937 | 23,826 | 25,049 | 25,051 |
| Total securities available-for-sale | \$ 1,023,573 | \$ 1,044,319 | \$ 550,553 | \$ 547,776 |

OFG BANCORP

NOTES TO UNAUDITED CONSOLIDATED FINANCIAL STATEMENTS – (Continued)

The Company, as part of its asset/liability management, may purchase U.S. Treasury securities and U.S. government-sponsored agency discount notes close to their maturities as alternatives to cash deposits at correspondent banks or as a short term vehicle to reinvest the proceeds of sale transactions until investment securities with attractive yields can be purchased. During the six-month period ended June 30, 2015 and 2014, the Company sold \$63.5 million and \$48.1 million, respectively, of available-for-sale Government National Mortgage Association (“GNMA”) certificates that were sold as part of its recurring mortgage loan origination and securitization activities. These sales did not realize any gains or losses during such periods.

For the six-month periods ended June 30, 2015 and 2014, the Company recorded a net gain on sale of securities of \$2.6 million and \$4.4 million, respectively. The table below presents the gross realized gains by category for such periods:

| <u>Description</u> | Six-Month Period Ended June 30, 2015 | | | | Gross Losses |
|--|--------------------------------------|--------------------|-----------------|-------------|--------------|
| | Sale Price | Book Value at Sale | Gross Gains | | |
| | (In thousands) | | | | |
| Sale of securities available-for-sale | | | | | |
| Mortgage-backed securities | | | | | |
| FNMA and FHLMC certificates | \$ 40,307 | \$ 37,735 | \$ 2,571 | \$ - | |
| GNMA certificates | 63,524 | 63,523 | 1 | - | |
| Total | \$ 103,831 | \$ 101,258 | \$ 2,572 | \$ - | |

| <u>Description</u> | Six-Month Period Ended June 30, 2014 | | | | Gross Losses |
|--|--------------------------------------|--------------------|-----------------|-------------|--------------|
| | Sale Price | Book Value at Sale | Gross Gains | | |
| | (In thousands) | | | | |
| Sale of securities available-for-sale | | | | | |
| Mortgage-backed securities | | | | | |
| FNMA and FHLMC certificates | \$ 115,158 | \$ 110,792 | \$ 4,366 | \$ - | |
| GNMA certificates | 48,077 | 48,077 | - | - | |
| Total mortgage-backed securities | \$ 163,235 | \$ 158,869 | \$ 4,366 | \$ - | |

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NOTES TO UNAUDITED CONSOLIDATED FINANCIAL STATEMENTS – (Continued)

The following tables show the Company's gross unrealized losses and fair value of investment securities available-for-sale and held-to-maturity, aggregated by investment category and the length of time that individual securities have been in a continuous unrealized loss position at June 30, 2015 and December 31, 2014:

| | June 30, 2015 | | |
|--|----------------------------|--------------------------------------|-----------------------|
| | 12 months or more | | |
| | Amortized Cost | Unrealized Loss | Fair Value |
| | (In thousands) | | |
| Securities available-for-sale | | | |
| CMOs issued by US government-sponsored agencies | \$ 115,483 | \$ 2,807 | \$ 112,676 |
| Obligations of Puerto Rico government and political subdivisions | 20,988 | 6,259 | 14,729 |
| | \$ 136,471 | \$ 9,066 | \$ 127,405 |
| | Less than 12 months | | |
| | Amortized Cost | Unrealized Loss | Fair Value |
| | (In thousands) | | |
| Securities available-for-sale | | | |
| CMOs issued by US Government-sponsored agencies | \$ 28,596 | \$ 114 | \$ 28,482 |
| FNMA and FHLMC certificates | 163,733 | 1,192 | 162,541 |
| | 192,329 | 1,306 | 191,023 |
| Securities held-to-maturity | | | |
| FNMA and FHLMC Certificates | 358,591 | 3,757 | 354,834 |
| US Treasury Securities | 10,024 | 4 | 10,020 |
| | 368,615 | 3,761 | 364,854 |
| | \$ 560,944 | \$ 5,067 | \$ 555,877 |
| | Amortized Cost | Total Unrealized Loss | Fair Value |
| | (In thousands) | | |
| Securities available-for-sale | | | |
| CMOs issued by US government-sponsored agencies | \$ 144,079 | \$ 2,921 | \$ 141,158 |
| FNMA and FHLMC certificates | 163,733 | 1,192 | 162,541 |
| Obligations of Puerto Rico government and political subdivisions | 20,988 | 6,259 | 14,729 |
| | 328,800 | 10,372 | 318,428 |
| Securities held-to-maturity | | | |
| FNMA and FHLMC Certificates | 358,591 | 3,757 | 354,834 |
| US Treasury Securities | 10,024 | 4 | 10,020 |
| | 368,615 | 3,761 | 364,854 |
| | \$ 697,415 | \$ 14,133 | \$ 683,282 |

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NOTES TO UNAUDITED CONSOLIDATED FINANCIAL STATEMENTS – (Continued)

| | December 31, 2014 | | |
|--|----------------------------|-------------------|-------------------|
| | 12 months or more | | |
| | Amortized | Unrealized | Fair |
| | Cost | Loss | Value |
| | (In thousands) | | |
| Securities available-for-sale | | | |
| Obligations of Puerto Rico government and political subdivisions | \$ 20,939 | \$ 5,267 | \$ 15,672 |
| CMOs issued by US government-sponsored agencies | 143,928 | 3,086 | 140,842 |
| FNMA and FHLMC certificates | 113,376 | 1,172 | 112,204 |
| GNMA certificates | 77 | 8 | 69 |
| | \$ 278,320 | \$ 9,533 | \$ 268,787 |
| | | | |
| | Less than 12 months | | |
| | Amortized | Unrealized | Fair |
| | Cost | Loss | Value |
| | (In thousands) | | |
| Securities available-for-sale | | | |
| CMOs issued by US government-sponsored agencies | 15,172 | 67 | 15,105 |
| FNMA and FHLMC certificates | 63,736 | 31 | 63,705 |
| | \$ 78,908 | \$ 98 | \$ 78,810 |
| | | | |
| | Amortized | Total | Fair |
| | Cost | Unrealized | Value |
| | (In thousands) | | |
| Securities available-for-sale | | | |
| CMOs issued by US government-sponsored agencies | 159,100 | 3,153 | 155,947 |
| FNMA and FHLMC certificates | 177,112 | 1,203 | 175,909 |
| Obligations of Puerto Rico government and political subdivisions | 20,939 | 5,267 | 15,672 |
| GNMA certificates | 77 | 8 | 69 |
| | \$ 357,228 | \$ 9,631 | \$ 347,597 |

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NOTES TO UNAUDITED CONSOLIDATED FINANCIAL STATEMENTS – (Continued)

The Company performs valuations of the investment securities on a monthly basis. Moreover, the Company conducts quarterly reviews to identify and evaluate each investment in an unrealized loss position for other-than-temporary impairment. Any portion of a decline in value associated with credit loss is recognized in the statements of operations with the remaining noncredit-related component recognized in other comprehensive income (loss). A credit loss is determined by assessing whether the amortized cost basis of the security will be recovered by comparing the present value of cash flows expected to be collected from the security, discounted at the rate equal to the yield used to accrete current and prospective beneficial interest for the security. The shortfall of the present value of the cash flows expected to be collected in relation to the amortized cost basis is considered to be the “credit loss.”

Other-than-temporary impairment analysis is based on estimates that depend on market conditions and are subject to further change over time. In addition, while the Company believes that the methodology used to value these exposures is reasonable, the methodology is subject to continuing refinement, including those made as a result of market developments. Consequently, it is reasonably possible that changes in estimates or conditions could result in the need to recognize additional other-than-temporary impairment charges in the future.

Most of the investments (\$676.4 million, amortized cost, or 97%) with an unrealized loss position at June 30, 2015 consist of securities issued or guaranteed by the U.S. Treasury or U.S. government-sponsored agencies, all of which are highly liquid securities that have a large and efficient secondary market. Their aggregate losses and their variability from period to period are the result of changes in market conditions, and not due to the repayment capacity or creditworthiness of the issuers or guarantors of such securities.

The remaining investments (\$21.0 million, amortized cost, or 3%) with an unrealized loss position at June 30, 2015 consist of obligations issued or guaranteed by the government of Puerto Rico and its political subdivisions or instrumentalities. The decline in the market value of these securities is mainly attributed to an increase in volatility as a result of changes in market conditions that reflect the significant economic and fiscal challenges that Puerto Rico is facing, including a protracted economic recession, sizable government debt-service obligations and structural budget deficits, high unemployment and a shrinking population. Moreover, the negative rating decisions taken by the credit rating agencies have affected the market value and liquidity of these securities.

As of June 30, 2015, the Company applied a discounted cash flow analysis to the Puerto Rico government bonds to calculate the cash flows expected to be collected and determine if any portion of the decline in market value of these investments was considered an other-than-temporary impairment. The analysis derives an estimate of value based on the present value of risk-adjusted future cash flows of the underlying investments, and included the following components:

- The contractual future cash flows of the bonds are projected based on the key terms as set forth in the official statements for each investment. Such key terms include among others the interest rate, amortization schedule, if any, and maturity date.

- The risk-adjusted cash flows are calculated based on a monthly default probability and recovery rate assumptions based on the credit rating of each investment. Constant monthly default rates are assumed throughout the life of the bonds which are based on the respective security's credit rating as of the date of the analysis.
- The adjusted future cash flows are 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 cash flow analysis for the investments showed a cumulative default probability at maturity in the range of 5.953% to 38.650%, thus reflecting that it is more likely than not that the bonds will not default at all during their remaining terms (range between 61.349% and 94.046%). Based on this analysis, the Company determined that it is more likely than not that it will recover all interest and principal invested in the Puerto Rico government bonds and is therefore not required to recognize a credit loss as of June 30, 2015.

Also, the Bank's conclusion is based on the assessment of the specific source of repayment of each outstanding bond, and the bonds continue to perform. No principal is due on the bonds until July 1st, 2017, except for PRHTA that started the principal repayments on July 1st 2014 and was paid as scheduled. All scheduled interest payments are being collected from the three different issuers. The Bank has cash flow capacity, sufficient liquidity and a strong capital position to maintain the bonds and does not need to sell them in a loss position.

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NOTES TO UNAUDITED CONSOLIDATED FINANCIAL STATEMENTS – (Continued)

NOTE 4 - LOANS

The Company's loan portfolio is composed of covered loans and non-covered loans. Covered loans are subject to loss sharing agreements with the FDIC and non-covered loans are not subject to FDIC loss sharing agreements. The risks of covered loans are different from the risks of non-covered loans because of the loss protection provided by the FDIC to covered loans. Loans acquired in the BBVAPR Acquisition are included as non-covered loans in the unaudited consolidated statements of financial condition. Non-covered loans are further subdivided between originated and other loans, acquired loans accounted for under ASC 310-20 (loans with revolving feature and/or acquired at a premium), and acquired loans accounted for under ASC 310-30 (loans acquired with deteriorated credit quality, including those by analogy).

The composition of the Company's loan portfolio at June 30, 2015 and December 31, 2014 was as follows:

| | June 30, 2015 | December 31, 2014 |
|---|------------------|----------------------|
| | (In thousands) | |
| Non-covered loans: | | |
| Originated and other loans and leases held for investment: | | |
| Mortgage | \$ 757,187 | \$ 791,751 |
| Commercial | 1,363,851 | 1,289,732 |
| Consumer | 212,629 | 186,760 |
| Auto and leasing | 623,198 | 575,582 |
| | 2,956,865 | 2,843,825 |
| Acquired loans: | | |
| Accounted for under ASC 310-20 (Loans with revolving feature and/or acquired at a premium) | | |
| Commercial | 8,448 | 12,675 |
| Consumer | 41,505 | 45,344 |
| Auto | 142,570 | 184,782 |
| | 192,523 | 242,801 |
| Accounted for under ASC 310-30 (Loans acquired with deteriorated credit quality, including those by analogy) | | |
| Mortgage | 631,807 | 656,122 |
| Commercial | 406,447 | 452,201 |
| Construction | 93,263 | 106,361 |
| Consumer | 18,869 | 29,888 |
| Auto | 195,891 | 247,233 |
| | 1,346,277 | 1,491,805 |
| | 4,495,665 | 4,578,431 |
| Deferred loan cost, net | 3,877 | 4,282 |
| Loans receivable | 4,499,542 | 4,582,713 |

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| | | |
|---|---------------------|---------------------|
| Allowance for loan and lease losses on loans not accounted for under ASC 310-30 | (102,877) | (69,517) |
| Loans receivable, net | 4,396,665 | 4,513,196 |
| Mortgage loans held-for-sale | 20,768 | 14,539 |
| Total non-covered loans, net | 4,417,433 | 4,527,735 |
| Covered loans: | | |
| Loans secured by 1-4 family residential properties | 117,840 | 117,171 |
| Construction and development secured by 1-4 family residential properties | 19,152 | 19,562 |
| Commercial and other construction | 153,199 | 221,917 |
| Consumer | 3,295 | 4,506 |
| Total covered loans | 293,486 | 363,156 |
| Allowance for loan and lease losses on covered loans | (71,452) | (64,245) |
| Total covered loans, net | 222,034 | 298,911 |
| Total loans, net | \$ 4,639,467 | \$ 4,826,646 |

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NOTES TO UNAUDITED CONSOLIDATED FINANCIAL STATEMENTS – (Continued)

*Non-covered Loans*Originated and Other Loans and Leases Held for Investment

The Company's originated and other loans held for investment are encompassed within four portfolio segments: mortgage, commercial, consumer, and auto and leasing.

The following tables present the aging of the recorded investment in gross originated and other loans held for investment as of June 30, 2015 and December 31, 2014 by class of loans. Mortgage loans past due included delinquent loans in the GNMA buy-back option program. Servicers of loans underlying GNMA mortgage-backed securities must report as their own assets the defaulted loans that they have the option (but not the obligation) to repurchase, even when they elect not to exercise that option.

| | June 30, 2015 | | | | | | | |
|------------------------------------|------------------------------|------------------------------|----------------------------|--|-------------------------------|---------------------|----------------|---|
| | 30-59 Days Past Due | 60-89 Days Past Due | 90+ Days Past Due | Total Past Due (In thousands) | Current in Non- Accrual | Current Accruing | Total Loans | Loans 90+ Days Past Due and Still Accruing |
| Mortgage | | | | | | | | |
| Traditional (by origination year): | | | | | | | | |
| Up to the year 2002 | \$ 4,342 | \$ 2,258 | \$ 3,076 | \$ 9,676 | \$ - | \$ 51,533 | \$ 61,209 | \$ 42 |
| Years 2003 and 2004 | 8,460 | 4,616 | 6,260 | 19,336 | - | 84,968 | 104,304 | - |
| Year 2005 | 5,338 | 2,012 | 3,926 | 11,276 | - | 45,881 | 57,157 | - |
| Year 2006 | 6,496 | 3,315 | 7,601 | 17,412 | 170 | 64,292 | 81,874 | - |
| Years 2007, 2008 | | | | | | | | |
| and 2009 | 4,781 | 2,359 | 10,757 | 17,897 | - | 75,309 | 93,206 | 1,025 |
| Years 2010, 2011, 2012, 2013 | 3,399 | 1,528 | 9,063 | 13,990 | - | 205,934 | 219,924 | 168 |
| 2014 and 2015 | 32,816 | 16,088 | 40,683 | 89,587 | 170 | 527,917 | 617,674 | 1,235 |
| Non-traditional | 1,450 | 543 | 3,784 | 5,777 | - | 27,705 | 33,482 | - |

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| | | | | | | | | |
|------------------------------------|---------------|---------------|---------------|----------------|----------------|------------------|------------------|--------------|
| Loss mitigation program | 11,542 | 6,076 | 14,627 | 32,245 | 5,016 | 61,389 | 98,650 | 3,547 |
| | 45,808 | 22,707 | 59,094 | 127,609 | 5,186 | 617,011 | 749,806 | 4,782 |
| Home equity secured personal loans | - | - | - | - | - | 420 | 420 | - |
| GNMA's buy-back option program | - | - | 6,961 | 6,961 | - | - | 6,961 | - |
| | 45,808 | 22,707 | 66,055 | 134,570 | 5,186 | 617,431 | 757,187 | 4,782 |
| Commercial | | | | | | | | |
| Commercial secured by real estate: | | | | | | | | |
| Corporate | - | - | - | - | - | 201,251 | 201,251 | - |
| Institutional | - | - | - | - | - | 35,113 | 35,113 | - |
| Middle market | 3,929 | - | 2,180 | 6,109 | 8,216 | 183,736 | 198,061 | - |
| Retail | 611 | 153 | 7,280 | 8,044 | 2,048 | 193,319 | 203,411 | - |
| Floor plan | - | - | 50 | 50 | - | 3,047 | 3,097 | - |
| Real estate | - | - | - | - | - | 16,646 | 16,646 | - |
| | 4,540 | 153 | 9,510 | 14,203 | 10,264 | 633,112 | 657,579 | - |
| Other commercial and industrial: | | | | | | | | |
| Corporate | - | - | - | - | - | 65,344 | 65,344 | - |
| Institutional | - | - | - | - | 197,559 | 207,661 | 405,220 | - |
| Middle market | - | - | 225 | 225 | 479 | 102,281 | 102,985 | - |
| Retail | 325 | 284 | 772 | 1,381 | 930 | 92,935 | 95,246 | - |
| Floor plan | 153 | 77 | 23 | 253 | - | 37,224 | 37,477 | - |
| | 478 | 361 | 1,020 | 1,859 | 198,968 | 505,445 | 706,272 | - |
| | 5,018 | 514 | 10,530 | 16,062 | 209,232 | 1,138,557 | 1,363,851 | - |

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NOTES TO UNAUDITED CONSOLIDATED FINANCIAL STATEMENTS – (Continued)

June 30, 2015

| | 30-59 Days Past Due | 60-89 Days Past Due | 90+ Days Past Due | Total Past Due | Current in Non- Accrual | Current Accruing | Total Loans | Loans 90+ Days Past Due and Still Accruing |
|--------------------------------|---------------------------|---------------------------|-------------------------|----------------------|-------------------------------|---------------------|---------------------|---|
| (In thousands) | | | | | | | | |
| Consumer | | | | | | | | |
| Credit cards | 303 | 120 | 319 | 742 | - | 19,381 | 20,123 | - |
| Overdrafts | 22 | 2 | - | 24 | - | 293 | 317 | - |
| Personal lines of credit | 97 | 17 | 63 | 177 | 22 | 2,083 | 2,282 | - |
| Personal loans | 1,532 | 858 | 716 | 3,106 | 320 | 170,202 | 173,628 | - |
| Cash collateral personal loans | 87 | 51 | - | 138 | - | 16,141 | 16,279 | - |
| | 2,041 | 1,048 | 1,098 | 4,187 | 342 | 208,100 | 212,629 | - |
| Auto and leasing | 47,451 | 18,593 | 7,420 | 73,464 | 365 | 549,369 | 623,198 | - |
| Total | \$ 100,318 | \$ 42,862 | \$ 85,103 | \$ 228,283 | \$ 215,125 | \$ 2,513,457 | \$ 2,956,865 | \$ 4,782 |

OFG BANCORP

NOTES TO UNAUDITED CONSOLIDATED FINANCIAL STATEMENTS – (Continued)

| | December 31, 2014 | | | | | | | Loans 90+ Days Past Due and Still Accruing |
|--|------------------------------|------------------------------|----------------------------|----------------------|-------------------------------|---------------------|----------------|---|
| | 30-59 Days Past Due | 60-89 Days Past Due | 90+ Days Past Due | Total Past Due | Current in Non- Accrual | Current Accruing | Total Loans | |
| | (In thousands) | | | | | | | |
| Mortgage | | | | | | | | |
| Traditional (by origination year): | | | | | | | | |
| Up to the year 2002 | \$ 4,128 | \$ 3,157 | \$ 4,395 | \$ 11,680 | \$ - | \$ 54,064 | \$ 65,744 | \$ 134 |
| Years 2003 and 2004 | 10,484 | 4,735 | 6,489 | 21,708 | 455 | 87,506 | 109,669 | - |
| Year 2005 | 3,824 | 2,205 | 4,454 | 10,483 | 131 | 49,858 | 60,472 | - |
| Year 2006 | 5,706 | 3,298 | 8,667 | 17,671 | 548 | 67,331 | 85,550 | 89 |
| Years 2007, 2008 and 2009 | 5,283 | 1,809 | 7,646 | 14,738 | 761 | 77,990 | 93,489 | - |
| Years 2010, 2011, 2012, 2013 and 2014 | 3,684 | 2,992 | 6,900 | 13,576 | - | 190,848 | 204,424 | 365 |
| Non-traditional Loss mitigation program | 33,109 | 18,196 | 38,551 | 89,856 | 1,895 | 527,597 | 619,348 | 588 |
| Home equity secured personal loans GNMA's buy-back option program | 1,477 | 584 | 3,223 | 5,284 | - | 30,916 | 36,200 | - |
| | 8,199 | 7,106 | 14,114 | 29,419 | 6,358 | 57,666 | 93,443 | 2,766 |
| | 42,785 | 25,886 | 55,888 | 124,559 | 8,253 | 616,179 | 748,991 | 3,354 |
| | - | - | - | - | - | 517 | 517 | - |
| | - | - | 42,243 | 42,243 | - | - | 42,243 | - |
| | 42,785 | 25,886 | 98,131 | 166,802 | 8,253 | 616,696 | 791,751 | 3,354 |
| Commercial | | | | | | | | |
| Commercial secured by real estate: | | | | | | | | |
| Corporate | - | - | - | - | - | 133,076 | 133,076 | - |
| Institutional | - | - | - | - | - | 36,611 | 36,611 | - |
| Middle market | - | 645 | 396 | 1,041 | 8,494 | 154,515 | 164,050 | - |
| Retail | 330 | 561 | 7,275 | 8,166 | 1,445 | 166,017 | 175,628 | - |
| Floor plan | - | - | - | - | - | 1,650 | 1,650 | - |
| Real estate | - | - | - | - | - | 12,628 | 12,628 | - |
| | 330 | 1,206 | 7,671 | 9,207 | 9,939 | 504,497 | 523,643 | - |
| Other commercial and industrial: | | | | | | | | |
| Corporate | - | - | - | - | - | 63,746 | 63,746 | - |
| Institutional | - | - | - | - | - | 478,935 | 478,935 | - |
| Middle market | - | - | 618 | 618 | - | 91,716 | 92,334 | - |
| Retail | 866 | 412 | 1,061 | 2,339 | 1,047 | 86,785 | 90,171 | - |
| Floor plan | - | - | - | - | - | 40,903 | 40,903 | - |
| | 866 | 412 | 1,679 | 2,957 | 1,047 | 762,085 | 766,089 | - |

1,196 1,618 9,350 12,164 10,986 1,266,582 1,289,732 -

OFG BANCORP

NOTES TO UNAUDITED CONSOLIDATED FINANCIAL STATEMENTS – (Continued)

December 31, 2014

| | 30-59 Days Past Due | 60-89 Days Past Due | 90+ Days Past Due | Total Past Due | Current in Non- Accrual | Current Accruing | Total Loans | Loans 90+ Days Past Due and Still Accruing |
|--------------------------------|------------------------------|------------------------------|----------------------|----------------------|-------------------------------|---------------------|---------------------|---|
| (In thousands) | | | | | | | | |
| Consumer | | | | | | | | |
| Credit cards | 360 | 139 | 375 | 874 | - | 18,197 | 19,071 | - |
| Overdrafts | 20 | - | - | 20 | - | 287 | 307 | - |
| Personal lines of credit | 102 | 25 | 102 | 229 | 9 | 1,962 | 2,200 | - |
| Personal loans | 1,822 | 743 | 678 | 3,243 | 337 | 144,359 | 147,939 | - |
| Cash collateral personal loans | 275 | 39 | 9 | 323 | - | 16,920 | 17,243 | - |
| | 2,579 | 946 | 1,164 | 4,689 | 346 | 181,725 | 186,760 | - |
| Auto and leasing | 47,658 | 16,916 | 7,420 | 71,994 | 145 | 503,443 | 575,582 | - |
| Total | \$ 94,218 | \$ 45,366 | \$ 116,065 | \$ 255,649 | \$ 19,730 | \$ 2,568,446 | \$ 2,843,825 | \$ 3,354 |

At June 30, 2015 and December 31, 2014, the Company had \$347.5 million and \$450.2 million, respectively, in loans granted to the Puerto Rico government, including its instrumentalities, public corporations and municipalities as part of the institutional commercial loan segment. All loans granted to Puerto Rico government were current at June 30, 2015 and December 31, 2014. We, as part of the bank syndicate, agreed in August 2014 to extend our credit facilities with PREPA to March 31, 2015, and are currently extended to September 15, 2015. After the first extension, the Company classified the credit as substandard and a troubled-debt restructuring. The Company conducted an impairment analysis considering the probability of collection of principal and interest, which included a financial model to project the future liquidity status of PREPA under various scenarios and its capacity to service its financial obligations, and concluded that the PREPA had sufficient cash flows for the repayment of the line of credit. Despite the Company's analysis showing PREPA's capacity to repay the line of credit, the Company placed its participation in non-accrual and recorded a \$24 million provision during the first quarter of 2015. The impairment analysis was updated for the second quarter with no change in provision. For the quarter ended June 30, 2015, interest payments are being applied to principal

OFG BANCORP

NOTES TO UNAUDITED CONSOLIDATED FINANCIAL STATEMENTS – (Continued)

Acquired Loans Accounted for under ASC 310-20 (Loans with revolving feature and/or acquired at a premium)

Credit cards, retail and commercial revolving lines of credits, floor plans and performing auto loans with FICO scores over 660 acquired at a premium as part of the non-covered portfolio are accounted for under the guidance of ASC 310-20, which requires that any contractually required loan payment receivable in excess of the Company's initial investment in the loans be accreted into interest income on a level-yield basis over the life of the loan. Loans accounted for under ASC 310-20 are placed on non-accrual status when past due in accordance with the Company's non-accrual policy and any accretion of discount or amortization of premium is discontinued. Loans acquired in the non-covered portfolio that were accounted for under the provisions of ASC 310-20 are removed from the acquired loan category at the end of the reporting period upon refinancing, renewal or normal re-underwriting.

The following tables present the aging of the recorded investment in gross acquired loans accounted for under ASC 310-20 as of June 30, 2015 and December 31, 2014, by class of loans:

| | June 30, 2015 | | | | | | | Total Loans | Loans 90+ Days Past Due and Still Accruing |
|-----------------------------------|------------------------------|------------------------------|----------------------------|----------------------|----------------------------------|---------------------|----------------|----------------|---|
| | 30-59 Days Past Due | 60-89 Days Past Due | 90+ Days Past Due | Total Past Due | Current in Non- Accrual | Current Accruing | | | |
| (In thousands) | | | | | | | | | |
| Commercial | | | | | | | | | |
| Commercial secured by real estate | | | | | | | | | |
| Retail | \$ - | \$ - | \$ 344 | \$ 344 | \$ - | \$ - | \$ 344 | \$ - | |
| Floor plan | - | - | 496 | 496 | - | 2,267 | 2,763 | - | |
| | - | - | 840 | 840 | - | 2,267 | 3,107 | - | |
| Other commercial and industrial | | | | | | | | | |
| Retail | 145 | 32 | 173 | 350 | 2 | 3,608 | 3,960 | - | |
| Floor plan | 87 | 130 | 26 | 243 | 4 | 1,134 | 1,381 | - | |
| | 232 | 162 | 199 | 593 | 6 | 4,742 | 5,341 | - | |
| | 232 | 162 | 1,039 | 1,433 | 6 | 7,009 | 8,448 | - | |
| Consumer | | | | | | | | | |
| Credit cards | 1,005 | 361 | 1,023 | 2,389 | - | 35,870 | 38,259 | - | |
| Personal loans | 104 | 19 | 52 | 175 | - | 3,071 | 3,246 | - | |
| | 1,109 | 380 | 1,075 | 2,564 | - | 38,941 | 41,505 | - | |
| Auto | 9,364 | 3,209 | 1,075 | 13,648 | 65 | 128,857 | 142,570 | - | |

| | | | | | | | | |
|--------------|------------------|-----------------|-----------------|------------------|--------------|-------------------|-------------------|-------------|
| Total | \$ 10,705 | \$ 3,751 | \$ 3,189 | \$ 17,645 | \$ 71 | \$ 174,807 | \$ 192,523 | \$ - |
|--------------|------------------|-----------------|-----------------|------------------|--------------|-------------------|-------------------|-------------|

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OFG BANCORP

NOTES TO UNAUDITED CONSOLIDATED FINANCIAL STATEMENTS – (Continued)

December 31, 2014

| | 30-59 Days Past Due | 60-89 Days Past Due | 90+ Days Past Due | Total Past Due | Current in Non- Accrual | Current Accruing | Total Loans | Loans 90+ Days Past Due and Still Accruing |
|-----------------------------------|---------------------------|---------------------------|-------------------------|----------------------|----------------------------------|---------------------|-------------------|---|
| (In thousands) | | | | | | | | |
| Commercial | | | | | | | | |
| Commercial secured by real estate | | | | | | | | |
| Retail | \$ - | \$ - | \$ 351 | \$ 351 | \$ - | \$ - | \$ 351 | \$ - |
| Floor plan | - | 62 | 345 | 407 | - | 3,724 | 4,131 | - |
| | - | 62 | 696 | 758 | - | 3,724 | 4,482 | - |
| Other commercial and industrial | | | | | | | | |
| Retail | 155 | 67 | 192 | 414 | 2 | 3,705 | 4,121 | - |
| Floor plan | 202 | 134 | 223 | 559 | 10 | 3,503 | 4,072 | - |
| | 357 | 201 | 415 | 973 | 12 | 7,208 | 8,193 | - |
| | 357 | 263 | 1,111 | 1,731 | 12 | 10,932 | 12,675 | - |
| Consumer | | | | | | | | |
| Credit cards | 1,376 | 654 | 1,399 | 3,429 | - | 38,419 | 41,848 | - |
| Personal loans | 151 | 47 | 77 | 275 | - | 3,221 | 3,496 | - |
| | 1,527 | 701 | 1,476 | 3,704 | - | 41,640 | 45,344 | - |
| Auto | 11,003 | 3,453 | 1,262 | 15,718 | 76 | 168,988 | 184,782 | - |
| Total | \$ 12,887 | \$ 4,417 | \$ 3,849 | \$ 21,153 | \$ 88 | \$ 221,560 | \$ 242,801 | \$ - |

Acquired Loans Accounted for under ASC 310-30 (including those accounted for under ASC 310-30 by analogy)

Acquired loans that are part of the non-covered portfolio, except for credit cards, retail and commercial revolving lines of credits, floor plans and performing auto loans with FICO scores over 660 acquired at a premium, are accounted for by the Company in accordance with ASC 310-30.

The carrying amount corresponding to non-covered loans acquired with deteriorated credit quality, including those accounted under ASC 310-30 by analogy, in the statements of financial condition at June 30, 2015 and December 31, 2014 is as follows:

| | June 30, 2015 | December 31, 2014 |
|---|--------------------------|------------------------------|
| | (In thousands) | |
| Contractual required payments receivable | \$2,208,242 | \$2,394,378 |
| Less: Non-accretable discount | \$449,917 | \$456,627 |
| Cash expected to be collected | 1,758,325 | 1,937,751 |
| Less: Accretable yield | 412,048 | 445,946 |
| Carrying amount, gross | 1,346,277 | 1,491,805 |
| Less: allowance for loan and lease losses | 18,359 | 13,481 |
| Carrying amount, net | \$1,327,918 | \$1,478,324 |

At June 30, 2015 and December 31, 2014, the Company had \$167.8 million and \$168.8 million, respectively, in loans granted to the Puerto Rico government, including its instrumentalities, public corporations and municipalities as part of its non-covered acquired loans accounted for under ASC 310-30. This entire amount was current at June 30, 2015 and December 31, 2014.

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NOTES TO UNAUDITED CONSOLIDATED FINANCIAL STATEMENTS – (Continued)

The following tables describe the accretable yield and non-accretable discount activity of acquired loans accounted for under ASC 310-30 for the quarters and six-month periods ended June 30, 2015 and 2014, excluding covered loans:

| | Quarter Ended June 30, 2015 | | | | | |
|--|-----------------------------|------------------|------------------|------------------|------------------|-------------------|
| | Mortgage | Commercial | Construction | Auto | Consumer | Total |
| | (In thousands) | | | | | |
| Accretable Yield Activity: | | | | | | |
| Balance at beginning of period | \$ 284,612 | \$ 57,330 | \$ 19,390 | \$ 47,097 | \$ 5,601 | \$ 414,030 |
| Accretion | (8,813) | (9,597) | (2,143) | (6,163) | (1,287) | (28,003) |
| Change in Expected Cash Flows | - | 23,695 | 9,867 | - | - | 33,562 |
| Transfer (to) from non-accretable discount | 81 | 135 | (2,501) | (9,403) | 4,147 | (7,541) |
| Balance at end of period | \$ 275,880 | \$ 71,563 | \$ 24,613 | \$ 31,531 | \$ 8,461 | \$ 412,048 |
| Non-Accretable Discount Activity: | | | | | | |
| Balance at beginning of period | \$ 392,609 | \$ 15,826 | \$ 3,957 | \$ 14,543 | \$ 23,576 | \$ 450,511 |
| Change in actual and expected losses | (3,421) | (4,921) | 536 | (256) | (73) | (8,135) |
| Transfer from (to) accretable yield | (81) | (135) | 2,501 | 9,403 | (4,147) | 7,541 |
| Balance at end of period | \$ 389,107 | \$ 10,770 | \$ 6,994 | \$ 23,690 | \$ 19,356 | \$ 449,917 |
| Six- Month Period Ended June 30, 2015 | | | | | | |
| | Mortgage | Commercial | Construction | Auto | Consumer | Total |
| | (In thousands) | | | | | |
| Accretable Yield Activity: | | | | | | |
| Balance at beginning of period | \$ 298,364 | \$ 61,196 | \$ 25,829 | \$ 53,998 | \$ 6,559 | \$ 445,946 |
| Accretion | (17,800) | (20,356) | (5,953) | (13,151) | (2,213) | (59,473) |
| Change in Expected Cash Flows | - | 23,695 | 9,867 | - | - | 33,562 |
| Transfer (to) from non-accretable discount | (4,684) | 7,028 | (5,130) | (9,316) | 4,115 | (7,987) |
| Balance at end of period | \$ 275,880 | \$ 71,563 | \$ 24,613 | \$ 31,531 | \$ 8,461 | \$ 412,048 |
| Non-Accretable Discount Activity: | | | | | | |
| Balance at beginning of period | \$ 389,839 | \$ 23,069 | \$ 3,486 | \$ 16,215 | \$ 24,018 | \$ 456,627 |
| Change in actual and expected losses | (5,416) | (5,271) | (1,622) | (1,841) | (547) | (14,697) |
| Transfer from (to) accretable yield | 4,684 | (7,028) | 5,130 | 9,316 | (4,115) | 7,987 |
| Balance at end of period | \$ 389,107 | \$ 10,770 | \$ 6,994 | \$ 23,690 | \$ 19,356 | \$ 449,917 |

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NOTES TO UNAUDITED CONSOLIDATED FINANCIAL STATEMENTS – (Continued)

Quarter Ended June 30, 2014

| | Mortgage | Commercial | Construction | Auto | Consumer | Total |
|--|-------------------|------------------|------------------|------------------|------------------|-------------------|
| | (In thousands) | | | | | |
| Accretable Yield Activity: | | | | | | |
| Balance at beginning of period | \$ 278,468 | \$ 82,637 | \$ 35,005 | \$ 74,635 | \$ 11,256 | \$ 482,001 |
| Accretion | (9,363) | (12,217) | (5,973) | (10,593) | (1,568) | (39,714) |
| Transfer (to) from non-accretable discount | - | 71 | 1,640 | 578 | 30 | 2,319 |
| Balance at end of period | \$ 269,105 | \$ 70,491 | \$ 30,672 | \$ 64,620 | \$ 9,718 | \$ 444,606 |
| Non-Accretable Discount Activity: | | | | | | |
| Balance at beginning of period | \$ 458,648 | \$ 41,551 | \$ 7,248 | \$ 29,328 | \$ 26,519 | \$ 563,294 |
| Change in actual and expected losses | (2,859) | (430) | (220) | (1,471) | (1,271) | (6,251) |
| Transfer from (to) accretable yield | - | (71) | (1,640) | (578) | (30) | (2,319) |
| Balance at end of period | \$ 455,789 | \$ 41,050 | \$ 5,388 | \$ 27,279 | \$ 25,218 | \$ 554,724 |

Six- Month Period Ended June 30 , 2014

| | Mortgage | Commercial | Construction | Auto | Consumer | Total |
|--|-------------------|---------------|---------------|---------------|---------------|----------------|
| | (In thousands) | | | | | |
| Accretable Yield Activity: | | | | | | |
| Balance at beginning of period | \$ 287,841 | 96,139 | 42,993 | 77,845 | 12,735 | 517,553 |
| Accretion | (18,732) | (24,934) | (10,459) | (22,418) | (3,440) | (79,983) |
| Transfer (to) from non-accretable discount | (4) | (714) | (1,862) | 9,193 | 423 | 7,036 |
| Balance at end of period | \$ 269,105 | 70,491 | 30,672 | 64,620 | 9,718 | 444,606 |
| Non-Accretable Discount Activity: | | | | | | |
| Balance at beginning of period | \$ 463,166 | 42,515 | 5,851 | 39,645 | 28,410 | 579,587 |
| Change in actual and expected losses | (7,381) | (2,179) | (2,325) | (3,173) | (2,769) | (17,827) |
| Transfer from (to) accretable yield | 4 | 714 | 1,862 | (9,193) | (423) | (7,036) |
| Balance at end of period | \$ 455,789 | 41,050 | 5,388 | 27,279 | 25,218 | 554,724 |

Covered Loans

The carrying amount of covered loans at June 30, 2015 and December 31, 2014 is as follows:

| June 30 2015 | December 31 2014 |
|-----------------|---------------------|
| (In thousands) | |

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| | | | | |
|---|-----------|----------------|-----------|----------------|
| Contractual required payments receivable | \$ | 419,259 | \$ | 535,425 |
| Less: Non-accretable discount | | 21,132 | | 62,410 |
| Cash expected to be collected | | 398,127 | | 473,015 |
| Less: Accretable yield | | 104,641 | | 109,859 |
| Carrying amount, gross | | 293,486 | | 363,156 |
| Less: Allowance for covered loan and lease losses | | 71,452 | | 64,245 |
| Carrying amount, net | \$ | 222,034 | \$ | 298,911 |

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NOTES TO UNAUDITED CONSOLIDATED FINANCIAL STATEMENTS – (Continued)

The following tables describe the accretable yield and non-accretable discount activity of covered loans for the quarters and six-month periods ended June 30, 2015 and 2014:

| | Quarter Ended June 30, 2015 | | | | | | Total |
|--|--|-----------------------------------|---|-----------------|-----------------|-------------------|-------|
| | Loans Secured by 1-4 Family Residential Properties | Commercial and Other Construction | Construction & Development Secured by 1-4 Family Residential Properties | Leasing | Consumer | | |
| Accretable Yield Activity: | | | | | | | |
| Balance at beginning of period | \$ 58,332 | \$ 33,481 | \$ 20,806 | \$ 1,665 | \$ 2,004 | \$ 116,288 | |
| Accretion | (3,276) | (8,047) | (405) | (937) | (93) | (12,758) | |
| Transfer from (to) non-accretable discount | 750 | 2,039 | (2,052) | 375 | (1) | 1,111 | |
| Balance at end of period | \$ 55,806 | \$ 27,473 | \$ 18,349 | \$ 1,103 | \$ 1,910 | \$ 104,641 | |
| Non-Accretable Discount Activity: | | | | | | | |
| Balance at beginning of period | \$ 12,557 | \$ 10,493 | \$ - | \$ - | \$ 9,662 | \$ 32,712 | |
| Change in actual and expected losses | (405) | (8,454) | (2,052) | 375 | 67 | (10,469) | |
| Transfer from (to) accretable yield | (750) | (2,039) | 2,052 | (375) | 1 | (1,111) | |
| Balance at end of period | \$ 11,402 | \$ - | \$ - | \$ - | \$ 9,730 | \$ 21,132 | |

| | Six- Month Period Ended June 30, 2015 | | | | | | Total |
|--|--|-----------------------------------|---|-----------------|-----------------|-------------------|-------|
| | Loans Secured by 1-4 Family Residential Properties | Commercial and Other Construction | Construction & Development Secured by 1-4 Family Residential Properties | Leasing | Consumer | | |
| Accretable Yield Activity: | | | | | | | |
| Balance at beginning of period | \$ 47,636 | \$ 37,919 | \$ 20,753 | \$ 2,479 | \$ 1,072 | \$ 109,859 | |
| Accretion | (6,794) | (17,902) | (1,024) | (2,329) | (213) | (28,262) | |
| Transfer from (to) non-accretable discount | 14,964 | 7,456 | (1,380) | 953 | 1,051 | 23,044 | |
| Balance at end of period | \$ 55,806 | \$ 27,473 | \$ 18,349 | \$ 1,103 | \$ 1,910 | \$ 104,641 | |
| Non-Accretable Discount Activity: | | | | | | | |

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| | | | | | | |
|---------------------------------------|------------------|-------------|-------------|-------------|-----------------|------------------|
| Balance at beginning of period | \$ 27,348 | \$ 24,464 | \$ - | \$ - | \$ 10,598 | \$ 62,410 |
| Change in actual and expected losses | (982) | (17,008) | (1,380) | 953 | 183 | (18,234) |
| Transfer from (to) accretable yield | (14,964) | (7,456) | 1,380 | (953) | (1,051) | (23,044) |
| Balance at end of period | \$ 11,402 | \$ - | \$ - | \$ - | \$ 9,730 | \$ 21,132 |

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OFG BANCORP

NOTES TO UNAUDITED CONSOLIDATED FINANCIAL STATEMENTS – (Continued)

Quarter Ended June 30, 2014

Construction
&

Development

Secured

by 1-4

Family

Residential

Properties

Leasing

Consumer

Total

Loans
Secured
by 1-4
Family
Residential
PropertiesCommercial
and Other
Construction

Leasing

Accretable Yield Activity:

| | | | | | | |
|--|------------------|------------------|-------------|-----------------|-----------------|-------------------|
| Balance at beginning of period | \$ 54,619 | \$ 83,200 | \$ 209 | \$ 7,332 | \$ 2,407 | \$ 147,767 |
| Accretion | (4,033) | (17,141) | (1,070) | (2,377) | (259) | (24,880) |
| Transfer from (to) non-accretable discount | - | 4,168 | 861 | 145 | - | 5,174 |
| Balance at end of period | \$ 50,586 | \$ 70,227 | \$ - | \$ 5,100 | \$ 2,148 | \$ 128,061 |

Non-Accretable Discount Activity:

| | | | | | | |
|---------------------------------------|------------------|------------------|-------------|-------------|-----------------|------------------|
| Balance at beginning of period | \$ 31,340 | \$ 67,136 | \$ - | \$ - | \$ 8,847 | \$ 107,323 |
| Change in actual and expected losses | (1,481) | (16,372) | 861 | 145 | (78) | (16,925) |
| Transfer (to) from accretable yield | - | (4,168) | (861) | (145) | - | (5,174) |
| Balance at end of period | \$ 29,859 | \$ 46,596 | \$ - | \$ - | \$ 8,769 | \$ 85,224 |

Six- Month Period Ended June 30, 2014

Construction
&

Development

Secured

by 1-4

Family

Residential

Properties

Leasing

Consumer

Total

Loans
Secured
by 1-4
Family
Residential
PropertiesCommercial
and Other
Construction

Leasing

Accretable Yield Activity:

| | | | | | | |
|--|------------------|------------------|-------------|-----------------|-----------------|-------------------|
| Balance at beginning of period | \$ 53,250 | \$ 95,093 | \$ 1,690 | \$ 10,238 | \$ 2,688 | \$ 162,959 |
| Accretion | (8,197) | (31,993) | (2,150) | (5,388) | (540) | (48,268) |
| Transfer from (to) non-accretable discount | 5,533 | 7,127 | 460 | 250 | - | 13,370 |
| Balance at end of period | \$ 50,586 | \$ 70,227 | \$ - | \$ 5,100 | \$ 2,148 | \$ 128,061 |

Non-Accretable Discount Activity:

| | | | | | | |
|---------------------------------------|------------------|------------------|-------------|-------------|-----------------|------------------|
| Balance at beginning of period | \$ 39,182 | \$ 81,092 | \$ - | \$ - | \$ 9,203 | \$ 129,477 |
| Change in actual and expected losses | (3,790) | (27,369) | 460 | 250 | (434) | (30,883) |
| Transfer (to) from accretable yield | (5,533) | (7,127) | (460) | (250) | - | (13,370) |
| Balance at end of period | \$ 29,859 | \$ 46,596 | \$ - | \$ - | \$ 8,769 | \$ 85,224 |

OFG BANCORP

NOTES TO UNAUDITED CONSOLIDATED FINANCIAL STATEMENTS – (Continued)

Non-accrual Loans

The following table presents the recorded investment in loans in non-accrual status by class of loans as of June 30, 2015 and December 31, 2014:

| | June 30, 2015 | | December 31, 2014 |
|---|--------------------------|-----------|------------------------------|
| | (In thousands) | | |
| <u>Originated and other loans and leases held for investment</u> | | | |
| Mortgage | | | |
| Traditional (by origination year): | | | |
| Up to the year 2002 | \$ 3,104 | \$ | 4,427 |
| Years 2003 and 2004 | 6,317 | | 7,042 |
| Year 2005 | 3,926 | | 4,585 |
| Year 2006 | 7,861 | | 9,274 |
| Years 2007, 2008 and 2009 | 9,991 | | 8,579 |
| Years 2010, 2011, 2012, 2013, 2014 and 2015 | 9,183 | | 7,365 |
| | 40,382 | | 41,272 |
| Non-traditional | 3,784 | | 3,224 |
| Loss mitigation program | 19,504 | | 20,934 |
| | 63,670 | | 65,430 |
| Commercial | | | |
| Commercial secured by real estate | | | |
| Middle market | 14,325 | | 9,534 |
| Retail | 9,557 | | 9,000 |
| | 23,882 | | 18,534 |
| Other commercial and industrial | | | |
| Institutional | 197,559 | | - |
| Middle market | 703 | | 618 |
| Retail | 1,797 | | 2,527 |
| Floor plan | 23 | | - |
| | 200,082 | | 3,145 |
| | 223,964 | | 21,679 |
| Consumer | | | |
| Credit cards | 319 | | 375 |
| Personal lines of credit | 86 | | 110 |
| Personal loans | 1,107 | | 1,092 |
| Cash collateral personal loans | - | | 13 |
| | 1,512 | | 1,590 |
| Auto and leasing | 8,587 | | 8,668 |
| Total Non-accrual originated loans | \$ 297,733 | \$ | 97,367 |

OFG BANCORP

NOTES TO UNAUDITED CONSOLIDATED FINANCIAL STATEMENTS – (Continued)

| | June 30, 2015 | December 31, 2014 |
|--|-------------------|----------------------|
| | (In thousands) | |
| <u>Acquired loans accounted under ASC 310-20</u> | | |
| Commercial | | |
| Commercial secured by real estate | | |
| Retail | \$ 344 | \$ 351 |
| Floor plan | 496 | 407 |
| | 840 | 758 |
| Other commercial and industrial | | |
| Retail | 178 | 195 |
| Floor plan | 30 | 234 |
| | 208 | 429 |
| | 1,048 | 1,187 |
| Consumer | | |
| Credit cards | 1,023 | 1,399 |
| Personal loans | 52 | 77 |
| | 1,075 | 1,476 |
| Auto | 1,277 | 1,512 |
| Total non-accrual acquired loans accounted under ASC 310-20 | 3,400 | 4,175 |
| Total non-accrual loans | \$ 301,183 | \$ 101,542 |

Loans accounted for under ASC 310-30 are excluded from the above table as they are considered to be performing due to the application of the accretion method, in which these loans will accrete interest income over the remaining life of the loans using estimated cash flow analyses.

Delinquent residential mortgage loans insured or guaranteed under applicable FHA and VA programs are classified as non-performing loans when they become 90 days or more past due, but are not placed in non-accrual status until they become 18 months or more past due, since they are insured loans. Therefore, these loans are included as non-performing loans but excluded from non-accrual loans.

During the quarter ended March 31, 2015, the revolving line of credit to PREPA was classified as non-accrual. At June 30, 2015, this line of credit had an unpaid principal balance of \$197.6 million. For the quarter ended June 30, 2015, interest payments received were applied to principal. As of June 30, 2015, the specific reserve was maintained at \$24 million.

At June 30, 2015 and December 31, 2014, loans whose terms have been extended and which are classified as troubled-debt restructurings that are not included in non-accrual loans amounted to \$88.8 million and \$274.4 million, respectively, as they are performing under their new terms. At December 31, 2014, the balance included the revolving

line of credit to PREPA.

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NOTES TO UNAUDITED CONSOLIDATED FINANCIAL STATEMENTS – (Continued)

Impaired Loans

The Company evaluates all loans, some individually and others as homogeneous groups, for purposes of determining impairment. The total investment in impaired commercial loans was \$243.4 million and \$236.9 million at June 30, 2015 and December 31, 2014, respectively. Impaired commercial loans at June 30, 2015 and December 31, 2014 included the PREPA line of credit with an unpaid principal balance of \$197.6 million and \$200.0 million, respectively. The impaired commercial loans were measured based on the fair value of collateral or the present value of cash flows, including those identified as troubled-debt restructurings. The valuation allowance for impaired commercial loans amounted to \$27.4 million and \$841 thousand at June 30, 2015 and December 31, 2014, respectively. The valuation allowance for impaired commercial loans amounted to \$27.4 million including \$24.0 million of PREPA allowance placed during Q1 2015. The total investment in impaired mortgage loans was \$89.3 million and \$94.2 million at June 30, 2015 and December 31, 2014, respectively. Impairment on mortgage loans assessed as troubled-debt restructurings was measured using the present value of cash flows. The valuation allowance for impaired mortgage loans amounted to approximately \$8.3 million and \$9.0 million at June 30, 2015 and December 31, 2014, respectively.

Originated and Other Loans and Leases Held for Investment

The Company's recorded investment in non-covered commercial and mortgage loans categorized as originated and other loans and leases held for investment that were individually evaluated for impairment and the related allowance for loan and lease losses at June 30, 2015 and December 31, 2014 are as follows:

| | Unpaid Principal | June 30, 2015 | | Related Allowance | Coverage |
|--|-----------------------------|--------------------------------|------------------|------------------------------|-----------------|
| | | Recorded Investment | | | |
| | | (In thousands) | | | |
| Impaired loans with specific allowance: | | | | | |
| Commercial | \$ 215,139 | \$ 211,186 | \$ 27,401 | | 13% |
| Residential troubled-debt restructuring | 95,881 | 89,303 | 8,268 | | 9% |
| Impaired loans with no specific allowance: | | | | | |
| Commercial | 34,305 | 30,786 | N/A | | N/A |
| Total investment in impaired loans | \$ 345,325 | \$ 331,275 | \$ 35,669 | | 11% |

| | Unpaid Principal | December 31, 2014 | | Related Allowance | Coverage |
|--|-----------------------------|--------------------------------|--|------------------------------|-----------------|
| | | Recorded Investment | | | |
| | | (In thousands) | | | |

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| | | | | | | | |
|---|----|----------------|----|----------------|--------|--------------|-----------|
| Impaired loans with specific allowance | | | | | | | |
| Commercial | \$ | 6,349 | \$ | 6,226 | \$ 841 | 14% | |
| Residential troubled-debt restructuring | | 99,947 | | 94,185 | | 10% | |
| Impaired loans with no specific allowance | | | | | | | |
| Commercial | | 237,806 | | 230,044 | | N/A | |
| Total investment in impaired loans | \$ | 344,102 | \$ | 330,455 | \$ | 9,809 | 3% |

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OFG BANCORP

NOTES TO UNAUDITED CONSOLIDATED FINANCIAL STATEMENTS – (Continued)

Acquired Loans Accounted for under ASC 310-20 (Loans with revolving feature and/or acquired at a premium)

The Company's recorded investment in non-covered commercial loans categorized as non-covered acquired loans accounted for under ASC 310-20 that were individually evaluated for impairment and the related allowance for loan and lease losses at June 30, 2015 and December 31, 2014 are as follows:

| | June 30, 2015 | | | |
|---|---------------------|------------------------|----------------------|----------|
| | Unpaid Principal | Recorded Investment | Related Allowance | Coverage |
| | (In thousands) | | | |
| Impaired loans with no specific allowance | | | | |
| Commercial | \$ 1,435 | \$ 1,429 | N/A | N/A |
| Total investment in impaired loans | \$ 1,435 | \$ 1,429 | \$ - | - |

| | December 31, 2014 | | | |
|---|---------------------|------------------------|-----------------------|----------|
| | Unpaid Principal | Recorded Investment | Specific Allowance | Coverage |
| | (In thousands) | | | |
| Impaired loans with no specific allowance | | | | |
| Commercial | \$ 672 | \$ 672 | N/A | N/A |
| Total investment in impaired loans | \$ 672 | \$ 672 | \$ - | - |

Non-covered Acquired Loans Accounted for under ASC 310-30 (including those accounted for under ASC 310-30 by analogy)

The Company's recorded investment in non-covered acquired loan pools accounted for under ASC 310-30 and their related allowance for non-covered loan and lease losses at June 30, 2015 and December 31, 2014 are as follows:

| | June 30, 2015 | | | |
|----------------------------------|---------------------|------------------------|-----------|--|
| | Unpaid Principal | Recorded Investment | Allowance | Coverage to Recorded Investment |
| | (In thousands) | | | |
| Impaired non-covered loan pools: | | | | |
| Mortgage | \$ 22,901 | \$ 23,676 | \$ 557 | 2% |
| Commercial | 230,196 | 208,083 | 5,752 | 3% |
| Construction | 87,488 | 88,575 | 9,188 | 10% |
| Auto | 187,569 | 195,891 | 2,862 | 1% |

| | | | | | | | |
|--|-----------|----------------|-----------|----------------|-----------|---------------|-----------|
| Total investment in impaired non-covered loan pools | \$ | 528,154 | \$ | 516,225 | \$ | 18,359 | 4% |
|--|-----------|----------------|-----------|----------------|-----------|---------------|-----------|

| | December 31 , 2014 | | | Coverage to Recorded Investment |
|--|---------------------|------------------------|-----------------------------|--|
| | Unpaid Principal | Recorded Investment | Allowance (In thousands) | |
| Impaired non-covered loan pools: | | | | |
| Commercial | 289,228 | 255,619 | 5,506 | 2% |
| Construction | 90,786 | 83,751 | 7,970 | 10% |
| Consumer | 35,812 | 29,888 | 5 | 0% |
| Total investment in impaired non-covered loan pools | \$ 415,826 | \$ 369,258 | \$ 13,481 | 4% |

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NOTES TO UNAUDITED CONSOLIDATED FINANCIAL STATEMENTS – (Continued)

The tables above only present information with respect to non-covered loans and pools accounted for under ASC 310-30 if there is a recorded impairment to such loans or loan pools and a specific allowance for loan losses. As of June 30, 2015, the Company eliminated the specific allowance of \$5 thousand maintained on impaired non-covered acquired consumer loan pool accounted under ASC 310-30 because there was an increase in the net present value of cash flows expected to be collected from such pool when compared with the recorded investment. Likewise, the increase in mortgage and auto loan pools from December 31, 2014 to June 30, 2015 was caused by the establishment of a specific reserve with respect to impaired mortgage and auto loan pools that were required based on the net present value of the cash flows expected to be collected.

The following table presents the interest recognized in non-covered commercial and mortgage loans that were individually evaluated for impairment, excluding loans accounted for under ASC 310-30, for the quarters and six-month periods ended June 30, 2015 and 2014:

| | Quarter Ended June 30, | | | |
|--|----------------------------------|-----------------------------------|----------------------------------|-----------------------------------|
| | 2015 | | 2014 | |
| | Interest Income Recognized | Average Recorded Investment | Interest Income Recognized | Average Recorded Investment |
| | (In thousands) | | | |
| Originated and other loans held for investment: | | | | |
| Impaired loans with specific allowance | | | | |
| Commercial | \$ 45 | \$ 212,414 | \$ 39 | \$ 7,200 |
| Residential troubled-debt restructuring | 781 | 89,041 | 663 | 90,445 |
| Impaired loans with no specific allowance | | | | |
| Commercial | 316 | 30,015 | 77 | 21,951 |
| | 1,142 | 331,470 | 779 | 119,596 |
| Acquired loans accounted for under ASC 310-20: | | | | |
| Impaired loans with no specific allowance | | | | |
| Commercial | 11 | 1,446 | - | - |
| Total interest income from impaired loans | \$ 1,153 | \$ 332,916 | \$ 779 | \$ 119,596 |

| | Six-Month Period Ended June 30, | | | |
|--|----------------------------------|-----------------------------------|----------------------------------|-----------------------------------|
| | 2015 | | 2014 | |
| | Interest Income Recognized | Average Recorded Investment | Interest Income Recognized | Average Recorded Investment |
| | (In thousands) | | | |
| Originated and other loans held for investment: | | | | |
| Impaired loans with specific allowance | | | | |
| Commercial | \$ 90 | \$ 146,144 | \$ 78 | \$ 6,729 |
| Residential troubled-debt restructuring | 1,563 | 91,216 | 1,270 | 88,749 |

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| | | | | | |
|---|----------|------------|----------|------------|--|
| Impaired loans with no specific allowance | | | | | |
| Commercial | 631 | 95,791 | 154 | 21,790 | |
| | \$ 2,284 | \$ 333,151 | \$ 1,502 | \$ 117,268 | |
| Acquired loans accounted for under ASC 310-20: | | | | | |
| Impaired loans with no specific allowance | | | | | |
| Commercial | 21 | 1,923 | - | - | |
| Total interest income from impaired loans | \$ 2,305 | \$ 335,074 | \$ 1,502 | \$ 117,268 | |

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NOTES TO UNAUDITED CONSOLIDATED FINANCIAL STATEMENTS – (Continued)

Covered Loans

The Company's recorded investment in covered loan pools that have recorded impairments and their related allowance for covered loan and lease losses as of June 30, 2015 and December 31, 2014 are as follows:

| | June 30, 2015 | | | Coverage to Recorded Investment |
|---|-----------------------------|--------------------------------|-------------------------------|--|
| | Unpaid Principal | Recorded Investment | Allowance | |
| | (In thousands) | | | |
| Impaired covered loan pools: | | | | |
| Loans secured by 1-4 family residential properties | \$ 124,906 | \$ 106,937 | \$ 17,594 | 16% |
| Construction and development secured by 1-4 family residential properties | 46,732 | 19,152 | 12,300 | 64% |
| Commercial and other construction | 132,636 | 95,655 | 41,170 | 43% |
| Consumer | 6,102 | 1,718 | 389 | 23% |
| Total investment in impaired covered loan pools | \$ 310,376 | \$ 223,462 | \$ 71,453 | 32% |
| | | | | |
| | December 31, 2014 | | | Coverage to Recorded Investment |
| | Unpaid Principal | Recorded Investment | Specific Allowance | |
| | (In thousands) | | | |
| Impaired covered loan pools with specific allowance | | | | |
| Loans secured by 1-4 family residential properties | \$ 134,579 | \$ 106,116 | \$ 15,522 | 15% |
| Construction and development secured by 1-4 family residential properties | 57,123 | 19,562 | 10,724 | 55% |
| Commercial and other construction | 93,894 | 74,069 | 37,610 | 51% |
| Consumer | 7,992 | 4,506 | 389 | 9% |
| Total investment in impaired covered loan pools | \$ 293,588 | \$ 204,253 | \$ 64,245 | 31% |

| | Number of contracts | Pre-Modification Outstanding Investment Recorded | Pre-Modification Weighted Average Rate | Pre-Modification Weighted Average Term (in Months) | Post-Modification Outstanding Investment Recorded | Post-Modification Weighted Average Rate | Post-Modification Weighted Average Term (in Months) |
|------------|----------------------------|---|---|---|--|--|--|
| Mortgage | 88 | \$ 11,813 | 6.00% | 349 | \$ 11,446 | 4.26% | 390 |
| Commercial | 1 | 73 | 7.00% | 55 | 73 | 9.25% | 36 |
| Consumer | 8 | 66 | 13.00% | 70 | 68 | 13.31% | 68 |

Doubtful: Loans classified as “doubtful” have all the weaknesses inherent in those classified as substandard, with the added characteristic that the weaknesses make collection or liquidation in full, on the basis of currently existing facts, conditions, and values, questionable and improbable.

Loss: Loans classified as “loss” are considered uncollectible and of such little value that their continuance as bankable assets is not warranted. This classification does not mean that the asset has absolutely no recovery or salvage value, but rather that it is not practical or desirable to defer writing off this worthless loan even though partial recovery may be effected in the future.

Loans not meeting the criteria above that are analyzed individually as part of the above described process are considered to be pass rated loans.

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NOTES TO UNAUDITED CONSOLIDATED FINANCIAL STATEMENTS – (Continued)

As of June 30, 2015 and December 31, 2014, and based on the most recent analysis performed, the risk category of gross non-covered originated and other loans and acquired loans accounted for under ASC 310-20 subject to risk rating by class of loans is as follows:

| | Balance | | June 30, 2015 | | | | Individually Measured for Impairment |
|--|---------------------|---------------------|--------------------|-----------------|-------------|-------------------|---|
| | | | Risk Ratings | | | | |
| | Outstanding | Pass | Special Mention | Substandard | Doubtful | | |
| | (In thousands) | | | | | | |
| Commercial - originated and other loans held for investment | | | | | | | |
| Commercial secured by real estate: | | | | | | | |
| Corporate | \$ 201,251 | \$ 183,630 | \$ 15,306 | \$ - | \$ - | \$ 2,315 | |
| Institutional | 35,113 | 26,444 | 8,444 | - | - | 225 | |
| Middle market | 198,061 | 172,626 | 7,008 | 109 | - | 18,318 | |
| Retail | 203,411 | 182,468 | 6,229 | 4,399 | - | 10,315 | |
| Floor plan | 3,097 | 2,765 | 192 | - | - | 140 | |
| Real estate | 16,646 | 16,646 | - | - | - | - | |
| | 657,579 | 584,579 | 37,179 | 4,508 | - | 31,313 | |
| Other commercial and industrial: | | | | | | | |
| Corporate | 65,344 | 59,684 | - | - | - | 5,660 | |
| Institutional | 405,220 | 207,661 | - | - | - | 197,559 | |
| Middle market | 102,985 | 97,775 | - | - | - | 5,210 | |
| Retail | 95,246 | 91,455 | 484 | 1,672 | - | 1,635 | |
| Floor plan | 37,477 | 34,306 | 2,565 | 12 | - | 594 | |
| | 706,272 | 490,881 | 3,049 | 1,684 | - | 210,658 | |
| Total | 1,363,851 | 1,075,460 | 40,228 | 6,192 | - | 241,971 | |
| Commercial - acquired loans | | | | | | | |
| (under ASC 310-20) | | | | | | | |
| Commercial secured by real estate: | | | | | | | |
| Retail | 344 | - | - | 344 | - | - | |
| Floor plan | 2,763 | 1,521 | - | - | - | 1,242 | |
| | 3,107 | 1,521 | - | 344 | - | 1,242 | |
| Other commercial and industrial: | | | | | | | |
| Retail | 3,960 | 3,943 | - | 17 | - | - | |
| Floor plan | 1,381 | 1,264 | - | 30 | - | 87 | |
| | 5,341 | 5,207 | - | 47 | - | 87 | |
| Total | 8,448 | 6,728 | - | 391 | - | 1,329 | |
| Total | \$ 1,372,299 | \$ 1,082,188 | \$ 40,228 | \$ 6,583 | \$ - | \$ 243,300 | |

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NOTES TO UNAUDITED CONSOLIDATED FINANCIAL STATEMENTS – (Continued)

| | December 31, 2014 | | | | | Individually Measured for Impairment | |
|--|------------------------|---------------------|--------------------|-----------------|-------------|---|--|
| | Balance Outstanding | Risk Ratings | | | | | |
| | | Pass | Special Mention | Substandard | Doubtful | | |
| | | (In thousands) | | | | | |
| Commercial - originated and other loans held for investment | | | | | | | |
| Commercial secured by real estate: | | | | | | | |
| Corporate | \$ 133,076 | \$ 109,282 | \$ 15,615 | \$ - | \$ - | \$ 8,179 | |
| Institutional | 36,611 | 27,089 | 9,284 | - | - | 238 | |
| Middle market | 164,050 | 148,360 | 2,817 | - | - | 12,873 | |
| Retail | 175,628 | 159,209 | 3,690 | 2,637 | - | 10,092 | |
| Floor plan | 1,650 | 692 | 958 | - | - | - | |
| Real estate | 12,628 | 12,628 | - | - | - | - | |
| | 523,643 | 457,260 | 32,364 | 2,637 | - | 31,382 | |
| Other commercial and industrial: | | | | | | | |
| Corporate | 63,746 | 63,746 | - | - | - | - | |
| Institutional | 478,935 | 278,953 | - | - | - | 199,982 | |
| Middle market | 92,334 | 87,126 | 2,815 | - | - | 2,393 | |
| Retail | 90,171 | 85,941 | 259 | 2,575 | - | 1,396 | |
| Floor plan | 40,903 | 38,413 | 1,247 | 126 | - | 1,117 | |
| | 766,089 | 554,179 | 4,321 | 2,701 | - | 204,888 | |
| Total | 1,289,732 | 1,011,439 | 36,685 | 5,338 | - | 236,270 | |
| Commercial - acquired loans | | | | | | | |
| (under ASC 310-20) | | | | | | | |
| Commercial secured by real estate: | | | | | | | |
| Retail | 351 | - | - | 351 | - | - | |
| Floor plan | 4,131 | 3,724 | - | - | - | 407 | |
| | 4,482 | 3,724 | - | 351 | - | 407 | |
| Other commercial and industrial: | | | | | | | |
| Retail | 4,121 | 4,080 | 8 | 33 | - | - | |
| Floor plan | 4,072 | 3,807 | - | - | - | 265 | |
| | 8,193 | 7,887 | 8 | 33 | - | 265 | |
| Total | 12,675 | 11,611 | 8 | 384 | - | 672 | |
| Total | \$ 1,302,407 | \$ 1,023,050 | \$ 36,693 | \$ 5,722 | \$ - | \$ 236,942 | |

All loans individually measured for impairment are classified as substandard at June 30, 2015 and December 31, 2014.

OFG BANCORP

NOTES TO UNAUDITED CONSOLIDATED FINANCIAL STATEMENTS – (Continued)

At June 30, 2015 and December 31, 2014, the Company had outstanding credit facilities of approximately \$515.3 million and \$619.0 million, respectively, granted to the Puerto Rico government, including its instrumentalities, public corporations and municipalities. A substantial portion of the Company's credit exposure to Puerto Rico's government consists of collateralized loans or obligations that have a specific source of income or revenues identified for their repayment. Approximately \$214 million of these loans are general obligations debt of municipalities secured by *ad valorem* taxation, without limitation as to rate or amount, on all taxable property within the issuing municipalities. The good faith, credit and unlimited taxing power of each issuing municipality are pledged for the payment of its general obligations debt.

In addition, some of these obligations consist of senior and subordinated loans to public corporations that obtain revenues from rates charged for services or products, such as the Puerto Rico Electric Power Authority ("PREPA") and the State Insurance Fund Corporation. The Commonwealth's instrumentalities or public corporations have varying degrees of independence from the central government. Some instrumentalities or public corporations that provide essential or important government services, such as the University of Puerto Rico, the Puerto Rico Medical Services Administration and the Puerto Rico Metropolitan Bus Authority, are supported by the Commonwealth through budget appropriations, while others, such as PREPA, are owed substantial amounts for utility services rendered to the Commonwealth.

At June 30, 2015, we had approximately \$301.0 million of credit facilities to public corporations of the Commonwealth, including:

- PREPA with an outstanding balance of \$197.6 million;
- The State Insurance Fund Corporation with an outstanding balance of \$77.6 million, which is approximately 130% collateralized by a portfolio of A-plus rated securities; and
- The Puerto Rico Housing Finance Authority with an outstanding balance of \$25.2 million to be repaid from abandoned or unclaimed funds at financial institutions that revert to the government under a Puerto Rico escheat law.

The outstanding balance of credit facilities to public corporations decreased during the second quarter as a result of a repayment in full of a \$75 million loan by the Puerto Rico Aqueduct and Sewer Authority.

Oriental Bank is part of a four bank syndicate providing a \$550 million revolving line of credit to finance the purchase of fuel for PREPA's day-to-day power generation activities. Our participation in the line of credit has an unpaid principal balance of \$197.6 million as of June 30, 2015. As part of the bank syndicate, the Bank entered into a forbearance agreement with PREPA, which has been extended several times, most recently until September 15, 2015. In connection with such extensions, PREPA appointed a Chief Restructuring Officer to work alongside the Executive

Director to develop, organize and manage a financial and operational restructuring of PREPA subject to the approval of PREPA's Board of Directors. PREPA also has been in negotiations with its forbearing creditors to restructure its debts and obtain financing for capital improvements needed to its infrastructure. The Company has classified the credit facility to PREPA as substandard and on non-accrual status. The Company conducted an impairment analysis considering the probability of collection of principal and interest, which included a financial model to project the future liquidity status of PREPA under various scenarios and its capacity to service its financial obligations, and concluded that PREPA had sufficient cash flows for the repayment of the line of credit. This analysis has been further supported by the various restructuring proposals made by PREPA and its creditors. Despite the Company's analysis showing PREPA's capacity to repay the line of credit, the Company placed its participation in non-accrual and recorded a \$24 million provision during the first quarter of 2015. The impairment analysis was updated for the second quarter with no change in provision. For the quarter ended June 30, 2015, interest payments are being applied to principal.

PREPA's enabling act provides for local receivership upon request to any Puerto Rico court of competent jurisdiction in the event of a default in debt-service payments or other obligations in connection with PREPA's bonds. The receiver so appointed would be empowered, directly or through its agents and attorneys, to take possession of the undertakings, income and revenues pledged to the payment of the bonds in default; to have, hold, use, operate, manage and control the same; and to exercise all of PREPA's rights and powers with respect to such undertakings. However, any such receiver would not have the power to sell, assign, mortgage or otherwise dispose of PREPA's assets, and its powers would be limited to the operation and maintenance of such undertakings and the collection and application of the income and revenues therefrom. Although the Puerto Rico government is actively seeking the right to bankruptcy relief for some of its public instrumentalities, including PREPA, both through an amendment to the federal bankruptcy code and the enactment of a local debt restructuring law, such efforts have thus far been unsuccessful.

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NOTES TO UNAUDITED CONSOLIDATED FINANCIAL STATEMENTS – (Continued)

For residential and consumer loan classes, the Company evaluates credit quality based on the delinquency status of the loan. As of June 30, 2015 and December 31, 2014, and based on the most recent analysis performed, the risk category of non-covered gross originated and other loans and acquired loans accounted for under ASC 310-20 not subject to risk rating by class of loans is as follows:

| | June 30, 2015 Delinquency | | | | | | |
|---|--------------------------------------|------------------|-----------------------|-----------------------|------------------------|-------------------------|----------------------|
| | Balance | | | | | | |
| | Outstanding | 0-29 days | 30-59 days | 60-89 days | 90-119 days | 120-364 days | 365+ days |
| | (In thousands) | | | | | | |
| <u>Originated and other loans and leases held for investment</u> | | | | | | | |
| Mortgage | | | | | | | |
| Traditional | | | | | | | |
| (by origination year) | | | | | | | |
| Up to the year 2002 | \$ 61,209 | \$ 50,718 | \$ 4,340 | \$ 2,256 | \$ 585 | \$ 1,034 | \$ 1,364 |
| Years 2003 and 2004 | 104,304 | 83,388 | 8,292 | 4,616 | 1,899 | 1,676 | 2,685 |
| Year 2005 | 57,157 | 44,825 | 5,338 | 2,012 | 646 | 733 | 2,547 |
| Year 2006 | 81,874 | 60,987 | 6,496 | 3,314 | 508 | 2,311 | 4,672 |
| Years 2007, 2008 | 93,206 | 72,190 | 4,458 | 2,028 | 597 | 3,859 | 6,029 |
| and 2009 | | | | | | | |
| Years 2010, 2011, 2012 | | | | | | | |
| 2013, 2014 and 2015 | 219,924 | 203,847 | 3,398 | 1,528 | 384 | 2,738 | 3,599 |
| | 617,674 | 515,955 | 32,322 | 15,754 | 4,619 | 12,351 | 20,896 |
| Non-traditional | 33,482 | 27,705 | 1,450 | 543 | 803 | 1,421 | 1,560 |
| Loss mitigation program | 98,650 | 15,626 | 3,535 | 1,742 | 1,107 | 1,487 | 1,626 |
| | 749,806 | 559,286 | 37,307 | 18,039 | 6,529 | 15,259 | 24,082 |
| Home equity secured | | | | | | | |
| | 420 | 420 | - | - | - | - | - |
| personal loans | | | | | | | |
| GNMA's buy-back | | | | | | | |
| option program | 6,961 | - | - | - | 1,995 | 2,486 | 2,480 |
| | 757,187 | 559,706 | 37,307 | 18,039 | 8,524 | 17,745 | 26,562 |
| Consumer | | | | | | | |
| Credit cards | 20,123 | 19,381 | 303 | 120 | 152 | 167 | - |
| Overdrafts | 317 | 293 | 22 | 2 | - | - | - |
| Unsecured personal lines of credit | 2,282 | 2,105 | 97 | 17 | 25 | 38 | - |
| Unsecured personal loans | 173,628 | 170,523 | 1,533 | 858 | 714 | - | - |

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| | | | | | | | |
|---|--------------------|--------------------|-----------------|-----------------|-----------------|-----------------|-----------------|
| Cash collateral personal loans | 16,279 | 16,141 | 87 | 51 | - | - | - |
| | 212,629 | 208,443 | 2,042 | 1,048 | 891 | 205 | - |
| Auto and Leasing | 623,198 | 549,734 | 47,451 | 18,593 | 5,065 | 2,355 | - |
| | 1,593,014 | 1,317,883 | 86,800 | 37,680 | 14,480 | 20,305 | 26,562 |
| <u>Acquired loans (accounted for under ASC 310-20)</u> | | | | | | | |
| Consumer | | | | | | | |
| Credit cards | 38,259 | 35,870 | 1,005 | 361 | 430 | 593 | - |
| Personal loans | 3,246 | 3,070 | 104 | 19 | 14 | 39 | - |
| | 41,505 | 38,940 | 1,109 | 380 | 444 | 632 | - |
| Auto | 142,570 | 128,922 | 9,364 | 3,209 | 788 | 287 | - |
| | 184,075 | 167,862 | 10,473 | 3,589 | 1,232 | 919 | - |
| Total | \$1,777,089 | \$1,485,745 | \$97,273 | \$41,269 | \$15,712 | \$21,224 | \$26,562 |

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NOTES TO UNAUDITED CONSOLIDATED FINANCIAL STATEMENTS – (Continued)

| | December 31, 2014 | | | | | | | |
|---|-------------------|------------------|---------------|---------------|---------------|---------------|---------------|--|
| | Delinquency | | | | | | | |
| | Balance | | | | | | | |
| Outstanding | 0-29 days | 30-59 days | 60-89 days | 90-119 days | 120-364 days | 365+ days | | |
| (In thousands) | | | | | | | | |
| <u>Originated and other loans and leases held for investment</u> | | | | | | | | |
| Mortgage | | | | | | | | |
| Traditional | | | | | | | | |
| (by origination year) | | | | | | | | |
| Up to the year 2002 | \$ 65,744 | \$ 53,432 | \$ 3,963 | \$ 3,083 | \$ 1,044 | \$ 1,360 | \$ 1,975 | |
| Years 2003 and 2004 | 109,669 | 86,941 | 10,391 | 4,362 | 1,657 | 3,215 | 1,330 | |
| Year 2005 | 60,472 | 49,275 | 3,824 | 2,205 | 389 | 1,673 | 1,893 | |
| Year 2006 | 85,550 | 65,113 | 5,263 | 2,967 | 1,242 | 2,801 | 4,624 | |
| Years 2007, 2008 | | | | | | | | |
| | 93,489 | 76,246 | 4,230 | 1,809 | 337 | 3,986 | 2,813 | |
| and 2009 | | | | | | | | |
| Years 2010, 2011, 2012 | | | | | | | | |
| 2013 and 2014 | 204,424 | 190,650 | 2,988 | 2,490 | 938 | 1,397 | 1,296 | |
| | 619,348 | 521,657 | 30,659 | 16,916 | 5,607 | 14,432 | 13,931 | |
| Non-traditional | 36,200 | 30,916 | 1,477 | 584 | 478 | 600 | 2,096 | |
| Loss mitigation program | 93,443 | 10,882 | 995 | 1,123 | 802 | 405 | 1,246 | |
| | 748,991 | 563,455 | 33,131 | 18,623 | 6,887 | 15,437 | 17,273 | |
| Home equity secured | | | | | | | | |
| | 517 | 517 | - | - | - | - | - | |
| personal loans | | | | | | | | |
| GNMA's buy-back | | | | | | | | |
| option program | 42,243 | - | - | - | 6,416 | 20,729 | 15,098 | |
| | 791,751 | 563,972 | 33,131 | 18,623 | 13,303 | 36,166 | 32,371 | |
| Consumer | | | | | | | | |
| Credit cards | 19,071 | 18,198 | 360 | 139 | 171 | 203 | - | |
| Overdrafts | 307 | 287 | 20 | - | - | - | - | |
| Unsecured personal lines of credit | 2,200 | 1,970 | 102 | 25 | 38 | 62 | 3 | |
| Unsecured personal loans | 147,939 | 144,696 | 1,822 | 743 | 623 | 55 | - | |
| Cash collateral personal loans | 17,243 | 16,920 | 275 | 39 | 9 | - | - | |
| | 186,760 | 182,071 | 2,579 | 946 | 841 | 320 | 3 | |
| Auto and Leasing | 575,582 | 503,588 | 47,658 | 16,916 | 5,196 | 2,224 | - | |
| | 1,554,093 | 1,249,631 | 83,368 | 36,485 | 19,340 | 38,710 | 32,374 | |
| <u>Acquired loans (accounted for under ASC 310-20)</u> | | | | | | | | |
| Consumer | | | | | | | | |
| Credit cards | 41,848 | 38,419 | 1,376 | 654 | 589 | 810 | - | |

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| | | | | | | | |
|----------------|--------------------|--------------------|-----------------|-----------------|-----------------|-----------------|-----------------|
| Personal loans | 3,496 | 3,221 | 151 | 47 | 39 | 38 | - |
| | 45,344 | 41,640 | 1,527 | 701 | 628 | 848 | - |
| Auto | 184,782 | 169,064 | 11,003 | 3,453 | 767 | 495 | - |
| | 230,126 | 210,704 | 12,530 | 4,154 | 1,395 | 1,343 | - |
| Total | \$1,784,219 | \$1,460,335 | \$95,898 | \$40,639 | \$20,735 | \$40,053 | \$32,374 |

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NOTES TO UNAUDITED CONSOLIDATED FINANCIAL STATEMENTS – (Continued)

NOTE 5 – ALLOWANCE FOR LOAN AND LEASE LOSSES

The composition of the Company's allowance for loan and lease losses at June 30, 2015 and December 31, 2014 was as follows:

| | June 30, 2015 | | December 31, 2014 |
|---|-------------------|-----------|----------------------|
| | (In thousands) | | |
| Allowance for loans and lease losses on non-covered loans: | | | |
| Originated and other loans and leases held for investment: | | | |
| Mortgage | \$ 18,076 | \$ | 19,679 |
| Commercial | 34,779 | | 8,432 |
| Consumer | 10,464 | | 9,072 |
| Auto and leasing | 15,064 | | 14,255 |
| Unallocated | 606 | | 1 |
| | 78,989 | | 51,439 |
| Acquired loans: | | | |
| Accounted for under ASC 310-20 (Loans with revolving feature and/or acquired at a premium) | | | |
| Commercial | 54 | | 65 |
| Consumer | 2,616 | | 1,211 |
| Auto | 2,859 | | 3,321 |
| | 5,529 | | 4,597 |
| Accounted for under ASC 310-30 (Loans acquired with deteriorated credit quality, including those by analogy) | | | |
| Mortgage | 473 | | - |
| Commercial | 14,940 | | 13,476 |
| Consumer | 84 | | 5 |
| Auto | 2,862 | | - |
| | 18,359 | | 13,481 |
| | 102,877 | | 69,517 |
| Allowance for loans and lease losses on covered loans: | | | |
| Loans secured by 1-4 family residential properties | 17,593 | | 15,522 |
| Commercial and other construction | 53,470 | | 48,334 |
| Consumer | 389 | | 389 |
| | 71,452 | | 64,245 |
| Total allowance for loan and lease losses | \$ 174,329 | \$ | 133,762 |

Non-Covered Loans

The Company maintains an allowance for loan and lease losses at a level that management considers adequate to provide for probable losses based upon an evaluation of known and inherent risks. The Company's allowance for loan and lease losses policy provides for a detailed quarterly analysis of probable losses. The analysis includes a review of historical loan loss experience, value of underlying collateral, current economic conditions, financial condition of borrowers and other pertinent factors. While management uses available information in estimating probable loan losses, future additions to the allowance may be required based on factors beyond the Company's control. We also maintain an allowance for loan losses on acquired loans when: (i) for loans accounted for under ASC 310-30, there is deterioration in credit quality subsequent to acquisition, and (ii) for loans accounted for under ASC 310-20, the inherent losses in the loans exceed the remaining credit discount recorded at the time of acquisition.

As part of the Company's continuous enhancement to the allowance for loan and lease losses methodology, during the quarter ended June 30, 2015, an assessment of the look-back period and historical loss factor was performed for auto and leasing and consumer and commercial loan portfolios. The analysis was based on the trends observed and their relation with the economic cycle as of the period ended June 30, 2015. As a result, for the commercial portfolio, the look-back period was changed to 36 months from the previously determined 12 months. For auto and leasing and consumer, a look back period of 24 months was maintained. In addition, during the quarter ended June 30, 2015, an assessment of environmental factors was performed for commercial, auto, and consumer portfolios. As a result, the environmental factors continue to reflect our assessment of the impact to our portfolio, taking into consideration the

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NOTES TO UNAUDITED CONSOLIDATED FINANCIAL STATEMENTS – (Continued)

current evolution of the portfolio and expected impact, due to recent economic developments, changes in values of collateral and delinquencies, among others. These changes in the allowance for loan and lease losses' look-back period and the result of the assessment in economic factors for the commercial, auto, and consumer portfolios are considered a change in accounting estimate as per ASC 250-10 provisions, where adjustments should be made prospectively.

Originated and Other Loans and Leases Held for Investment

The following tables present the activity in our allowance for loan and lease losses and the related recorded investment of the associated loans for our originated and other loans held for investment portfolio by segment for the periods indicated:

| | Quarter Ended June 30, 2015 | | | |
|--|-----------------------------|------------------|------------------|----------------------------|
| | Mortgage | Commercial | Consumer | Auto and Unsecured Leasing |
| | (In thousands) | | | |
| Allowance for loan and lease losses for non-covered originated and other loans: | | | | |
| Balance at beginning of period | \$ 18,086 | \$ 33,123 | \$ 9,405 | \$ 15,762 |
| Charge-offs | (1,356) | (497) | (2,309) | (7,662) |
| Recoveries | 67 | 219 | 390 | 3,425 |
| Provision for non-covered | | | | |
| loan and lease losses | 1,279 | 1,934 | 2,978 | 3,539 |
| Balance at end of period | \$ 18,076 | \$ 34,779 | \$ 10,464 | \$ 15,064 |

| | Six-Month Period Ended June 30, 2015 | | | |
|--|--------------------------------------|------------------|------------------|----------------------------|
| | Mortgage | Commercial | Consumer | Auto and Unsecured Leasing |
| | (In thousands) | | | |
| Allowance for loan and lease losses for non-covered originated and other loans: | | | | |
| Balance at beginning of period | \$ 19,679 | \$ 8,432 | \$ 9,072 | \$ 14,255 |
| Charge-offs | (2,770) | (1,489) | (3,985) | (15,798) |
| Recoveries | 67 | 309 | 543 | 6,809 |
| Provision for non-covered | | | | |
| loan and lease losses | 1,100 | 27,527 | 4,834 | 9,798 |
| Balance at end of period | \$ 18,076 | \$ 34,779 | \$ 10,464 | \$ 15,064 |

June 30, 2015

| | Mortgage | Commercial | Consumer | Aut and Leasi (In thousands) |
|---|-------------------|---------------------|-------------------|---------------------------------------|
| Allowance for loan and lease losses on non-covered originated and other loans: | | | | |
| Ending allowance balance attributable | | | | |
| to loans: | | | | |
| Individually evaluated for impairment | \$ 8,268 | \$ 27,401 | \$ - | \$ - |
| Collectively evaluated for impairment | 9,808 | 7,378 | 10,464 | 15,000 |
| Total ending allowance balance | \$ 18,076 | \$ 34,779 | \$ 10,464 | \$ 15,000 |
| Loans: | | | | |
| Individually evaluated for impairment | \$ 89,304 | \$ 241,971 | \$ - | \$ - |
| Collectively evaluated for impairment | 667,884 | 1,121,879 | 212,629 | 623,000 |
| Total ending loan balance | \$ 757,188 | \$ 1,363,850 | \$ 212,629 | \$ 623,000 |

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NOTES TO UNAUDITED CONSOLIDATED FINANCIAL STATEMENTS – (Continued)

| | Quarter Ended June 30, 2015 | | | |
|--|--------------------------------------|---------------------|-------------------|---------------------|
| | Mortgage | Commercial | Consumer | Auto and Leasing |
| | (In thousands) | | | |
| Allowance for loan and lease losses for non-covered originated and other loans: | | | | |
| Balance at beginning of period | \$ 19,511 | \$ 13,994 | \$ 7,135 | \$ 8,731 |
| Charge-offs | (987) | (543) | (1,397) | (5,956) |
| Recoveries | 88 | 115 | 244 | 2,136 |
| Provision (recapture) for non-covered loan and lease losses | 450 | (1,143) | 1,905 | 6,216 |
| Balance at end of period | \$ 19,062 | \$ 12,423 | \$ 7,887 | \$ 11,127 |
| | | | | |
| | Six-Month Period Ended June 30, 2015 | | | |
| | Mortgage | Commercial | Consumer | Auto and Leasing |
| | (In thousands) | | | |
| Allowance for loan and lease losses for non-covered originated and other loans: | | | | |
| Balance at beginning of period | \$ 19,937 | \$ 14,897 | \$ 6,006 | \$ 7,866 |
| Charge-offs | (2,201) | (962) | (2,235) | (10,601) |
| Recoveries | 236 | 213 | 391 | 3,660 |
| Provision (recapture) for non-covered loan and lease losses | 1,090 | (1,725) | 3,725 | 10,202 |
| Balance at end of period | \$ 19,062 | \$ 12,423 | \$ 7,887 | \$ 11,127 |
| | | | | |
| | December 31, 2014 | | | |
| | Mortgage | Commercial | Consumer | Auto and Leasing |
| | (In thousands) | | | |
| Allowance for loan and lease losses on non-covered originated and other loans: | | | | |
| Ending allowance balance attributable | | | | |
| to loans: | | | | |
| Individually evaluated for impairment | \$ 8,968 | \$ 841 | \$ - | \$ - |
| Collectively evaluated for impairment | 10,711 | 7,591 | 9,072 | 14,300 |
| Total ending allowance balance | \$ 19,679 | \$ 8,432 | \$ 9,072 | \$ 14,300 |
| Loans: | | | | |
| Individually evaluated for impairment | \$ 94,185 | \$ 236,270 | \$ - | \$ - |
| Collectively evaluated for impairment | 697,566 | 1,053,462 | 186,760 | 575,000 |
| Total ending loan balance | \$ 791,751 | \$ 1,289,732 | \$ 186,760 | \$ 575,000 |

During the quarter ended March 31, 2015 the Company placed its \$200 million participation in a line of credit to PREPA on non-accrual status and recorded a \$24.0 million provision for loan and lease losses. During the quarter ended June 30, 2015, interest payments received were applied to principal. As of June 30, 2015, the specific reserve

was maintained at \$24 million.

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NOTES TO UNAUDITED CONSOLIDATED FINANCIAL STATEMENTS – (Continued)

Acquired Loans accounted for under ASC 310-20 (Loans with revolving feature and/or acquired at a premium)

The following tables present the activity in our allowance for loan losses and related recorded investment of the associated loans in our non-covered acquired loan portfolio, excluding loans accounted for under ASC 310-30, for the periods indicated:

| | Quarter Ended June 30, 2015 | | | | |
|--|------------------------------------|-----------------|-----------------|--------------------|-----------------|
| | Commercial | Consumer | Auto | Unallocated | Total |
| | (In thousands) | | | | |
| Allowance for loan and lease losses | | | | | |
| for non-covered acquired loans | | | | | |
| accounted for under ASC 310-20: | | | | | |
| Balance at beginning of period | \$ 49 | \$ 1,885 | \$ 3,516 | \$ - | \$ 5,450 |
| Charge-offs | (16) | (1,303) | (1,038) | - | (2,357) |
| Recoveries | 7 | 429 | 502 | - | 938 |
| Provision (recapture) for non-covered acquired | | | | | |
| loan and lease losses accounted for | 14 | 1,605 | (121) | - | 1,498 |
| under ASC 310-20 | | | | | |
| Balance at end of period | \$ 54 | \$ 2,616 | \$ 2,859 | \$ - | \$ 5,529 |

| | Six-Month Period Ended June 30, 2015 | | | | |
|--|---|-----------------|-------------|--------------------|--------------|
| | Commercial | Consumer | Auto | Unallocated | Total |
| | (In thousands) | | | | |
| Allowance for loan and lease losses | | | | | |
| for non-covered acquired loans | | | | | |
| accounted for under ASC 310-20: | | | | | |
| Balance at beginning of period | \$ 65 | \$ 1,211 | \$ 3,321 | \$ - | \$ 4,597 |
| Charge-offs | (16) | (2,686) | (2,304) | - | (5,006) |
| Recoveries | 17 | 563 | 1,072 | - | 1,652 |
| (Recapture) Provision for non-covered acquired | | | | | |
| loan and lease losses accounted for | (12) | 3,528 | 770 | - | 4,286 |
| under ASC 310-20 | | | | | |

| | | | | | |
|---------------------------------|--------------|-----------------|-----------------|-------------|-----------------|
| Balance at end of period | \$ 54 | \$ 2,616 | \$ 2,859 | \$ - | \$ 5,529 |
|---------------------------------|--------------|-----------------|-----------------|-------------|-----------------|

| | Commercial | Consumer | June 30, 2015 Auto (In thousands) | Unallocated | Total |
|--|-------------------|------------------|--|--------------------|-------------------|
| Allowance for loan and lease losses on non-covered acquired loans accounted for under ASC 310-20: | | | | | |
| Ending allowance balance attributable | | | | | |
| to loans: | | | | | |
| Collectively evaluated for impairment | \$ 54 | \$ 2,616 | \$ 2,859 | \$ - | \$ 5,529 |
| Total ending allowance balance | \$ 54 | \$ 2,616 | \$ 2,859 | \$ - | \$ 5,529 |
| Loans: | | | | | |
| Individually evaluated for impairment | \$ 1,429 | \$ - | \$ - | \$ - | \$ 1,429 |
| Collectively evaluated for impairment | 7,019 | 41,505 | 142,570 | - | 191,094 |
| Total ending loan balance | \$ 8,448 | \$ 41,505 | \$ 142,570 | \$ - | \$ 192,523 |

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NOTES TO UNAUDITED CONSOLIDATED FINANCIAL STATEMENTS – (Continued)

| | Quarter Ended June 30, 2014 | | | | |
|--|-----------------------------|----------|----------|-------------|----------|
| | Commercial | Consumer | Auto | Unallocated | Total |
| | (In thousands) | | | | |
| Allowance for loan and lease losses | | | | | |
| for non-covered acquired loans | | | | | |
| accounted for under ASC 310-20: | | | | | |
| Balance at beginning of period | \$ 867 | \$ 504 | \$ 2,247 | \$ - | \$ 3,618 |
| Charge-offs | (110) | (1,952) | (1,370) | - | (3,432) |
| Recoveries | 30 | 124 | 535 | - | 689 |
| Provision (recapture) for non-covered acquired | | | | | |
| loan and lease losses accounted for | (323) | 1,662 | 1,230 | - | 2,569 |
| under ASC 310-20 | | | | | |
| Balance at end of period | \$ 464 | \$ 338 | \$ 2,642 | \$ - | \$ 3,444 |

| | Six-Month Period Ended June 30, 2014 | | | | |
|---|--------------------------------------|----------|----------|-------------|----------|
| | Commercial | Consumer | Auto | Unallocated | Total |
| | (In thousands) | | | | |
| Allowance for loan and lease losses | | | | | |
| for non-covered acquired loans | | | | | |
| accounted for under ASC 310-20: | | | | | |
| Balance at beginning of period | \$ 926 | \$ - | \$ 1,428 | \$ - | \$ 2,354 |
| Charge-offs | (284) | (4,010) | (2,666) | - | (6,960) |
| Recoveries | 30 | 224 | 985 | - | 1,239 |
| Provision (recapture)for non-covered acquired | | | | | |
| loan and lease losses accounted for | (208) | 4,124 | 2,895 | - | 6,811 |
| under ASC 310-20 | | | | | |
| Balance at end of period | \$ 464 | \$ 338 | \$ 2,642 | \$ - | \$ 3,444 |

| | Commercial | Consumer |
|--|------------------|-----------------|
| | (In | (In |
| Allowance for loan and lease losses on non-covered acquired loans accounted for under ASC 310-20: | | |
| Ending allowance balance attributable | | |
| to loans: | | |
| Collectively evaluated for impairment | \$ 65 | \$ 1,21 |
| Total ending allowance balance | \$ 65 | \$ 1,21 |
| Loans: | | |
| Individually evaluated for impairment | \$ 672 | \$ |
| Collectively evaluated for impairment | 12,003 | 45,34 |
| Total ending loan balance | \$ 12,675 | \$ 45,34 |

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NOTES TO UNAUDITED CONSOLIDATED FINANCIAL STATEMENTS – (Continued)

Acquired Loans Accounted for under ASC 310-30 (including those accounted for under ASC 310-30 by analogy)

The following tables present the activity in our allowance for loan losses and related recorded investment of the associated loans in our non-covered acquired loan portfolio accounted for under ASC 310-30, for the periods indicated:

| | Quarter Ended June 30, 2015 | | | | | Total |
|---|------------------------------------|-------------------|-----------------|-----------------|--|------------------|
| | Mortgage | Commercial | Consumer | Auto | | |
| | (In thousands) | | | | | |
| Allowance for loan and lease losses for non-covered loans accounted for under ASC 310-30: | | | | | | |
| Balance at beginning of period | \$ 473 | \$ 13,687 | \$ 6 | \$ - | | \$ 14,166 |
| Provision (recapture) for non-covered acquired loan and lease losses accounted for under ASC 310-30 | - | 1,253 | 78 | 2,862 | | 4,193 |
| Balance at end of period | \$ 473 | \$ 14,940 | \$ 84 | \$ 2,862 | | \$ 18,359 |

| | Six-Month Period Ended June 30, 2015 | | | | | Total |
|---|---|-------------------|-----------------|-----------------|--|------------------|
| | Mortgage | Commercial | Consumer | Auto | | |
| | (In thousands) | | | | | |
| Allowance for loan and lease losses for non-covered loans accounted for under ASC 310-30: | | | | | | |
| Balance at beginning of period | \$ - | \$ 13,476 | \$ 5 | \$ - | | \$ 13,481 |
| Provision (recapture) for non-covered acquired loan and lease losses accounted for under ASC 310-30 | 473 | 1,464 | 79 | 2,862 | | 4,878 |
| Balance at end of period | \$ 473 | \$ 14,940 | \$ 84 | \$ 2,862 | | \$ 18,359 |

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NOTES TO UNAUDITED CONSOLIDATED FINANCIAL STATEMENTS – (Continued)

| | Quarter Ended June 30, 2014 | | | | Total |
|--|--------------------------------------|------------|----------|--------|----------|
| | Mortgage | Commercial | Consumer | Auto | |
| | (In thousands) | | | | |
| Allowance for loan and lease losses for non-covered loans accounted for under ASC 310-30: | | | | | |
| Balance at beginning of period | \$ - | \$ 2,653 | \$ 405 | \$ - | \$ 3,058 |
| Provision (recapture) for non-covered acquired | | | | | |
| loan and lease losses accounted for | | | | | |
| under ASC 310-30 | - | 3,563 | (343) | - | 3,220 |
| Balance at end of period | \$ - | \$ 6,216 | \$ 62 | \$ - | \$ 6,278 |
| | | | | | |
| | Six-Month Period Ended June 30, 2014 | | | | Total |
| | Mortgage | Commercial | Consumer | Auto | |
| | (In thousands) | | | | |
| Allowance for loan and lease losses for non-covered loans accounted for under ASC 310-30: | | | | | |
| Balance at beginning of period | \$ - | \$ 1,713 | \$ 418 | \$ 732 | \$ 2,863 |
| Provision (recapture) for non-covered acquired | | | | | |
| loan and lease losses accounted for | - | 4,503 | (356) | (732) | 3,415 |
| under ASC 310-30 | | | | | |
| Balance at end of period | \$ - | \$ 6,216 | \$ 62 | \$ - | \$ 6,278 |

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NOTES TO UNAUDITED CONSOLIDATED FINANCIAL STATEMENTS – (Continued)

Covered Loans

For covered loans, as part of the evaluation of actual versus expected cash flows, the Company assesses on a quarterly basis the credit quality of these loans based on delinquency, severity factors and risk ratings, among other assumptions. Migration and credit quality trends are assessed at the pool level, by comparing information from the latest evaluation period through the end of the reporting period.

The changes in the allowance for loan and lease losses on covered loans for the quarters and six-month periods ended June 30, 2015 and 2014 were as follows:

| | Quarter Ended June 30, 2015 | | | |
|--|---|-------------------|---------------------|-----------------------|
| | Mortgage | Commercial | Construction | Leasing Total |
| | (In thousands) | | | |
| Allowance for loan and lease losses for covered loans: | | | | |
| Balance at beginning of period | \$ 17,340 | \$ 52,922 | \$ 389 | \$ - \$ 70,651 |
| Provision for covered loan and lease losses, net | 148 | (253) | - | - |
| FDIC shared-loss portion of provision for covered loan and lease losses, net | 105 | 801 | - | - |
| Balance at end of period | \$ 17,593 | \$ 53,470 | \$ 389 | \$ - \$ 71,452 |
| | | | | |
| | Six-Month Period Ended June 30, 2015 | | | |
| | Mortgage | Commercial | Construction | Leasing Total |
| | (In thousands) | | | |
| Allowance for loan and lease losses for covered loans: | | | | |
| Balance at beginning of period | \$ 15,522 | \$ 48,334 | \$ 389 | \$ - \$ 64,245 |
| Provision for (recapture) covered loan and lease losses, net | 1,966 | 2,738 | - | - |
| FDIC shared-loss portion of provision for covered loan and lease losses, net | 105 | 2,398 | - | - |
| Balance at end of period | \$ 17,593 | \$ 53,470 | \$ 389 | \$ - \$ 71,452 |

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NOTES TO UNAUDITED CONSOLIDATED FINANCIAL STATEMENTS – (Continued)

| | Quarter Ended June 30, 2014 | | | | |
|--|---|-------------------|---------------------|----------------|------------------|
| | Mortgage | Commercial | Construction | Leasing | Total |
| | (In thousands) | | | | |
| Allowance for loan and lease losses for covered loans: | | | | | |
| Balance at beginning of period | \$ 14,221 | \$ 39,562 | \$ 615 | \$ - | \$ 54,398 |
| Provision for covered loan and lease losses, net | 411 | 1,184 | - | - | 1,595 |
| FDIC shared-loss portion of provision for covered loan and lease losses, net | 292 | 3,230 | - | - | 3,522 |
| Balance at end of period | \$ 14,924 | \$ 43,976 | \$ 615 | \$ - | \$ 59,515 |
| | | | | | |
| | Six-Month Period Ended June 30, 2014 | | | | |
| | Mortgage | Commercial | Construction | Leasing | Total |
| | (In thousands) | | | | |
| Allowance for loan and lease losses for covered loans: | | | | | |
| Balance at beginning of period | \$ 12,495 | \$ 39,619 | \$ 615 | \$ - | \$ 52,729 |
| Provision for (recapture) covered loan and lease losses, net | 2,309 | 915 | - | - | 3,224 |
| FDIC shared-loss portion of provision for covered loan and lease losses, net | 120 | 3,442 | - | - | 3,562 |
| Balance at end of period | \$ 14,924 | \$ 43,976 | \$ 615 | \$ - | \$ 59,515 |

FDIC shared-loss portion of provision for (recapture of) covered loans and lease losses net, represents the credit impairment losses to be covered under the FDIC loss-share agreement which is increasing (decreasing) the FDIC loss-share indemnification asset.

Net provision for covered loans includes both additional reserves and reserve releases for different pools. The pools for which there were releases are also subject to a reduction to the FDIC shared-loss indemnification asset because of lower expected losses which are recognized as recaptures.

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NOTES TO UNAUDITED CONSOLIDATED FINANCIAL STATEMENTS – (Continued)

NOTE 6- FDIC INDEMNIFICATION ASSET AND TRUE-UP PAYMENT OBLIGATION

In connection with the FDIC assisted acquisition, the Bank and the FDIC entered into shared-loss agreements pursuant to which the FDIC covers a substantial portion of any losses on loans (and related unfunded loan commitments), foreclosed real estate and other repossessed properties covered by the agreements.

The acquired loans, foreclosed real estate, and other repossessed properties subject to the shared-loss agreements are collectively referred to as “covered assets.” Under the terms of the shared-loss agreements, the FDIC absorbs 80% of losses and shares in 80% of loss recoveries on covered assets. The term of the shared-loss agreement covering single family residential mortgage loans is ten years with respect to losses and loss recoveries, while the term of the shared-loss agreement covering commercial loans is five years with respect to losses and eight years with respect to loss recoveries, from the April 30, 2010 acquisition date. The shared-loss agreements also provide for certain costs directly related to the collection and preservation of covered assets to be reimbursed at an 80% level. The FDIC indemnification asset represents the portion of estimated losses covered by the shared-loss agreements between the Bank and the FDIC.

The following table presents the activity in the FDIC indemnification asset and true-up payment obligation for the quarters and six-month periods ended June 30, 2015 and 2014:

| | Quarter Ended June 30, | | Six-Month Period Ended | |
|---|------------------------|-------------------|------------------------|-------------------|
| | 2015 | 2014 | 2015 | 2014 |
| | (In thousands) | | | |
| <u>FDIC indemnification asset:</u> | | | | |
| Balance at beginning of period | \$ 75,221 | \$ 166,194 | \$ 97,378 | \$ 189,240 |
| Shared-loss agreements reimbursements from the FDIC | (24,387) | (10,464) | (38,087) | (18,700) |
| Increase (decrease) in expected credit losses to be | | | | |
| covered under shared-loss agreements, net | 906 | 3,522 | 2,503 | 3,562 |
| FDIC indemnification asset expense | (22,512) | (17,499) | (34,733) | (35,121) |
| Incurring expenses to be reimbursed under shared-loss | | | | |
| agreements | (6,524) | 1,907 | (4,357) | 4,679 |
| Balance at end of period | \$ 22,704 | \$ 143,660 | \$ 22,704 | \$ 143,660 |
| <u>True-up payment obligation:</u> | | | | |
| Balance at beginning of period | \$ 22,844 | \$ 19,375 | \$ 21,981 | \$ 18,510 |
| Change in true-up payment obligation | 733 | 856 | 1,596 | 1,721 |
| Balance at end of period | \$ 23,577 | \$ 20,231 | \$ 23,577 | \$ 20,231 |

The FDIC shared-loss expense bears an inverse relationship with a change in the yield of covered loan pools in accordance with ASC 310-30. ASC 310-30 dictates that such pools should be subject to increases in their yield when the present value of the expected cash flows is higher than the pool's carrying balance. When the increases in cash flow expectations are driven by reductions in the expected credit losses, the Bank recognizes that such losses are no longer expected to be collected from the FDIC. Accordingly, the Bank reduces the FDIC indemnification asset by amortizing the reduction in expected collections throughout the remaining life of the underlying pools. This amortization is recognized in the FDIC shared-loss expense.

The underlying factors that caused an increase in the expected cash flows and resulting reduction in projected losses are derived from the pool-level cash flow forecasts. Credit loss assumptions used to develop each pool-level cash flow forecast are based on the behavior of defaults, recoveries and losses of the corresponding pool of covered loans.

OFG BANCORP**NOTES TO UNAUDITED CONSOLIDATED FINANCIAL STATEMENTS – (Continued)**

The FDIC loss share coverage for the commercial loans and other non-single family loans was in effect until June 30, 2015. The coverage for the single family residential loans will expire on June 30, 2020. Accordingly, the Company amortized the remaining portion of the FDIC indemnification asset attributable to non-single family loans at the close of the second quarter of 2015. At June 30, 2015, the Company had a \$39.5 million receivable from the FDIC, included in other assets in the unaudited statement of financial condition, corresponding to \$12.9 million for the Q1 2015 loss-share certification that was received during July 2015 and \$26.6 million for the Q2 2015 loss-share certifications for commercial and other non-single family loans. At June 30, 2015, the FDIC indemnification asset reflects the balance only for single family residential mortgage loans. Notwithstanding the expiration of loss share coverage of non-single family loans, on July 2, 2015, the Company entered into an agreement with the FDIC pursuant to which the FDIC concurred with a potential sale of a pool of loss share assets covered under the non-single family loss share agreement. Pursuant to such agreement, the FDIC agreed to pay up to \$20 million in loss share coverage with respect to the aggregate loss resulting from any portfolio sale within 120 days of the agreement.

The FDIC indemnification asset expense of \$22.5 million for the quarter increased when compared to \$17.5 million for the second quarter of 2014. The expense of \$34.7 million for the six-month period ended June 30, 2015 stayed relatively flat when compared to \$35.1 million for the same period in 2014. The increase during the quarter was principally driven by differences between the expected losses realized during the last months of the non-single family shared loss agreement and the losses that were ultimately realized and are expected to be collected from the FDIC. For the six-month periods ended June 30, 2015 and 2014, the amortization expense totaled \$2.1 million and \$2 thousand, respectively was from stepped up cost recoveries on certain construction, commercial, and leasing pools.

Also in connection with the FDIC assisted acquisition, the Bank agreed to make a true-up payment, also known as a clawback liability or clawback provision, to the FDIC on the date that is 45 days following the last day (such day, the “True-Up Measurement Date”) of the final shared-loss month, or upon the final disposition of all covered assets under the shared-loss agreements in the event losses thereunder fail to reach expected levels. Under the shared-loss agreements, the Bank will pay to the FDIC 50% of the excess, if any, of: (i) 20% of the Intrinsic Loss Estimate of \$906.0 million (or \$181.2 million) (as determined by the FDIC) less (ii) the sum of: (A) 25% of the asset premium (discount) of (\$227.5 million) (or (\$56.9 million)); plus (B) 25% of the cumulative shared-loss payments (defined as the aggregate of all of the payments made or payable to the Bank minus the aggregate of all of the payments made or payable to the FDIC); plus (C) the sum of the period servicing amounts for every consecutive twelve-month period prior to and ending on the True-Up Measurement Date in respect of each of the shared-loss agreements during which the shared-loss provisions of the applicable shared-loss agreement is in effect (defined as the product of the simple average of the principal amount of shared-loss loans and shared-loss assets at the beginning and end of such period times 1%). The true-up payment represents an estimated liability of \$23.6 million and \$22.0 million, net of discount, as of June 30, 2015 and December 31, 2014, respectively. The estimated liability is included within accrued expenses and other liabilities in the unaudited consolidated statements of financial condition.

The true-up payment obligation, also known as clawback liability, may increase if actual and expected losses decline. The Company measures the true-up payment obligation at fair value. During the quarters and six-month periods ended June 30, 2015 and 2014 the fair value of the true-up payment obligation increased by \$733 thousand and \$856 thousand and \$1.6 million and \$1.7 million, respectively. These changes in fair value are included as change in

true-up payment obligation within FDIC shared-loss expense, net in the consolidated statements of operations.

The following table provides the fair value and the undiscounted amount of the true-up payment obligation at June 30, 2015 and December 31, 2014:

| | | June 30, 2015 | | December 31, 2014 |
|------------------------------|----|--------------------------|----|------------------------------|
| | | (In thousands) | | |
| Carrying amount (fair value) | \$ | 23,577 | \$ | 21,981 |
| Undiscounted amount | \$ | 37,456 | \$ | 40,266 |

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OFG BANCORP**NOTES TO UNAUDITED CONSOLIDATED FINANCIAL STATEMENTS – (Continued)****NOTE 7 - SERVICING ASSETS**

The Company periodically sells or securitizes mortgage loans while retaining the obligation to perform the servicing of such loans. In addition, the Company may purchase or assume the right to service mortgage loans originated by others. Whenever the Company undertakes an obligation to service a loan, management assesses whether a servicing asset and/or liability should be recognized. A servicing asset is recognized whenever the compensation for servicing is expected to more than adequately compensate the Company for servicing the loans and leases. Likewise, a servicing liability would be recognized in the event that servicing fees to be received are not expected to adequately compensate the Company for its expected cost.

All separately recognized servicing assets are recognized at fair value using the fair value measurement method. Under the fair value measurement method, the Company measures servicing rights at fair value at each reporting date, reports changes in fair value of servicing assets in earnings in the period in which the changes occur, and includes these changes, if any, with mortgage banking activities in the consolidated statements of operations. The fair value of servicing rights is subject to fluctuations as a result of changes in estimated and actual prepayment speeds and default rates and losses.

The fair value of servicing rights is estimated by using a cash flow valuation model which calculates the present value of estimated future net servicing cash flows, taking into consideration actual and expected loan prepayment rates, discount rates, servicing costs, and other economic factors, which are determined based on current market conditions.

At June 30, 2015, the servicing asset amounted to \$5.8 million (\$14.0 million — December 31, 2014) related to mortgage servicing rights.

During the second quarter of 2015, the Company completed the sale of certain servicing assets to Scotiabank Puerto Rico for approximately \$7.0 million. The Company recognized a loss of \$2.7 million related to this transaction, which is included as other non-interest (loss) income in the unaudited consolidated statements of operations.

The following table presents the changes in servicing rights measured using the fair value method for the quarters and six-month periods ended June 30, 2015 and 2014:

| Quarter Ended June 30, | Six-Month Period Ended June 30, |
|-----------------------------------|--|
|-----------------------------------|--|

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| | 2015 | 2014 | 2015 | 2014 |
|--|-----------------------|------------------|-----------------------|------------------|
| | (In thousands) | | (In thousands) | |
| Fair value at beginning of year | \$ 12,164 | \$ 13,970 | \$ 13,992 | \$ 13,801 |
| Sale of mortgage servicing rights | (6,985) | - | (6,985) | - |
| Servicing from mortgage securitizations or asset transfers | 1,529 | 490 | 2,060 | 1,053 |
| Changes due to payments on loans | (313) | (271) | (732) | (465) |
| Changes in fair value related to price of MSR's held for sale | (835) | - | (2,716) | - |
| Changes in fair value due to changes in valuation model inputs or assumptions | | | | |
| | 231 | (534) | 172 | (734) |
| Fair value at end of year | \$ 5,791 | \$ 13,655 | \$ 5,791 | \$ 13,655 |

The following table presents key economic assumption ranges used in measuring the mortgage-related servicing asset fair value for the six month periods June 30, 2015 and 2014:

| | Six-Month Period Ended June 30, | |
|---------------------------------|--|-----------------|
| | 2015 | 2014 |
| Constant prepayment rate | 4.10% - 10.22% | 5.60% - 10.08% |
| Discount rate | 10.00% - 12.00% | 10.00% - 12.00% |

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NOTES TO UNAUDITED CONSOLIDATED FINANCIAL STATEMENTS – (Continued)

The sensitivity of the current fair value of servicing assets to immediate 10 percent and 20 percent adverse changes in the above key assumptions were as follows:

| | June 30, 2015 (In thousands) | |
|---|---|---------|
| <u>Mortgage-related servicing asset</u> | | |
| Carrying value of mortgage servicing asset | \$ | 5,791 |
| Constant prepayment rate | | |
| Decrease in fair value due to 10% adverse change | \$ | (391) |
| Decrease in fair value due to 20% adverse change | \$ | (765) |
| Discount rate | | |
| Decrease in fair value due to 10% adverse change | \$ | (680) |
| Decrease in fair value due to 20% adverse change | \$ | (1,306) |

These sensitivities are hypothetical and should be used with caution. As the figures indicate, changes in fair value based on a 10 percent variation in assumptions generally cannot be extrapolated because the relationship of the change in assumption to the change in fair value may not be linear. Also, in this table, the effect of a variation in a particular assumption on the fair value of the retained interest is calculated without changing any other assumption.

Changes in one factor may result in changes in another (for example, increases in market interest rates may result in lower prepayments), which may magnify or offset the sensitivities. Mortgage banking activities, a component of total banking and financial service revenue in the consolidated statements of operations, include the changes from period to period in the fair value of the mortgage loan servicing rights, which may result from changes in the valuation model inputs or assumptions (principally reflecting changes in discount rates and prepayment speed assumptions) and other changes, including changes due to collection/realization of expected cash flows.

Servicing fee income is based on a contractual percentage of the outstanding principal balance and is recorded as income when earned. Servicing fees on mortgage loans for the quarter and six-month period ended June 30, 2015 totaled \$378 thousand and \$618 thousand, respectively. Servicing fees on mortgage loans for the quarter and six-month period ended June 30, 2014 totaled \$323 thousand and \$444 thousand, respectively.

OFG BANCORP

NOTES TO UNAUDITED CONSOLIDATED FINANCIAL STATEMENTS – (Continued)

NOTE 8 — DERIVATIVES

The following table presents the Company's derivative assets and liabilities at June 30, 2015 and December 31, 2014:

| | June 30, 2015 | | December 31, 2014 |
|--|------------------|-----------|----------------------|
| | (In thousands) | | |
| Derivative assets: | | | |
| Options tied to S&P 500 Index | \$ 2,137 | \$ | 5,555 |
| Interest rate swaps not designated as hedges | 2,154 | | 2,399 |
| Interest rate caps | 65 | | 152 |
| Other | 20 | | 1 |
| | \$ 4,376 | \$ | 8,107 |
| Derivative liabilities: | | | |
| Interest rate swaps designated as cash flow hedges | 6,514 | | 8,585 |
| Interest rate swaps not designated as hedges | 2,154 | | 2,399 |
| Interest rate caps | 65 | | 152 |
| Other | 6 | | 85 |
| | \$ 8,739 | \$ | 11,221 |

Interest Rate Swaps

The Company enters into interest rate swap contracts to hedge the variability of future interest cash flows of forecasted wholesale borrowings attributable to changes in a predetermined variable index rate. The interest rate swaps effectively fix the Company's interest payments on an amount of forecasted interest expense attributable to the variable index rate corresponding to the swap notional stated rate. These swaps are designated as cash flow hedges for the forecasted wholesale borrowing transactions, are properly documented as such, and therefore, qualify for cash flow hedge accounting. Any gain or loss associated with the effective portion of the cash flow hedges is recognized in other comprehensive income (loss) and is subsequently reclassified into operations in the period during which the hedged forecasted transactions affect earnings. Changes in the fair value of these derivatives are recorded in accumulated other comprehensive income to the extent there is no significant ineffectiveness in the cash flow hedging relationships. Currently, the Company does not expect to reclassify any amount included in other comprehensive income (loss) related to these interest rate swaps to operations in the next twelve months.

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NOTES TO UNAUDITED CONSOLIDATED FINANCIAL STATEMENTS – (Continued)

The following table shows a summary of these swaps and their terms at June 30, 2015:

| Type | Notional Amount (In thousands) | Fixed Rate | Variable Rate Index | Trade Date | Settlement Date | Maturity Date |
|---------------------|-----------------------------------|------------|---------------------|------------|-----------------|---------------|
| Interest Rate Swaps | \$ 25,000 | 2.4365% | 1-Month LIBOR | 05/05/11 | 05/04/12 | 05/04/16 |
| | 25,000 | 2.6200% | 1-Month LIBOR | 05/05/11 | 07/24/12 | 07/24/16 |
| | 25,000 | 2.6350% | 1-Month LIBOR | 05/05/11 | 07/30/12 | 07/30/16 |
| | 50,000 | 2.6590% | 1-Month LIBOR | 05/05/11 | 08/10/12 | 08/10/16 |
| | 100,000 | 2.6750% | 1-Month LIBOR | 05/05/11 | 08/16/12 | 08/16/16 |
| | 38,658 | 2.4210% | 1-Month LIBOR | 07/03/13 | 07/03/13 | 08/01/23 |
| | \$ 263,658 | | | | | |

An accumulated unrealized loss of \$6.5 million and \$8.6 million was recognized in accumulated other comprehensive income (loss) related to the valuation of these swaps at June 30, 2015 and December 31, 2014, respectively, and the related liability is being reflected in the accompanying unaudited consolidated statements of financial condition.

For June 30, 2015 and December 31, 2014, interest rate swaps not designated as hedging instruments that were offered to clients represented an asset of \$2.2 million and \$2.4 million, respectively, and were included as part of derivative assets in the unaudited consolidated statements of financial position. The credit risk to these clients stemming from these derivatives, if any, is not material. At June 30, 2015 and December 31, 2014, interest rate swaps not designated as hedging instruments that are the mirror-images of the derivatives offered to clients represented a liability of \$2.2 million and \$2.4 million, respectively, and were included as part of derivative liabilities in the unaudited consolidated statements of financial condition.

The following table shows a summary of these interest rate swaps not designated as hedging instruments and their terms at June 30, 2015:

| Type | Notional Amount (In thousands) | Fixed Rate | Variable Rate Index | Settlement Date | Maturity Date |
|--|-----------------------------------|------------|---------------------|-----------------|---------------|
| Interest Rate Swaps - Derivatives Offered to Clients | \$ 3,865 | 5.1300% | 1-Month LIBOR | 07/03/06 | 07/03/16 |
| | 12,500 | 5.5050% | 1-Month LIBOR | 04/11/09 | 04/11/19 |
| | \$ 16,365 | | | | |
| Interest Rate Swaps - Mirror Image Derivatives | \$ 3,865 | 5.1300% | 1-Month LIBOR | 07/03/06 | 07/03/16 |

12,500 5.5050% 1-Month LIBOR 04/11/09 04/11/19
\$ 16,365

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NOTES TO UNAUDITED CONSOLIDATED FINANCIAL STATEMENTS – (Continued)

Options Tied to Standard & Poor's 500 Stock Market Index

The Company has offered its customers certificates of deposit with an option tied to the performance of the S&P 500 Index. The Company uses option agreements with major broker-dealers to manage its exposure to changes in this index. Under the terms of the option agreements, the Company receives the average increase in the month-end value of the index in exchange for a fixed premium. The changes in fair value of the option agreements used to manage the exposure in the stock market in the certificates of deposit are recorded in earnings. At June 30, 2015 and December 31, 2014, the purchased options used to manage exposure to the S&P 500 Index on stock indexed deposits represented an asset of \$2.1 million (notional amount of \$5.0 million) and \$5.6 million (notional amount of \$10.7 million), respectively, and the options sold to customers embedded in the certificates of deposit and recorded as deposits in the unaudited consolidated statements of financial condition, represented a liability of \$2.0 million (notional amount of \$4.8 million) and \$5.5 million (notional amount of \$10.5 million), respectively.

Interest rate caps

The Company has entered into interest rate cap transactions with various clients with floating-rate debt who wish to protect their financial results against increases in interest rates. In these cases, the Company simultaneously enters into mirror-image interest rate cap transactions with financial counterparties. None of these cap transactions qualify for hedge accounting, and therefore, they are marked to market through earnings. For both June 30, 2015 and December 31, 2014, the outstanding total notional amount of interest rate caps was \$110.0 million. At June 30, 2015 and December 31, 2014, the interest rate caps sold to clients represented a liability of \$65 thousand and \$152 thousand, respectively, and were included as part of derivative liabilities in the unaudited consolidated statements of financial condition. At June 30, 2015 and December 31, 2014, the interest rate caps purchased as mirror-images represented an asset of \$65 thousand and \$152 thousand, respectively, and were included as part of derivative assets in the unaudited consolidated statements of financial condition.

NOTE 9 — ACCRUED INTEREST RECEIVABLE AND OTHER ASSETS

Accrued interest receivable at June 30, 2015 and December 31, 2014 consists of the following:

| | | June 30, 2015 | | December 31, 2014 |
|-------------------|----|--------------------------|----|------------------------------|
| | | (In thousands) | | |
| Non-covered loans | \$ | 14,606 | \$ | 17,005 |
| Investments | | 4,648 | | 4,340 |

\$ 19,254 \$ 21,345

Other assets at June 30, 2015 and December 31, 2014 consist of the following:

| | June 30, 2015 | December 31, 2014 |
|--|--------------------------|------------------------------|
| | (In thousands) | |
| Prepaid expenses | \$ 16,492 | \$ 16,018 |
| Core deposit and customer relationship intangibles | 8,791 | 9,743 |
| Other repossessed assets | 14,661 | 21,800 |
| Mortgage tax credits | 6,277 | 6,277 |
| Investment in Statutory Trust | 1,083 | 1,083 |
| FDIC certification receivable | 39,548 | 14,974 |
| Accounts receivable and other assets | 45,439 | 38,830 |
| | \$ 132,291 | \$ 108,725 |

OFG BANCORP**NOTES TO UNAUDITED CONSOLIDATED FINANCIAL STATEMENTS – (Continued)**

Prepaid expenses amounting to \$16.5 million and \$16.0 million at June 30, 2015 and December 31, 2014, respectively, include prepaid municipal, property and income taxes aggregating to \$9.6 million, at each period.

In connection with the FDIC-assisted acquisition and the BBVAPR Acquisition, the Company recorded a core deposit intangible representing the value of checking and savings deposits acquired. At June 30, 2015 and December 31, 2014, this core deposit intangible amounted to \$5.8 million and \$6.5 million, respectively. In addition, the Company recorded a customer relationship intangible amounting to \$5.0 million representing the value of customer relationships acquired with the acquisition of the securities broker-dealer and insurance agency in the BBVAPR Acquisition as of December 31, 2012. At June 30, 2015 and December 31, 2014, this customer relationship intangible amounted to \$3.0 million and \$3.3 million, respectively.

Other repossessed assets totaled \$14.7 million and \$21.8 million at June 30, 2015 and December 31, 2014, respectively, include repossessed automobiles amounting to \$14.0 million and \$20.7 million, respectively, which are recorded at their net realizable value.

At both June 30, 2015 and December 31, 2014, tax credits for the Company totaled \$6.3 million. These tax credits do not have an expiration date.

At June 30, 2015, the FDIC certification receivable included a \$12.9 million receivable corresponding to the FDIC loss-share certification from the first quarter of 2015 that was received in July 2015. In addition, it included a \$26.6 million receivable corresponding to the FDIC loss-share certification from the second quarter of 2015 for non-single family residential loans, as the loss share period on these loans was in effect until June 30, 2015. At December 31, 2014, the FDIC certification receivable included a \$15.0 million receivable corresponding to the FDIC loss-share certification from the third quarter of 2014 that was received in January 2015.

NOTE 10— DEPOSITS AND RELATED INTEREST

Total deposits, including related accrued interest payable, as of June 30, 2015 and December 31, 2014 consist of the following:

| June 30, 2015 | December 31, 2014 |
|--------------------------|------------------------------|
| (In thousands) | |

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| | | | | |
|--|----|------------------|----|------------------|
| Non-interest bearing demand deposits | \$ | 838,600 | \$ | 745,142 |
| Interest-bearing savings and demand deposits | | 2,348,478 | | 2,544,665 |
| Individual retirement accounts | | 276,185 | | 303,049 |
| Retail certificates of deposit | | 447,115 | | 452,150 |
| Institutional certificates of deposit | | 233,945 | | 260,090 |
| Total core deposits | | 4,144,323 | | 4,305,096 |
| Brokered deposits | | 605,361 | | 619,310 |
| Total deposits | \$ | 4,749,684 | \$ | 4,924,406 |

Brokered deposits include \$522.6 million in certificates of deposits and \$83.0 million in money market accounts at June 30, 2015, and \$526.2 million in certificates of deposits and \$93.1 million in money market accounts at December 31, 2014.

The weighted average interest rate of the Company's deposits was 0.65% at June 30, 2015 and 0.66% at December 31, 2014. Interest expense for the quarters and six-month periods ended June 30, 2015 and 2014 was as follows:

| | Quarter Ended June 30, | | Six-Month Period Ended June 30, | |
|-----------------------------|------------------------|-----------------|---------------------------------|------------------|
| | 2015 | 2014 | 2015 | 2014 |
| | (In thousands) | | (In thousands) | |
| Demand and savings deposits | \$ 3,100 | \$ 4,804 | \$ 6,482 | \$ 9,832 |
| Certificates of deposit | 3,504 | 4,361 | 7,226 | 8,311 |
| | \$ 6,604 | \$ 9,165 | \$ 13,708 | \$ 18,143 |

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NOTES TO UNAUDITED CONSOLIDATED FINANCIAL STATEMENTS – (Continued)

At June 30, 2015 and December 31, 2014, demand and interest-bearing deposits and certificates of deposit included deposits of Puerto Rico Cash & Money Market Fund, Inc., which amounted to \$98.7 million and \$96.8 million, respectively, with a weighted average rate of 0.77% and 0.78%, and were collateralized with investment securities with a fair value of \$80.0 million and \$76.3 million, respectively.

At June 30, 2015 and December 31, 2014, time deposits in denominations of \$100 thousand or higher, excluding accrued interest and unamortized discounts, amounted to \$588.1 million and \$608.1 million, respectively. Such amounts include public fund time deposits from various Puerto Rico government municipalities, agencies, and corporations of \$9.0 million at a weighted average rate of 0.49% at June 30, 2015, and \$6.9 million at a weighted average rate of 0.50% at December 31, 2014.

At June 30, 2015 and December 31, 2014, total public fund deposits from various Puerto Rico government municipalities, agencies, and corporations amounted to \$171.0 million and \$318.5 million, respectively. These public funds were collateralized with commercial loans amounting to \$411.4 million and \$414.5 million at June 30, 2015 and December 31, 2014, respectively.

Excluding equity indexed options in the amount of \$2.0 million, which are used by the Company to manage its exposure to the S&P 500 Index, and also excluding accrued interest of \$1.2 million and unamortized deposit discount in the amount of \$442 thousand, the scheduled maturities of certificates of deposit at June 30, 2015 are as follows:

| | June 30, 2015 | |
|------------------------------|-----------------------|------------------|
| | (In thousands) | |
| Within one year: | | |
| Three (3) months or less | \$ | 304,391 |
| Over 3 months through 1 year | | 637,132 |
| | | 941,523 |
| Over 1 through 2 years | | 358,217 |
| Over 2 through 3 years | | 123,227 |
| Over 3 through 4 years | | 11,660 |
| Over 4 through 5 years | | 41,100 |
| | \$ | 1,475,727 |

The table of scheduled maturities of certificates of deposits above includes brokered deposits.

The aggregate amount of overdrafts in demand deposit accounts that were reclassified to loans amounted to \$2.1 million and \$845 thousand as of June 30, 2015 and December 31, 2014, respectively.

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NOTES TO UNAUDITED CONSOLIDATED FINANCIAL STATEMENTS – (Continued)

NOTE 11 — BORROWINGS AND RELATED INTEREST

Securities Sold under Agreements to Repurchase

At June 30, 2015, securities underlying agreements to repurchase were delivered to, and are being held by, the counterparties with whom the repurchase agreements were transacted. The counterparties have agreed to resell to the Company the same or similar securities at the maturity of these agreements.

At June 30, 2015 and December 31, 2014, securities sold under agreements to repurchase (classified by counterparty), excluding accrued interest in the amount of \$3.6 million and \$2.3 million, respectively, were as follows:

| | June 30, 2015 | | December 31, 2014 | |
|---------------------------------------|------------------------------|--|------------------------------|--|
| | Borrowing Balance | Fair Value of Underlying Collateral | Borrowing Balance | Fair Value of Underlying Collateral |
| | (In thousands) | | | |
| JP Morgan Chase Bank NA | 428,902 | 469,599 | 307,816 | 328,198 |
| Credit Suisse Securities (USA) LLC | 670,000 | 749,286 | 670,000 | 760,327 |
| Bank of America | 27,200 | 28,989 | - | - |
| Nomura | 32,843 | 34,679 | - | - |
| Total | \$ 1,158,945 | \$ 1,282,553 | \$ 977,816 | \$ 1,088,525 |

The following table shows a summary of the Company's repurchase agreements and their terms, excluding accrued interest in the amount of \$3.6 million, at June 30, 2015:

| Year of Maturity | Borrowing Balance | Weighted- Average Coupon | Settlement Date | Maturity Date |
|-------------------------|------------------------------|---|------------------------|--------------------------|
| | (In thousands) | | | |
| 2015 | \$ 24,494 | 0.380% | 5/18/2015 | 8/18/2015 |
| | 27,064 | 0.400% | 6/16/2015 | 9/16/2015 |
| | 32,843 | 0.430% | 5/19/2015 | 8/17/2015 |
| | 59,159 | 0.390% | 5/20/2015 | 8/20/2015 |

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| | | | | | |
|------|----|------------------|---------------|------------|-----------|
| | | 70,685 | 0.390% | 2/21/2015 | 8/21/2015 |
| | | 27,200 | 0.500% | 6/17/2015 | 9/15/2015 |
| 2016 | | 170,000 | 1.500% | 12/6/2012 | 12/8/2016 |
| | | 247,500 | 0.950% | 12/10/2012 | 9/30/2016 |
| 2017 | | 500,000 | 4.780% | 3/2/2007 | 3/2/2017 |
| | \$ | 1,158,945 | 2.570% | | |

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NOTES TO UNAUDITED CONSOLIDATED FINANCIAL STATEMENTS – (Continued)

The following table presents the repurchase liability associated with the repurchase agreement transactions (excluding accrued interest) by maturity. Also, it includes the carrying value and approximate market value of collateral (excluding accrued interest) at June 30, 2015 and December 31, 2014. The information excludes repurchase agreement transactions which were collateralized with cash.

June 30, 2015

Market Value of Underlying Collateral

| | Repurchase Liability | Weighted Average Rate | FNMA and FHLMC Certificates | GNMA Certificates | Total |
|------------------------|-------------------------|-----------------------------|-----------------------------------|----------------------|---------------------|
| (Dollars in thousands) | | | | | |
| Less than 90 days | 241,445 | 0.41% | 257,353 | - | 257,353 |
| Over 90 days | 917,500 | 3.12% | 1,022,195 | 3,005 | 1,025,200 |
| Total | \$ 1,158,945 | 2.57% | \$ 1,279,548 | \$ 3,005 | \$ 1,282,553 |

December 31, 2014

Market Value of Underlying Collateral

| | Repurchase Liability | Weighted Average Rate | FNMA and FHLMC Certificates | GNMA Certificates | Total |
|------------------------|-------------------------|-----------------------------|-----------------------------------|----------------------|---------------------|
| (Dollars in thousands) | | | | | |
| Less than 90 days | \$ 52,816 | 0.39% | \$ 56,066 | \$ - | \$ 56,066 |
| Over 90 days | 925,000 | 2.83% | 1,031,206 | 1,253 | 1,032,459 |
| Total | \$ 977,816 | 2.41% | \$ 1,087,272 | \$ 1,253 | \$ 1,088,525 |

Advances from the Federal Home Loan Bank of New York

Advances are received from the Federal Home Loan Bank of New York (the "FHLB-NY") under an agreement whereby the Company is required to maintain a minimum amount of qualifying collateral with a fair value of at least 110% of the outstanding advances. At June 30, 2015 and December 31, 2014, these advances were secured by mortgage and commercial loans amounting to \$1.1 billion and \$1.2 billion, respectively. Also, at June 30, 2015 and December 31, 2014, the Company had an additional borrowing capacity with the FHLB-NY of \$612 million and \$606.6 million, respectively. At June 30, 2015 and December 31, 2014, the weighted average remaining maturity of FHLB's advances was 7.5 months and 8.8 months, respectively. The original terms of these advances range between one day and seven years, and the FHLB-NY does not have the right to exercise put options at par on any advances outstanding as of June 30, 2015.

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NOTES TO UNAUDITED CONSOLIDATED FINANCIAL STATEMENTS – (Continued)

The following table shows a summary of these advances and their terms, excluding accrued interest in the amount of \$325 thousand, at June 30, 2015:

| Year of Maturity | Borrowing Balance (In thousands) | Weighted- Average Coupon | Settlement Date | Maturity Date |
|------------------|--|--------------------------------|-----------------|------------------|
| 2015 | \$ 25,000 | 0.35% | 6/4/2015 | 7/6/2015 |
| | 50,000 | 0.34% | 6/10/2015 | 7/10/2015 |
| | 100,000 | 0.35% | 6/16/2015 | 7/16/2015 |
| | 25,000 | 0.35% | 6/24/2015 | 7/24/2015 |
| | 25,000 | 0.34% | 6/30/2015 | 7/30/2015 |
| | 38,658 | 0.35% | 6/1/2015 | 7/1/2015 |
| | 263,658 | | | |
| 2017 | 4,384 | 1.24% | 4/3/2012 | 4/3/2017 |
| 2018 | 30,000 | 2.19% | 1/16/2013 | 1/16/2018 |
| | 25,000 | 2.18% | 1/16/2013 | 1/16/2018 |
| | 55,000 | | | |
| 2020 | 10,024 | 2.59% | 7/19/2013 | 7/20/2020 |
| | \$ 333,066 | 0.74% | | |

All of the advances referred to above with maturity dates up to the date of this report were renewed as one-month short-term advances.

Subordinated Capital Notes

Subordinated capital notes amounted to \$102.1 million at June 30, 2015 and \$101.6 million at December 31, 2014.

Under the requirements of Puerto Rico Banking Act, the Bank must establish a redemption fund for the subordinated capital notes by transferring from undivided profits pre-established amounts as follows:

| | | Redemption fund (In thousands) | |
|---------------------------------|----|---|---------------|
| Redemption fund - June 30, 2015 | \$ | | 58,625 |
| 2015 | | | 3,350 |
| 2016 | | | 5,025 |
| | \$ | | 67,000 |

Other borrowings

Other borrowings, presented in the unaudited consolidated statements of financial condition amounted to \$2.1 million and \$4.0 million at June 30, 2015 and December 31, 2014, respectively, which mainly consists of unsecured fixed-rate borrowings.

OFG BANCORP

NOTES TO UNAUDITED CONSOLIDATED FINANCIAL STATEMENTS – (Continued)

NOTE 12 – OFFSETTING OF FINANCIAL ASSETS AND LIABILITIES

The Company's derivatives are subject to agreements which allow a right of set-off with each respective counterparty. In addition, the Company's securities purchased under agreements to resell and securities sold under agreements to repurchase have a right of set-off with the respective counterparty under the supplemental terms of the master repurchase agreements. In an event of default, each party has a right of set-off against the other party for amounts owed in the related agreements and any other amount or obligation owed in respect of any other agreement or transaction between them. Security collateral posted to open and maintain a master netting agreement with a counterparty, in the form of cash and securities, may from time to time be segregated in an account at a third-party custodian pursuant to a an account control agreement.

The following table presents the potential effect of rights of set-off associated with the Company's recognized financial assets and liabilities at June 30, 2015 and December 31, 2014:

| | June 30, 2015 | | | Gross Amounts Not Offset in the Statement of Financial Condition | | |
|-------------|---|---|---|--|--------------------------------|---------------|
| | Gross Amount of Recognized Assets | Gross Amounts Offset in the Statement of Financial Condition | Net Amount of Assets Presented in Statement of Financial Condition (In thousands) | Financial Instruments | Cash Collateral Received | Net Amount |
| Derivatives | \$ 4,376 | \$ - | \$ 4,376 | \$ 2,013 | \$ - | \$ 2,363 |

| | December 31, 2014 | | | Gross Amounts Not Offset in the Statement of Financial Condition | | |
|--|-------------------|---|--|--|--|--|
| | Gross Amount | Gross Amounts Offset in the Statement of | Net amount of Assets Presented in Statement | Cash | | |

| | of Recognized Assets | Financial Condition | of Financial Condition | Financial Instruments | Collateral Received | Net Amount |
|--------------------|-------------------------------------|--------------------------------|-----------------------------------|----------------------------------|--------------------------------|-----------------------|
| Derivatives | \$ 8,107 | \$ - | \$ 8,107 | \$ 2,006 | \$ - | \$ 6,101 |

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NOTES TO UNAUDITED CONSOLIDATED FINANCIAL STATEMENTS – (Continued)

June 30, 2015

Gross Amounts Not Offset in
the Statement of Financial
Condition

| | Gross Amount of Recognized Liabilities | Gross Amounts Offset in the Statement of Financial Condition | Net Amount of Liabilities Presented in Statement of Financial Condition | Gross Amounts Not Offset in the Statement of Financial Condition | | Net Amount |
|--|--|---|---|--|--------------------------------|---------------------|
| | | | | Financial Instruments (In thousands) | Cash Collateral Provided | |
| Derivatives | \$ 10,783 | \$ - | \$ 10,783 | \$ - | \$ 2,980 | \$ 7,803 |
| Securities sold under agreements to repurchase | 1,158,945 | - | 1,158,945 | 1,282,553 | - | (123,608) |
| Total | \$ 1,169,728 | \$ - | \$ 1,169,728 | \$ 1,282,553 | \$ 2,980 | \$ (115,805) |

December 31, 2014

Gross Amounts Not Offset in
the Statement of Financial
Condition

| | Gross Amount of Recognized Liabilities | Gross Amounts Offset in the Statement of Financial Condition | Net Amount of Liabilities Presented in Statement of Financial Condition | Gross Amounts Not Offset in the Statement of Financial Condition | | Net Amount |
|--|--|---|---|--|--------------------------------|--------------------|
| | | | | Financial Instruments (In thousands) | Cash Collateral Provided | |
| Derivatives | \$ 16,698 | \$ - | \$ 16,698 | \$ - | \$ 2,980 | \$ 13,718 |
| Securities sold under agreements to repurchase | 977,816 | - | 977,816 | 1,088,525 | - | (110,709) |
| Total | \$ 994,514 | \$ - | \$ 994,514 | \$ 1,088,525 | \$ 2,980 | \$ (96,991) |

NOTE 13 — RELATED PARTY TRANSACTIONS

The Bank grants loans to its directors, executive officers and to certain related individuals or organizations in the ordinary course of business. These loans are offered at the same terms as loans to unrelated third parties. The activity and balance of these loans for the quarters and the six-month periods ended June 30, 2015 and 2014 were as follows:

| | Quarter Ended June 30, | | Six-Month Period Ended June 30, | |
|---|-------------------------------|------------------|--|------------------|
| | 2015 | 2014 | 2015 | 2014 |
| | (In thousands) | | (In thousands) | |
| Balance at the beginning of period | \$ 27,508 | \$ 19,267 | \$ 27,011 | \$ 18,963 |
| New loans | 3,768 | 13,847 | 7,623 | 13,847 |
| Repayments and sales | 2,042 | (8,963) | (1,316) | (8,659) |
| Balance at the end of period | \$ 33,318 | \$ 24,151 | \$ 33,318 | \$ 24,151 |

OFG BANCORP**NOTES TO UNAUDITED CONSOLIDATED FINANCIAL STATEMENTS – (Continued)****NOTE 14 — INCOME TAXES**

On May 29, 2015 the Governor signed Act No. 72 of 2015. The main purpose of this Act is to increase government collections in order to alleviate the structural deficit. The most relevant provisions of the Act, as applicable to the Company, for taxable years beginning after December 31, 2014, are as follows: (1) establishes a new definition of “large taxpayers,” which require them to file its tax return following a special procedure established by the Secretary of the Treasury, (2) net operating losses carried forward may be deducted up to 70% of the alternative minimum net income for purposes of computing the alternative minimum tax, and (3) net operating losses carried forward may be deducted up to 80% of the net income for purposes of computing the regular corporate income tax.

At June 30, 2015 and December 31, 2014, the Company’s net deferred tax asset amounted to \$138.4 million and \$108.7 million, respectively. In assessing the realizability of the deferred tax asset, management considers whether it is more likely than not that some portion or the entire deferred tax asset will not be realized. The ultimate realization of the deferred tax asset is dependent upon the generation of future taxable income during the periods in which those temporary differences become deductible. Management considers the scheduled reversal of deferred tax liabilities, projected future taxable income, and tax planning strategies in making this assessment. Based upon the level of historical taxable income and projections for future taxable income over the periods in which the deferred tax asset are deductible, management believes it is more likely than not that the Company will realize the deferred tax asset, net of the existing valuation allowances recorded at June 30, 2015 and December 31, 2014. The amount of the deferred tax asset that is considered realizable could be reduced in the near term if estimates of future taxable income during the carry forward period are reduced.

At June 30, 2015 and December 31, 2014, Oriental International Bank Inc. (“OIB”), the Bank’s international banking entity subsidiary, had \$165 thousand and \$186 thousand, respectively, in income tax effect of unrecognized gain on available-for-sale securities included in other comprehensive income. Following the change in OIB’s applicable tax rate from 5% to 0% as a result of a Puerto Rico law adopted in 2011, this remaining tax balance will flow through income as these securities are repaid or sold in future periods. During the quarters ended June 30, 2015 and 2014, \$12 thousand and \$10 thousand, respectively, related to this residual tax effect from OIB was reclassified from accumulated other comprehensive income (loss) into income tax provision. During the period ended June 30, 2015 and 2014, \$22 thousand and \$147 thousand, respectively, related to this residual tax effect from OIB was reclassified from accumulated other comprehensive income (loss) into income tax provision.

The Company classifies unrecognized tax benefits in income taxes payable. These gross unrecognized tax benefits would affect the effective tax rate if realized. The balance of unrecognized tax benefits at June 30, 2015 and December 31, 2014 was \$2.5 million and \$2.6 million, respectively. The Company had accrued \$566 thousand at June 30, 2015 and \$470 thousand at December 31, 2014 for the payment of interest and penalties relating to unrecognized tax benefits. During this quarter \$100 thousand was released based on negotiations with the IRS.

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For the quarter ended June 30, 2015, income tax expense was \$769 thousand compared to \$10.6 million for the same period in 2014. For the six-month period ended June 30, 2015, income tax expense was \$1.7 million compared to \$22.4 million for the same period in 2014.

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NOTES TO UNAUDITED CONSOLIDATED FINANCIAL STATEMENTS – (Continued)

NOTE 15 — REGULATORY CAPITAL REQUIREMENTS

Regulatory Capital Requirements

The Company (on a consolidated basis) and the Bank are subject to various regulatory capital requirements administered by federal and Puerto Rico banking agencies. Failure to meet minimum capital requirements can initiate certain mandatory and possibly additional discretionary actions by regulators that, if undertaken, could have a direct material effect on the Company's financial statements. Under capital adequacy guidelines and the regulatory framework for prompt corrective action, the Company and the Bank must meet specific capital guidelines that involve quantitative measures of their assets, liabilities and certain off-balance sheet items as calculated under regulatory accounting practices. The capital amounts and classification are also subject to qualitative judgments by the regulators about components, risk weightings, and other factors.

Pursuant to the Dodd-Frank Act, federal banking regulators have adopted new capital rules that became effective January 1, 2015 for the Company and the Bank (subject to certain phase-in periods through January 1, 2019) and that replaced their general risk-based capital rules, advanced approaches rule, market risk rule, and leverage rules. Among other matters, the new capital rules: (i) introduce a new capital measure called "Common Equity Tier 1" ("CET1") and related regulatory capital ratio of CET1 to risk-weighted assets; (ii) specify that Tier 1 capital consists of CET1 and "Additional Tier 1 capital" instruments meeting certain revised requirements; (iii) mandate that most deductions/adjustments to regulatory capital measures be made to CET1 and not to the other components of capital; and (iv) expand the scope of the deductions from and adjustments to capital as compared to prior regulations. The new capital rules prescribe a new standardized approach for risk weightings that expand the risk-weighting categories from the current four Basel I-derived categories (0%, 20%, 50% and 100%) to a larger and more risk-sensitive number of categories, depending on the nature of the assets, and resulting in higher risk weights for a variety of asset classes.

Pursuant to the new capital rules, the minimum capital ratios requirements as of January 1, 2015 are as follows:

4.5% CET1 to risk-weighted assets;

6.0% Tier 1 capital (that is, CET1 *plus* Additional Tier 1 capital) to risk-weighted assets;

8.0% Total capital (that is, Tier 1 capital *plus* Tier 2 capital) to risk-weighted assets; and

4.0% Tier 1 capital to average consolidated assets as reported on consolidated financial statements (known as the "leverage ratio").

As of June 30, 2015 and December 31, 2014, the Company and the Bank met all capital adequacy requirements to which they are subject. As of June 30, 2015 and December 31, 2014, the Bank is “well capitalized” under the regulatory framework for prompt corrective action. To be categorized as “well capitalized,” an institution must maintain minimum CET1 risk-based, Tier 1 risk-based, total risk-based, and Tier 1 leverage ratios as set forth in the tables presented below.

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NOTES TO UNAUDITED CONSOLIDATED FINANCIAL STATEMENTS – (Continued)

The Company's and the Bank's actual capital amounts and ratios as of June 30, 2015 and December 31, 2014 are as follows:

| | Actual | | Minimum Capital Requirement | | Minimum to be Well Capitalized | |
|--|------------|--------|-----------------------------|-------|--------------------------------|--------|
| | Amount | Ratio | Amount | Ratio | Amount | Ratio |
| (Dollars in thousands) | | | | | | |
| Company Ratios | | | | | | |
| <u>As of June 30, 2015</u> | | | | | | |
| Total capital to risk-weighted assets | \$ 868,568 | 17.41% | \$ 399,100 | 8.00% | \$ 498,875 | 10.00% |
| Tier 1 capital to risk-weighted assets | \$ 790,936 | 15.85% | \$ 299,325 | 6.00% | \$ 399,100 | 8.00% |
| Common equity tier 1 capital to risk-weighted assets | \$ 611,541 | 12.26% | \$ 224,494 | 4.50% | \$ 324,269 | 6.50% |
| Tier 1 capital to average total assets | \$ 790,936 | 11.05% | \$ 286,262 | 4.00% | \$ 357,827 | 5.00% |
| <u>As of December 31, 2014</u> | | | | | | |
| Total capital to risk-weighted assets | \$ 851,437 | 17.57% | \$ 387,772 | 8.00% | \$ 484,715 | 10.00% |
| Tier 1 capital to risk-weighted assets | \$ 776,525 | 16.02% | \$ 193,886 | 4.00% | \$ 290,829 | 6.00% |
| Tier 1 capital to average total assets | \$ 776,525 | 10.61% | \$ 292,738 | 4.00% | \$ 365,922 | 5.00% |

| | Actual | | Minimum Capital Requirement | | Minimum to be Well Capitalized | |
|--|------------|--------|-----------------------------|-------|--------------------------------|--------|
| | Amount | Ratio | Amount | Ratio | Amount | Ratio |
| (Dollars in thousands) | | | | | | |
| Bank Ratios | | | | | | |
| <u>As of June 30, 2015</u> | | | | | | |
| Total capital to risk-weighted assets | \$ 819,436 | 16.48% | \$ 397,716 | 8.00% | \$ 497,145 | 10.00% |
| Tier 1 capital to risk-weighted assets | \$ 742,098 | 14.93% | \$ 298,287 | 6.00% | \$ 397,716 | 8.00% |
| Common equity tier 1 capital to risk-weighted assets | \$ 742,098 | 14.93% | \$ 223,715 | 4.50% | \$ 323,144 | 6.50% |
| Tier 1 capital to average total assets | \$ 742,098 | 10.44% | \$ 284,228 | 4.00% | \$ 355,285 | 5.00% |
| <u>As of December 31, 2014</u> | | | | | | |
| Total capital to risk-weighted assets | \$ 820,884 | 16.99% | \$ 386,444 | 8.00% | \$ 483,055 | 10.00% |
| Tier 1 capital to risk-weighted assets | \$ 746,177 | 15.45% | \$ 193,222 | 4.00% | \$ 289,833 | 6.00% |
| Tier 1 capital to average total assets | \$ 746,177 | 10.26% | \$ 290,879 | 4.00% | \$ 363,599 | 5.00% |

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NOTES TO UNAUDITED CONSOLIDATED FINANCIAL STATEMENTS – (Continued)

NOTE 16 – STOCKHOLDERS' EQUITY

Additional Paid-in Capital

Additional paid-in capital represents contributed capital in excess of par value of common and preferred stock net of the costs of issuance. As of June 30, 2015 and December 31, 2014 accumulated issuance costs charged against additional paid in capital amounted to \$10.1 million and \$13.6 million for preferred and common stock, respectively.

Legal Surplus

The Puerto Rico Banking Act requires that a minimum of 10% of the Bank's net income or loss for the year be transferred to a reserve fund until such fund (legal surplus) equals the total paid in capital on common and preferred stock. At June 30, 2015 and December 31, 2014, the Bank's legal surplus amounted to \$69.9 million and \$70.5 million, respectively. The amount transferred to the legal surplus account is not available for the payment of dividends to shareholders.

Treasury Stock

Under the Company's current stock repurchase program it is authorized to purchase in the open market up to \$70 million of its outstanding shares of common stock, of which approximately \$12.4 million of authority remains. The shares of common stock repurchased are to be held by the Company as treasury shares. During the quarter ended June 30, 2015 the Company purchased 303,985 shares under this program for a total of \$4.2 million, at an average price of \$13.9 per share. There were no repurchases during the quarter ended June 30, 2014.

The number of shares that may yet be purchased under the \$70 million program is estimated at 1,164,671 and was calculated by dividing the remaining balance of \$12.4 million by \$10.67 (closing price of the Company common stock at June 30, 2015). The Company did not purchase any shares of its common stock during the six-month period ended June 30, 2015, or during the during the six-month period ended June 30, 2014, other than through its publicly announced stock repurchase program.

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The activity in connection with common shares held in treasury by the Company for the six-month periods ended June 30, 2015 and 2014 is set forth below:

| | Six-Month Period Ended June 30, 2015 | | 2014 | |
|---|---|------------------|------------------|------------------|
| | Shares | Dollar Amount | Shares | Dollar Amount |
| | (In thousands, except shares data) | | | |
| Beginning of period | 8,012,254 | \$ 97,070 | 7,030,101 | \$ 80,642 |
| Common shares used upon lapse of restricted stock units | (58,279) | (640) | (30,552) | (323) |
| Common shares repurchased as part of the stock repurchase program | 303,985 | 4,238 | 707,400 | 10,393 |
| | | 100,668 | | |
| End of period | 8,257,960 | \$ | 7,706,949 | \$ 90,712 |

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NOTES TO UNAUDITED CONSOLIDATED FINANCIAL STATEMENTS – (Continued)

NOTE 17 - ACCUMULATED OTHER COMPREHENSIVE INCOME

Accumulated other comprehensive income, net of income tax, as of June 30, 2015 and December 31, 2014 consisted of:

| | June 30, 2015 | December 31, 2014 |
|---|------------------|----------------------|
| | (In thousands) | |
| Unrealized gain on securities available-for-sale which are not other-than-temporarily impaired | \$ 21,562 | \$ 28,743 |
| Income tax effect of unrealized gain on securities available-for-sale | (2,730) | (2,978) |
| Net unrealized gain on securities available-for-sale which are not other-than-temporarily impaired | 18,832 | 25,765 |
| Unrealized loss on cash flow hedges | (6,514) | (8,585) |
| Income tax effect of unrealized loss on cash flow hedges | 1,983 | 2,531 |
| Net unrealized loss on cash flow hedges | (4,531) | (6,054) |
| Accumulated other comprehensive income, net of taxes | \$ 14,301 | \$ 19,711 |

The following table presents changes in accumulated other comprehensive income by component, net of taxes, for the quarters and six-month periods ended June 30, 2015 and 2014:

| | Quarter Ended June 30, | | | | | |
|--|---|--|---|---|--|---|
| | 2015 | | | 2014 | | |
| | Net unrealized gains on securities available-for-sale | Net unrealized loss on cash flow hedges | Accumulated other comprehensive income | Net unrealized gains on securities available-for-sale | Net unrealized loss on cash flow hedges | Accumulated other comprehensive income |
| | (In thousands) | | | | | |
| Beginning balance | \$ 30,214 | \$ (5,890) | \$ 24,324 | \$ 16,035 | \$ (8,013) | \$ 8,022 |
| Other comprehensive income (loss) before reclassifications | (11,523) | (180) | (11,703) | 13,714 | (1,633) | 12,081 |
| Amounts reclassified out of accumulated other comprehensive income | 141 | 1,539 | 1,680 | 10 | 1,642 | 1,652 |
| Other comprehensive income | (11,382) | 1,359 | (10,023) | 13,724 | 9 | 13,733 |
| Ending balance | \$ 18,832 | \$ (4,531) | \$ 14,301 | \$ 29,759 | \$ (8,004) | \$ 21,755 |

| | Six-Month Period Ended June 30, | | | | | |
|--|---|--|---|---|--|---|
| | 2015 | | | 2014 | | |
| | Net unrealized gains on securities available-for-sale | Net unrealized loss on cash flow hedges | Accumulated other comprehensive income | Net unrealized gains on securities available-for-sale | Net unrealized loss on cash flow hedges | Accumulated other comprehensive income |

| | gains on securities available-for-sale | loss on cash flow hedges | other comprehensive income | gains on securities available-for-sale | loss on cash flow hedges | ot compr inc |
|--|--|-----------------------------------|----------------------------------|---|-----------------------------------|--------------------|
| | (In thousands) | | | | | |
| Beginning balance | \$ 25,764 | \$ (6,053) | \$ 19,711 | \$ 11,433 | \$ (8,242) | \$ |
| Other comprehensive income before reclassifications | (7,212) | (1,549) | (8,761) | 18,179 | (3,025) | 1 |
| Amounts reclassified out of accumulated other comprehensive income | 280 | 3,071 | 3,351 | 147 | 3,263 | 1 |
| Other comprehensive income (loss) | (6,932) | 1,522 | (5,410) | 18,326 | 238 | 1 |
| Ending balance | \$ 18,832 | \$ (4,531) | \$ 14,301 | 29,759 | \$ (8,004) | \$ 2 |

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NOTES TO UNAUDITED CONSOLIDATED FINANCIAL STATEMENTS – (Continued)

The following table presents reclassifications out of accumulated other comprehensive income for the quarters and six-month periods ended June 30, 2015 and 2014:

| | Amount reclassified out of accumulated other comprehensive income | | Affected Line Item in Consolidated Statement of Operations |
|--|---|-----------------|--|
| | Quarter Ended June 30, 2015 (In thousands) | 2014 | |
| Cash flow hedges: | | | |
| Interest-rate contracts | \$ 1,614 | \$ 1,642 | Net interest expense |
| Tax effect from increase in capital gains tax rate | (75) | | - Income tax expense |
| Available-for-sale securities: | | | |
| Residual tax effect from OIB's change in applicable tax rate | 12 | 10 | Income tax expense |
| Tax effect from increase in capital gains tax rate | 129 | | - Income tax expense |
| | \$ 1,680 | \$ 1,652 | |

| | Amount reclassified out of accumulated other comprehensive income | | Affected Line Item in Consolidated Statement of Operations |
|--|---|-----------------|--|
| | Six-Month Period Ended June 30, 2015 (In thousands) | 2014 | |
| Cash flow hedges: | | | |
| Interest-rate contracts | \$ 3,220 | \$ 3,263 | Net interest expense |
| Tax effect from increase in capital gains tax rate | (149) | | - Income tax expense |
| Available-for-sale securities: | | | |
| Residual tax effect from OIB's change in applicable tax rate | 22 | 147 | Income tax expense |
| Tax effect from increase in capital gains tax rate | 258 | | - Income tax expense |
| | \$ 3,351 | \$ 3,410 | |

OFG BANCORP

NOTES TO UNAUDITED CONSOLIDATED FINANCIAL STATEMENTS – (Continued)

NOTE 18 – (LOSS) EARNINGS PER COMMON SHARE

The calculation of (loss) earnings per common share for the quarters and six-month periods ended June 30, 2015 and 2014 is as follows:

| | Quarter Ended June 30, 2015 2014 | |
|--|--|------------------|
| | (In thousands except per share data) | |
| Net (loss) income | \$ (3,109) | \$ 21,300 |
| Less: Dividends on preferred stock | | |
| Non-convertible preferred stock (Series A, B, and D) | (1,628) | (1,628) |
| Convertible preferred stock (Series C) | (1,838) | (1,838) |
| (Loss) income available to common shareholders | \$ (6,575) | \$ 17,834 |
| Effect of assumed conversion of the convertible preferred stock | 1,838 | 1,838 |
| (Loss) income available to common shareholders assuming conversion | \$ (4,737) | \$ 19,672 |
| | | |
| Weighted average common shares and share equivalents: | | |
| Average common shares outstanding | 44,505 | 45,000 |
| Effect of dilutive securities: | | |
| Average potential common shares-options | 110 | 200 |
| Average potential common shares-assuming conversion of convertible preferred stock | 7,159 | 7,135 |
| Total weighted average common shares outstanding and equivalents | 51,774 | 52,365 |
| (Loss) earnings per common share - basic | \$ (0.15) | \$ 0.40 |
| (Loss) earnings per common share - diluted | \$ (0.15) | \$ 0.37 |

In computing diluted (loss) earnings per common share, the 84,000 shares of convertible preferred stock, which remain outstanding at June 30, 2015, with a conversion rate, subject to certain conditions, of 86.0355 shares of common stock per share, were included as average potential common shares from the date they were issued and outstanding. Moreover, in computing diluted earnings per common share, the dividends declared during the quarters ended June 30, 2015 and 2014 on the convertible preferred stock were added back as income available to common shareholders.

For the quarters ended June 30, 2015 and 2014, weighted-average stock options with an anti-dilutive effect on (loss) earnings per share not included in the calculation amounted to 566,025 and 364,604, respectively. For the six-month periods ended June 30, 2015 and 2014, weighted-average stock options with an anti-dilutive effect on (loss) earnings

per share not included in the calculation amounted to \$457,467 and \$304,491, respectively.

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NOTES TO UNAUDITED CONSOLIDATED FINANCIAL STATEMENTS – (Continued)

NOTE 19 – GUARANTEES

At June 30, 2015, the unamortized balance of the obligations undertaken in issuing the guarantees under standby letters of credit represented a liability of \$15.0 million (December 31, 2014 - \$33.0 million).

As a result of the BBVAPR Acquisition, the Company assumed a liability for residential mortgage loans sold subject to credit recourse, pursuant to FNMA's residential mortgage loan sales and securitization programs. At June 30, 2015 and December 31, 2014, the unpaid principal balance of residential mortgage loans sold subject to credit recourse was \$45.6 million and \$67.8 million, respectively.

The following table shows the changes in the Company's liability for estimated losses from these credit recourse agreements, included in the unaudited consolidated statements of financial condition during the quarters and six-month periods ended June 30, 2015 and 2014.

| | Quarter Ended June 30, | | Six-Month Period Ended June | |
|---------------------------------------|------------------------|----------|-----------------------------|----------|
| | 2015 | 2014 | 2015 | 2014 |
| | (In thousands) | | | |
| Balance at beginning of period | \$ 487 | \$ 1,549 | \$ 927 | \$ 1,955 |
| Net charge-offs/terminations | (198) | (239) | (638) | (645) |
| Balance at end of period | \$ 289 | \$ 1,310 | \$ 289 | \$ 1,310 |

The estimated losses to be absorbed under the credit recourse arrangements were recorded as a liability when the credit recourse was assumed, and are updated on a quarterly basis. The expected loss, which represents the amount expected to be lost on a given loan, considers the probability of default and loss severity. The probability of default represents the probability that a loan in good standing would become 120 days delinquent, in which case the Company is obligated to repurchase the loan. At June 30, 2015, \$29.1 million or 64% of the recourse obligation will be extinguished before the end of 2015.

If a borrower defaults, pursuant to the credit recourse provided, the Company is required to repurchase the loan or reimburse the third party investor for the incurred loss. The maximum potential amount of future payments that the Company would be required to make under the recourse arrangements is equivalent to the total outstanding balance of the residential mortgage loans serviced with recourse and interest, if applicable. During the quarter and six-month period ended June 30, 2015 the Company repurchased approximately \$1.2 million and \$3.4 million, respectively, of unpaid principal balance in mortgage loans subject to the credit recourse provisions. During the quarter and six-month period ended June 30, 2014 the Company repurchased approximately \$2.1 million and \$3.7 million, respectively, of unpaid principal balance in mortgage loans subject to the credit recourse provisions. If a borrower defaults, the Company has rights to the underlying collateral securing the mortgage loan. The Company suffers losses on these

mortgage loans when the proceeds from a foreclosure sale of the collateral property are less than the outstanding principal balance of the loan, any uncollected interest advanced, and the costs of holding and disposing the related property. At June 30, 2015, the Company's liability for estimated credit losses related to loans sold with credit recourse amounted to \$289 thousand (December 31, 2014— \$927 thousand).

OFG BANCORP**NOTES TO UNAUDITED CONSOLIDATED FINANCIAL STATEMENTS – (Continued)**

When the Company sells or securitizes mortgage loans, it generally makes customary representations and warranties regarding the characteristics of the loans sold. The Company's mortgage operations division groups conforming mortgage loans into pools which are exchanged for FNMA and GNMA mortgage-backed securities, which are generally sold to private investors, or are sold directly to FNMA or other private investors for cash. As required under such mortgage backed securities programs, quality review procedures are performed by the Company to ensure that asset guideline qualifications are met. To the extent the loans do not meet specified characteristics, the Company may be required to repurchase such loans or indemnify for losses and bear any subsequent loss related to the loans. At June 30, 2015, under the Company's representation and warranty arrangements, excluding mortgage loans subject to credit recourse provisions referred to above, approximated \$11.7 million in unpaid principal balance (December 31, 2014 – \$10.7 million). A substantial amount of these loans are reinstated to performing status or have mortgage insurance, and thus the ultimate losses on the loans are not deemed significant.

During the quarter and six-month period ended June 30, 2015, the Company recognized \$476 thousand and \$583 thousand in losses from the repurchase of residential mortgage loans sold subject to credit recourse, and \$742 thousand and \$1.5 million in losses from the repurchase of residential mortgage loans as a result of breaches of the customary representations and warranties. During the quarter and six-month period ended June 30, 2014, the Company recognized \$95 thousand and \$145 thousand, respectively, in losses from the repurchase of residential mortgage loans sold subject to credit recourse, and \$494 thousand and \$929 thousand in losses from the repurchase of residential mortgage loans as a result of breaches of the customary representations and warranties.

Servicing agreements relating to the mortgage-backed securities programs of FNMA and GNMA, and to mortgage loans sold or serviced to certain other investors, including the Federal Home Loan Mortgage Corporation ("FHLMC"), require the Company to advance funds to make scheduled payments of principal, interest, taxes and insurance, if such payments have not been received from the borrowers. At June 30, 2015, the Company serviced \$580 million in mortgage loans for third-parties. The Company generally recovers funds advanced pursuant to these arrangements from the mortgage owner, from liquidation proceeds when the mortgage loan is foreclosed or, in the case of FHA/VA loans, under the applicable FHA and VA insurance and guarantees programs. However, in the meantime, the Company must absorb the cost of the funds it advances during the time the advance is outstanding. The Company must also bear the costs of attempting to collect on delinquent and defaulted mortgage loans. In addition, if a defaulted loan is not cured, the mortgage loan would be canceled as part of the foreclosure proceedings and the Company would not receive any future servicing income with respect to that loan. At June 30, 2015, the outstanding balance of funds advanced by the Company under such mortgage loan servicing agreements was approximately \$468 thousand (December 31, 2014 - \$391 thousand). To the extent the mortgage loans underlying the Company's servicing portfolio experience increased delinquencies, the Company would be required to dedicate additional cash resources to comply with its obligation to advance funds as well as incur additional administrative costs related to increases in collection efforts.

OFG BANCORP**NOTES TO UNAUDITED CONSOLIDATED FINANCIAL STATEMENTS – (Continued)****NOTE 20— COMMITMENTS AND CONTINGENCIES***Loan Commitments*

In the normal course of business, the Company becomes a party to credit-related financial instruments with off-balance-sheet risk to meet the financing needs of its customers. These financial instruments include commitments to extend credit, standby and commercial letters of credit, and financial guarantees. Those instruments involve, to varying degrees, elements of credit and interest rate risk in excess of the amounts recognized in the consolidated statements of financial condition. The contract or notional amount of those instruments reflects the extent of the Company's involvement in particular types of financial instruments.

The Company's exposure to credit losses in the event of nonperformance by the counterparty to the financial instrument for commitments to extend credit, including commitments under credit card arrangements, and commercial letters of credit is represented by the contractual notional amounts of those instruments, which do not necessarily represent the amounts potentially subject to risk. In addition, the measurement of the risks associated with these instruments is meaningful only when all related and offsetting transactions are identified. The Company uses the same credit policies in making commitments and conditional obligations as it does for on-balance-sheet instruments.

Credit-related financial instruments at June 30, 2015 and December 31, 2014 were as follows:

| | June 30, 2015 | December 31, 2014 |
|------------------------------|--------------------------|------------------------------|
| | (In thousands) | |
| Commitments to extend credit | \$ 492,455 | \$ 493,248 |
| Commercial letters of credit | 1,447 | 885 |

Commitments to extend credit represent agreements to lend to a customer as long as there is no violation of any condition established in the contract. Commitments generally have fixed expiration dates or other termination clauses and may require payment of a fee. The Company evaluates each customer's creditworthiness on a case-by-case basis. The amount of collateral obtained, if it is deemed necessary by the Company upon the extension of credit, is based on management's credit evaluation of the counterparty.

At June 30, 2015 and December 31, 2014, commitments to extend credit consisted mainly of undisbursed available amounts on commercial lines of credit, construction loans, and revolving credit card arrangements. Since many of the unused commitments are expected to expire unused or be only partially used, the total amount of these unused commitments does not necessarily represent future cash requirements. These lines of credit had a reserve of \$647 thousand at June 30, 2015 and \$621 thousand at December 31, 2014.

Commercial letters of credit are issued or confirmed to guarantee payment of customers' payables or receivables in short-term international trade transactions. Generally, drafts will be drawn when the underlying transaction is consummated as intended. However, the short-term nature of this instrument serves to mitigate the risk associated with these contracts.

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NOTES TO UNAUDITED CONSOLIDATED FINANCIAL STATEMENTS – (Continued)

The summary of instruments that are considered financial guarantees in accordance with the authoritative guidance related to guarantor’s accounting and disclosure requirements for guarantees, including indirect guarantees of indebtedness of others, at June 30, 2015 and December 31, 2014, is as follows:

| | June 30, 2015 | December 31, 2014 |
|--|--------------------------|------------------------------|
| | (In thousands) | |
| Standby letters of credit and financial guarantees | \$ 15,016 | \$ 32,970 |
| Loans sold with recourse | 45,565 | 67,803 |
| Commitments to sell or securitize mortgage loans | 18,853 | 10,207 |

Standby letters of credit and financial guarantees are written conditional commitments issued by the Company to guarantee the payment and/or performance of a customer to a third party (“beneficiary”). If the customer fails to comply with the agreement, the beneficiary may draw on the standby letter of credit or financial guarantee as a remedy. The amount of credit risk involved in issuing letters of credit in the event of nonperformance is the face amount of the letter of credit or financial guarantee. These guarantees are primarily issued to support public and private borrowing arrangements, including commercial paper, bond financing, and similar transactions. The amount of collateral obtained, if it is deemed necessary by the Company upon extension of credit, is based on management’s credit evaluation of the customer.

Lease Commitments

The Company has entered into various operating lease agreements for branch facilities and administrative offices. Rent expense for the quarters ended June 30, 2015 and 2014, amounted to \$2.3 million and \$2.4 million, respectively. For the six-month periods ended June 30, 2015 and 2014, rent expense amounted to \$4.7 million and \$4.9 million, respectively, and is included in the “occupancy and equipment” caption in the unaudited consolidated statements of operations. Future rental commitments under leases in effect at June 30, 2015, exclusive of taxes, insurance, and maintenance expenses payable by the Company, are summarized as follows:

| <u>Year Ending December 31,</u> | Minimum Rent (In thousands) | |
|--|--|---------------|
| 2015 | \$ | 4,059 |
| 2016 | | 7,794 |
| 2017 | | 7,141 |
| 2018 | | 6,050 |
| 2019 | | 5,887 |
| Thereafter | | 17,064 |
| | \$ | 47,995 |

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NOTES TO UNAUDITED CONSOLIDATED FINANCIAL STATEMENTS – (Continued)

Contingencies

The Company and its subsidiaries are defendants in a number of legal proceedings incidental to their business. In the ordinary course of business, the Company and its subsidiaries are also subject to governmental and regulatory examinations. Certain subsidiaries of the Company, including the Bank (and its subsidiary OIB), Oriental Financial Services, and Oriental Insurance, are subject to regulation by various U.S., Puerto Rico and other regulators.

The Company seeks to resolve all litigation and regulatory matters in the manner management believes is in the best interests of the Company and its shareholders, and contests allegations of liability or wrongdoing and, where applicable, the amount of damages or scope of any penalties or other relief sought as appropriate in each pending matter.

Subject to the accounting and disclosure framework under the provisions of ASC 450, it is the opinion of the Company's management, based on current knowledge and after taking into account its current legal accruals, that the eventual outcome of all matters would not be likely to have a material adverse effect on the consolidated statements of financial condition of the Company. Nonetheless, given the substantial or indeterminate amounts sought in certain of these matters, and the inherent unpredictability of such matters, an adverse outcome in certain of these matters could, from time to time, have a material adverse effect on the Company's consolidated results of operations or cash flows in particular quarterly or annual periods. The Company has evaluated all litigation and regulatory matters where the likelihood of a potential loss is deemed reasonably possible. The Company has determined that the estimate of the reasonably possible loss is not significant.

NOTE 21 - FAIR VALUE OF FINANCIAL INSTRUMENTS

The Company follows the fair value measurement framework under GAAP.

Fair Value Measurement

The fair value measurement framework defines fair value as the exchange price that would be received for an asset or paid to transfer a liability (an exit price) in the principal or most advantageous market for the asset or liability in an orderly transaction between market participants on the measurement date. This framework also establishes a fair value hierarchy which requires an entity to maximize the use of observable inputs and minimize the use of unobservable inputs when measuring fair value.

Money market investments

The fair value of money market investments is based on the carrying amounts reflected in the consolidated statements of financial condition as these are reasonable estimates of fair value given the short-term nature of the instruments.

Investment securities

The fair value of investment securities is based on quoted market prices, when available, or market prices provided by recognized broker-dealers. Such securities are classified as level 1 or level 2 depending on the basis for determining fair value. If listed prices or quotes are not available, fair value is based upon externally developed models that use both observable and unobservable inputs depending on the market activity of the instrument, and such securities are classified as level 3. At June 30, 2015 and December 31, 2014, the Company did not have investment securities classified as Level 3.

OFG BANCORP

NOTES TO UNAUDITED CONSOLIDATED FINANCIAL STATEMENTS – (Continued)

Derivative instruments

The fair value of the interest rate swaps is largely a function of the financial market's expectations regarding the future direction of interest rates. Accordingly, current market values are not necessarily indicative of the future impact of derivative instruments on earnings. This will depend, for the most part, on the shape of the yield curve, the level of interest rates, as well as the expectations for rates in the future. The fair value of most of these derivative instruments is based on observable market parameters, which include discounting the instruments' cash flows using the U.S. dollar LIBOR-based discount rates, and also applying yield curves that account for the industry sector and the credit rating of the counterparty and/or the Company.

Certain other derivative instruments with limited market activity are valued using externally developed models that consider unobservable market parameters. Based on their valuation methodology, derivative instruments are classified as Level 2 or Level 3. The Company has offered its customers certificates of deposit with an option tied to the performance of the S&P Index and uses equity indexed option agreements with major broker-dealers to manage its exposure to changes in this index. Their fair value is obtained through the use of an external based valuation that was thoroughly evaluated and adopted by management as its measurement tool for these options. The payoff of these options is linked to the average value of the S&P Index on a specific set of dates during the life of the option. The methodology uses an average rate option or a cash-settled option whose payoff is based on the difference between the expected average value of the S&P Index during the remaining life of the option and the strike price at inception. The assumptions, which are uncertain and require a degree of judgment, include primarily S&P Index volatility, forward interest rate projections, estimated index dividend payout, and leverage.

Servicing assets

Servicing assets do not trade in an active market with readily observable prices. Servicing assets are priced using a discounted cash flow model. The valuation model considers servicing fees, portfolio characteristics, prepayment assumptions, delinquency rates, late charges, other ancillary revenues, cost to service and other economic factors. Due to the unobservable nature of certain valuation inputs, the servicing rights are classified as Level 3.

Impaired Loans.

Impaired loans are carried at the present value of expected future cash flows using the loan's existing rate in a discounted cash flow calculation, or the fair value of the collateral if the loan is collateral-dependent. Expected cash

flows are based on internal inputs reflecting expected default rates on contractual cash flows. This method of estimating fair value does not incorporate the exit-price concept of fair value described in Accounting Standards Codification (“ASC”) 820-10 and would generally result in a higher value than the exit-price approach. For loans measured using the estimated fair value of collateral less costs to sell, fair value is generally determined based on the fair value of the collateral, which is derived from appraisals that take into consideration prices in observed transactions involving similar assets in similar locations, in accordance with the provisions of ASC 310-10-35 less disposition costs. Currently, the associated loans considered impaired are classified as Level 3.

Foreclosed real estate

Foreclosed real estate includes real estate properties securing residential mortgage and commercial loans. The fair value of foreclosed real estate may be determined using an external appraisal, broker price option or an internal valuation. These foreclosed assets are classified as Level 3 given certain internal adjustments that may be made to external appraisals.

Other repossessed assets

Other repossessed assets include repossessed automobile loans and leases. The fair value of the repossessed automobiles may be determined using internal valuation and an external appraisal. These repossessed assets are classified as Level 3 given certain internal adjustments that may be made to external appraisals.

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NOTES TO UNAUDITED CONSOLIDATED FINANCIAL STATEMENTS – (Continued)

Assets and liabilities measured at fair value on a recurring and non-recurring basis, are summarized below:

| | June 30, 2015 | | | | Total |
|--|--------------------------------|---------------------|-------------------|---------------------|--------------|
| | Fair Value Measurements | | | | |
| | Level 1 | Level 2 | Level 3 | | |
| | (In thousands) | | | | |
| Recurring fair value measurements: | | | | | |
| Investment securities available-for-sale | \$ - | \$ 1,044,319 | \$ - | \$ 1,044,319 | |
| Money market investments | 5,795 | - | - | 5,795 | |
| Derivative assets | - | 2,238 | 2,138 | 4,376 | |
| Servicing assets | - | - | 5,791 | 5,791 | |
| Derivative liabilities | - | (8,739) | (2,044) | (10,783) | |
| | \$ 5,795 | \$ 1,037,818 | \$ 5,885 | \$ 1,049,498 | |
| Non-recurring fair value measurements: | | | | | |
| Impaired commercial loans | \$ - | \$ - | \$ 243,401 | \$ 243,401 | |
| Foreclosed real estate | - | - | 81,333 | 81,333 | |
| Other repossessed assets | - | - | 14,661 | 14,661 | |
| | \$ - | \$ - | \$ 339,395 | \$ 339,395 | |

| | December 31, 2014 | | | | Total |
|--|--------------------------------|---------------------|-------------------|---------------------|--------------|
| | Fair Value Measurements | | | | |
| | Level 1 | Level 2 | Level 3 | | |
| | (In thousands) | | | | |
| Recurring fair value measurements: | | | | | |
| Investment securities available-for-sale | \$ - | \$ 1,216,538 | \$ - | \$ 1,216,538 | |
| Money market investments | 4,675 | - | - | 4,675 | |
| Derivative assets | - | 2,552 | 5,555 | 8,107 | |
| Servicing assets | - | - | 13,992 | 13,992 | |
| Derivative liabilities | - | (11,221) | (5,477) | (16,698) | |
| | \$ 4,675 | \$ 1,207,869 | \$ 14,070 | \$ 1,226,614 | |
| Non-recurring fair value measurements: | | | | | |
| Impaired commercial loans | \$ - | \$ - | \$ 236,942 | \$ 236,942 | |
| Foreclosed real estate | - | - | 95,661 | 95,661 | |
| Other repossessed assets | - | - | 21,800 | 21,800 | |
| | \$ - | \$ - | \$ 354,403 | \$ 354,403 | |

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NOTES TO UNAUDITED CONSOLIDATED FINANCIAL STATEMENTS – (Continued)

The table below presents a reconciliation of all assets and liabilities measured at fair value on a recurring basis using significant unobservable inputs (Level 3) for the quarters and six-month periods ended June 30, 2015 and 2014:

| Level 3 Instruments Only | Quarter Ended June 30, 2015 | | | |
|---|--|---------------------|---|-----------------|
| | Derivative asset (S&P Purchased Options) | Servicing assets | Derivative liability (S&P Embedded Options) | Total |
| Balance at beginning of period | \$ 3,734 | \$ 12,164 | \$ (3,617) | \$ 12,281 |
| (Losses) gains included in earnings | (1,596) | - | 1,517 | (79) |
| Sale of mortgage servicing rights held-for-sale | - | (6,985) | - | (6,985) |
| Changes due to payments on loans | - | (313) | - | (313) |
| New instruments acquired | - | 1,529 | - | 1,529 |
| Changes in fair value related to price of MSR's held for sale | - | (835) | - | (835) |
| Amortization | - | - | 56 | 56 |
| Changes in fair value of servicing assets | - | 231 | - | 231 |
| Balance at end of period | \$ 2,138 | \$ 5,791 | \$ (2,044) | \$ 5,885 |

| Level 3 Instruments Only | Six-Month Period Ended June 30, 2015 | | | |
|---|--|---------------------|---|-----------------|
| | Derivative asset (S&P Purchased Options) | Servicing assets | Derivative liability (S&P Embedded Options) | Total |
| Balance at beginning of period | \$ 5,555 | \$ 13,992 | \$ (5,477) | \$ 14,070 |
| (Losses) gains included in earnings | (3,417) | - | 3,299 | (118) |
| Sale of mortgage servicing rights held-for-sale | - | (6,985) | - | (6,985) |
| Changes due to payments on loans | - | (732) | - | (732) |
| New instruments acquired | - | 2,060 | - | 2,060 |
| Amortization | - | - | 134 | 134 |
| Changes in fair value related to price of MSR's held for sale | - | (2,716) | - | (2,716) |
| Changes in fair value of servicing assets | - | 172 | - | 172 |
| Balance at end of period | \$ 2,138 | \$ 5,791 | \$ (2,044) | \$ 5,885 |

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NOTES TO UNAUDITED CONSOLIDATED FINANCIAL STATEMENTS – (Continued)

| Level 3 Instruments Only | Quarter Ended June 30, 2014 | | | | | Total |
|--|--|--|------------------|---|-----------|-------|
| | Other debt securities available-for-sale | Derivative asset (S&P Purchased Options) | Servicing assets | Derivative liability (S&P Embedded Options) | | |
| Balance at beginning of period | \$ 20,053 | \$ 12,555 | \$ 13,970 | \$ (12,120) | \$ 34,458 | |
| (Losses) gains included in earnings | - | (5,975) | - | 5,591 | (384) | |
| Changes in fair value of investment securities available for sale included | | | | | | |
| in other comprehensive income | (53) | - | - | - | (53) | |
| New instruments acquired | - | - | 490 | - | 490 | |
| Principal repayments | (20,000) | - | (271) | - | (20,271) | |
| Amortization | - | - | - | 161 | 161 | |
| Changes in fair value of servicing assets | - | - | (534) | - | (534) | |
| Balance at end of period | \$ - | \$ 6,580 | \$ 13,655 | \$ (6,368) | \$ 13,867 | |

| Level 3 Instruments Only | Six-Month Period Ended June 30, 2014 | | | | | Total |
|--|--|--|------------------|---|-----------|-------|
| | Other debt securities available-for-sale | Derivative asset (S&P Purchased Options) | Servicing assets | Derivative liability (S&P Embedded Options) | | |
| Balance at beginning of period | \$ 19,680 | \$ 16,430 | \$ 13,801 | \$ (15,736) | \$ 34,175 | |
| Gains (losses) included in earnings | - | (9,850) | - | 8,964 | (886) | |
| Changes in fair value of investment securities available for sale included | | | | | | |
| in other comprehensive income | 320 | - | - | - | 320 | |
| New instruments acquired | - | - | 1,053 | - | 1,053 | |
| Principal repayments | (20,000) | - | (465) | - | (20,465) | |
| Amortization | - | - | - | 404 | 404 | |
| Changes in fair value of servicing assets | - | - | (734) | - | (734) | |
| Balance at end of period | \$ - | \$ 6,580 | \$ 13,655 | \$ (6,368) | \$ 13,867 | |

During the quarters and six-month periods ended June 30, 2015 and 2014, there were purchases and sales of assets and liabilities measured at fair value on a recurring basis. There were no transfers into and out of Level 1 and Level 2 fair value measurements during such periods.

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NOTES TO UNAUDITED CONSOLIDATED FINANCIAL STATEMENTS – (Continued)

The table below presents quantitative information for all assets and liabilities measured at fair value on a recurring and non-recurring basis using significant unobservable inputs (Level 3) at June 30, 2015:

| | | | June 30, 2015 | |
|--------------------------------|------------------------------|------------------------|--|-----------------------------------|
| | Fair Value (In thousands) | Valuation Technique | Unobservable Input | Range |
| Derivative assets (S&P | | | | |
| Purchased Options) | \$ 2,138 | Option pricing model | Implied option volatility Counterparty credit risk | 30.23%- 38.69% |
| | | | (based on 5-year credit default swap ("CDS") spread) | 72.89%- 72.89% |
| Servicing assets | \$ 5,791 | Cash flow valuation | Constant prepayment rate Discount rate | 4.10% - 10.22% 10.00% - 12.00% |
| Derivative liability (S&P | | | | |
| Embedded Options) | \$ (2,044) | Option pricing model | Implied option volatility Counterparty credit risk (based on 5-year CDS spread) | 30.23%- 38.69% 72.89%- 72.89% |
| Collateral dependant | | Fair value of property | | |
| impaired loans | \$ 40,893 | or collateral | Appraised value less disposition costs | 20.20% - 27.20% |
| Puerto Rico Electric Power | | | | |
| Authority line of credit | \$ 173,565 | Cash flow valuation | Discount rate | 7.25% |
| Other non-collateral dependant | 4,949 | Cash flow valuation | Discount rate | 4.25% - 9.25% |

impaired loans

| | | | | |
|--------------------------------|-----------|---------------------------|--|-----------------|
| | | Fair value of property | | |
| Foreclosed real estate | \$ 81,333 | or collateral | Appraised value less disposition costs | 20.20% - 27.20% |
| | | Fair value of property | | |
| Other repossessed assets | \$ 14,661 | or collateral | Appraised value less disposition costs | 20.20% - 27.20% |

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NOTES TO UNAUDITED CONSOLIDATED FINANCIAL STATEMENTS – (Continued)

Information about Sensitivity to Changes in Significant Unobservable Inputs

Other debt securities – The significant unobservable inputs used in the fair value measurement of one of the Company’s other debt securities are indicative comparable pricing, option adjusted spread (“OAS”), yield to maturity, and spread to maturity. Significant changes in any of those inputs in isolation would result in a significantly different fair value measurement. Generally, a change in the assumption used for indicative comparable pricing is accompanied by a directionally opposite change in the assumption used for OAS and a directionally, although not equally proportional, opposite change in the assumptions used for yield to maturity and spread to maturity.

Derivative asset (S&P Purchased Options) – The significant unobservable inputs used in the fair value measurement of the Company’s derivative assets related to S&P purchased options are implied option volatility and counterparty credit risk. Significant changes in any of those inputs in isolation would result in a significantly different fair value measurement. Generally, a change in the assumption used for implied option volatility is not necessarily accompanied by directionally similar or opposite changes in the assumption used for counterparty credit risk.

Servicing assets – The significant unobservable inputs used in the fair value measurement of the Company’s servicing assets are constant prepayment rates and discount rates. Changes in one factor may result in changes in another (for example, increases in market interest rates may result in lower prepayments), which may magnify or offset the sensitivities. Mortgage banking activities, a component of total banking and financial service revenue in the consolidated statements of operations, include the changes from period to period in the fair value of the mortgage loan servicing rights, which may result from changes in the valuation model inputs or assumptions (principally reflecting changes in discount rates and prepayment speed assumptions) and other changes, including changes due to collection/realization of expected cash flows.

Derivative liability (S&P Embedded Options) – The significant unobservable inputs used in the fair value measurement of the Company’s derivative liability related to S&P purchased options are implied option volatility and counterparty credit risk. Significant changes in any of those inputs in isolation would result in a significantly different fair value measurement. Generally, a change in the assumption used for implied option volatility is not necessarily accompanied by directionally similar or opposite changes in the assumption used for counterparty credit risk.

Fair Value of Financial Instruments

The information about the estimated fair value of financial instruments required by GAAP is presented hereunder. The aggregate fair value amounts presented do not necessarily represent management’s estimate of the underlying value of the Company.

The estimated fair value is subjective in nature, involves uncertainties and matters of significant judgment and, therefore, cannot be determined with precision. Changes in assumptions could affect these fair value estimates. The fair value estimates do not take into consideration the value of future business and the value of assets and liabilities

that are not financial instruments. Other significant tangible and intangible assets that are not considered financial instruments are the value of long-term customer relationships of retail deposits, and premises and equipment.

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NOTES TO UNAUDITED CONSOLIDATED FINANCIAL STATEMENTS – (Continued)

The estimated fair value and carrying value of the Company's financial instruments at June 30, 2015 and December 31, 2014 is as follows:

| | June 30, 2015 | | December 31, 2014 | |
|--|------------------|-------------------|----------------------|-------------------|
| | Fair Value | Carrying Value | Fair Value | Carrying Value |
| | (In thousands) | | | |
| Level 1 | | | | |
| Financial Assets: | | | | |
| Cash and cash equivalents | \$ 553,535 | \$ 553,535 | \$ 573,427 | \$ 573,427 |
| Restricted cash | 6,086 | 6,086 | 8,407 | 8,407 |
| Level 2 | | | | |
| Financial Assets: | | | | |
| Trading securities | 786 | 786 | 1,594 | 1,594 |
| Investment securities available-for-sale | 1,044,319 | 1,044,319 | 1,216,538 | 1,216,538 |
| Investment securities held-to-maturity | 547,776 | 550,553 | 164,154 | 162,752 |
| Federal Home Loan Bank (FHLB) stock | 20,826 | 20,826 | 21,169 | 21,169 |
| Other investments | 3 | 3 | 3 | 3 |
| Derivative assets | 2,238 | 2,238 | 2,552 | 2,552 |
| Financial Liabilities: | | | | |
| Derivative liabilities | 8,739 | 8,739 | 11,221 | 11,221 |
| Level 3 | | | | |
| Financial Assets: | | | | |
| Total loans (including loans held-for-sale) | | | | |
| Non-covered loans, net | 4,733,607 | 4,417,433 | 4,563,701 | 4,527,735 |
| Covered loans, net | 253,902 | 222,034 | 345,660 | 298,911 |
| Derivative assets | 2,138 | 2,138 | 5,555 | 5,555 |
| FDIC indemnification asset | 12,746 | 22,704 | 75,969 | 97,378 |
| Accrued interest receivable | 19,254 | 19,254 | 21,345 | 21,345 |
| Servicing assets | 5,791 | 5,791 | 13,992 | 13,992 |
| Financial Liabilities: | | | | |
| Deposits | 4,737,965 | 4,749,684 | 4,893,247 | 4,924,406 |
| Securities sold under agreements to repurchase | 1,193,574 | 1,161,136 | 1,020,621 | 980,087 |
| Advances from FHLB | 338,033 | 333,391 | 339,172 | 334,331 |
| Other borrowings | 1,883 | 2,090 | 3,979 | 4,004 |
| Subordinated capital notes | 91,996 | 102,109 | 104,288 | 101,584 |
| Accrued expenses and other liabilities | 113,537 | 113,537 | 133,290 | 133,290 |
| Derivative liabilities | 2,044 | 2,044 | 5,477 | 5,477 |

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NOTES TO UNAUDITED CONSOLIDATED FINANCIAL STATEMENTS – (Continued)

The following methods and assumptions were used to estimate the fair values of significant financial instruments at June 30, 2015 and December 31, 2014:

- Cash and cash equivalents (including money market investments and time deposits with other banks), restricted cash, accrued interest receivable, and accrued expenses and other liabilities have been valued at the carrying amounts reflected in the consolidated statements of financial condition as these are reasonable estimates of fair value given the short-term nature of the instruments.
- Investments in FHLB-NY stock are valued at their redemption value.
- The fair value of investment securities, including trading securities and other investments, is based on quoted market prices, when available, or market prices provided by recognized broker-dealers. If listed prices or quotes are not available, fair value is based upon externally developed models that use both observable and unobservable inputs depending on the market activity of the instrument.
- The fair value of the FDIC indemnification asset represents the present value of the net estimated cash payments expected to be received from the FDIC for future losses on covered assets based on the credit assumptions on estimated cash flows for each covered asset pool and the loss sharing percentages. The ultimate collectability of the FDIC indemnification asset is dependent upon the performance of the underlying covered loans, the passage of time and claims paid by the FDIC which are impacted by the Bank's adherence to certain guidelines established by the FDIC.
- The fair value of servicing asset is estimated by using a cash flow valuation model which calculates the present value of estimated future net servicing cash flows, taking into consideration actual and expected loan prepayment rates, discount rates, servicing costs, and other economic factors, which are determined based on current market conditions.
- The fair values of the derivative instruments are provided by valuation experts and counterparties. Certain derivatives with limited market activity are valued using externally developed models that consider unobservable market parameters. The Company has offered its customers certificates of deposit with an option tied to the performance of the S&P Index, and uses equity indexed option agreements with major broker-dealers to manage its exposure to changes in this index. Their fair value is obtained through the use of an external based valuation that was thoroughly evaluated and adopted by management as its measurement tool for these options. The payoff of these options is linked to the average value of the S&P Index on a specific set of dates during the life of the option. The methodology uses an average rate option or a cash-settled option whose payoff is based on the difference between the

expected average value of the S&P Index during the remaining life of the option and the strike price at inception. The assumptions, which are uncertain and require a degree of judgment, include primarily S&P Index volatility, forward interest rate projections, estimated index dividend payout, and leverage.

- Fair value of derivative liabilities, which include interest rate swaps and forward-settlement swaps, are based on the net discounted value of the contractual projected cash flows of both the pay-fixed receive-variable legs of the contracts. The projected cash flows are based on the forward yield curve, and discounted using current estimated market rates.
- The fair value of the covered and non-covered loan portfolio (including loans held-for-sale) is estimated by segregating by type, such as mortgage, commercial, consumer, auto and leasing. Each loan segment is further segmented into fixed and adjustable interest rates and by performing and non-performing categories. The fair value of performing loans is calculated by discounting contractual cash flows, adjusted for prepayment estimates (voluntary and involuntary), if any, using estimated current market discount rates that reflect the credit and interest rate risk inherent in the loan. This fair value is not currently an indication of an exit price as that type of assumption could result in a different fair value estimate. Non-performing loans have been valued at the carrying amounts.

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NOTES TO UNAUDITED CONSOLIDATED FINANCIAL STATEMENTS – (Continued)

- The fair value of demand deposits and savings accounts is the amount payable on demand at the reporting date. The fair value of fixed-maturity certificates of deposit is based on the discounted value of the contractual cash flows, using estimated current market discount rates for deposits of similar remaining maturities.
- The fair value of long-term borrowings, which include securities sold under agreements to repurchase, advances from FHLB-NY, other borrowings, and subordinated capital notes, is based on the discounted value of the contractual cash flows using current estimated market discount rates for borrowings with similar terms, remaining maturities and put dates.

NOTE 22 – BUSINESS SEGMENTS

The Company segregates its businesses into the following major reportable segments of business: Banking, Wealth Management, and Treasury. Management established the reportable segments based on the internal reporting used to evaluate performance and to assess where to allocate resources. Other factors such as the Company's organization, nature of its products, distribution channels and economic characteristics of the products were also considered in the determination of the reportable segments. The Company measures the performance of these reportable segments based on pre-established goals of different financial parameters such as net income, net interest income, loan production, and fees generated. The Company's methodology for allocating non-interest expenses among segments is based on several factors such as revenue, employee headcount, occupied space, dedicated services or time, among others. These factors are reviewed on a periodical basis and may change if the conditions warrant.

Banking includes the Bank's branches and traditional banking products such as deposits and commercial, consumer and mortgage loans. Mortgage banking activities are carried out by the Bank's mortgage banking division, whose principal activity is to originate mortgage loans for the Company's own portfolio. As part of its mortgage banking activities, the Company may sell loans directly into the secondary market or securitize conforming loans into mortgage-backed securities.

Wealth Management is comprised of the Bank's trust division, Oriental Financial Services, Oriental Insurance, and OPC. The core operations of this segment are financial planning, money management and investment banking, brokerage services, insurance sales activity, corporate and individual trust and retirement services, as well as retirement plan administration services.

The Treasury segment encompasses all of the Company's asset/liability management activities, such as purchases and sales of investment securities, interest rate risk management, derivatives, and borrowings. Intersegment sales and transfers, if any, are accounted for as if the sales or transfers were to third parties, that is, at current market prices.

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NOTES TO UNAUDITED CONSOLIDATED FINANCIAL STATEMENTS – (Continued)

Following are the results of operations and the selected financial information by operating segment for the quarters and six-month periods ended June 30, 2015 and 2014:

| | Quarter Ended June 30, 2015 | | | | | | Consolidated Total |
|---|-----------------------------|----------------------|---------------------|-------------------------|------------------|-----------|-----------------------|
| | Banking | Wealth Management | Treasury | Total Major Segments | Eliminations | | |
| | (In thousands) | | | | | | |
| Interest income | \$ 90,504 | \$ 24 | \$ 8,885 | \$ 99,413 | \$ - | \$ | 99,413 |
| Interest expense | (7,110) | - | (10,011) | (17,121) | - | - | (17,121) |
| Net interest income | 83,394 | 24 | (1,126) | 82,292 | - | - | 82,292 |
| Provision for non-covered loan and lease losses | (15,644) | - | - | (15,644) | - | - | (15,644) |
| Provision for covered loan and lease losses | 105 | - | - | 105 | - | - | 105 |
| Non-interest income (loss) | (11,713) | 6,893 | 164 | (4,656) | - | - | (4,656) |
| Non-interest expenses | (56,844) | (6,733) | (860) | (64,437) | - | - | (64,437) |
| Intersegment revenue | 163 | - | 61 | 224 | (224) | - | - |
| Intersegment expenses | (61) | (87) | (76) | (224) | 224 | - | - |
| Income before income taxes | \$ (600) | \$ 97 | \$ (1,837) | \$ (2,340) | \$ - | \$ | (2,340) |
| Total assets | \$ 6,153,663 | \$ 21,157 | \$ 2,136,293 | \$ 8,311,113 | (912,788) | \$ | 7,398,325 |

| | Quarter Ended June 30, 2014 | | | | | | Consolidated Total |
|---|-----------------------------|----------------------|-----------|-------------------------|--------------|----|-----------------------|
| | Banking | Wealth Management | Treasury | Total Major Segments | Eliminations | | |
| | (In thousands) | | | | | | |
| Interest income | \$ 112,971 | \$ 46 | \$ 12,883 | \$ 125,900 | \$ - | \$ | 125,900 |
| Interest expense | (10,828) | - | (8,994) | (19,822) | - | - | (19,822) |
| Net interest income | 102,143 | 46 | 3,889 | 106,078 | - | - | 106,078 |
| Provision for non-covered loan and lease losses | (13,220) | - | - | (13,220) | - | - | (13,220) |
| Provision for covered loan and lease losses | (1,595) | - | - | (1,595) | - | - | (1,595) |
| Non-interest income (loss) | (6,507) | 7,502 | (488) | 507 | - | - | 507 |
| Non-interest expenses | (49,651) | (6,367) | (3,830) | (59,848) | - | - | (59,848) |

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| | | | | | | |
|-----------------------------------|---------------------|------------------|---------------------|---------------------|------------------|---------------------|
| Intersegment revenue | 435 | - | - | 435 | (435) | - |
| Intersegment expenses | - | (327) | (108) | (435) | 435 | - |
| Income before income taxes | \$ 31,605 | \$ 854 | \$ (537) | \$ 31,922 | \$ - | \$ 31,922 |
| Total assets | \$ 6,508,432 | \$ 25,345 | \$ 2,089,516 | \$ 8,623,293 | (913,148) | \$ 7,710,145 |

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NOTES TO UNAUDITED CONSOLIDATED FINANCIAL STATEMENTS – (Continued)

Six-Month Period Ended June 30, 2015

| | Wealth | | Total | | Consolidated | |
|--|-------------------|-----------------|-------------------|-------------------|--------------|-------------------|
| | Banking | Management | Treasury | Major Segment | | Eliminations |
| | (In thousands) | | | | | |
| Interest income | \$ 187,986 | \$ 47 | \$ 18,381 | \$ 206,414 | \$ - | \$ 206,414 |
| Interest expense | (14,564) | - | (19,923) | (34,487) | - | (34,487) |
| Net interest income | 173,422 | 47 | (1,542) | 171,927 | - | 171,927 |
| Provision for non-covered loan and lease losses | (53,027) | - | - | (53,027) | - | (53,027) |
| Provision for covered loan and lease losses, net | (4,705) | - | - | (4,705) | - | (4,705) |
| Non-interest income(loss) | (13,962) | 13,903 | 2,284 | 2,225 | - | 2,225 |
| Non-interest expenses | (106,156) | (11,524) | (3,089) | (120,769) | - | (120,769) |
| Intersegment revenue | 707 | - | 160 | 866 | (866) | - |
| Intersegment expenses | (159) | (518) | (189) | (866) | 866 | - |
| Income before income taxes | \$ (3,880) | \$ 1,908 | \$ (2,376) | \$ (4,349) | \$ - | \$ (4,349) |

Six-Month Period Ended June 30, 2014

| | Wealth | | Total | | Consolidated | |
|--|------------------|-----------------|-----------------|------------------|--------------|------------------|
| | Banking | Management | Treasury | Major Segment | | Eliminations |
| | (In thousands) | | | | | |
| Interest income | \$ 221,602 | \$ 86 | \$ 27,286 | \$ 248,974 | \$ - | \$ 248,974 |
| Interest expense | (18,344) | - | (21,154) | (39,498) | - | (39,498) |
| Net interest income | 203,258 | 86 | 6,132 | 209,476 | - | 209,476 |
| Provision for non-covered loan and lease losses | (23,282) | - | - | (23,282) | - | (23,282) |
| Provision for covered loan and lease losses, net | (3,224) | - | - | (3,224) | - | (3,224) |
| Non-interest income(loss) | (11,603) | 14,024 | 3,315 | 5,736 | - | 5,736 |
| Non-interest expenses | (103,198) | (11,146) | (6,908) | (121,252) | - | (121,252) |
| Intersegment revenue | 979 | - | - | 979 | (979) | - |
| Intersegment expenses | - | (759) | (220) | (979) | 979 | - |
| Income (loss) before income taxes | \$ 62,930 | \$ 2,205 | \$ 2,319 | \$ 67,454 | \$ - | \$ 67,454 |

ITEM 2. MANAGEMENT’S DISCUSSION AND ANALYSIS OF FINANCIAL CONDITION AND RESULTS OF OPERATIONS

INTRODUCTION

The following discussion of the Company’s financial condition and results of operations should be read in conjunction with the “Selected Financial Data” and the Company’s unaudited consolidated financial statements and related notes. This discussion and analysis contains forward-looking statements. Please see “Forward-Looking Statements” and the risk factors set forth in our Form 10-K for the year ended December 31, 2014 (the “2014 Form 10-K”), for discussion of the uncertainties, risks and assumptions associated with these statements.

The Company is a publicly-owned financial holding company that provides a full range of banking and financial services through its subsidiaries, including commercial, consumer, auto and mortgage lending; checking and savings accounts; financial planning, insurance and securities brokerage services; and corporate and individual trust and retirement services. The Company operates through three major business segments: Banking, Wealth Management, and Treasury, and distinguishes itself based on quality service. The Company has 52 branches in Puerto Rico and a subsidiary in Boca Raton, Florida. The Company’s long-term goal is to strengthen its banking and financial services franchise by expanding its lending businesses, increasing the level of integration in the marketing and delivery of banking and financial services, maintaining effective asset-liability management, growing non-interest revenue from banking and financial services, and improving operating efficiencies.

The Company’s diversified mix of businesses and products generates both the interest income traditionally associated with a banking institution and non-interest income traditionally associated with a financial services institution (generated by such businesses as securities brokerage, fiduciary services, investment banking, insurance agency, and retirement plan administration). Although all of these businesses, to varying degrees, are affected by interest rate and financial market fluctuations and other external factors, the Company’s commitment is to continue producing a balanced and growing revenue stream.

CRITICAL ACCOUNTING POLICIES AND ESTIMATES

The preparation of financial statements in accordance with U.S. Generally Accepted Accounting Principles (“GAAP”) requires management to make a number of judgments, estimates and assumptions that affect the reported amount of assets, liabilities, income and expenses in the consolidated financial statements. Understanding our accounting policies and the extent to which we use management judgment and estimates in applying these policies is integral to understanding our financial statements. We provide a summary of our significant accounting policies in “Note 1—Summary of Significant Accounting Policies” of our 2014 Form 10-K.

In the “Management’s Discussion and Analysis of Financial Condition and Results of Operations—Critical Accounting Policies and Estimates” section of our 2014 Form 10-K, we identified the following accounting policies as critical

because they require significant judgments and assumptions about highly complex and inherently uncertain matters and the use of reasonably different estimates and assumptions could have a material impact on our reported results of operations or financial condition:

- Business combination
- Allowance for loan and lease losses
- Financial instruments

We evaluate our critical accounting estimates and judgments on an ongoing basis and update them as necessary based on changing conditions. Management has reviewed and approved these critical accounting policies and has discussed its judgments and assumptions with the Audit Committee of our Board of Directors. As part of the Company's continuous enhancement to the allowance for loan and lease losses methodology, during the quarter ended June 30, 2015, an assessment of the look-back period and historical loss factor was performed for auto and leasing and consumer and commercial loan portfolios. The analysis was based on the trends observed and their relation with the economic cycle as of the period ended June 30, 2015. As a result, for the commercial portfolio, the look-back period was changed to 36 months from the previously determined 12 months. For auto and leasing and consumer, a look back period of 24 months was maintained. In addition, during the quarter ended June 30, 2015, an assessment of environmental factors was performed for commercial, auto, and consumer portfolios. As a result, the environmental factors continue to reflect our assessment of the impact to our portfolio, taking into consideration the current evolution of the portfolio and expected impact, due to recent economic developments, changes in values of collateral and delinquencies, among others. These changes in the allowance for loan and lease losses' look-back period and the result of the assessment in economic factors for the commercial, auto, and consumer

portfolios are considered a change in accounting estimate as per ASC 250-10 provisions, where adjustments should be made prospectively. As part from these changes, there have been no other material changes in the methods used to formulate these critical accounting estimates from those discussed in our 2014 Form 10-K.

OVERVIEW OF FINANCIAL PERFORMANCE

SELECTED FINANCIAL DATA

| | Quarter Ended June 30, | | | Six-Month Period Ended June 30, | | |
|--|------------------------|------------------|----------------|---------------------------------|------------------|----------------|
| | 2015 | 2014 | Variance % | 2015 | 2014 | Variance % |
| EARNINGS DATA: | | | | | | |
| (In thousands, except per share data) | | | | | | |
| Interest income | \$ 99,413 | \$ 125,900 | -21.0% | \$ 206,414 | \$ 248,974 | -17.1% |
| Interest expense | 17,121 | 19,822 | -13.6% | 34,487 | 39,498 | -12.7% |
| Net interest income | 82,292 | 106,078 | -22.4% | 171,927 | 209,476 | -17.9% |
| Provision for non-covered loan and lease losses | 15,644 | 13,220 | 18.3% | 53,027 | 23,282 | 127.8% |
| Provision for covered loan and lease losses, net | (105) | 1,595 | -106.6% | 4,705 | 3,224 | 45.9% |
| Total provision for loan and lease losses, net | 15,539 | 14,815 | 4.9% | 57,732 | 26,506 | 117.8% |
| Net interest income after provision for loan and lease losses | 66,753 | 91,263 | -26.9% | 114,195 | 182,970 | -37.6% |
| Non-interest income | (4,656) | 507 | -1018.3% | 2,225 | 5,736 | -61.2% |
| Non-interest expenses | 64,437 | 59,848 | 7.7% | 120,769 | 121,252 | -0.4% |
| (Loss) income before taxes | (2,340) | 31,922 | -107.3% | (4,349) | 67,454 | -106.4% |
| Income tax expense (benefit) | 769 | 10,613 | -92.8% | 1,748 | 22,398 | -92.2% |
| Net (loss) income | (3,109) | 21,309 | -114.6% | (6,097) | 45,056 | -113.5% |
| Less: dividends on preferred stock | (3,466) | (3,466) | 153.0% | (6,931) | (6,931) | 153.0% |
| (Loss) income available to common shareholders | \$ (6,575) | \$ 17,843 | -136.8% | \$ (13,028) | \$ 38,125 | -134.2% |
| PER SHARE DATA: | | | | | | |
| Basic | \$ (0.15) | \$ 0.40 | -137.3% | \$ (0.29) | \$ 0.84 | -134.6% |
| Diluted | \$ (0.15) | \$ 0.38 | -139.3% | \$ (0.29) | \$ 0.80 | -136.7% |
| Average common shares outstanding | 44,505 | 45,014 | -1.1% | 44,569 | 45,170 | -1.3% |
| Average common shares outstanding and equivalents | 51,774 | 52,352 | -1.1% | 51,876 | 52,476 | -1.1% |
| Cash dividends declared per common share | \$ 0.10 | \$ 0.08 | 25.4% | \$ 0.20 | \$ 0.16 | 25.4% |
| Cash dividends declared on common shares | \$ 4,457 | \$ 3,560 | 25.2% | \$ 8,920 | \$ 7,218 | 23.6% |
| PERFORMANCE RATIOS: | | | | | | |
| Return on average assets (ROA) | -0.17% | 1.10% | -115.4% | -0.17% | 1.14% | -114.5% |
| Return on average tangible common equity | -3.93% | 10.96% | -135.9% | -3.84% | 11.89% | -132.3% |
| Return on average common equity (ROE) | -3.44% | 9.54% | -136.1% | -3.37% | 10.32% | -132.7% |
| Equity-to-assets ratio | 12.32% | 12.00% | 2.7% | 12.32% | 12.00% | 2.7% |
| Efficiency ratio | 63.39% | 47.89% | 32.4% | 57.37% | 48.99% | 17.1% |
| Interest rate spread | 4.68% | 5.91% | -20.8% | 4.91% | 5.78% | -15.1% |
| Interest rate margin | 4.92% | 6.10% | -19.4% | 5.14% | 5.96% | -13.7% |

SELECTED FINANCIAL DATA - (Continued)

| | June 30, 2015 | December 31, 2014 | Variance % |
|---|---------------------|----------------------|---------------|
| PERIOD END BALANCES AND CAPITAL RATIOS: | | | |
| (In thousands, except per share data) | | | |
| Investments and loans | | | |
| Investment securities | \$ 1,616,487 | \$ 1,402,056 | 15.3% |
| Loans and leases not covered under shared-loss | 4,417,433 | 4,527,735 | -2.4% |
| agreements with the FDIC, net | | | |
| Loans and leases covered under shared-loss | 222,034 | 298,911 | -25.7% |
| agreements with the FDIC, net | | | |
| Total investments and loans | \$ 6,255,954 | \$ 6,228,702 | 0.4% |
| Deposits and borrowings | | | |
| Deposits | \$ 4,749,684 | \$ 4,924,406 | -3.5% |
| Securities sold under agreements to repurchase | 1,161,136 | 980,087 | 18.5% |
| Other borrowings | 437,590 | 439,919 | -0.5% |
| Total deposits and borrowings | \$ 6,348,410 | \$ 6,344,412 | 0.1% |
| Stockholders' equity | | | |
| Preferred stock | \$ 176,000 | \$ 176,000 | 0.0% |
| Common stock | 52,626 | 52,626 | 0.0% |
| Additional paid-in capital | 539,669 | 539,311 | 0.1% |
| Legal surplus | 69,934 | 70,467 | -0.8% |
| Retained earnings | 159,737 | 181,152 | -11.8% |
| Treasury stock, at cost | (100,668) | (97,070) | -3.7% |
| Accumulated other comprehensive income | 14,301 | 19,711 | -27.4% |
| Total stockholders' equity | \$ 911,599 | \$ 942,197 | -3.2% |
| Per share data | | | |
| Book value per common share | \$ 16.81 | \$ 17.40 | -3.4% |
| Tangible book value per common share | \$ 14.67 | \$ 15.25 | -3.8% |
| Market price at end of period | \$ 10.67 | \$ 16.65 | -35.9% |
| Capital ratios | | | |
| Leverage capital | 11.05% | 10.61% | 4.1% |
| Tier 1 common equity to risk-weighted assets | N/A | 11.88% | N/A |
| Common equity Tier 1 capital ratio | 12.25% | N/A | N/A |
| Tier 1 risk-based capital | 15.85% | 16.02% | -1.1% |
| Total risk-based capital | 17.41% | 17.57% | -0.9% |
| Financial assets managed | | | |
| Trust assets managed | \$ 2,793,489 | \$ 2,841,111 | -1.7% |
| Broker-dealer assets gathered | \$ 2,554,825 | \$ 2,622,001 | -2.6% |

FINANCIAL HIGHLIGHTS OF THE SECOND QUARTER OF 2015

During the second quarter of 2015, the Company reported a loss to common shareholders of \$6.6 million, or \$0.15 per share, compared to a loss of \$6.5 million, or \$0.14 per share, in the first quarter of 2015, and to a profit of \$17.8 million, or \$0.38 per share diluted, in the second quarter of 2014.

When compared to the first quarter of 2015, this quarter was adversely affected by:

- Absence of \$4.2 million decrease in tax free interest income from loans to Puerto Rico Electric Power Authority (“PREPA”) and Puerto Rico Aqueduct and Sewer Authority (PRASA). The \$200 million PREPA loan was placed on non-accrual status in the first quarter of 2015. While it continues to perform, interest payments are being used to reduce the principal amount. The \$75 million remaining balance of the PRASA loan was paid-off on June 1, 2015.
- \$10.2 million increase in the FDIC commercial loss share amortization related to the scheduled expiration of the Eurobank loss share coverage for commercial loans.
- \$4.5 million of additional loss in other real estate owned (“OREO”) due to revised collateral values as part of the Company’s ongoing and proactive de-risking efforts.

The foregoing adverse items were partially offset by a \$26.7 million decline in total provision for loan and lease losses, which had an after tax impact of \$21.3 million. This reflects management’s determination that no PREPA provision other than the \$24 million recorded in the first quarter of 2015, because the government utility and its creditors are actively working on a repayment agreement. Additionally, no additional provision was required on FDIC-covered commercial loans, compared to \$4.8 million recorded in the first quarter of 2015.

In the second quarter of 2015, net interest margin declined to 4.92%.

The efficiency ratio increased to 63.39%. Tangible book value and book value per common share decreased to \$14.67 and \$16.81, respectively, from \$15.12 and \$17.25 in the preceding quarter.

The credit balances of the Puerto Rico central government and its public corporations with the Company declined 20.7% to \$301.3 million at June 30, 2015 from \$380.1 million at March 31, 2015. This excludes \$214.0 million in term loans to five Puerto Rico municipalities, which are separate local governmental entities with their own sources of tax revenues.

Interest Income

Total interest income decreased by \$26.4 million to \$99.4 million, compared to \$125.9 million in the second quarter of 2014, reflecting the transition in our loan portfolio as originated loans with more normal yields grow as higher-yielding acquired loans decrease, due to repayments and maturities. The yield on interest-earning assets decreased to 5.94% in the second quarter of 2015 from 7.24% in the same quarter of 2014.

Interest Expense

Total interest expense decreased by 13.6% in the second quarter of 2015 as compared to the same period in 2014. Such decrease reflects the lower cost of deposits before fair value premium amortization and core deposit intangible amortization (0.65% vs. 0.87%). Such lower cost reflects continuing progress in the repricing of the Company's core retail deposits and other reductions in its cost of funds.

Net Interest Income

Net interest income decreased \$23.8 million for the second quarter of 2015. Such decrease reflects a decrease in net interest margin of 118 basis points to 4.92% when compared to the second quarter of 2014.

Provision for Loan and Lease Losses

Provision for loan and lease losses increased \$723 thousand to \$15.5 million when compared to \$14.8 million for the second quarter of 2014, reflecting an increase of \$2.4 million to \$15.6 million in provision for non-covered loan and lease losses. No provision was required on FDIC covered commercial loans for the second quarter of 2015, compared to \$1.6 million for the same period in 2014. No additional provision was required to the PREPA loan of credit for the second quarter of 2015.

Non-Interest Income

Core banking and wealth management revenues increased to \$19.4 million as compared to the same period in 2014, primarily reflecting an increase of \$308 thousand and \$217 thousand in mortgage banking service revenues and banking service revenues, respectively, and a decrease of \$51 thousand in wealth management revenue.

The fluctuation in the FDIC shared-loss expense of \$22.5 million, compared to \$17.5 million for the same period in 2014, resulted from the ongoing evaluation of expected cash flows of the covered loan portfolio, which resulted in reduced projected losses expected to be collected from the FDIC and the improved accretable yield on the covered loans.

Other non-interest loss of \$847 thousand, compared to income of \$224 thousand for the same period in 2014, is primarily from the recognition of a \$835 thousand loss, in the sale of mortgage servicing rights during the second quarter of 2015. During the first quarter of 2015, the Company recognized a \$1.9 million loss in the valuation of the mortgage servicing assets, as part of servicing asset sale transaction.

Non-Interest Expense

Non-interest expense of \$64.4 million, increased \$4.6 million or 7.7% compared to the same period in 2014, primarily reflecting an increase in foreclosure, repossession and other real estate expenses of \$3.7 million, mostly from the \$4.5 million loss on the revision of collateral values as part of the Company's de-risking efforts during the second quarter of 2015. The Company's efficiency ratio for the second quarter of 2015 was 63.39%, compared to 47.89% for the same period in 2014.

Income Tax Expense

Income tax expense was \$769 thousand, compared to \$10.6 million for the same period in 2014. Decrease in income tax expense reflects the net loss before income taxes of \$2.3 million for the second quarter ended June 30, 2015, compared to net income before income taxes of \$31.9 million for the year ago quarter.

(Loss) Income Available to Common Shareholders

The Company's loss to common shareholders amounted to \$6.6 million, compared to net income available to common shareholders of \$17.8 million for the same period in 2014. Loss per basic common share and fully diluted common share was \$0.15 for both, compared to income per basic common share and fully diluted common share of \$0.40 and \$0.38, respectively, for the second quarter of 2014.

Interest Earning Assets

The loan portfolio declined to \$4.639 billion at June 30, 2015, compared to \$4.725 billion at March 31, 2015, primarily due to repayments and maturities. This reduction primarily reflects the \$75.0 million repayment by PRASA. The investment portfolio of \$1.616 billion at June 30, 2015 increased 22.4% compared to \$1.321 billion at March 31, 2015.

Interest Bearing Liabilities

Total deposits amounted to \$4.750 billion at June 30, 2015, a decrease of 3.0% compared to \$4.894 billion at March 31, 2015. Demand and savings deposits decreased 5.19% to \$3.187 billion. Cost of deposits, which averaged 0.65% at June 30, 2015 and 0.70% at March 31, 2015, continue to decrease.

Stockholders' Equity

Stockholders' equity at June 30, 2015 was \$911.6 million compared to \$942.2 million at December 31, 2014, a decrease of 3.2%. This reflects a decrease of \$21.4 million in retained earnings and a decrease of \$5.4 million on accumulated other comprehensive income. Book value per share was \$16.81 at June 30, 2015 compared to \$17.40 at December 31, 2014.

The Company maintains capital ratios in excess of regulatory requirements. At June 30, 2015, Tier 1 Leverage Capital Ratio was 11.05% (December 31, 2014 – 10.61%), Tier 1 Risk-Based Capital Ratio was 15.84% (December 31, 2014 – 16.02%), and Total Risk-Based Capital Ratio was 17.40% (December 31, 2014 – 17.57%). Common Equity Tier 1 capital ratio under the new capital rules was 12.25% at June 30, 2015.

Return on Average Assets and Common Equity

Return on average common equity ("ROE") was (3.44%) compared to 9.54% for the quarter ended June 30, 2014. Return on average assets ("ROA") was (0.17%) compared to 1.10% for the same period in 2014. Both decreases reflect the net loss for the second quarter of 2015.

Assets under Management

At June 30, 2015, total assets managed by the Company's trust division and OPC decreased to \$2.793 billion compared to \$2.912 billion at March 31, 2015. At June 30, 2015, total assets gathered by the securities broker-dealer subsidiary from its customer investment accounts decreased by 3.9% to \$2.555 billion, compared to \$2.660 billion at March 31, 2015. Changes in trust and broker-dealer related assets primarily reflect a decrease in portfolio balances and fluctuations in market values.

Lending

Total loan production of \$286.7 million increased by 29.4% compared to the same period in 2014. Total commercial loan production of \$120.5 million increased by 165.2% from \$45.4 million for the same period in 2014.

Mortgage loan production of \$64.8 million increased by 24.7% from \$52.0 million for the same period in 2014, as the Company continued to capture market share formerly held by Doral Bank.

In the aggregate, consumer loan and auto and leasing production totaled \$101.4 million, a decrease of 18.3% from the same period in 2014. Such decrease is mostly due to a decrease of 31.33% in auto production.

Total loan portfolio declined by \$85.1 million from \$4.725 billion at March 31, 2015 to \$4.639 billion at June 30, 2015, mostly as the result of scheduled pay downs and maturities in both the non-covered and covered loan portfolios. In addition, this reflects the \$75.0 million repaid by PRASA as we continue to decrease our exposure to the Puerto Rico government.

Credit Quality on Non-Covered Loans

Net credit losses, excluding acquired loans, increased \$1.4 million to \$7.7 million, representing 1.06% of average non-acquired loans outstanding versus 0.96% in the same period in 2014. The allowance for loan and lease losses on non-covered loans at June 30, 2015, increased to \$102.9 million compared to \$96.4 million at March 31, 2015. The allowances for loan and lease losses, excluding acquired loans, increased to \$79.0 million (2.71% of total non-covered loans, excluding acquired loans) at June 30, 2015, compared to \$76.8 million (2.64% of total non-covered loans, excluding acquired loans) at March 31, 2015.

Non-performing loans (“NPLs”), which exclude loans covered under shared-loss agreements with the FDIC and loans acquired in the BBVAPR Acquisition accounted under ASC 310-30, decreased slightly to \$312.2 million at June 30, 2015 compared to \$313.1 million at March 31, 2015.

Non-GAAP Measures

The Company uses certain non-GAAP measures of financial performance to supplement the unaudited consolidated financial statements presented in accordance with GAAP. The Company presents non-GAAP measures that management believes are useful and meaningful to investors. Non-GAAP measures do not have any standardized meaning, are not required to be uniformly applied, and are not audited. Therefore, they are unlikely to be comparable to similar measures presented by other companies. The presentation of non-GAAP measures is not intended to be a substitute for, and should not be considered in isolation from, the financial measures reported in accordance with GAAP.

The Company's management has reported and discussed the results of operations herein both on a GAAP basis and on a pre-tax pre-provision operating income basis (defined as net interest income, plus banking and financial services revenue, less non-interest expenses, as calculated on the table below). The Company's management believes that, given the nature of the items excluded from the definition of pre-tax pre-provision operating income, it is useful to state what the results of operations would have been without them so that investors can see the financial trends from the Company's continuing business.

During the quarter ended June 30, 2015, the Company's pre-tax pre-provision operating income decreased 42.8% to \$37.2 million as compared to \$65.1 million for the same period in 2014. Pre-tax pre-provision operating income is calculated as follows:

| | Quarter Ended June 30, | | Six-Month Period Ended June 30, | |
|--|------------------------|------------------|------------------------------------|-------------------|
| | 2015 | 2014 | 2015 | 2014 |
| | (In thousands) | | (In thousands) | |
| <u>PRE-TAX PRE-PROVISION OPERATING INCOME</u> | | | | |
| Net interest income | \$ 82,292 | \$ 106,078 | \$ 171,927 | \$ 209,476 |
| Core non-interest income: | | | | |
| Banking service revenue | 10,212 | 9,995 | 20,417 | 20,552 |
| Wealth management revenue | 7,285 | 7,336 | 14,440 | 14,203 |
| Mortgage banking activities | 1,862 | 1,554 | 3,725 | 3,249 |
| Total core non-interest income | 19,359 | 18,885 | 38,582 | 38,004 |
| Non-interest expenses | 64,437 | 59,848 | 120,769 | 121,252 |
| Total pre-tax pre-provision operating income | \$ 37,214 | \$ 65,115 | \$ 89,740 | \$ 126,228 |

Tangible common equity consists of common equity less goodwill, core deposit intangibles and customer relationship intangible. Tangible book value per common share consists of tangible common equity divided by common stock

outstanding at the end of the period. Ratios of tangible common equity to total assets, tangible common equity to risk-weighted assets, total equity to risk-weighted assets, tier 1 common equity to risk-weighted assets, and common equity tier 1 to risk-weighted assets and tangible book value per common share are non-GAAP measures.

At June 30, 2015, tangible common equity to total assets decreased to 8.80% from 9.29% and tangible common equity to risk-weighted assets decreased to 13.05% from 13.46% at March 31, 2015. Total equity to risk-weighted assets decreased to 18.27% from 18.67% at March 31, 2015.

Management and many stock analysts use tangible common equity in conjunction with more traditional bank capital ratios to compare the capital adequacy of banking organizations. Tangible common equity or related measures should not be considered in isolation or as a substitute for stockholders' equity, total assets or any other measure calculated in accordance with GAAP.

ANALYSIS OF RESULTS OF OPERATIONS

The following tables show major categories of interest-earning assets and interest-bearing liabilities, their respective interest income, expenses, yields and costs, and their impact on net interest income due to changes in volume and rates for the quarters and six-month periods ended June 30, 2015 and 2014:

TABLE 1 - QUARTERLY ANALYSIS OF NET INTEREST INCOME AND CHANGES DUE TO VOLUME/RATE FOR THE QUARTERS ENDED JUNE 30, 2015 AND 2014

| | Interest | | Average rate | | Average balance | |
|---|---------------|---------------|--------------|--------------|------------------|------------------|
| | June 2015 | June 2014 | June 2015 | June 2014 | June 2015 | June 2014 |
| (Dollars in thousands) | | | | | | |
| A - TAX EQUIVALENT SPREAD | | | | | | |
| Interest-earning assets | \$ 99,413 | \$ 125,900 | 5.94% | 7.24% | \$ 6,708,519 | \$ 6,972,133 |
| Tax equivalent adjustment | 3,811 | 9,926 | 0.23% | 0.57% | - | - |
| Interest-earning assets - tax equivalent | 103,224 | 135,826 | 6.18% | 7.81% | 6,708,519 | 6,972,133 |
| Interest-bearing liabilities | 17,121 | 19,822 | 1.26% | 1.33% | 5,452,804 | 5,985,225 |
| Tax equivalent net interest income / spread | 86,103 | 116,004 | 4.92% | 6.50% | 1,255,715 | 986,908 |
| Tax equivalent interest rate margin | | | 5.15% | 6.67% | | |
| B - NORMAL SPREAD | | | | | | |
| Interest-earning assets: | | | | | | |
| Investments: | | | | | | |
| Investment securities | 8,587 | 12,606 | 2.33% | 3.64% | 1,476,867 | 1,393,523 |
| Interest bearing cash and money market investments | 322 | 351 | 0.27% | 0.25% | 483,507 | 559,230 |
| Total investments | 8,909 | 12,957 | 1.84% | 2.69% | 1,960,374 | 1,952,753 |
| Loans not covered under shared-loss agreements | | | | | | |
| with the FDIC: | | | | | | |
| Originated | | | | | | |
| Mortgage | 9,698 | 10,341 | 4.97% | 5.36% | 782,753 | 773,425 |
| Commercial | 14,375 | 16,451 | 4.32% | 5.46% | 1,333,276 | 1,209,346 |
| Consumer | 4,953 | 3,641 | 10.32% | 9.92% | 192,572 | 147,230 |
| Auto and leasing | 15,213 | 12,650 | 9.86% | 10.47% | 618,746 | 484,536 |
| Total originated non-covered loans | 44,239 | 43,083 | 6.06% | 6.61% | 2,927,347 | 2,614,537 |
| Acquired | | | | | | |
| Mortgage | 8,813 | 9,363 | 5.57% | 5.37% | 634,794 | 698,720 |
| Commercial | 11,770 | 18,959 | 9.49% | 11.35% | 497,422 | 669,983 |
| Consumer | 3,445 | 3,992 | 16.91% | 13.84% | 81,713 | 115,676 |

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| | | | | | | |
|---|---------------|----------------|---------------|---------------|------------------|------------------|
| Auto | 9,479 | 12,667 | 10.23% | 8.80% | 371,494 | 577,114 |
| Total acquired non-covered loans | 33,507 | 44,981 | 8.48% | 8.75% | 1,585,422 | 2,061,493 |
| Total non-covered loans | 77,746 | 88,064 | 6.91% | 7.55% | 4,512,769 | 4,676,030 |
| Loans covered under shared loss agreements with the FDIC | 12,758 | 24,879 | 21.74% | 29.06% | 235,376 | 343,350 |
| Total loans | 90,504 | 112,943 | 7.65% | 9.03% | 4,748,145 | 5,019,380 |
| Total interest earning assets | 99,413 | 125,900 | 5.94% | 7.24% | 6,708,519 | 6,972,133 |

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| | Interest | | Average rate | | Average balance | |
|---|------------------------|-------------------|--------------|--------------|---------------------|-------------------|
| | June 2015 | June 2014 | June 2015 | June 2014 | June 2015 | June 2014 |
| | (Dollars in thousands) | | | | | |
| Interest-bearing liabilities: | | | | | | |
| Deposits: | | | | | | |
| Now Accounts | 1,073 | 2,207 | 0.38% | 0.61% | 1,144,931 | 1,443,824 |
| Savings and money market | 1,662 | 2,192 | 0.51% | 0.75% | 1,300,001 | 1,168,911 |
| Individual retirement accounts | 600 | 940 | 0.85% | 1.14% | 283,587 | 329,584 |
| Retail certificates of deposits | 1,326 | 1,741 | 1.31% | 1.30% | 405,302 | 535,203 |
| Total core deposits | 4,661 | 7,080 | 0.60% | 0.82% | 3,133,821 | 3,477,522 |
| Institutional deposits | 698 | 1,290 | 1.00% | 1.58% | 280,930 | 327,660 |
| Brokered deposits | 1,085 | 1,468 | 0.76% | 0.83% | 571,950 | 709,374 |
| Total wholesale deposits | 1,783 | 2,758 | 0.84% | 1.07% | 852,880 | 1,037,034 |
| | 6,444 | 9,838 | 0.65% | 0.87% | 3,986,701 | 4,514,556 |
| Deposits fair value premium amortization | (131) | (1,010) | 0.00% | 0.00% | - | - |
| Core deposit intangible amortization | 292 | 336 | 0.00% | 0.00% | - | - |
| Total deposits | 6,605 | 9,164 | 0.66% | 0.81% | 3,986,701 | 4,514,556 |
| Borrowings: | | | | | | |
| Securities sold under agreements to repurchase | 7,394 | 7,372 | 2.91% | 2.93% | 1,020,077 | 1,010,000 |
| Advances from FHLB and other borrowings | 2,248 | 2,289 | 2.62% | 2.55% | 344,088 | 360,130 |
| Subordinated capital notes | 875 | 996 | 3.44% | 3.97% | 101,938 | 100,539 |
| Total borrowings | 10,517 | 10,657 | 2.88% | 2.91% | 1,466,103 | 1,470,669 |
| Total interest bearing liabilities | 17,122 | 19,821 | 1.26% | 1.33% | 5,452,804 | 5,985,225 |
| Net interest income / spread | \$ 82,292 | \$ 106,078 | 4.68% | 5.91% | | |
| Interest rate margin | | | 4.92% | 6.10% | | |
| Excess of average interest-earning assets | | | | | \$ 1,255,715 | \$ 986,908 |
| over average interest-bearing liabilities | | | | | | |
| Average interest-earning assets to average | | | | | 123.03% | 116.49% |
| interest-bearing liabilities ratio | | | | | | |

C - CHANGES IN NET INTEREST INCOME DUE TO:

| | Volume | Rate | Total |
|-------------------------------|-------------------|--------------------|--------------------|
| | (In thousands) | | |
| Interest Income: | | | |
| Investments | \$ 51 | \$ (4,099) | \$ (4,048) |
| Loans | (10,899) | (11,539) | (22,438) |
| Total interest income | (10,848) | (15,638) | (26,486) |
| Interest Expense: | | | |
| Deposits | (1,072) | (1,488) | (2,560) |
| Repurchase agreements | 74 | (52) | 22 |
| Other borrowings | (104) | (58) | (162) |
| Total interest expense | (1,102) | (1,598) | (2,700) |
| Net Interest Income | \$ (9,746) | \$ (14,040) | \$ (23,786) |

TABLE 1/A - YEAR-TO-DATE ANALYSIS OF NET INTEREST INCOME AND CHANGES DUE TO VOLUME/RATE FOR THE SIX-MONTH PERIODS ENDED JUNE 30, 2015 AND 2014

| | Interest | | Average rate | | Average balance | |
|---|------------------------|------------|--------------|-----------|-----------------|------------|
| | June 2015 | June 2014 | June 2015 | June 2014 | June 2015 | June 2014 |
| | (Dollars in thousands) | | | | | |
| A - TAX EQUIVALENT SPREAD | | | | | | |
| Interest-earning assets | \$ 206,413 | \$ 248,974 | 6.17% | 7.08% | \$ 6,741,247 | \$ 7,093,5 |
| Tax equivalent adjustment | 20,756 | 13,033 | 0.62% | 0.37% | - | |
| Interest-earning assets - tax equivalent | 227,169 | 262,007 | 6.80% | 7.45% | 6,741,247 | 7,093,5 |
| Interest-bearing liabilities | 34,486 | 39,498 | 1.26% | 1.30% | 5,499,113 | 6,124,7 |
| Tax equivalent net interest income / spread | 192,683 | 222,509 | 5.53% | 6.16% | 1,242,134 | 968,8 |
| Tax equivalent interest rate margin | | | 5.76% | 6.33% | | |
| B - NORMAL SPREAD | | | | | | |
| Interest-earning assets: | | | | | | |
| Investments: | | | | | | |
| Investment securities | 17,746 | 26,690 | 2.54% | 3.58% | 1,409,926 | 1,503,7 |
| Trading securities | 36 | 75 | 6.15% | 8.06% | 1,181 | 1,8 |
| Interest bearing cash and money market investments | 645 | 635 | 0.25% | 0.22% | 523,649 | 574,5 |
| Total investments | 18,427 | 27,400 | 1.92% | 2.66% | 1,934,756 | 2,080,1 |
| Loans not covered under shared-loss agreements | | | | | | |
| with the FDIC: | | | | | | |
| Originated | | | | | | |
| Mortgage | 19,908 | 20,799 | 5.11% | 5.49% | 785,029 | 763,4 |
| Commercial | 31,329 | 30,797 | 4.85% | 5.33% | 1,301,367 | 1,165,8 |
| Consumer | 9,538 | 6,780 | 10.28% | 9.92% | 187,049 | 137,7 |
| Auto and leasing | 29,747 | 23,639 | 9.89% | 10.56% | 606,819 | 451,4 |
| Total originated non-covered loans | 90,522 | 82,015 | 6.34% | 6.57% | 2,880,264 | 2,518,5 |
| Acquired | | | | | | |
| Mortgage | 17,800 | 18,732 | 5.59% | 5.35% | 642,063 | 705,9 |
| Commercial | 26,342 | 37,671 | 10.34% | 10.79% | 513,950 | 704,0 |
| Consumer | 6,634 | 8,209 | 15.64% | 13.48% | 85,541 | 122,8 |
| Auto | 18,426 | 26,680 | 8.65% | 8.78% | 429,618 | 612,5 |
| Total acquired non-covered loans | 69,202 | 91,292 | 8.35% | 8.58% | 1,671,173 | 2,145,4 |
| Total non-covered loans | 159,724 | 173,307 | 7.08% | 7.49% | 4,551,437 | 4,663,9 |
| Loans covered under shared loss agreements with the FDIC | 28,262 | 48,267 | 22.35% | 27.86% | 255,053 | 349,4 |
| Total loans | 187,986 | 221,574 | 7.89% | 8.91% | 4,806,491 | 5,013,4 |
| Total interest earning assets | 206,413 | 248,974 | 6.17% | 7.08% | 6,741,247 | 7,093,5 |

| | Interest | | Average rate | | Average balance | |
|---|-------------------|-------------------|--------------|--------------|---------------------|-------------------|
| | June 2015 | June 2014 | June 2015 | June 2014 | June 2015 | June 2014 |
| (Dollars in thousands) | | | | | | |
| Interest-bearing liabilities: | | | | | | |
| Deposits: | | | | | | |
| Now Accounts | \$ 2,354 | \$ 4,531 | 0.39% | 0.63% | \$ 1,202,621 | \$ 1,451,547 |
| Savings and money market | 3,396 | 4,488 | 0.52% | 0.79% | 1,307,141 | 1,148,918 |
| Individual retirement accounts | 1,371 | 1,998 | 0.95% | 1.20% | 289,877 | 336,175 |
| Retail certificates of deposits | 2,733 | 3,681 | 1.32% | 1.34% | 416,608 | 553,527 |
| Institutional deposits | 1,497 | 2,699 | 1.11% | 1.54% | 272,991 | 352,456 |
| Total core deposits | 11,351 | 17,397 | 0.66% | 0.91% | 3,489,238 | 3,842,623 |
| Brokered deposits | 2,251 | 2,984 | 0.77% | 0.82% | 586,986 | 730,349 |
| | 13,602 | 20,381 | 0.67% | 0.90% | 4,076,224 | 4,572,972 |
| Deposits fair value premium amortization | (479) | (2,908) | 0.00% | 0.00% | - | - |
| Core deposit intangible amortization | 585 | 670 | 0.00% | 0.00% | - | - |
| Total deposits | 13,708 | 18,143 | 0.68% | 0.80% | 4,076,224 | 4,572,972 |
| Borrowings: | | | | | | |
| Securities sold under agreements to repurchase | 14,559 | 14,784 | 3.00% | 2.75% | 979,950 | 1,082,968 |
| Advances from FHLB and other borrowings | 4,484 | 4,583 | 2.65% | 2.51% | 340,709 | 367,953 |
| Subordinated capital notes | 1,735 | 1,988 | 3.44% | 3.99% | 101,808 | 100,357 |
| Total borrowings | 20,778 | 21,355 | 2.95% | 2.78% | 1,422,467 | 1,551,278 |
| Total interest bearing liabilities | 34,486 | 39,498 | 1.26% | 1.30% | 5,498,691 | 6,124,250 |
| Net interest income / spread | \$ 171,927 | \$ 209,476 | 4.91% | 5.78% | | |
| Interest rate margin | | | 5.14% | 5.96% | | |
| Excess of average interest-earning assets over | | | | | \$ 1,242,580 | \$ 969,310 |
| average interest-bearing liabilities | | | | | | |
| Average interest-earning assets to average | | | | | 122.60% | 115.83% |
| interest-bearing liabilities ratio | | | | | | |

C - CHANGES IN NET INTEREST INCOME DUE TO:

| | Volume | Rate | Total |
|-------------------------------|--------------------|--------------------|--------------------|
| (In thousands) | | | |
| Interest Income: | | | |
| Investments | \$ (1,915) | \$ (7,058) | \$ (8,973) |
| Loans | (17,217) | (16,371) | (33,588) |
| Total interest income | (19,132) | (23,429) | (42,561) |
| Interest Expense: | | | |
| Deposits | (1,971) | (2,464) | (4,435) |
| Repurchase agreements | (1,406) | 1,181 | (225) |
| Other borrowings | (362) | 10 | (352) |
| Total interest expense | (3,739) | (1,273) | (5,012) |
| Net Interest Income | \$ (15,393) | \$ (22,156) | \$ (37,549) |

Net Interest Income

Comparison of quarters ended June 30, 2015 and 2014

Net interest income of \$82.3 million decreased 22.42% compared with \$106.1 million reported in the same quarter of 2014, reflecting a decrease of 21.0% in interest income from loans and a decrease of 33.3% in interest income from investments.

Interest rate spread decreased 123 basis points from 5.91% to 4.68%. This decrease is mainly due to the net effect of a 130 basis points decrease in the average yield of interest-earning assets from 7.24% to 5.94%.

Interest income decreased to \$99.4 million from \$125.9 million in the same quarter in 2014. Such decrease reflects decreases of \$10.8 million and \$15.6 million in the volume and interest rate, respectively, on interest-earning assets. Interest income from loans decreased 19.9% to \$90.5 million, reflecting a decrease in both, volume and interest rate of \$10.9 million and \$11.5 million, respectively, primarily due to the \$4.1 million decrease in interest income from loans to PREPA, which was placed in non-accrual at the end of the first quarter of 2015, and PRASA, which was paid off during the second quarter of 2015, and to lower acquired loan balances and yields. Originated loans interest income increased 2.7% to \$44.2 million as balances grew 12.0% and yield contracted 55 basis points to 6.06%. Acquired non-covered loans interest income fell 25.5% to \$33.5 million as balances declined 23.1% and yield reduced 27 basis points to 8.48%. Covered loans interest income fell 48.7% to \$12.8 million as balances declined 31.4% and yield reduced 732 basis points to 21.7%. Interest income from investments decreased 31.2% to \$8.9 million, reflecting a decrease in interest rate of \$4.1 million. Such decrease in interest income from investments reflects a higher premium amortization on existing securities.

Interest expense decreased 13.6% to \$17.1 million, primarily because of a \$1.1 million decrease in the volume of interest-bearing liabilities and decrease of \$1.6 million in interest rate. The decrease in interest-bearing liabilities is mostly due to the decrease in deposits volume of \$1.1 million and in interest rate of \$1.5 million. The cost of deposits before fair value amortization and core deposit intangible amortization decreased 22 basis points to 0.65% for the second quarter of 2015, compared to 0.87% for the same quarter of 2014. Cost of borrowings decreased 3 basis points to 2.88% from 2.91%.

The average balance of total interest-earning assets was \$6.709 billion, a decrease of 3.8% from the same period in 2014. The decrease in average balance of interest-earning assets was mainly attributable to a decrease of 12% in average loans.

Comparison of six-month periods ended June 30, 2015 and 2014

Net interest income of \$171.9 million decreased 17.9% compared with \$209.5 million reported in the six-month periods of 2014, reflecting a decrease of 15.2% in interest income from loans and a decrease of 32.7% in interest income from investments.

Interest rate spread decreased 87 basis points from 5.78% to 4.91%. This decrease is mainly due to the net effect of a 91 basis points decrease in the average yield of interest-earning assets from 7.08% to 6.17%.

Interest income decreased to \$206.4 million from \$249.0 million in the same period in 2014. Such decrease reflects decreases of \$19.1 million and \$23.4 million in the volume and in interest rate, respectively, of interest-earning assets. Interest income from loans decreased 15.2% to \$188.0 million, reflecting a decrease in both, volume and interest rate of \$17.2 million and \$16.4 million, respectively, primarily due to the \$4.1 million decrease in interest income from loans to PREPA, which was placed in non-accrual at the end of the first quarter of 2015, and PRASA, which was paid off during the second quarter of 2015, and to lower acquired loan balances and yields. Originated loans interest income increased 10.4% to \$90.5 million as balances grew 14.4% and yield contracted 23 basis points to 6.34%. Acquired non-covered loans interest income fell 24.2% to \$69.2 million as balances declined 22.1% and yield reduced 23 basis points to 8.35%. Covered loans interest income fell 41.4% to \$28.3 million as balances declined 27.0% and yield reduced 551 basis points to 22.35%. Interest income from investments decreased 32.7% to \$18.4 million, reflecting a decrease in both, volume and interest rate of \$1.9 million and \$7.1 million, respectively. Such decrease in interest income from investments reflects a decrease in investment securities from redemptions, maturities and sales, and higher premium amortization on existing securities.

Interest expense decreased 12.7% to \$34.5 million, primarily because of a \$3.7 million decrease in the volume of interest-bearing liabilities and an decrease of \$1.3 million in interest rate. The decrease in interest-bearing liabilities is mostly due to the decrease in deposits volume and interest rate of \$1.9 million and \$2.4 million, respectively, and a decrease in repurchase agreements volume of \$1.4 million which was partially offset by an increase in interest rate of \$1.1 million. The cost of deposits before fair value amortization and core deposit intangible amortization decreased 23 basis points to 0.67% for the second quarter of 2015, compared to 0.90% for the same quarter of 2014. The decrease in the cost of deposits was partially offset by an increase in the cost of borrowings, which increased 17 basis points to 2.95% from 2.78%.

The average balance of total interest-earning assets was \$6.741 billion, a decrease of 5.0% from the same period in 2014. The decrease in average balance of interest-earning assets was mainly attributable to a decrease of 7.0% in average investments and a decrease of 4.1% in average loans.

TABLE 2 - NON-INTEREST INCOME SUMMARY

| | Quarter Ended | | | Six-Month Period | | |
|--|------------------------|---------------|-----------------|------------------------|-----------------|---------------|
| | June 30, | | Variance | Ended | | Variance |
| | 2015 | 2014 | | 2015 | 2014 | |
| | (Dollars in thousands) | | | (Dollars in thousands) | | |
| Banking service revenue | \$ 10,212 | \$ 9,995 | 2.2% | \$ 20,417 | \$ 20,552 | -0.7% |
| Wealth management revenue | 7,285 | 7,336 | -0.7% | 14,440 | 14,203 | 1.7% |
| Mortgage banking activities | 1,862 | 1,554 | 19.8% | 3,725 | 3,249 | 14.7% |
| Total banking and financial service revenue | 19,359 | 18,885 | 2.5% | 38,582 | 38,004 | 1.5% |
| FDIC shared-loss expense, net: | | | | | | |
| FDIC indemnification asset expense | (22,512) | (17,499) | -28.6% | (34,733) | (35,121) | 1.1% |
| Change in true-up payment obligation | (733) | (856) | 14.4% | (1,596) | (1,721) | 7.3% |
| | (23,245) | (18,355) | -26.6% | (36,329) | (36,842) | 1.4% |
| Net gain (loss) on: | | | | | | |
| Sale of securities available for sale | - | - | 0.0% | 2,572 | 4,366 | -41.1% |
| Derivatives | 77 | (247) | 131.2% | (13) | (470) | 97.2% |
| Other non-interest (loss) income | (847) | 224 | -478.1% | (2,587) | 678 | -481.6% |
| | (24,015) | (18,378) | -30.7% | (36,357) | (32,268) | -12.7% |
| Total non-interest income, net | \$ (4,656) | \$ 507 | -1018.3% | \$ 2,225 | \$ 5,736 | -61.2% |

Non-Interest Income

Non-interest income is affected by the level of trust assets under management, transactions generated by clients' financial assets serviced by the securities broker-dealer and insurance agency subsidiaries, the level of mortgage banking activities, and the fees generated from loans and deposit accounts. It is also affected by the FDIC shared-loss expense, which varies depending on the results of the on-going evaluation of expected cash flows of the loan portfolio acquired in the FDIC-assisted acquisition. In addition, it is affected by the amount of securities, derivatives and trading transactions.

Comparison of quarters ended June 30, 2015 and 2014

As shown in Table 2 above, the Company recorded a non-interest loss in the amount of \$4.7 million, compared to an income of \$507 thousand for the same period in 2014, a decrease of 1018.3%, or \$5.1 million.

The FDIC shared-loss expense, net, increased to \$23.2 million as compared to \$18.4 million for the same period in 2014, which primarily resulted from the increase of the FDIC commercial loss share amortization related to the expiration of the non-single family loss share coverage by the FDIC. The increase is also related to the ongoing evaluation of expected cash flows of the covered loan portfolio and from changes in the fair value of the true-up payment obligation (also known as a clawback liability). The majority of the FDIC indemnification asset was recorded for projected claimable losses on non-single family residential loans whose loss share period was effective until June 30, 2015, although the recovery share period extends for an additional three-year period. The FDIC indemnification asset expense increased to \$22.5 million from \$17.5 million compared with the same quarter in 2014. The true-up

payment obligation decreased slightly to \$733 thousand as compared to \$856 thousand for the same quarter in 2014. The true-up payment obligation may increase if actual and expected losses decline. The Company measures the true-up payment obligation at fair value. Notwithstanding the expiration of loss share coverage a non-single family loans, on July 2, 2015, the Company entered into an agreement with the FDIC pursuant to which the FDIC concurred with a potential sale of a pool of loss share assets covered under the non-single family loss share agreement. Pursuant to such agreement, the FDIC agreed to pay up to \$20 million in loss share coverage with respect to the aggregate loss resulting from any portfolio sale within 120 days of the agreement.

Banking service revenue, which consists primarily of fees generated by deposit accounts, electronic banking services, and customer services, increased 2.2% to \$10.2 million, from \$10.0 million for the same period in 2014. The increase is mainly due to higher customer service revenues and checking account fees.

Wealth management revenue, which consists of commissions and fees from fiduciary activities, and securities brokerage and insurance activities, remained at \$7.3 million.

Income generated from mortgage banking activities increased 19.8% to \$1.9 million, compared to \$1.6 million for the same quarter in 2014. The increase in mortgage banking activities is mainly due to higher servicing income, higher cost or market adjustment made to mortgage loans held-for-sale and an increase in sales, partially offset by higher losses in repurchased loans, when compared to same period in 2014.

Other non-interest income declined \$1.1 million, mainly related to the sale of mortgage servicing rights consisting of loans owned by GNMA and sold to Scotiabank Puerto Rico for approximately \$7.0 million, which closed during the second quarter of 2015. The Company recognized an additional loss of \$835 thousand during the quarter related to this transaction.

Comparison of six-month periods ended June 30, 2015 and 2014

The Company recorded non-interest income in the amount of \$2.2 million, compared to \$5.7 million for the same period in 2014, a decrease of 61.2%, or \$3.5 million.

The FDIC shared-loss expense, net, decreased to \$36.3 million as compared to \$36.8 million for the same period in 2014, which resulted from the ongoing evaluation of expected cash flows of the covered loan portfolio and from changes in the fair value of the true-up payment obligation. The FDIC indemnification asset expense decreased to \$34.7 million from \$35.1 million compared with the same period in 2014. The true-up payment obligation decreased to \$1.6 million as compared to \$1.7 million for the same period in 2014. The true-up payment obligation may increase

if actual and expected losses decline. The Company measures the true-up payment obligation at fair value.

Banking service revenue, which consists primarily of fees generated by deposit accounts, electronic banking services, and customer services, decreased to \$20.4 million, from \$20.5 million for the same period in 2014. The decrease is mainly due to lower checking account fees of \$687 thousand, lower combined cycle fees, non-sufficient funds and overdrawn fees of \$695 thousand as customers shift to the “Cuenta Libre” deposit product, a decrease in branch service commissions from safe deposit box fees of \$194 thousand, and a decrease of \$208 thousand in lease servicing and other loan fees mainly from auto loans, partially offset by higher electronic banking fees of \$1.2 million.

Wealth management revenue, which consists of commissions and fees from fiduciary activities, and securities brokerage and insurance activities, increased 1.7% to \$14.4 million, compared to \$14.2 million for the same period in 2014. Such increase is mostly due to an increase of \$409 thousand from insurance income, offset by a decrease of \$236 thousand in broker-dealer commissions.

Income generated from mortgage banking activities increased 14.7% to \$3.7 million, compared to \$3.2 million for the same period in 2014. The increase in mortgage banking activities is mainly due to higher servicing income, higher cost or market adjustment made to mortgage loans held-for-sale and an increase in sales, partially offset by higher losses in repurchased loans, when compared to same period in 2014.

Gains from the sale of securities were \$2.6 million compared to \$4.4 million for the same period in 2014. Losses from derivative activities were \$13 thousand, compared to \$470 thousand for the same period in 2014.

Other non-interest income declined \$3.3 million, mainly related to the sale of mortgage servicing rights consisting of loans owned by GNMA and sold to Scotiabank Puerto Rico for approximately \$7.0 million, which closed during the second quarter of 2015. The Company recognized a loss of \$2.7 million related to this transaction.

**TABLE 3 - NON-INTEREST EXPENSES
SUMMARY**

| | Quarter Ended June 30, | | | Six-Month Period Ended June 30, | | |
|--|---------------------------|------------------|---------------|---------------------------------------|-------------------|---------------|
| | 2015 | 2014 | Variance % | 2015 | 2014 | Variance % |
| | (Dollars in thousands) | | | (Dollars in thousands) | | |
| Compensation and employee benefits | \$ 19,260 | \$ 20,707 | -7.0% | \$ 39,440 | \$ 42,494 | -7.2% |
| Professional and service fees | 4,143 | 3,512 | 18.0% | 8,324 | 7,719 | 7.8% |
| Occupancy and equipment | 8,883 | 8,605 | 3.2% | 17,519 | 16,914 | 3.6% |
| Insurance | 2,251 | 2,333 | -3.5% | 4,204 | 4,407 | -4.6% |
| Electronic banking charges | 5,851 | 4,796 | 22.0% | 11,218 | 9,449 | 18.7% |
| Information technology expenses | 1,543 | 1,485 | 3.9% | 2,997 | 3,300 | -9.2% |
| Advertising, business promotion, and strategic initiatives | 1,558 | 1,669 | -6.7% | 3,186 | 3,450 | -7.7% |
| Foreclosure, repossession and other real estate expenses | 10,337 | 6,656 | 55.3% | 15,783 | 13,043 | 21.0% |
| Loan servicing and clearing expenses | 2,594 | 1,669 | 55.4% | 4,947 | 3,728 | 32.7% |
| Taxes, other than payroll and income taxes | 2,703 | 3,776 | -28.4% | 4,182 | 7,511 | -44.3% |
| Communication | 770 | 813 | -5.3% | 1,460 | 1,770 | -17.5% |
| Printing, postage, stationery and supplies | 582 | 645 | -9.8% | 1,219 | 1,200 | 1.6% |
| Director and investor relations | 289 | 293 | -1.4% | 583 | 544 | 7.2% |
| Other operating expenses | 3,673 | 2,889 | 27.1% | 5,707 | 5,723 | -0.3% |
| Total non-interest expenses | \$ 64,437 | \$ 59,848 | 7.7% | \$ 120,769 | \$ 121,252 | -0.4% |
| Relevant ratios and data: | | | | | | |
| Efficiency ratio | 63.39% | 47.89% | | 57.37% | 48.99% | |
| Compensation and benefits to non-interest expense | 29.89% | 34.60% | | 32.66% | 35.05% | |
| Compensation to average total assets owned | 1.05% | 1.07% | | 1.07% | 1.08% | |
| Average number of employees | 1,509 | 1,566 | | 1,509 | 1,559 | |
| Average compensation per employee | \$ 12.8 | \$ 13.2 | | \$ 26.1 | \$ 27.3 | |
| Average loans per average employee | \$ 3,147 | \$ 3,205 | | \$ 3,185 | \$ 3,216 | |

Non-Interest Expenses

Comparison of quarters ended June 30, 2015 and 2014

Non-interest expense for the quarter was \$64.4 million, representing an increase of 7.7% compared to \$59.8 million in the same quarter of the previous year.

Foreclosure, repossession and other real estate expenses increased 55.3% to \$10.3 million, as compared to \$6.7 million in the same period of the previous year, principally due to a \$2.9 million increase in other real estate owned and mortgage properties markdowns, as part of ongoing and proactive de-risking efforts.

Electronic banking charges increased 22.0% to \$5.9 million, mostly due to the increase in expenses related to merchant business and card interchange transactions resulting from the continued growth of our banking business.

Loan servicing and clearing expenses increased 55.4% or \$925 thousand to \$2.6 million from \$1.7 million for the same quarter in 2014, mainly to an increase of \$901 thousand in servicing expenses.

The increases in the foregoing non-interest expenses were partially offset by decreases in compensation and employee benefits and in taxes, other than payroll and income taxes.

Compensation and employee benefits decreased 7.0% to \$19.3 million from \$20.7 million for the second quarter of 2014. The decrease is due mainly to lower salaries and lower benefits as a result of a headcount reduction.

Taxes, other than payroll and income taxes decreased by \$1.1 million or 28.4%, mostly due to a decrease of \$1.3 million in the local gross receipts tax that was repealed for taxable years commencing after December 31, 2014.

Efficiency ratio was 63.39% compared to 47.89% for the same period in 2014. The efficiency ratio measures how much of the Company's revenues is used to pay operating expenses. The Company computes its efficiency ratio by dividing non-interest expenses by the sum of its net interest income and non-interest income, but excluding gains on the sale of investment securities, derivatives gains or losses, credit-related other-than-temporary impairment losses, FDIC shared-loss expense, losses on the early extinguishment of debt, other gains and losses, and other income that may be considered volatile in nature. Management believes that the exclusion of those items permits consistent comparability. Amounts presented as part of non-interest (losses) income that are excluded from the efficiency ratio computation amounted to losses of \$24.0 million, compared to \$18.4 million for the same quarter of 2014.

Comparison of six-month periods ended June 30, 2015 and 2014

Non-interest expense for the six-month period was \$120.8 million, representing a decrease of 0.4% compared to \$121.3 million in the same period of the previous year.

Compensation and employee benefits decreased 7.2% to \$39.4 million from \$42.5 million for the same period of 2014. The decrease is due mainly to lower salaries and lower benefits as a result of a headcount reduction from 1,559 to 1,509 as a result of the voluntary early retirement program offered by the Company in December 2014 for qualified employees as a cost savings initiative.

Taxes, other than payroll and income taxes decreased by \$3.3 million or 44.32%, mostly due to a decrease of \$3.9 million in the local gross receipts tax that was repealed for taxable years commencing after December 31, 2014.

The decreases in the foregoing non-interest expenses were partially offset by increases in foreclosure, repossession and other real estate, electronic banking charges and loan servicing and clearing expenses.

Foreclosure, repossession and other real estate expenses increased 21.01% to \$15.8 million, as compared to \$13.0 million in the same period for the previous year, principally due to a \$3.0 million increase in other real estate owned and mortgage properties markdowns, as part of our ongoing and proactive de-risking efforts.

Electronic banking charges increased 18.7% to \$11.2 million, mostly due to the increase in expenses related to merchant business and card interchange transactions resulting from the continued growth of our banking business.

Loan servicing and clearing expenses increased 32.7% or \$1.2 million to \$4.9 million from \$3.7 million for the same period in 2014, mainly due to an increase of \$850 thousand in servicing expenses and \$327 thousand in mortgage servicing migration.

Efficiency ratio was 57.37% compared to 48.99% for the same period in 2014. The efficiency ratio measures how much of the Company's revenues is used to pay operating expenses. The Company computes its efficiency ratio by dividing non-interest expenses by the sum of its net interest income and non-interest income, but excluding gains on the sale of investment securities, derivatives gains or losses, credit-related other-than-temporary impairment losses, FDIC shared-loss expense, losses on the early extinguishment of debt, other gains and losses, and other income that may be considered volatile in nature. Management believes that the exclusion of those items permits consistent comparability. Amounts presented as part of non-interest (losses) income that are excluded from the efficiency ratio computation amounted to losses of \$36.4 million, compared to \$32.3 million for the same period of 2014.

Provision for Loan and Lease Losses

Comparison of quarters ended June 30, 2015 and 2014

Provision for non-covered loan and lease losses increased 18.33%, or \$2.4 million, to \$15.6 million from \$13.2 million when compared with the same period in 2014. Management determined that no additional PREPA provision was required on the PREPA line of credit due to the ongoing active negotiation of a repayment agreement.

Management also determined that no additional provision was required on FDIC covered commercial loans for the second quarter of 2015, compared to \$1.6 million for the same quarter of 2014, as loss-share agreement with the FDIC for non-single family loans was in effect until June 30, 2015.

Based on an analysis of the credit quality and the composition of the Company's loan portfolio, management determined that the provision for the quarter was adequate in order to maintain the allowance for loan and lease losses at an adequate level to provide for probable losses based upon an evaluation of known and inherent risks.

Provision for non-covered loans, excluding acquired loans, increased 33.9% to \$10.0 million from \$7.4 million when compared with the same quarter in 2014.

Total charge-offs on non-covered loans, excluding acquired loans, increased 33.1% to \$11.8 million, as compared to \$8.9 million for the same quarter in 2014. Auto and leasing charge-offs increased \$1.7 million to \$7.7 million and

consumer charge-offs increased \$912 thousand to \$2.3 million.

Total recoveries on non-covered loans, excluding acquired loans, increased from \$1.1 million to \$3.8 million. As a result, the recoveries to charge-offs ratio increased from 30.41% to 31.95%. Net credit losses, excluding acquired loans, increased \$1.9 million to \$8.0 million, representing 1.10% of average non-covered loans outstanding versus 0.94% for the same quarter in 2014, annualized.

The non-covered acquired loans accounted for under ASC 310-20 required a provision for loan and lease losses of \$1.5 million, as compared to \$2.6 million for the same period in 2014.

Non-covered acquired loans accounted for under ASC 310-30 required a provision for loan and lease losses of \$4.2 million, as compared to \$3.2 million for the same quarter in 2014. No provision was required on FDIC covered commercial loans for the second quarter of 2015, compared to \$1.6 million for the same quarter in 2014. The provision for loan and lease losses for loans accounted for under ASC 310-30 reflects the Company's revision of the expected cash flows in the covered loan portfolio considering actual experiences and changes in the Company's expectations for the remaining terms of the loan pools.

Comparison of six-month periods ended June 30, 2015 and 2014

Provision for non-covered loan and lease losses increased 127.8%, or \$29.7 million, to \$53.0 million from \$23.3 million when compared with the same period in 2014. Such increase was primarily due to the classification of \$200 million participation in the PREPA line of credit on non-accrual status and the recognition of a \$24.0 million provision for loan and lease losses on such line during the first quarter of 2015.

Provision for covered loan and lease losses increased 45.9% to \$4.7 million from \$3.2 million when compared to the same period in 2014. Provision for the six-month period ended in 2015 included an additional \$3.5 million provision for covered loan and lease losses related to the commercial shared loss coverage with the FDIC, which was effective until June 30, 2015.

Based on an analysis of the credit quality and the composition of the Company's loan portfolio, management determined that the provision for the six-month period ended June 30, 2015 was adequate in order to maintain the allowance for loan and lease losses at an adequate level to provide for probable losses based upon an evaluation of known and inherent risks.

Provision for non-covered loans, excluding acquired loans, increased 236.0% to \$43.9 million from \$13.1 million when compared with the same period in 2014. This was the result of the aforementioned \$24.0 million provision for loan and lease losses taken on the PREPA line of credit during the first quarter of 2015.

Total charge-offs on non-covered loans, excluding acquired loans, increased 50.3% to \$24.0 million, as compared to \$16.0 million for the same period in 2014. Auto and leasing charge-offs increased \$5.2 million to \$15.8 million and consumer charge-offs increased \$1.8 million to \$4.0 million.

Total recoveries increased from \$4.5 million to \$7.7 million. As a result, the recoveries to charge-offs ratio increased from 28.13% to 32.14%. Net credit losses, excluding acquired loans, increased \$4.8 million to \$16.3 million, representing 1.15% of average non-covered loans outstanding versus 0.91% for the same period in 2014, annualized.

The non-covered acquired loans accounted for under ASC 310-20 required a provision for loan and lease losses of \$4.3 million, as compared to \$6.8 million for the same period in 2014.

Non-covered acquired loans accounted for under ASC 310-30 required a provision for loan and lease losses of \$4.9 million, as compared to \$3.4 million for the same period in 2014. Provision for covered loan and lease losses was \$4.7 million, compared to \$3.2 million for the same period in 2014. The provision for loan and lease losses for loans

accounted for under ASC 310-30 reflects the Company's revision of the expected cash flows in the covered loan portfolio considering actual experiences and changes in the Company's expectations for the remaining terms of the loan pools.

Income Taxes

Comparison of quarters ended June 30, 2015 and 2014

Income tax expense decreased \$9.8 million to \$769 thousand, compared to \$10.6 million for the same quarter in 2014. Decrease in income tax expense reflects the net loss before income taxes of \$2.3 million for the quarter, compared to net income before income taxes of \$32.0 million for the year ago quarter.

Comparison of six-month periods ended June 30, 2015 and 2014

Income tax expense decreased \$20.7 million to \$1.7 million, compared to \$22.4 million for the same period in 2014. Decrease in income tax expense reflects the net loss before income taxes of \$4.3 million for the six-month period ended June 30, 2015, compared to net income before income taxes of \$67.5 million for the year ago six-month period.

Business Segments

The Company segregates its businesses into the following major reportable segments: Banking, Wealth Management, and Treasury. Management established the reportable segments based on the internal reporting used to evaluate performance and to assess where to allocate resources. Other factors such as the Company's organization, nature of its products, distribution channels and economic characteristics of the products were also considered in the determination of the reportable segments. The Company measures the performance of these reportable segments based on pre-established goals of different financial parameters such as net income, net interest income, loan production, and fees generated. The Company's methodology for allocating non-interest expenses among segments is based on several factors such as revenue, employee headcount, occupied space, dedicated services or time, among others. Following are the results of operations and the selected financial information by operating segment for the quarters and six-month periods ended June 30, 2015 and 2014:

| | Quarter Ended June 30, 2015 | | | | | | Consolidated Total |
|---|-----------------------------|----------------------|---------------------|-------------------------|------------------|-----------|-----------------------|
| | Banking | Wealth Management | Treasury | Total Major Segments | Eliminations | | |
| | (In thousands) | | | | | | |
| Interest income | \$ 90,504 | \$ 24 | \$ 8,885 | \$ 99,413 | \$ - | \$ | 99,413 |
| Interest expense | (7,110) | - | (10,011) | (17,121) | - | - | (17,121) |
| Net interest income | 83,394 | 24 | (1,126) | 82,292 | - | - | 82,292 |
| Provision for non-covered loan and lease losses | (15,644) | - | - | (15,644) | - | - | (15,644) |
| Provision for covered loan and lease losses | 105 | - | - | 105 | - | - | 105 |
| Non-interest income (loss) | (11,713) | 6,893 | 164 | (4,656) | - | - | (4,656) |
| Non-interest expenses | (56,844) | (6,733) | (860) | (64,437) | - | - | (64,437) |
| Intersegment revenue | 163 | - | 61 | 224 | (224) | - | - |
| Intersegment expenses | (61) | (87) | (76) | (224) | 224 | - | - |
| Income before income taxes | \$ (600) | \$ 97 | \$ (1,837) | \$ (2,340) | \$ - | \$ | (2,340) |
| Total assets | \$ 6,153,663 | \$ 21,157 | \$ 2,136,293 | \$ 8,311,113 | (912,788) | \$ | 7,398,325 |

| | Quarter Ended June 30, 2014 | | | | | | Consolidated Total |
|---------------------|-----------------------------|----------------------|-----------|-------------------------|--------------|----|-----------------------|
| | Banking | Wealth Management | Treasury | Total Major Segments | Eliminations | | |
| | (In thousands) | | | | | | |
| Interest income | \$ 112,971 | \$ 46 | \$ 12,883 | \$ 125,900 | \$ - | \$ | 125,900 |
| Interest expense | (10,828) | - | (8,994) | (19,822) | - | - | (19,822) |
| Net interest income | 102,143 | 46 | 3,889 | 106,078 | - | - | 106,078 |

Provision for
non-covered

| | | | | | | |
|-----------------------------|--------------|-----------|--------------|--------------|-----------|--------------|
| loan and lease losses | (13,220) | - | - | (13,220) | - | (13,220) |
| Provision for covered | | | | | | |
| loan and lease losses | (1,595) | - | - | (1,595) | - | (1,595) |
| Non-interest income | | | | | | |
| (loss) | (6,507) | 7,502 | (488) | 507 | - | 507 |
| Non-interest expenses | (49,651) | (6,367) | (3,830) | (59,848) | - | (59,848) |
| Intersegment revenue | 435 | - | - | 435 | (435) | - |
| Intersegment expenses | - | (327) | (108) | (435) | 435 | - |
| Income before income | | | | | | |
| taxes | \$ 31,605 | \$ 854 | \$ (537) | \$ 31,922 | \$ - | \$ 31,922 |
| Total assets | \$ 6,508,432 | \$ 25,345 | \$ 2,089,516 | \$ 8,623,293 | (913,148) | \$ 7,710,145 |

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Six-Month Period Ended June 30, 2015

| | Wealth | | Total | | Consolidated | |
|--|-------------------|-----------------|-------------------|-------------------|--------------|-------------------|
| | Banking | Management | Treasury | Major Segment | | Eliminations |
| | (In thousands) | | | | | Total |
| Interest income | \$ 187,986 | \$ 47 | \$ 18,381 | \$ 206,414 | \$ - | \$ 206,414 |
| Interest expense | (14,564) | - | (19,923) | (34,487) | - | (34,487) |
| Net interest income | 173,422 | 47 | (1,542) | 171,927 | - | 171,927 |
| Provision for non-covered loan and lease losses | (53,027) | - | - | (53,027) | - | (53,027) |
| Provision for covered loan and lease losses, net | (4,705) | - | - | (4,705) | - | (4,705) |
| Non-interest income(loss) | (13,962) | 13,903 | 2,284 | 2,225 | - | 2,225 |
| Non-interest expenses | (106,156) | (11,524) | (3,089) | (120,769) | - | (120,769) |
| Intersegment revenue | 707 | - | 160 | 866 | (866) | - |
| Intersegment expenses | (159) | (518) | (189) | (866) | 866 | - |
| Income before income taxes | \$ (3,880) | \$ 1,908 | \$ (2,376) | \$ (4,349) | \$ - | \$ (4,349) |

Six-Month Period Ended June 30, 2014

| | Wealth | | Total | | Consolidated | |
|--|------------------|-----------------|-----------------|------------------|--------------|------------------|
| | Banking | Management | Treasury | Major Segment | | Eliminations |
| | (In thousands) | | | | | Total |
| Interest income | \$ 221,602 | \$ 86 | \$ 27,286 | \$ 248,974 | \$ - | \$ 248,974 |
| Interest expense | (18,344) | - | (21,154) | (39,498) | - | (39,498) |
| Net interest income | 203,258 | 86 | 6,132 | 209,476 | - | 209,476 |
| Provision for non-covered loan and lease losses | (23,282) | - | - | (23,282) | - | (23,282) |
| Provision for covered loan and lease losses, net | (3,224) | - | - | (3,224) | - | (3,224) |
| Non-interest income(loss) | (11,603) | 14,024 | 3,315 | 5,736 | - | 5,736 |
| Non-interest expenses | (103,198) | (11,146) | (6,908) | (121,252) | - | (121,252) |
| Intersegment revenue | 979 | - | - | 979 | (979) | - |
| Intersegment expenses | - | (759) | (220) | (979) | 979 | - |
| Income (loss) before income taxes | \$ 62,930 | \$ 2,205 | \$ 2,319 | \$ 67,454 | \$ - | \$ 67,454 |

*Comparison of quarters ended June 30, 2015 and 2014***Banking**

Net interest income of the Company's Banking segment decreased \$18.7 million for the second quarter of 2015, or 18.4%, reflecting a decrease of 19.9% in interest income from loans. Interest income from loans reflects a decrease in both, volume and interest rate by \$10.9 million and \$11.5 million, respectively, primarily due to a decrease of \$4.1 million in interest income from loans to PREPA, which was placed in non-accrual at the end of the first quarter of 2015, and PRASA, which was paid off during the second quarter of 2015, and to lower acquired loan balances and yields.

Provision for non-covered loans losses increased \$2.4 million when compared to \$13.2 million for the second quarter of 2014. During the second quarter of 2015 no provision was registered, representing a decrease of 107% when compared to the second quarter of 2014, as a result of the commercial shared loss coverage with the FDIC that ended on June 30, 2015.

Banking service revenue, which consists primarily of fees generated by deposit accounts, electronic banking services, and customer services, slightly increased 2.2% to \$10.2 million, from \$10.0 million for the same period in 2014. The increase is mainly due to higher customer service revenues and checking account fees.

During the quarter ended June 30, 2015, the Company recognized a loss of \$835 thousand related to the sale of its mortgage servicing rights to Scotiabank Puerto Rico. It is included as other non-interest (loss) income.

During the second quarter of 2015 the FDIC indemnification asset expense increased by \$5.0 million to \$22.5 million from \$17.5 million for the quarter in 2014. The majority of the FDIC indemnification asset is recorded for projected claimable losses whose loss share period was in effect until June 30, 2015, although the recovery share period extends for an additional three-year period. During the second quarter of 2015, the true-up payment obligation decreased by \$123 thousand when compared to an \$856 thousand decrease in the same quarter in 2014. The true-up payment obligation may increase if actual and expected losses decline.

Non-interest expense of \$56.8 million increased \$7.2 million or 14.5% when compared to the same period in 2014. The increase in non-interest expense is mainly due to foreclosure, repossession and other real estate expenses increase of 55.3% to \$10.3 million, as compared to \$6.7 million in the same period for the previous year, principally due to a \$2.9 increase in markdown of foreclosed real estate. In addition, electronic banking charges increased \$1.1 million, mainly from merchant business and debit/credit card interchange transactions as our banking business continues to grow.

Wealth Management

Wealth management revenue, which consists of commissions and fees from fiduciary activities, and securities brokerage and insurance activities, decreased 8% when compared with the second quarter in 2014. Decline in this business segment is mostly due to a decrease of \$131 thousand in public finance fees.

Non-interest expenses increased by 5.7% to \$6.8 million, due to a payment of \$2.1 million required by our broker-dealer's regulator, partially offset by a decrease in commissions paid when compared to the same period in 2014.

Treasury

Interest income from investments decreased 31.2% to \$8.9 million, reflecting a decrease in interest rate of \$4.1 million. Such decrease in interest income from investments reflects a higher premium amortization on existing securities.

Non-interest expenses, mainly composed of indirect expenses allocated from support departments decreased 75.8% to \$860 thousand as part of the Company's cost reduction strategy.

Comparison of six-month periods ended June 30, 2015 and 2014

Banking

Net interest income of the Company's Banking segment decreased \$29.8 million for the six-month period ended June 30, 2015, or 14.7%, reflecting a decrease of 15.2% in interest income from loans. Interest income from loans reflects a decrease in volume and interest rate by \$17.2 million and \$16.4 million, respectively, primarily due to a decrease of \$4.1 million in interest income from the loan to PREPA, which was placed in non-accrual at the end of the first quarter of 2015, and the loan to PRASA, which was paid off during the second quarter of 2015, and to lower acquired loan balances and yields.

Provision for non-covered loans losses increased \$29.7 million to \$53.0 million when compared to \$23.3 million for the same period in 2014. During the first quarter of 2015, the Company recorded an additional provision for loan and lease losses of \$24 million related to its participation in the line of credit to PREPA. Provision for covered loans losses decreased \$1.5 million when compared to the same period of 2014, as a result of the commercial shared loss agreement with the FDIC which ended on June 30, 2015.

Banking service revenue, which consists primarily of fees generated by deposit accounts, electronic banking services, and customer services, slightly decreased to \$20.4 million, from \$20.5 million for the same period in 2014. The decrease is mainly due to lower checking account fees of \$687 thousand, lower combined cycle fees, non-sufficient funds and overdrawn fees of \$695 thousand as customers shift to the “Cuenta Libre” deposit product, a decrease in branch service commissions from safe deposit box fees of \$194 thousand, and a decrease of \$208 thousand in lease servicing and other loan fees mainly from auto loans, partially offset by higher electronic banking fees of \$1.2 million.

During the six-month period ended June 30, 2015, the Company recognized a loss of \$835 thousand related to the sale of its mortgage servicing assets to Scotiabank Puerto Rico. It is included as other non-interest (loss) income.

During the six-month periods ended June 30, 2015 and 2014, the FDIC indemnification asset expense slightly decreased to \$34.7 million from \$35.1 million for the same period in 2014. The majority of the FDIC indemnification asset is recorded for projected claimable losses on whose loss share period was in effect until June 30, 2015, although the recovery share coverage extends for an additional three-year period. During the six-month period ended June 30, 2015, the change in the true-up payment obligation decreased slightly by \$1.6 million as compared to a \$1.7 million decrease for the same period in 2014. The true-up payment obligation may increase if actual and expected losses decline.

Non-interest expense of \$106.2 million increased 2.9% when compared to the same period in 2014. The increase in non-interest expense is mainly due to an increase in foreclosure, repossession and other real estate expenses of 21.0% to \$15.8 million, as compared to \$13.0 million in the same period for the previous year, principally due to a \$3.0 million increase in markdown of foreclosed real estate, as part of de-risking efforts during the second quarter of 2015. In addition, electronic banking charges increased \$1.8 million, mainly from merchant business and credit/debit card interchange transactions as our banking business continues to grow.

Wealth Management

Wealth management revenue, which consists of commissions and fees from fiduciary activities, and securities brokerage and insurance activities, remained leveled at \$14 million compared to the same period in 2014.

Non-interest expenses increased by 3.4% to \$11.5 million, due to a payment of \$2.1 million required by our broker-dealer’s regulator, partially offset by a decrease in commissions paid when compared to the same period in 2014.

Treasury

The investment portfolio of \$1.616 billion at June 30, 2015 increased 15.3% compared to \$1.402 billion at December 31, 2014. Interest income from investments decreased 32.7% to \$18.4 million, reflecting a decrease in both, volume and interest rate of \$1.9 million and \$7.1 million, respectively. Such decrease in interest income from investments reflects a higher premium amortization on existing securities.

ANALYSIS OF FINANCIAL CONDITION

Assets Owned

At June 30, 2015, the Company's total assets amounted to \$7.398 billion representing a decrease of 0.7% when compared to \$7.449 billion at December 31, 2014. This reduction is mainly due to a decrease in the loan portfolio. The loan portfolio decreased \$187.2 million from \$4.827 billion at December 31, 2014 to \$4.639 billion, which included the full repayment of the \$75 million loan to PRASA during the quarter ended June 30, 2015. Investments securities increased \$214.4 million from \$1.402 billion at December 31, 2014 to \$1.616 billion.

At June 30, 2015, loans represented 74% of total interest-earning assets while investments represented 26%, compared to 77% and 23%, respectively, at December 31, 2014.

The Company's loan portfolio is comprised of residential mortgage loans, commercial loans collateralized by mortgages on real estate located in Puerto Rico, other commercial and industrial loans, consumer loans, and auto loans. At June 30, 2015, the Company's loan portfolio decreased by 4% to \$4.639 billion compared to \$4.827 billion at December 31, 2014, primarily due to lower acquired loan balances. Our loan portfolio is transitioning as originated loans grow at a slower pace than acquired loans decrease, due to repayments and maturities and the Company continues to reduce its exposure to the Puerto Rico government. At June 30, 2015, the originated loan portfolio increased \$113.0 million, or 4.0%, the acquired non-covered loan portfolio decreased \$196.0 million, or 11.3%, and the covered loan portfolio decreased \$76.9 million, or 25.7% from December 31, 2014.

The FDIC indemnification asset amounted to \$23.0 million at June 30, 2015 and \$97.4 million as of December 31, 2014, representing a 76.7% reduction. The decrease in the FDIC indemnification asset is mainly related to collections and the amortization of the FDIC indemnification asset of \$24.4 million and \$22.5 million, respectively, for the second quarter ended June 30, 2015, as loss-share period for non-single family loans was effective until June 30, 2015.

Investments principally consist of U.S. government and agency bonds, mortgage-backed securities, and Puerto Rico government and agency bonds. At June 30, 2015, the investment portfolio increased 15.3% to \$1.616 billion from \$1.402 billion at December 31, 2014. During the quarter ended June 30, 2015 the Company sold \$101.3 million of mortgage-backed securities available for sale and reduced some interest rate sensitivity. Recent purchases of investment securities were categorized as held-to-maturity. The Company's management will determine the category of upcoming investment securities purchases based on the Company's expectations at such time.

Financial Assets Managed

The Company's financial assets managed include those managed by the Company's trust division, retirement plan administration subsidiary, and assets gathered by its broker-dealer subsidiary. The Company's trust division offers various types of IRAs and manages 401(k) and Keogh retirement plans and custodian and corporate trust accounts, while the retirement plan administration subsidiary, OPC, manages private retirement plans. At June 30, 2015, total assets managed by the Company's trust division and OPC amounted to \$2.793 billion, compared to \$2.841 billion at December 31, 2014. Oriental Financial Services offers a wide array of investment alternatives to its client base, such as tax-advantaged fixed income securities, mutual funds, stocks, bonds and money management wrap-fee programs. At June 30, 2015, total assets gathered by Oriental Financial Services from its customer investment accounts decreased to \$2.555 billion, compared to \$2.622 billion at December 31, 2014. Changes in trust and broker-dealer related assets primarily reflect an increase in portfolio and differences in market values.

TABLE 4 - ASSETS SUMMARY AND COMPOSITION

| | June 30 2015 | December 31 2014 | Variance % |
|--|---------------------|---------------------|---------------|
| (Dollars in thousands) | | | |
| Investments: | | | |
| FNMA and FHLMC certificates | \$ 1,387,077 | \$ 1,172,262 | 18.3% |
| Obligations of US government-sponsored agencies | 6,128 | 7,182 | -14.7% |
| US Treasury securities | 25,049 | - | 100.0% |
| CMOs issued by US government-sponsored agencies | 155,046 | 176,129 | -12.0% |
| GNMA certificates | 3,874 | 4,752 | -18.5% |
| Puerto Rico government and public instrumentalities | 14,729 | 15,671 | -6.0% |
| FHLB stock | 20,826 | 21,169 | -1.6% |
| Other debt securities | 2,969 | 3,294 | -9.9% |
| Other investments | 789 | 1,597 | -50.6% |
| Total investments | 1,616,487 | 1,402,056 | 15.3% |
| Loans: | | | |
| Non-covered loans | 4,499,542 | 4,582,713 | -1.8% |
| Allowance for loan and lease losses on non-covered loans | (102,877) | (69,517) | 48.0% |
| Non-covered loans receivable, net | 4,396,665 | 4,513,196 | -2.6% |
| Mortgage loans held for sale | 20,768 | 14,539 | 42.8% |
| Total non-covered loans, net | 4,417,433 | 4,527,735 | -2.4% |
| Covered loans | 293,486 | 363,156 | -19.2% |
| Allowance for loan and lease losses on covered loans | (71,452) | (64,245) | 11.2% |
| Total covered loans, net | 222,034 | 298,911 | -25.7% |
| Total loans, net | 4,639,467 | 4,826,646 | -3.9% |
| Total securities and loans | 6,255,954 | 6,228,702 | 0.4% |
| Other assets: | | | |
| Cash and due from banks (including restricted cash) | 553,826 | 577,159 | -4.0% |
| Money market investments | 5,795 | 4,675 | 24.0% |
| FDIC indemnification asset | 22,704 | 97,378 | -76.7% |
| Foreclosed real estate | 81,333 | 95,661 | -15.0% |
| Accrued interest receivable | 19,254 | 21,345 | -9.8% |
| Deferred tax asset, net | 138,406 | 108,708 | 27.3% |
| Premises and equipment, net | 76,486 | 80,599 | -5.1% |
| Servicing assets | 5,791 | 13,992 | -58.6% |
| Derivative assets | 4,376 | 8,107 | -46.0% |
| Goodwill | 86,069 | 86,069 | 0.0% |
| Other assets and customers' liability on acceptances | 148,331 | 126,714 | 17.1% |
| Total other assets | 1,142,371 | 1,220,407 | -6.4% |
| Total assets | \$ 7,398,325 | \$ 7,449,109 | -0.7% |
| Investments portfolio composition: | | | |
| FNMA and FHLMC certificates | 85.9% | 83.7% | |
| Obligations of US government-sponsored agencies | 0.4% | 0.5% | |
| US Treasury securities | 1.5% | 0.0% | |
| CMOs issued by US government-sponsored agencies | 9.6% | 12.6% | |
| GNMA certificates | 0.2% | 0.3% | |
| Puerto Rico government and public instrumentalities | 0.9% | 1.1% | |

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| | | |
|---|---------------|---------------|
| FHLB stock | 1.3% | 1.5% |
| Other debt securities and other investments | 0.2% | 0.3% |
| | 100.0% | 100.0% |

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TABLE 5 — LOANS RECEIVABLE COMPOSITION

| | June 30 2015 | December 31 2014 | Variance % |
|---|------------------------|------------------------|---------------|
| | (Dollars in thousands) | | |
| Non-covered loans: | | | |
| Originated and other loans and leases held for investment: | | | |
| Mortgage | \$ 757,187 | \$ 791,751 | -4.4% |
| Commercial | 1,363,851 | 1,289,732 | 5.7% |
| Consumer | 212,629 | 186,760 | 13.9% |
| Auto and leasing | 623,198 | 575,582 | 8.3% |
| Total originated and other loans and leases held for investment | 2,956,865 | 2,843,825 | 4.0% |
| Acquired loans: | | | |
| Accounted for under ASC 310-20 | | | |
| Commercial | 8,448 | 12,675 | -33.3% |
| Consumer | 41,505 | 45,344 | -8.5% |
| Auto | 142,570 | 184,782 | -22.8% |
| | 192,523 | 242,801 | -20.7% |
| Accounted for under ASC 310-30 | | | |
| Mortgage | 631,807 | 656,122 | -3.7% |
| Commercial | 406,447 | 452,201 | -10.1% |
| Construction | 93,263 | 106,361 | -12.3% |
| Consumer | 18,869 | 29,888 | -36.9% |
| Auto | 195,891 | 247,233 | -20.8% |
| | 1,346,277 | 1,491,805 | -9.8% |
| Allowance for loan and lease losses on non-covered loans accounted for under ASC -30 | (18,359) | (13,481) | -36.2% |
| | 1,327,918 | 1,478,324 | -10.2% |
| | 1,520,441 | 1,721,125 | -11.7% |
| | 4,477,306 | 4,564,950 | -1.9% |
| Deferred loans fees, net | 3,877 | 4,282 | -9.5% |
| Loans receivable | 4,481,183 | 4,569,232 | -1.9% |
| Allowance for loan and lease losses on loans not accounted for under ASC 310-30 | (84,518) | (56,036) | -50.8% |
| Loans receivable, net | 4,396,665 | 4,513,196 | -2.6% |
| Mortgage loans held-for-sale | 20,768 | 14,539 | 42.8% |
| Total non-covered loans, net | 4,417,433 | 4,527,735 | -2.4% |
| Covered loans: | | | |
| Loans secured by 1-4 family residential properties | 117,840 | 117,171 | 0.6% |
| Construction and development secured by 1-4 family residential properties | 19,152 | 19,562 | -2.1% |
| Commercial and other construction | 153,199 | 221,917 | -31.0% |
| Consumer | 3,295 | 4,506 | -26.9% |
| Total covered loans | 293,486 | 363,156 | -19.2% |
| Allowance for loan and lease losses on covered loans | (71,452) | (64,245) | -11.2% |
| Total covered loans, net | 222,034 | 298,911 | -25.7% |
| Total loans receivable, net | \$ 4,639,467 | \$ 4,826,646 | -3.9% |

As shown in Table 5 above, total loans, net, amounted to \$4.639 billion at June 30, 2015 and \$4.827 billion at December 31, 2014.

The Company's originated and other loans held-for-investment portfolio composition and trends were as follows:

- Mortgage loan portfolio amounted to \$757.2 million (25.6% of the gross originated loan portfolio) compared to \$791.8 million (27.8% of the gross originated loan portfolio) at December 31, 2014. Mortgage loan production totaled \$64.8 million and \$126.5 million for the quarter and six-month period ended June 30, 2015, respectively, which represents an increase of 24.6% and 23.1% from \$52.0 million and \$102.8 million for the same periods in 2014. Mortgage loans included delinquent loans in the GNMA buy-back option program amounting to \$7.0 million and \$42.2 million for the periods ended June 30, 2015 and December 31, 2014, respectively. Servicers of loans underlying GNMA mortgage-backed securities must report as their own assets the defaulted loans that they have the option (but not the obligation) to repurchase, even when they elect not to exercise that option. The decrease is mostly due to the sale of mortgage servicing rights of most of these loans to Scotiabank de Puerto Rico during the second quarter of 2015.
- Commercial loan portfolio amounted to \$1.364 billion (46.1% of the gross originated loan portfolio) compared to \$1.290 billion (45.4% of the gross originated loan portfolio) at December 31, 2014. Commercial loan production increased 165.2% to \$120.5 million for the second quarter of 2015 from \$45.4 million for the same period in 2014, and 142.0% to \$206.2 million for the six-month period ended June 30, 2015 from \$85.2 million for the same period in 2014.
- Consumer loan portfolio amounted to \$212.6 million (7.2% of the gross originated loan portfolio) compared to \$186.8 million (6.6% of the gross originated loan portfolio) at December 31, 2014. Consumer loan production increased 15.4% to \$39.8 million for the quarter ended June 30, 2015 from \$34.5 million for the same period in 2014, and 5.9% to \$66.0 million for the six-month period ended June 30, 2015 from \$62.3 million for the same period in 2014.
- Auto loans and leasing portfolio amounted to \$623.2 million (21.1% of the gross originated loan portfolio) compared to \$575.6 million (20.2% of the gross originated loan portfolio) at December 31, 2014. Auto production was \$61.5 million for the quarter ended June 30, 2015 and \$127.5 million for the six-month period ended June 30, 2015 compared to \$89.6 million and \$183.4 million for the same period in 2014.

At June 30, 2015 and December 31, 2014, the Company's non-covered acquired loan portfolio composition was as follows:

| Portfolio Type | June 30, 2015 | | December 31, 2014 | |
|----------------|------------------|--|-------------------|--|
| | Carrying Amounts | % of Gross Non-Covered Acquired Loan Portfolio | Carrying Amounts | % of Gross Non-Covered Acquired Loan Portfolio |
| | | | | |

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| | | | | (Dollars in thousands) |
|------------|----|------------------|--|-------------------------------|
| Mortgage | \$ | 631,334 | | 41.5% \$ 656,122 |
| Commercial | | 493,218 | | 32.4% 557,761 |
| Consumer | | 60,290 | | 4.0% 75,227 |
| Auto | | 335,599 | | 22.1% 432,015 |
| | \$ | 1,520,441 | | 100.00% \$ 1,721,125 |

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TABLE 6 — HIGHER RISK RESIDENTIAL MORTGAGE LOANS

| | June 30, 2015 | | | | | | | | |
|--|--|------------------|-----------------|----------------------------|------------------|-----------------|---------------------------------|------------------|-----------------|
| | Higher-Risk Residential Mortgage Loans* | | | | | | | | |
| | Junior Lien Mortgages | | | Interest Only Loans | | | High Loan-to-Value Ratio | | |
| | Carrying | | | Carrying | | | Mortgages | | |
| | Value | Allowance | Coverage | Value | Allowance | Coverage | LTV 90% and over | Carrying | Coverage |
| | Value | Allowance | Coverage | Value | Allowance | Coverage | Value | Allowance | Coverage |
| | (In thousands) | | | | | | | | |
| <u>Delinquency:</u> | | | | | | | | | |
| 0 - 89 days | \$ 12,697 | \$ 258 | 2.03% | \$ 20,012 | \$ 425 | 2.12% | \$ 94,121 | \$ 1,909 | 2.03% |
| 90 - 119 days | 156 | 1 | 0.58% | 803 | 17 | 2.12% | 966 | 27 | 2.80% |
| 120 - 179 days | 106 | 7 | 6.60% | - | - | 0.00% | 1,228 | 82 | 6.68% |
| 180 - 364 days | 138 | 9 | 6.52% | 560 | 25 | 4.46% | 1,997 | 117 | 5.86% |
| 365+ days | 211 | 35 | 16.59% | 459 | 73 | 15.90% | 8,973 | 994 | 11.08% |
| Total | \$ 13,308 | \$ 310 | 2.33% | \$ 21,834 | \$ 540 | 2.47% | \$ 107,285 | \$ 3,129 | 2.92% |
| Percentage of total loans excluding | | | | | | | | | |
| acquired loans accounted for under ASC 310-30 | | | 0.42% | | | 0.69% | | | 3.38% |
| <u>Refinanced or Modified Loans:</u> | | | | | | | | | |
| Amount | \$ 2,120 | \$ 197 | 9.29% | \$ 196 | \$ 19 | 9.69% | \$ 20,535 | \$ 1,501 | 7.31% |
| Percentage of Higher-Risk Loan | | | 15.93% | | | 0.90% | | | 19.14% |
| Category | | | | | | | | | |
| <u>Loan-to-Value Ratio:</u> | | | | | | | | | |
| Under 70% | \$ 8,116 | \$ 199 | 2.45% | \$ 1,708 | \$ 35 | 2.05% | \$ - | \$ - | - |
| 70% - 79% | 2,294 | 64 | 2.79% | 2,785 | 57 | 2.05% | - | - | - |
| 80% - 89% | 754 | 23 | 3.05% | 6,904 | 220 | 3.19% | - | - | - |
| 90% and over | 2,144 | 24 | 1.12% | 10,437 | 228 | 2.18% | 107,285 | 3,129 | 2.92% |
| | \$ 13,308 | \$ 310 | 2.33% | \$ 21,834 | \$ 540 | 2.47% | \$ 107,285 | \$ 3,129 | 2.92% |

* Loans may be included in more than one higher-risk loan category and excludes acquired residential mortgage loans.

The following table includes the Company's lending and investment exposure to the Puerto Rico government, including its agencies, instrumentalities, municipalities and public corporations:

TABLE 7 - PUERTO RICO GOVERNMENT RELATED LOANS AND SECURITIES

| Loans and Securities: | Carrying Value | June 30, 2015 Maturity | | | Comments |
|-----------------------|-------------------|------------------------------------|------------------|-------------------|---|
| | | Less than 1 Year (In thousands) | 1 to 3 Years | More than 3 Years | |
| Central government | \$ 25,218 | \$ - | \$ - | \$ 25,218 | Repayment sources include all available revenues of the Commonwealth \$80.0 million which matures in more than 3 years, with pledged securities (rating > A) Repayment from property taxes Revenues derived from trustee properties, leased facilities and Teodoro Moscoso Bridge operations. |
| Public corporations | 276,085 | 197,559 | 909 | 77,617 | |
| Municipalities | 213,971 | - | 51,139 | 162,832 | |
| Investment securities | 20,987 | - | 10,521 | 10,466 | |
| Total | \$ 536,261 | \$ 197,559 | \$ 62,569 | \$ 276,133 | |

Some highlights follow on the data included above:

- Loans to municipalities are backed by their unlimited taxing power or real and personal property taxes.
- 45% of loans and securities balances mature in 12-months or less.
- Deposits from municipalities, central government and other government entities totaled \$171.0 million at June 30, 2015. However, this amount may decline as a result of recently enacted legislation to improve the liquidity of the Government Development Bank for Puerto Rico ("GDB") by requiring the Commonwealth's agencies, instrumentalities and public corporations to maintain certain deposits at GDB.
- Oriental Bank, is part of a four bank syndicate providing a \$550 million dollar revolving line of credit to finance the purchase of fuel for the day to day power generation activities of PREPA. The Bank's participation in the line of credit has an unpaid principal balance of \$197.6 million as of June 30, 2015. During the first quarter of 2015, the Bank placed its participation in such line of credit on non-accrual status and recorded a \$24.0 million provision for loan and lease losses related thereto. There was no change to the PREPA provision during the second quarter of 2015. For such quarter, interest payments received were applied to principal.

Credit Risk Management

Allowance for Loan and Lease Losses

The Company maintains an allowance for loan and lease losses at a level that management considers adequate to provide for probable losses based upon an evaluation of known and inherent risks. The Company's allowance for loan and lease losses policy provides for a detailed quarterly analysis of probable losses. Tables 8 through 12 set forth an analysis of activity in the allowance for loan and lease losses and present selected loan loss statistics. In addition, Table 5 sets forth the composition of the loan portfolio.

At June 30, 2015, the Company's allowance for non-covered loan and lease losses amounted to \$102.9 million, an increase from \$69.5 million at December 31, 2014. Such increase is mostly due to the \$24.0 million provision for loan and lease losses related to the PREPA line of credit during the first quarter of 2015.

At June 30, 2015, \$79.0 million of the allowance corresponded to originated and other loans held for investment, or 2.67% of total non-covered originated and other loans held for investment, compared to \$51.4 million or 1.81% of total non-covered originated and other loans held for investment at December 31, 2014. The allowance increased as a result of a \$43.9 million provision for loan and lease losses and \$7.7 million of recoveries, which were partially offset by charge-offs of \$24.0 million during the six-month period ended June 30, 2015. During the first quarter of 2015, the Company recorded a \$24.0 million provision for loan and lease losses for the PREPA line of credit. The allowance for commercial loans increased 312.5% (or \$26.3 million), when compared with the balances recorded at December 31, 2014. The allowance for residential mortgage loans decreased by 8.1% (or \$1.6 million), when compared with the balances recorded at December 31, 2014. The allowance for consumer loans and auto and leases increased by 15.3% (or \$1.4 million) and 5.7% (or \$809 thousand), respectively, when compared with the balances recorded at December 31, 2014. The unallocated allowance at June 30, 2015 increased \$605 thousand, when compared with the balance recorded at December 31, 2014. Changes are related to the evolution and the current trends of the portfolio. In the mortgage loan portfolios, losses have decreased, and therefore, less reserve was required. In the consumer and auto loan portfolios, losses had increased, and therefore, a higher reserve was required. In the commercial loan portfolio losses increased, and therefore, a higher reserve was required in addition to the \$24.0 million PREPA provision for loan and lease losses.

Allowance for loan and lease losses recorded for acquired non-covered loans accounted for under the provisions of ASC 310-20 at June 30, 2015 was \$5.5 million compared to \$4.6 million at December 31, 2014, a 20.3% increase. The allowance increased as a result of a \$4.3 million provision for loan and lease losses and \$1.7 million of recoveries, which were partially offset by \$5.0 million in charge-offs during the six-month period ended June 30, 2015. The allowance for commercial loans decreased by 16.9% (or \$11 thousand), when compared with the balance recorded at December 31, 2014. The allowance for consumer loans increased by 116.0% (or \$1.4 million) and auto loans decreased by 13.9% (or \$462 thousand), respectively, when compared with the balances recorded at December 31, 2014, due to the normal amortization of credit discount of these acquired loans.

Allowance for loan and lease losses recorded for acquired non-covered loans accounted for under ASC-310-30 at June 30, 2015 was \$18.4 million as compared to \$13.5 million at December 31, 2014. The allowance increased as a result of a \$4.9 million provision for loan and lease losses during the six-month period ended June 30, 2015. The allowance for commercial loans increased by 10.9% (or \$1.5 million), when compared with the balance recorded at December 31, 2014. The allowance for residential mortgage loans increased \$473 thousand, when compared with the balances recorded at December 31, 2014. The allowance for consumer loans and auto loans increased by \$79 thousand and \$2.9 million, respectively, when compared with the balances recorded at December 31, 2014.

Allowance for loan and lease losses recorded for covered loans at June 30, 2015 was \$71.5 million as compared to \$64.2 million at December 31, 2014. The allowance increased as a result of a \$4.7 million provision for loan and lease losses and a provision of \$2.5 million of FDIC shared-loss portion for covered loan and lease losses during the six-month period ended June 30, 2015. The allowance for loan and lease losses on covered loans is accounted for under the provisions of ASC 310-30. Under this accounting guidance, the allowance for loan and lease losses on covered loans is evaluated at each financial reporting period, based on forecasted cash flows. Credit related decreases in expected cash flows, compared to those previously forecasted, are recognized by recording a provision for credit losses on covered loans when it is probable that all cash flows expected at acquisition will not be collected. The portion of the loss on covered loans reimbursable from the FDIC is recorded as an offset to the provision for credit losses and increases the FDIC indemnification asset.

Please refer to the “Provision for Loan and Lease Losses” section in this MD&A for a more detailed analysis of provisions for loan and lease losses.

Non-performing Assets

The Company's non-performing assets include non-performing loans and foreclosed real estate (see Tables 11 and 12). At June 30, 2015 and December 31, 2014, the Company had \$301.2 million and \$101.5 million, respectively, of non-accrual loans, including acquired loans accounted for under ASC 310-20 (loans with revolving feature and/or acquired at a premium). During the second quarter of 2015, the Company placed its \$200.0 million participation in the PREPA line of credit, which was previously classified as troubled-debt-restructuring, on non-accrual status. At June 30, 2015 and December 31, 2014, loans whose terms have been extended and which are classified as troubled-debt restructuring that are not included in non-performing assets amounted to \$88.8 million and \$274.4 million, respectively.

Oriental Bank is part of a four bank syndicate providing a \$550 million revolving line of credit to finance the purchase of fuel for PREPA's day-to-day power generation activities. Our participation in the line of credit has an unpaid principal balance of \$197.6 million as of June 30, 2015. As part of the bank syndicate, the Bank entered into a forbearance agreement with PREPA, which has been extended several times, most recently until September 15, 2015. In connection with such extensions, PREPA appointed a Chief Restructuring Officer to work alongside the Executive Director to develop, organize and manage a financial and operational restructuring of PREPA subject to the approval of PREPA's Board of Directors. PREPA also has been in negotiations with its forbearing creditors to restructure its debts and obtain financing for capital improvements needed to its infrastructure. The Company has classified the credit facility to PREPA as substandard and on non-accrual status. The Company conducted an impairment analysis considering the probability of collection of principal and interest, which included a financial model to project the future liquidity status of PREPA under various scenarios and its capacity to service its financial obligations, and concluded that PREPA had sufficient cash flows for the repayment of the line of credit. This analysis has been further supported by the various restructuring proposals made by PREPA and its creditors. Despite the Company's analysis showing PREPA's capacity to repay the line of credit, the Company placed its participation in non-accrual and recorded a \$24 million provision during the first quarter of 2015. The impairment analysis was updated for the second quarter with no change in provision. For the quarter ended June 30, 2015, interest payments are being applied to principal.

Delinquent residential mortgage loans insured or guaranteed under applicable FHA and VA programs are classified as non-performing loans when they become 90 days or more past due, but are not placed in non-accrual status until they become 18 months or more past due, since they are insured loans. Therefore, these loans are included as non-performing loans but excluded from non-accrual loans.

Covered loans and loans acquired in the BBVAPR Acquisition with credit deterioration are considered to be performing due to the application of the accretion method under ASC 310-30, in which these loans will accrete interest income over the remaining life of the loans using estimated cash flow analyses. Credit related decreases in expected cash flows, compared to those previously forecasted are recognized by recording a provision for credit losses on non-covered loans when it is probable that all cash flows expected at acquisition will not be collected.

At June 30, 2015, the Company's non-performing assets increased by 107.1% to \$368.9 million (6.35% of total assets, excluding covered assets and acquired loans with deteriorated credit quality) from \$178.1 million (4.30% of total assets, excluding covered assets and acquired loans with deteriorated credit quality) at December 31, 2014. The Company does not expect non-performing loans to result in significantly higher losses as most are well-collateralized with adequate loan-to-value ratios. At June 30, 2015, the allowance for originated loan and lease losses to non-performing loans coverage ratio was 25.59% (49.11% at December 31, 2014).

The Company follows a conservative residential mortgage lending policy, with more than 90% of its residential mortgage portfolio consisting of fixed-rate, fully amortizing, fully documented loans that do not have the level of risk associated with subprime loans offered by certain major U.S. mortgage loan originators. Furthermore, the Company has never been active in negative amortization loans or adjustable rate mortgage loans, including those with teaser rates.

The following items comprise non-performing assets:

- Originated and other loans held for investment:

Mortgage loans — are placed on non-accrual status when they become 90 days or more past due and are written-down, if necessary, based on the specific evaluation of the collateral underlying the loan, except for FHA and VA insured mortgage loans which are placed in non-accrual when they become 18 months or more past due. At June 30, 2015, the Company's originated non-performing mortgage loans totaled \$74.5 million (23.9% of the Company's non-performing loans), a 2.4% increase from \$72.8 million (66.8% of the Company's non-performing loans) at December 31, 2014. Non-performing loans in this category are primarily residential mortgage loans.

Commercial loans — are placed on non-accrual status when they become 90 days or more past due and are written-down, if necessary, based on the specific evaluation of the underlying collateral, if any. At June 30, 2015, the Company's originated non-performing commercial loans amounted to \$224.0 million (71.8% of the Company's non-performing loans), a 933.3% increase from \$21.7 million at December 31, 2014 (19.9% of the Company's non-performing loans). Most of this portfolio is collateralized by commercial real estate properties. During the first quarter of 2015, the Company placed its \$200.0 million participation in the PREPA line of credit, which was previously classified as troubled-debt-restructuring, on non-accrual status. At June 30, 2015, the PREPA line of credit had an outstanding principal balance of \$197.6 million.

Consumer loans — are placed on non-accrual status when they become 90 days past due and written-off when payments are delinquent 120 days in personal loans and 180 days in credit cards and personal lines of credit. At June 30, 2015, the Company's originated non-performing consumer loans totaled \$1.5 million (0.5% of the Company's non-performing loans), a 4.9% decrease from \$1.6 million (1.5% of the Company's non-performing loans) at December 31, 2014.

Auto loans and leases — are placed on non-accrual status when they become 90 days past due, partially written-off to collateral value when payments are delinquent 120 days, and fully written-off when payments are delinquent 180 days. At June 30, 2015, the Company's originated non-performing auto loans and leases amounted to \$8.6 million (2.8% of the Company's total non-performing loans), a decrease of 0.9% from \$8.7 million at December 31, 2014 (8.0% of the Company's total non-performing loans).

- Acquired loans accounted for under ASC 310-20 (loans with revolving features and/or acquired at premium):

Commercial revolving lines of credit and credit cards — are placed on non-accrual status when they become 90 days or more past due and are written-down, if necessary, based on the specific evaluation of the underlying collateral, if any. At June 30, 2015, the Company's acquired non-performing commercial lines of credit accounted for under ASC 310-20 amounted to \$1.0 million (0.3% of the Company's non-performing loans), a 11.8% decrease from \$1.2 million at December 31, 2014 (1.1% of the Company's non-performing loans).

Consumer revolving lines of credit and credit cards — are placed on non-accrual status when they become 90 days past due and written-off when payments are delinquent 180 days. At June 30, 2015, the Company's acquired non-performing consumer lines of credit and credit cards accounted for under ASC 310-20 totaled \$1.1 million (0.3% of the Company's non-performing loans), a 27.2% decrease from \$1.5 million at December 31, 2014 (1.4% of the Company's non-performing loans).

Auto loans acquired at premium - are placed on non-accrual status when they become 90 days past due, partially written-off to collateral value when payments are delinquent 120 days, and fully written-off when payments are delinquent 180 days. At June 30, 2015, the Company's acquired non-performing auto loans accounted for under ASC 310-20 totaled \$1.3 million (0.4% of the Company's non-performing loans), a 15.5% decrease from \$1.5 million at December 31, 2014 (1.4% of the Company's non-performing loans).

The Company has two mortgage loan modification programs. These are the Loss Mitigation Program and the Non-traditional Mortgage Loan Program. Both programs are intended to help responsible homeowners to remain in their homes and avoid foreclosure, while also reducing the Company's losses on non-performing mortgage loans.

The Loss Mitigation Program helps mortgage borrowers who are or will become financially unable to meet the current or scheduled mortgage payments. Loans that qualify under this program are those guaranteed by FHA, VA, RHS, "Banco de la Vivienda de Puerto Rico," conventional loans guaranteed by Mortgage Guaranty Insurance Corporation (MGIC), conventional loans sold to FNMA and FHLMC, and conventional loans retained by the Company. The program offers diversified alternatives such as regular or reduced payment plans, payment moratorium, mortgage loan modification, partial claims (only FHA), short sale, and payment in lieu of foreclosure.

The Non-traditional Mortgage Loan Program is for non-traditional mortgages, including balloon payment, interest only / interests first, variable interest rate, adjustable interest rate and other qualified loans. Non-traditional mortgage loan portfolios are segregated into the following categories: performing loans that meet secondary market requirement and are refinanced under the credit underwriting guidelines of FHA/VA/FNMA/ FHLMC, and performing loans not meeting secondary market guidelines processed by the Company's current credit and underwriting guidelines. The Company achieved an affordable and sustainable monthly payment by taking specific, sequential, and necessary steps such as reducing the interest rate, extending the loan term, capitalizing arrearages, deferring the payment of principal or, if the borrower qualifies, refinancing the loan.

There may not be a foreclosure sale scheduled within 60 days prior to a loan modification under any such programs. This requirement does not apply to loans where the foreclosure process has been stopped by the Company. In order to apply for any of the loan modification programs, the borrower may not be in active bankruptcy or have been discharged from Chapter 7 bankruptcy since the loan was originated. Loans in these programs are to be evaluated by management for troubled-debt restructuring classification if the Company grants a concession for legal or economic reasons due to the debtor's financial difficulties.

**TABLE 8 — ALLOWANCE FOR
LOAN AND LEASE LOSSES
SUMMARY**

| | Quarter Ended June 30, | | | Six-Month Period Ended | | |
|--|------------------------|------------------|--------------|------------------------|------------------|--------------|
| | 2015 | 2014 | Variance % | June 30, 2015 | 2014 | Variance % |
| | (Dollars in thousands) | | | (Dollars in thousands) | | |
| Non-covered loans | | | | | | |
| Originated and other loans: | | | | | | |
| Balance at beginning of period | \$ 76,759 | \$ 49,507 | 55.0% | \$ 51,439 | \$ 49,081 | 4.8% |
| Provision for non-covered | | | | | | |
| loan and lease losses | 9,953 | 7,431 | 33.9% | 43,864 | 13,056 | 236.0% |
| Charge-offs | (11,824) | (8,883) | 33.1% | (24,042) | (15,999) | 50.3% |
| Recoveries | 4,101 | 2,583 | 58.8% | 7,728 | 4,500 | 71.7% |
| | 78,989 | 50,638 | 56.0% | 78,989 | 50,638 | 56.0% |
| Acquired loans accounted for | | | | | | |
| under ASC 310-20: | | | | | | |
| Balance at beginning of period | \$ 5,450 | \$ 3,618 | 50.6% | \$ 4,597 | \$ 2,354 | 95.3% |
| Provision for non-covered | | | | | | |
| loan and lease losses | 1,498 | 2,569 | -41.7% | 4,286 | 6,811 | -37.1% |
| Charge-offs | (2,357) | (3,432) | -31.3% | (5,006) | (6,960) | -28.1% |
| Recoveries | 938 | 689 | 36.1% | 1,652 | 1,239 | 33.3% |
| | 5,529 | 3,444 | 60.5% | 5,529 | 3,444 | 60.5% |
| Acquired loans accounted for | | | | | | |
| under ASC 310-30: | | | | | | |
| Balance at beginning of period | \$ 14,166 | \$ 3,058 | 363.2% | \$ 13,481 | \$ 2,863 | 370.9% |
| Provision for non-covered | | | | | | |
| loan and lease losses | 4,193 | 3,220 | 30.2% | 4,878 | 3,415 | 42.8% |
| | 18,359 | 6,278 | 192.4% | 18,359 | 6,278 | 192.4% |
| Total non-covered loans balance | \$ 102,877 | \$ 60,360 | 70.4% | \$ 102,877 | \$ 60,360 | 70.4% |
| at end of period | | | | | | |
| Allowance for loans and lease | | | | | | |
| losses on originated and other | | | | | | |
| loans to: | | | | | | |
| Total originated loans | 2.67% | 1.92% | 39.1% | 2.67% | 1.92% | 39.1% |
| Non-performing originated loans | 25.59% | 56.53% | -54.7% | 25.59% | 56.53% | -54.7% |
| Allowance for loans and lease | | | | | | |

losses on acquired loans**accounted for under****ASC 310-20 to:**

Total acquired loans accounted

| | | | | | | |
|--------------------------------|---------|--------|--------|---------|--------|--------|
| for under ASC 310-20 | 2.87% | 1.05% | 173.5% | 2.87% | 1.05% | 173.5% |
| Non-performing acquired loans | 162.67% | 76.88% | 111.6% | 162.67% | 76.88% | 111.6% |
| accounted for under ASC 310-20 | | | | | | |

Covered loans

| | | | | | | | | | | |
|---------------------------------------|----|---------------|----|---------------|--------------|----|---------------|----|---------------|--------------|
| Balance at beginning of period | \$ | 70,651 | \$ | 54,398 | 29.9% | \$ | 64,245 | \$ | 52,729 | 21.8% |
| Provision for covered | | (105) | | 1,595 | -106.6% | | 4,704 | | 3,224 | 45.9% |
| loan and lease losses, net | | | | | | | | | | |
| FDIC shared-loss portion on | | | | | | | | | | |
| (provision for) recapture of loan | | | | | | | | | | |
| and lease losses | | 906 | | 3,522 | -74.3% | | 2,503 | | 3,562 | -29.7% |
| Balance at end of period | \$ | 71,452 | \$ | 59,515 | 20.1% | \$ | 71,452 | \$ | 59,515 | 20.1% |

TABLE 9 — ALLOWANCE FOR NON-COVERED LOAN AND LEASE LOSSES BREAKDOWN

| | June 30, 2015 | December 31, 2014 | Variance % |
|---|--------------------------|------------------------------|-----------------------|
| (Dollars in thousands) | | | |
| <u>Originated and other loans held for investment</u> | | | |
| Allowance balance: | | | |
| Mortgage | \$ 18,076 | \$ 19,679 | -8.1% |
| Commercial | 34,779 | 8,432 | 312.5% |
| Consumer | 10,464 | 9,072 | 15.3% |
| Auto and leasing | 15,064 | 14,255 | 5.7% |
| Unallocated allowance | 606 | 1 | 60500.0% |
| Total allowance balance | \$ 78,989 | \$ 51,439 | 53.6% |
| Allowance composition: | | | |
| Mortgage | 22.88% | 38.26% | -40.2% |
| Commercial | 44.03% | 16.39% | 168.6% |
| Consumer | 13.25% | 17.64% | -24.9% |
| Auto and leasing | 19.07% | 27.71% | -31.2% |
| Unallocated allowance | 0.77% | 0.00% | -1% |
| | 100.00% | 100.00% | |
| Allowance coverage ratio at end of period applicable to: | | | |
| Mortgage | 2.39% | 2.49% | -4.0% |
| Commercial | 2.55% | 0.65% | 290.0% |
| Consumer | 4.92% | 4.86% | 1.3% |
| Auto and leasing | 2.42% | 2.48% | -2.4% |
| Total allowance to total originated loans | 2.67% | 1.81% | 47.7% |
| Allowance coverage ratio to non-performing loans: | | | |
| Mortgage | 24.25% | 27.03% | -10.3% |
| Commercial | 15.53% | 38.89% | -60.1% |
| Consumer | 692.06% | 570.57% | 21.3% |
| Auto and leasing | 175.43% | 164.46% | 6.7% |
| Total | 25.59% | 49.11% | -47.9% |
| <u>Acquired loans accounted for under ASC 310-20</u> | | | |
| Allowance balance: | | | |
| Commercial | \$ 54 | \$ 65 | -16.9% |
| Consumer | 2,616 | 1,211 | 116.0% |
| Auto | 2,859 | 3,321 | -13.9% |
| Total allowance balance | \$ 5,529 | \$ 4,597 | 20.3% |
| Allowance composition: | | | |
| Commercial | 0.98% | 1.41% | -30.5% |
| Consumer | 47.31% | 26.34% | 79.6% |
| Auto | 51.71% | 72.25% | -28.4% |
| | 100.00% | 100.00% | |
| Allowance coverage ratio at end of period applicable to: | | | |
| Commercial | 0.64% | 0.51% | 24.6% |
| Consumer | 6.30% | 2.67% | 136.0% |
| Auto | 2.01% | 1.80% | 11.6% |
| Total allowance to total acquired loans | 2.87% | 1.89% | 51.7% |
| Allowance coverage ratio to non-performing loans: | | | |
| Commercial | 5.16% | 5.48% | -5.8% |

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| | | | |
|--------------|----------------|----------------|---------------|
| Consumer | 243.35% | 82.05% | 196.6% |
| Auto | 223.88% | 219.64% | 1.9% |
| Total | 162.67% | 219.64% | -25.9% |

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**TABLE 9 — ALLOWANCE FOR NON-COVERED LOAN AND LEASE LOSSES BREAKDOWN
(CONTINUED)**

| | June 30, 2015 | December 31, 2014 | Variance % |
|---|-------------------------------|------------------------------|-----------------------|
| | (Dollars in thousands) | | |
| <u>Acquired loans accounted for under ASC 310-30</u> | | | |
| Allowance balance: | | | |
| Mortgage | \$ 473 | \$ - | 100.0% |
| Commercial | 14,940 | 13,476 | 10.9% |
| Consumer | 84 | 5 | 1580.0% |
| Auto | 2,862 | - | 100.0% |
| Total allowance balance | \$ 18,359 | \$ 13,481 | 36.2% |
| Allowance composition: | | | |
| Mortgage | 2.58% | 0.00% | 100.0% |
| Commercial | 81.38% | 99.96% | -18.6% |
| Consumer | 0.46% | 0.04% | 1133.6% |
| Auto | 15.59% | 0.00% | 0% |
| | 100.00% | 100.00% | 0.0% |

TABLE 10 — NET CREDIT LOSSES STATISTICS ON LOAN AND LEASES, EXCLUDING LOANS ACCOUNTED FOR UNDER ASC 310-30

| | Quarter Ended June 30, | | Variance % | Six-Month Period Ended June 30, | | Variance % |
|---|------------------------|---------------------|---------------|------------------------------------|---------------------|---------------|
| | 2015 | 2014 | | 2015 | 2014 | |
| (Dollar in thousands) | | | | | | |
| Originated and other loans and leases: | | | | | | |
| Mortgage | | | | | | |
| Charge-offs | \$ (1,356) | \$ (987) | 37.4% | \$ (2,770) | \$ (2,201) | 25.9% |
| Recoveries | 67 | 88 | -23.9% | 67 | 236 | 100.0% |
| Total | (1,289) | (899) | 43.4% | (2,703) | (1,965) | 37.6% |
| Commercial | | | | | | |
| Charge-offs | (497) | (543) | -8.5% | (1,489) | (962) | 54.8% |
| Recoveries | 219 | 115 | 90.4% | 309 | 213 | 45.1% |
| Total | (278) | (428) | -35.0% | (1,180) | (749) | 57.5% |
| Consumer | | | | | | |
| Charge-offs | (2,309) | (1,397) | 65.3% | (3,985) | (2,235) | 78.3% |
| Recoveries | 67 | 244 | -72.5% | 543 | 391 | 38.9% |
| Total | (2,242) | (1,153) | 94.4% | (3,442) | (1,844) | 86.7% |
| Auto | | | | | | |
| Charge-offs | (7,662) | (5,956) | 28.6% | (15,798) | (10,601) | 49.0% |
| Recoveries | 3,425 | 2,136 | 60.3% | 6,809 | 3,660 | 86.0% |
| Total | (4,237) | (3,820) | 10.9% | (8,989) | (6,941) | 29.5% |
| Net credit losses | | | | | | |
| Total charge-offs | (11,824) | (8,883) | 33.1% | (24,042) | (15,999) | 50.3% |
| Total recoveries | 3,778 | 2,583 | 46.3% | 7,728 | 4,500 | 71.7% |
| Total | \$ (8,046) | \$ (6,300) | 27.7% | \$ (16,314) | \$ (11,499) | 41.9% |
| Net credit losses to average | | | | | | |
| loans outstanding: | | | | | | |
| Mortgage | 0.66% | 0.46% | 43.5% | 0.69% | 0.51% | 35.3% |
| Commercial | 0.08% | 0.14% | -42.9% | 0.18% | 0.13% | 38.5% |
| Consumer | 4.66% | 3.13% | 48.9% | 3.68% | 2.68% | 37.3% |
| Auto | 2.74% | 3.15% | -13.0% | 2.96% | 3.07% | -3.6% |
| Total | 1.10% | 0.96% | 14.6% | 1.13% | 0.91% | 24.2% |
| Recoveries to charge-offs | 31.95% | 29.08% | 9.9% | 32.14% | 28.13% | 14.3% |
| Average originated loans: | | | | | | |
| Mortgage | \$ 782,753 | \$ 773,425 | 1.2% | \$ 785,029 | \$ 763,400 | 2.8% |
| Commercial | 1,333,276 | 1,209,346 | 10.2% | 1,301,367 | 1,165,891 | 11.6% |
| Consumer | 192,572 | 147,230 | 30.8% | 187,049 | 137,787 | 35.8% |
| Auto | 618,746 | 484,536 | 27.7% | 606,819 | 451,488 | 34.4% |
| Total | \$ 2,927,347 | \$ 2,614,537 | 12.0% | \$ 2,880,264 | \$ 2,518,566 | 14.4% |

**TABLE 10 — NET CREDIT LOSSES STATISTICS ON LOAN AND LEASES,
EXCLUDING LOANS ACCOUNTED FOR UNDER ASC 310-30 (CONTINUED)**

| | Quarter Ended | | | Six-Month Period | | |
|---|-------------------|-------------------|---------------|-------------------|-------------------|----------------|
| | June 30, | | Variance | Ended June 30, | | Variance |
| | 2015 | 2014 | % | 2015 | 2014 | % |
| (Dollars in thousands) | | | | | | |
| Acquired loans accounted for under ASC 310-20: | | | | | | |
| Commercial | | | | | | |
| Charge-offs | \$ (16) | \$ (110) | -85.5% | \$ (16) | \$ (284) | -94.4% |
| Recoveries | 7 | 30 | 100.0% | 17 | 30 | - |
| Total | (9) | (80) | -88.8% | 1 | (254) | -100.4% |
| Consumer | | | | | | |
| Charge-offs | (1,303) | (1,952) | -33.2% | (2,686) | (4,010) | -33.0% |
| Recoveries | 429 | 124 | 246.0% | 563 | 224 | 151.3% |
| Total | (874) | (1,828) | -52.2% | (2,123) | (3,786) | -43.9% |
| Auto | | | | | | |
| Charge-offs | (1,038) | (1,370) | -24.2% | (2,304) | (2,666) | -13.6% |
| Recoveries | 502 | 535 | -6.2% | 17 | 985 | -98.3% |
| Total | (536) | (835) | -35.8% | (2,287) | (1,681) | 36.0% |
| Net credit losses | | | | | | |
| Total charge-offs | (2,357) | (3,432) | -31.3% | (5,006) | (6,960) | -28.1% |
| Total recoveries | 938 | 689 | 36.1% | 597 | 1,239 | -51.8% |
| Total | \$ (1,419) | \$ (2,743) | -48.3% | \$ (4,409) | \$ (5,721) | -22.9% |
| Net credit losses to average | | | | | | |
| loans outstanding: | | | | | | |
| Commercial | 5.10% | 1.29% | 296.1% | -0.2% | 1.04% | -118.5% |
| Consumer | 5.70% | 10.96% | -48.1% | 6.8% | 11.09% | -38.65% |
| Auto | 1.26% | 1.34% | -5.5% | 2.1% | 1.27% | 67.6% |
| Total | 2.45% | 3.22% | -23.7% | 3.2% | 2.99% | 5.7% |
| Recoveries to charge-offs | 39.80% | 20.08% | 98.2% | 11.93% | 17.80% | -33.0% |
| Average loans accounted for under ASC 310-20: | | | | | | |
| Commercial | \$ 706 | \$ 24,855 | -97.2% | \$ 1,039 | \$ 48,868 | -97.9% |
| Consumer | 61,382 | 66,690 | -8.0% | 62,425 | 68,294 | -8.6% |
| Auto | 169,644 | 249,395 | -32.0% | 215,454 | 265,459 | -18.8% |
| Total | \$ 231,732 | \$ 340,940 | -32.0% | \$ 278,918 | \$ 382,621 | -27.1% |

TABLE 11 — NON-PERFORMING ASSETS

| | June 30 2015 | December 31 2014 | Variance (%) |
|---|-------------------------------|-----------------------------|-------------------------|
| | (Dollars in thousands) | | |
| Non-performing assets: | | | |
| Non-accruing loans | | | |
| Troubled-Debt Restructuring loans | \$ 223,395 | \$ 27,707 | 706.3% |
| Other loans | 77,787 | 73,835 | 5.4% |
| Accruing loans | | | |
| Troubled-Debt Restructuring loans | 8,397 | 3,862 | 117.4% |
| Other loans | 2,461 | 3,523 | -30.1% |
| Total non-performing loans | \$ 312,040 | \$ 108,927 | 186.5% |
| Foreclosed real estate not covered under the shared-loss agreements with the FDIC | 42,392 | 48,147 | -12.0% |
| Other repossessed assets | 14,470 | 21,043 | -31.2% |
| | \$ 368,902 | \$ 178,117 | 107.1% |
| Non-performing assets to total assets, excluding covered assets and acquired loans with deteriorated credit quality (including those by analogy) | 6.35% | 4.30% | 47.8% |
| Non-performing assets to total capital | 40.47% | 18.90% | 114.1% |

| | Quarter Ended June 30, | | Six-Month Period June 30, | |
|--|-----------------------------------|---------------|----------------------------------|-----------------|
| | 2015 | 2014 | 2015 | 2014 |
| | (In thousands) | | | |
| Interest that would have been recorded in the period if the loans had not been classified as non-accruing loans | \$ 890 | \$ 723 | \$ 1,597 | \$ 1,213 |

TABLE 12 — NON-PERFORMING LOANS

| | June 30, 2015 | December 31, 2014 | Variance % |
|--|-------------------|-------------------------|---------------|
| (Dollars in thousands) | | | |
| Non-performing loans: | | | |
| Originated and other loans held for investment | | | |
| Mortgage | \$ 74,528 | \$ 72,815 | 2.4% |
| Commercial | 224,014 | 21,679 | 933.3% |
| Consumer | 1,512 | 1,590 | -4.9% |
| Auto and leasing | 8,587 | 8,668 | -0.9% |
| | 308,641 | 104,752 | 194.6% |
| Acquired loans accounted for under ASC 310-20 (Loans with revolving feature and/or acquired at a premium) | | | |
| Commercial | 1,047 | 1,187 | -11.8% |
| Consumer | 1,075 | 1,476 | -27.2% |
| Auto | 1,277 | 1,512 | -15.5% |
| | 3,399 | 4,175 | -18.6% |
| Total | \$ 312,040 | \$ 108,927 | 186.5% |
| Non-performing loans composition percentages: | | | |
| Originated loans | | | |
| Mortgage | 23.9% | 66.8% | |
| Commercial | 71.8% | 19.9% | |
| Consumer | 0.5% | 1.5% | |
| Auto and leasing | 2.8% | 8.0% | |
| Acquired loans accounted for under ASC 310-20 (Loans with revolving feature and/or acquired at a premium) | | | |
| Commercial | 0.3% | 1.1% | |
| Consumer | 0.3% | 1.4% | |
| Auto | 0.4% | 1.4% | |
| Total | 100.0% | 100.0% | |
| Non-performing loans to: | | | |
| Total loans, excluding covered loans and loans accounted for | | | |
| under ASC 310-30 (including those by analogy) | 9.91% | 3.53% | 180.8% |
| Total assets, excluding covered assets and loans accounted for | | | |
| under ASC 310-30 (including those by analogy) | 5.37% | 2.63% | 104.4% |
| Total capital | 34.23% | 11.56% | 196.1% |
| Non-performing loans with partial charge-offs to: | | | |
| Total loans, excluding covered loans and loans accounted for | | | |
| under ASC 310-30 (including those by analogy) | 1.09% | 1.04% | 4.39% |
| Non-performing loans | 10.96% | 29.42% | -62.8% |
| Other non-performing loans ratios: | | | |
| Charge-off rate on non-performing loans to non-performing loans | 59.28% | 53.42% | 11.0% |

on which charge-offs have been taken
Allowance for loan and lease losses to non-performing

| | | | |
|---|---------------|---------------|---------------|
| loans on which no charge-offs have been taken | 30.42% | 72.88% | -58.3% |
|---|---------------|---------------|---------------|

FDIC Indemnification Asset

The Company recorded the FDIC indemnification asset, measured separately from the covered loans, as part of the Eurobank FDIC-assisted transaction. Based on the accounting guidance in ASC Topic 805, at each reporting date subsequent to the initial recording of the indemnification asset, the Company measures the indemnification asset on the same basis as the covered loans and assesses its collectability. The amount to be ultimately collected for the indemnification asset is dependent upon the performance of the underlying covered assets, the passage of time, claims submitted to the FDIC and the Corporation's compliance with the terms of the loss sharing agreements. Refer to Note 6 to the consolidated financial statements for additional information on the FDIC loss share agreements.

On July 2, 2015, the Bank entered into an agreement with the FDIC pursuant to which the FDIC concurred with a proposed sale of a pool of shared loss assets under the commercial shared loss agreement. Pursuant to such agreement, the FDIC agreed to pay the Bank up to \$20 million in loss share coverage with respect to the aggregate loss resulting from any portfolio sale of such shared loss assets that may occur within 120 days of the agreement.

TABLE 13 - ACTIVITY OF FDIC INDEMNIFICATION ASSET

| | Quarter Ended June 30, | |
|--|-------------------------------|-------------------|
| | 2015 | 2014 |
| | (In thousands) | |
| <u>FDIC indemnification asset:</u> | | |
| Balance at beginning of period | \$ 75,221 | \$ 166,194 |
| Shared-loss agreements reimbursements from the FDIC | (24,387) | (10,464) |
| Increase in expected credit losses to be | | |
| covered under shared-loss agreements, net | 906 | 3,522 |
| FDIC indemnification asset expense | (22,512) | (17,499) |
| Incurring expenses to be reimbursed under shared-loss agreements | (6,524) | 1,907 |
| Balance at end of period | \$ 22,704 | \$ 143,660 |

TABLE 14 - ACTIVITY IN THE REMAINING FDIC INDEMNIFICATION ASSET DISCOUNT

| | Quarter Ended June 30, | |
|---------------------------------------|-------------------------------|------------------|
| | 2015 | 2014 |
| | (In thousands) | |
| Balance at beginning of period | \$ 4,755 | \$ 60,023 |
| Amortization of negative discount | (22,531) | (17,499) |
| Impact of lower projected losses | 27,733 | 6,483 |
| Balance at end of period | \$ 9,957 | \$ 49,007 |

TABLE 15 - LIABILITIES SUMMARY AND COMPOSITION

| | June 30, 2015 | December 31, 2014 | Variance % |
|--|------------------------|----------------------|---------------|
| | (Dollars in thousands) | | |
| Deposits: | | | |
| Non-interest bearing deposits | \$ 838,600 | \$ 745,142 | 12.5% |
| NOW accounts | 1,097,997 | 1,251,943 | -12.3% |
| Savings and money market accounts | 1,333,201 | 1,385,823 | -3.8% |
| Certificates of deposit | 1,478,629 | 1,539,752 | -4.0% |
| Total deposits | 4,748,427 | 4,922,660 | -3.5% |
| Accrued interest payable | 1,257 | 1,746 | -28.0% |
| Total deposits and accrued interest payable | 4,749,684 | 4,924,406 | -3.5% |
| Borrowings: | | | |
| Securities sold under agreements to repurchase | 1,161,136 | 980,087 | 18.5% |
| Advances from FHLB | 333,391 | 334,331 | -0.3% |
| Other term notes | 2,090 | 4,004 | -47.8% |
| Subordinated capital notes | 102,109 | 101,584 | 0.5% |
| Total borrowings | 1,598,726 | 1,420,006 | 12.6% |
| Total deposits and borrowings | 6,348,410 | 6,344,412 | 0.1% |
| Other Liabilities: | | | |
| Derivative liabilities | 8,739 | 11,221 | -22.1% |
| Acceptances outstanding | 16,040 | 17,989 | -10.8% |
| Other liabilities | 113,537 | 133,290 | -14.8% |
| Total liabilities | \$ 6,486,726 | \$ 6,506,912 | -0.3% |
| Deposits portfolio composition percentages: | | | |
| Non-interest bearing deposits | 17.7% | 15.1% | |
| NOW accounts | 23.1% | 25.4% | |
| Savings and money market accounts | 28.1% | 28.2% | |
| Certificates of deposit | 31.1% | 31.3% | |
| | 100.0% | 100.0% | |
| Borrowings portfolio composition percentages: | | | |
| Securities sold under agreements to repurchase | 72.6% | 69.0% | |
| Advances from FHLB | 20.9% | 23.5% | |
| Other term notes | 0.1% | 0.3% | |
| Subordinated capital notes | 6.4% | 7.2% | |
| | 100.0% | 100.0% | |
| Securities sold under agreements to repurchase (excluding accrued interest) | | | |
| Amount outstanding at period-end | \$ 1,158,944 | \$ 977,816 | |
| Daily average outstanding balance | \$ 982,862 | \$ 1,041,378 | |
| Maximum outstanding balance at any month-end | \$ 1,166,445 | \$ 1,149,167 | |

Liabilities and Funding Sources

As shown in Table 15 above, at June 30, 2015, the Company's total liabilities were \$6.487 billion, 0.3% less than the \$6.507 billion reported at December 31, 2014. Deposits and borrowings, the Company's funding sources, amounted to \$6.348 billion at June 30, 2015 versus \$6.344 billion at December 31, 2014, a 0.1% decrease.

At June 30, 2015, deposits represented 75% and borrowings represented 25% of interest-bearing liabilities. At June 30, 2015, deposits, the largest category of the Company's interest-bearing liabilities, were \$4.750 billion, a decrease of 3.5% from \$4.924 billion at December 31, 2014. Demand and savings deposits decreased 3.3% to \$3.270 billion, brokered deposits declined 2.3% to \$605.4 million and higher-priced time deposits declined 5.7% to \$957.2 million as part of our efforts to reduce the cost of deposits, which averaged 0.66% at December 31, 2014, to 0.68% at June 30, 2015.

Borrowings consist mainly of repurchase agreements, FHLB-NY advances and subordinated capital notes. At June 30, 2015, borrowings amounted to \$1.599 billion, representing an increase of 12.6% when compared with the \$1.420 billion reported at December 31, 2014. Repurchase agreements as of June 30, 2015 increased \$181.0 million to \$1.161 billion from \$980.1 million at December 31, 2014, as the Company entered into new three month short-term repurchase agreements.

As a member of the FHLB-NY, the Bank can obtain advances from the FHLB-NY secured by the FHLB-NY stock owned by the Bank as well as by certain of the Bank's mortgage loans and investment securities. Advances from the FHLB-NY amounted to \$333.4 million as of June 30, 2015 and \$334.3 million as of December 31, 2014. These advances mature from July 2015 through 2020.

Stockholders' Equity

At June 30, 2015, the Company's total stockholders' equity was \$911.6 million, a 3.25% decrease when compared to \$942.2 million at December 31, 2014. This decline in stockholders' equity reflects decreases in retained earnings by \$21.4 million, in accumulated comprehensive income by \$5.4 million and in treasury stock by \$3.6 million, which in turn reflects the net loss and dividends declared for the period. Book value per share was \$16.81 at June 30, 2015 compared to \$17.40 at December 31, 2014.

From December 31, 2014 to June 30, 2015, tangible common equity to total assets decreased to 8.80% from 9.14%, Tier 1 Leverage Capital Ratio increased to 11.05% from 10.61%, Tier 1 Risk-Based Capital Ratio decreased to 15.85% from 16.02%, and Total Risk-Based Capital Ratio decreased to 17.41% from 17.57%. Common Equity Tier 1

Capital Ratio under the new capital rules was 12.26% as of June 30, 2015.

New Capital Rules to Implement Basel III Capital Requirements

In July 2013, the Board of Governors of the Federal Reserve System (the “Board”), the Office of the Comptroller of the Currency (the “OCC”) and the FDIC (together with the Board and the OCC, the “Agencies”) approved new rules (“New Capital Rules”) to establish a revised comprehensive regulatory capital framework for all U.S. banking organizations. The New Capital Rules generally implement the Basel Committee on Banking Supervision’s (the “Basel Committee”) December 2010 final capital framework referred to as “Basel III” for strengthening international capital standards. The New Capital Rules substantially revise the risk-based capital requirements applicable to bank holding companies and their depository institution subsidiaries, including the Company and the Bank, as compared to the current U.S. general risk-based capital rules. The New Capital Rules revise the definitions and the components of regulatory capital, as well as address other issues affecting the numerator in banking institutions’ regulatory capital ratios. The New Capital Rules also address asset risk weights and other matters affecting the denominator in banking institutions’ regulatory capital ratios and replace the existing general risk-weighting approach, which was derived from the Basel Committee’s 1988 “Basel I” capital accords, with a more risk-sensitive approach based, in part, on the “standardized approach” in the Basel Committee’s 2004 “Basel II” capital accords. In addition, the New Capital Rules implement certain provisions of Dodd-Frank Act, including the requirements of Section 939A to remove references to credit ratings from the federal agencies’ rules. The New Capital Rules became effective for the Company and the Bank on January 1, 2015, subject to phase-in periods for certain of their components and other provisions. Among other matters, the New Capital Rules: (i) introduce a new capital measure called “Common Equity Tier 1” (“CET1”) and related regulatory capital ratio of CET1 to risk-weighted assets; (ii) specify that Tier 1 capital consists of CET1 and “Additional Tier 1 capital” instruments meeting certain revised requirements; (iii) mandate that most deductions/adjustments to regulatory capital measures be made to CET1 and not to the other components of capital; and (iv) expand the scope of the deductions from and adjustments to capital as compared to existing regulations. Under the New Capital Rules, for most banking organizations, including the Company, the most common form of Additional Tier 1 capital is noncumulative perpetual preferred stock and the most common

form of Tier 2 capital is subordinated notes and a portion of the allocation for loan and lease losses, in each case, subject to the New Capital Rules' specific requirements.

Pursuant to the New Capital Rules, the minimum capital ratios as of January 1, 2015 were as follows:

- 4.5% CET1 to risk-weighted assets;
- 6.0% Tier 1 capital (that is, CET1 *plus* Additional Tier 1 capital) to risk-weighted assets;
- 8.0% Total capital (that is, Tier 1 capital *plus* Tier 2 capital) to risk-weighted assets; and
- 4% Tier 1 capital to average consolidated assets as reported on consolidated financial statements (known as the "leverage ratio").

The New Capital Rules also introduce a new 2.5% "capital conservation buffer", composed entirely of CET1, on top of the three minimum risk-weighted asset ratios. The capital conservation buffer is designed to absorb losses during periods of economic stress. Banking institutions with a ratio of CET1 to risk-weighted assets above the minimum but below the capital conservation buffer will face constraints on dividends, equity repurchases and compensation based on the amount of the shortfall. Thus, when fully phased-in on January 1, 2019, the Company and the Bank will be required to maintain an additional capital conservation buffer of 2.5% of CET1, effectively resulting in minimum ratios of (i) CET1 to risk-weighted assets of at least 7%, (ii) Tier 1 capital to risk-weighted assets of at least 8.5%, and (iii) Total capital to risk-weighted assets of at least 10.5%.

The New Capital Rules provide for a number of deductions from and adjustments to CET1. These include, for example, the requirement that mortgage servicing rights, deferred tax assets arising from temporary differences that could not be realized through net operating loss carrybacks and significant investments in non-consolidated financial entities be deducted from CET1 to the extent that any one such category exceeds 10% of CET1 or all such items, in the aggregate, exceed 15% of CET1.

In addition (as noted above), under the current general risk-based capital rules, the effects of AOCI items included in shareholders' equity (for example, mark-to-market adjustments to the value of securities held in the available for sale portfolio) under U.S. GAAP are reversed for the purposes of determining regulatory capital ratios. Pursuant to the New Capital Rules, the effects of certain AOCI items are not excluded; however, non-advanced approach banking organizations may make a one-time permanent election to continue to exclude these items. The Company and the Bank made the election to continue to exclude these items in order to avoid significant variations in the level of capital depending upon the impact of interest rate fluctuations on the fair value of their securities portfolio, concurrently with the first filing of the Company's and Oriental Bank's periodic regulatory reports in the beginning of 2015. The New Capital Rules also preclude certain hybrid securities, such as trust preferred securities, from inclusion in bank holding companies' Tier 1 capital, subject to phase-out, in the case of bank holding companies that had \$15 billion or more in total consolidated assets as of December 31, 2009. Therefore, the Company is permitted to continue to include its existing trust preferred securities as Tier 1 capital.

Implementation of the deductions and other adjustments to CET1 began on January 1, 2015 and will be phased-in over a 4-year period (beginning at 40% on January 1, 2015 and an additional 20% per year thereafter). The implementation of the capital conservation buffer will begin on January 1, 2016 at the 0.625% level and increase by 0.625% on each subsequent January 1, until it reaches 2.5% on January 1, 2019.

With respect to the Bank, the New Capital Rules revise the “prompt corrective action” (“PCA”) regulations adopted pursuant to Section 38 of the Federal Deposit Insurance Act by: (i) introducing a CET1 ratio requirement at each PCA category (other than critically undercapitalized), with the required CET1 ratio being 6.5% for well-capitalized status; (ii) increasing the minimum Tier 1 capital ratio requirement for each category, with the minimum Tier 1 capital ratio for well-capitalized status being 8% (as compared to the current 6%); and (iii) eliminating the current provision that provides that a bank with a composite supervisory rating of 1 may have a 3% leverage ratio and still be adequately capitalized. The New Capital Rules do not change the total risk-based capital requirement for any PCA category.

The New Capital Rules prescribe a new standardized approach for risk weightings that expand the risk-weighting categories from the current four Basel I-derived categories (0%, 20%, 50% and 100%) to a larger and more risk-sensitive number of categories, depending on the nature of the assets, and resulting in higher risk weights for a variety of asset classes.

The following are the consolidated capital ratios of the Company under the New Capital Rules at June 30, 2015 and December 31, 2014:

TABLE 16 — CAPITAL, DIVIDENDS AND STOCK DATA

| | June 30, 2015 | December 31, 2014 | Variance % |
|---|--|------------------------------|-----------------------|
| | (Dollars in thousands, except per share data) | | |
| Capital data: | | | |
| Stockholders' equity | \$ 911,599 | \$ 942,197 | -3.2% |
| Regulatory Capital Ratios data: | | | |
| Common equity tier 1 capital ratio | 12.26% | N/A | N/A |
| Minimum common equity tier 1 capital ratio required | 4.50% | N/A | N/A |
| Actual common equity tier 1 capital | \$ 611,541 | N/A | N/A |
| Minimum common equity tier 1 capital required | \$ 224,494 | N/A | N/A |
| Excess over regulatory requirement | \$ 387,047 | N/A | N/A |
| Risk-weighted assets | \$ 4,988,754 | N/A | N/A |
| Tier 1 risk-based capital ratio | 15.85% | 16.02% | -1.1% |
| Minimum tier 1 risk-based capital ratio required | 6.00% | 4.00% | |
| Actual tier 1 risk-based capital | \$ 790,936 | \$ 776,525 | 1.9% |
| Minimum tier 1 risk-based capital required | \$ 299,325 | \$ 193,886 | 54.4% |
| Excess over regulatory requirement | \$ 491,611 | \$ 582,639 | -15.6% |
| Risk-weighted assets | \$ 4,988,754 | \$ 4,847,150 | 2.9% |
| Total risk-based capital ratio | 17.41% | 17.57% | -0.9% |
| Minimum total risk-based capital ratio required | 8.00% | 8.00% | |
| Actual total risk-based capital | \$ 868,568 | \$ 851,437 | 2.0% |
| Minimum total risk-based capital required | \$ 399,100 | \$ 387,772 | 2.9% |
| Excess over regulatory requirement | \$ 469,468 | \$ 463,665 | 1.3% |
| Risk-weighted assets | \$ 4,988,754 | \$ 4,847,150 | 2.9% |
| Leverage capital ratio | 11.05% | 10.61% | 4.1% |
| Minimum leverage capital ratio required | 4.00% | 4.00% | |
| Actual tier 1 capital | \$ 790,936 | \$ 776,525 | 1.9% |
| Minimum tier 1 capital required | \$ 286,262 | \$ 292,738 | -2.2% |
| Excess over regulatory requirement | \$ 504,674 | \$ 483,787 | 4.3% |
| Tangible common equity to total assets | 8.80% | 9.14% | -3.7% |
| Tangible common equity to risk-weighted assets | 13.05% | 14.04% | -7.1% |
| Total equity to total assets | 12.32% | 12.65% | -2.6% |
| Total equity to risk-weighted assets | 18.27% | 19.44% | -6.0% |
| Stock data: | | | |
| Outstanding common shares | 44,367,909 | 44,613,615 | -0.6% |
| Book value per common share | \$ 16.81 | \$ 17.40 | -3.4% |
| Tangible book value per common share | \$ 14.67 | \$ 15.25 | -3.8% |
| Market price at end of period | \$ 10.67 | \$ 16.65 | -35.9% |
| Market capitalization at end of period | \$ 473,406 | \$ 742,817 | -36.3% |

The following table presents a reconciliation of the Company's total stockholders' equity to tangible common equity and total assets to tangible assets at June 30, 2015 and December 31, 2014:

| | June 30, 2015 | | December 31, 2014 |
|--|--|------------------|------------------------------|
| | (In thousands, except share or per share information) | | |
| Total stockholders' equity | \$ | 911,599 | \$ 942,197 |
| Preferred stock | | (176,000) | (176,000) |
| Preferred stock issuance costs | | 10,130 | 10,130 |
| Goodwill | | (86,069) | (86,069) |
| Core deposit intangible | | (5,878) | (6,463) |
| Customer relationship intangible | | (2,912) | (3,280) |
| Total tangible common equity | \$ | 650,870 | \$ 680,515 |
| Total assets | | 7,398,325 | 7,449,109 |
| Goodwill | | (86,069) | (86,069) |
| Core deposit intangible | | (5,878) | (6,463) |
| Customer relationship intangible | | (2,912) | (3,280) |
| Total tangible assets | \$ | 7,303,466 | \$ 7,353,297 |
| Tangible common equity to tangible assets | | 8.91% | 9.25% |
| Common shares outstanding at end of period | | 44,367,909 | 44,613,615 |
| Tangible book value per common share | \$ | 14.67 | \$ 15.25 |

The tangible common equity ratio and tangible book value per common share are non-GAAP measures. Management and many stock analysts use the tangible common equity ratio and tangible book value per common share in conjunction with more traditional bank capital ratios to compare the capital adequacy of banking organizations. Neither tangible common equity nor tangible assets or related measures should be considered in isolation or as a substitute for stockholders' equity, total assets or any other measure calculated in accordance with GAAP. Moreover, the manner in which the Company calculates its tangible common equity, tangible assets and any other related measures may differ from that of other companies reporting measures with similar names.

Non-GAAP financial measures have inherent limitations, are not required to be uniformly applied and are not audited. To mitigate these limitations, the Company has procedures in place to calculate these measures using the appropriate GAAP or regulatory components. Although these non-GAAP financial measures are frequently used by stakeholders in the evaluation of a company, they have limitations as analytical tools and should not be considered in isolation or as a substitute for analyses of results as reported under GAAP.

The following table presents the Company's capital adequacy information under the New Capital Rules at June 30:

| | June 30 2015 | |
|--|-------------------------------|------------------|
| | (Dollars in thousands) | |
| Risk-based capital: | | |
| Common equity tier 1 capital | \$ | 611,541 |
| Additional tier 1 capital | | 179,395 |
| Tier 1 capital | | 790,936 |
| Additional Tier 2 capital | | 77,632 |
| Total risk-based capital | \$ | 868,568 |
| Risk-weighted assets: | | |
| Balance sheet items | \$ | 4,943,632 |
| Off-balance sheet items | | 45,123 |
| Total risk-weighted assets | \$ | 4,988,754 |
| Ratios: | | |
| Common equity tier 1 capital (minimum required - 4.5%) | | 12.26% |
| Tier 1 capital (minimum required - 6%) | | 15.85% |
| Total capital (minimum required - 8%) | | 17.41% |
| Leverage ratio | | 11.05% |
| Equity to assets | | 12.32% |
| Tangible common equity to assets | | 8.80% |

The Bank is considered "well capitalized" under the regulatory framework for prompt corrective action. The table below shows the Bank's regulatory capital ratios at June 30, 2015 and December 31, 2014:

| | June 30 2015 | December 31 2014 | Variance % |
|---|-------------------------------|-----------------------------|-----------------------|
| | (Dollars in thousands) | | |
| Oriental Bank Regulatory Capital Ratios: | | | |
| Common Equity Tier 1 Capital to Risk-Weighted Assets | 14.93% | N/A | N/A |
| Actual common equity tier 1 capital | \$ 742,098 | N/A | N/A |
| Minimum capital requirement (4.5%) | \$ 223,715 | N/A | N/A |
| Minimum to be well capitalized (6.5%) | \$ 323,144 | N/A | N/A |
| Tier 1 Capital to Risk-Weighted Assets | 14.93% | 15.45% | -3.4% |
| Actual tier 1 risk-based capital | \$ 742,098 | \$ 746,524 | -0.6% |
| Minimum capital requirement (6%) | \$ 298,287 | \$ 193,222 | 54.4% |
| Minimum to be well capitalized (8%) | \$ 397,716 | \$ 289,833 | 37.2% |
| Total Capital to Risk-Weighted Assets | 16.48% | 16.99% | -3.0% |
| Actual total risk-based capital | \$ 819,436 | \$ 820,884 | -0.2% |
| Minimum capital requirement (8%) | \$ 397,716 | \$ 386,444 | 2.9% |
| Minimum to be well capitalized (10%) | \$ 497,145 | \$ 483,055 | 2.9% |
| Total Tier 1 Capital to Average Total Assets | 10.44% | 10.26% | 1.8% |

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| | | | | | |
|-------------------------------------|----|---------|----|---------|-------|
| Actual tier 1 capital | \$ | 742,098 | \$ | 746,177 | -0.5% |
| Minimum capital requirement (4%) | \$ | 284,228 | \$ | 290,879 | -2.3% |
| Minimum to be well capitalized (5%) | \$ | 355,285 | \$ | 363,599 | -2.3% |

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The Company's common stock is traded on the New York Stock Exchange ("NYSE") under the symbol "OFG." At June 30, 2015 and December 31, 2014, the Company's market capitalization for its outstanding common stock was \$473.4 million (\$10.67 per share) and \$742.8 million (\$16.65 per share), respectively.

The following table provides the high and low prices and dividends per share of the Company's common stock for each quarter of the last two calendar years:

| | | Price | | | Cash Dividend Per share |
|--------------------|----|-------|----|-------|-------------------------|
| | | High | | Low | |
| 2015 | | | | | |
| June 30, 2015 | \$ | 17.04 | \$ | 10.67 | \$ 0.10 |
| March 31, 2015 | \$ | 17.70 | \$ | 14.88 | \$ 0.10 |
| 2014 | | | | | |
| December 31, 2014 | \$ | 16.76 | \$ | 14.35 | \$ 0.10 |
| September 30, 2014 | \$ | 18.89 | \$ | 14.92 | \$ 0.08 |
| June 30, 2014 | \$ | 18.88 | \$ | 16.38 | \$ 0.08 |
| March 31, 2014 | \$ | 17.54 | \$ | 14.30 | \$ 0.08 |
| 2013 | | | | | |
| December 31, 2013 | \$ | 17.34 | \$ | 14.74 | \$ 0.08 |
| September 30, 2013 | \$ | 18.97 | \$ | 16.13 | \$ 0.06 |
| June 30, 2013 | \$ | 18.11 | \$ | 14.26 | \$ 0.06 |
| March 31, 2013 | \$ | 15.83 | \$ | 13.85 | \$ 0.06 |

Under the Company's current stock repurchase program it is authorized to purchase in the open market up to \$70 million of its outstanding shares of common stock, of which approximately \$12.4 million of authority remains. The shares of common stock repurchased are to be held by the Company as treasury shares. During the six-month period ended June 30, 2015 the Company purchased 303,985 shares under this program for a total of \$4.2 million, at an average price of \$13.9 per share. There were no repurchases during the six-month period ended June 30, 2014.

The number of shares that may yet be purchased under the \$70 million program is estimated at 1,164,671 and was calculated by dividing the remaining balance of \$12.4 million by \$10.67 (closing price of the Company common stock at June 30, 2015). The Company did not purchase any shares of its common stock during the six-month periods ended June 30, 2015, or during the six-month periods ended June 30, 2014, other than through its publicly announced stock repurchase program.

ITEM 3. *QUANTITATIVE AND QUALITATIVE DISCLOSURES ABOUT MARKET RISK*

Background

The Company's risk management policies are established by its Board of Directors (the "Board") and implemented by management through the adoption of a risk management program, which is overseen and monitored by the Chief Risk Officer and the Risk Management and Compliance Committee. The Company has continued to refine and enhance its risk management program by strengthening policies, processes and procedures necessary to maintain effective risk management.

All aspects of the Company's business activities are susceptible to risk. Consequently, risk identification and monitoring are essential to risk management. As more fully discussed below, the Company's primary risk exposures include, market, interest rate, credit, liquidity, operational and concentration risks.

Market Risk

Market risk is the risk to earnings or capital arising from adverse movements in market rates or prices, such as interest rates or prices. The Company evaluates market risk together with interest rate risk. The Company's financial results and capital levels are constantly exposed to market risk. The Board and management are primarily responsible for ensuring that the market risk assumed by the Company complies with the guidelines established by policies approved by the Board. The Board has delegated the management of this risk to the Asset/Liability Management Committee ("ALCO") which is composed of certain executive officers from the business, treasury and finance areas. One of ALCO's primary goals is to ensure that the market risk assumed by the Company is within the parameters established in such policies.

Interest Rate Risk

Interest rate risk is the exposure of the Company's earnings or capital to adverse movements in interest rates. It is a predominant market risk in terms of its potential impact on earnings. The Company manages its asset/liability position in order to limit the effects of changes in interest rates on net interest income. ALCO oversees interest rate risk, liquidity management and other related matters.

In executing its responsibilities, ALCO examines current and expected conditions in global financial markets, competition and prevailing rates in the local deposit market, liquidity, unrealized gains and losses in securities, recent or proposed changes to the investment portfolio, alternative funding sources and their costs, hedging and the possible purchase of derivatives such as swaps, and any tax or regulatory issues which may be pertinent to these areas.

On a quarterly basis, the Company performs a net interest income simulation analysis on a consolidated basis to estimate the potential change in future earnings from projected changes in interest rates. These simulations are carried out over a five-year time horizon, assuming certain gradual upward and downward interest rate movements, achieved during a twelve-month period. Instantaneous interest rate movements are also modeled. Simulations are carried out in two ways:

- (i) using a static balance sheet as the Company had on the simulation date, and
- (ii) using a dynamic balance sheet based on recent growth patterns and business strategies.

The balance sheet is divided into groups of assets and liabilities detailed by maturity or re-pricing and their corresponding interest yields and costs. As interest rates rise or fall, these simulations incorporate expected future lending rates, current and expected future funding sources and costs, the possible exercise of options, changes in prepayment rates, deposits decay and other factors which may be important in projecting the future growth of net interest income.

The Company uses a software application to project future movements in the Company's balance sheet and income statement. The starting point of the projections generally corresponds to the actual values of the balance sheet on the date of the simulations.

These simulations are complex, and use many assumptions that are intended to reflect the general behavior of the Company over the period in question. There can be no assurance that actual events will match these assumptions in all cases. For this reason, the results of these simulations are only approximations of the true sensitivity of net interest income to changes in market interest rates. The following table presents the results of the simulations at June 30, 2015 for the most likely scenario, assuming a one-year time horizon:

| | Net Interest Income Risk (one year projection) | | | |
|---------------------------------------|---|----------------|---------------------------|----------------|
| | Static Balance Sheet | | Growing Simulation | |
| | Amount | Percent | Amount | Percent |
| <u>Change in interest rate</u> | Change | Change | Change | Change |
| | (Dollars in thousands) | | | |
| + 200 Basis points | \$ 7,405 | 2.11% | \$ 8,239 | 2.31% |
| + 100 Basis points | \$ 3,926 | 1.12% | \$ 4,341 | 1.22% |
| - 50 Basis points | \$ (1,932) | -0.55% | \$ (1,997) | -0.56% |

The impact of -100 and -200 basis point reductions in interest rates is not presented in view of current level of the federal funds rate and other short-term interest rates.

Future net interest income could be affected by the Company's investments in callable securities, prepayment risk related to mortgage loans and mortgage-backed securities, and any structured repurchase agreements and advances from the FHLB-NY in which it may enter into from time to time. As part of the strategy to limit the interest rate risk and reduce the re-pricing gaps of the Company's assets and liabilities, the Company has executed certain transactions which include extending the maturity and the re-pricing frequency of the liabilities to longer terms reducing the amounts of its structured repurchase agreements and entering into hedge-designated swaps to hedge the variability of future interest cash flows of forecasted wholesale borrowings that only consist of advances from the FHLB-NY as of June 30, 2015.

The Company maintains an overall interest rate risk management strategy that incorporates the use of derivative instruments to minimize significant unplanned fluctuations in earnings that are caused by interest rate volatility. The Company's goal is to manage interest rate sensitivity by modifying the repricing or maturity characteristics of certain balance sheet assets and liabilities so that the net interest margin is not, on a material basis, adversely affected by movements in interest rates. As a result of interest rate fluctuations, hedged fixed-rate assets and liabilities will appreciate or depreciate in market value. Also, for some fixed-rate assets or liabilities, the effect of this variability in earnings is expected to be substantially offset by the Company's gains and losses on the derivative instruments that are linked to the forecasted cash flows of these hedged assets and liabilities. The Company considers its strategic use of derivatives to be a prudent method of managing interest-rate sensitivity as it reduces the exposure of earnings and the market value of its equity to undue risk posed by changes in interest rates. The effect of this unrealized appreciation or depreciation is expected to be substantially offset by the Company's gains or losses on the derivative instruments that are linked to these hedged assets and liabilities. Another result of interest rate fluctuations is that the contractual interest income and interest expense of hedged variable-rate assets and liabilities, respectively, will increase or decrease.

Derivative instruments that are used as part of the Company's interest risk management strategy include interest rate swaps, forward-settlement swaps, futures contracts, and option contracts that have indices related to the pricing of specific balance sheet assets and liabilities. Interest rate swaps generally involve the exchange of fixed and variable-rate interest payments between two parties based on a common notional principal amount and maturity date. Interest rate futures generally involve exchanged-traded contracts to buy or sell U.S. Treasury bonds and notes in the future at specified prices. Interest rate options represent contracts that allow the holder of the option to (i) receive cash or (ii) purchase, sell, or enter into a financial instrument at a specified price within a specified period. Some purchased option contracts give the Company the right to enter into interest rate swaps and cap and floor agreements with the writer of the option. In addition, the Company enters into certain transactions that contain embedded derivatives. When the embedded derivative possesses economic characteristics that are not clearly and closely related to the economic characteristics of the host contract, it is bifurcated and carried at fair value. Please refer to Note 8 to the accompanying unaudited consolidated financial statements for further information concerning the Company's derivative activities.

Following is a summary of certain strategies, including derivative activities, currently used by the Company to manage interest rate risk:

Interest rate swaps — The Company entered into hedge-designated swaps to hedge the variability of future interest cash flows of forecasted wholesale borrowings attributable to changes in the one-month LIBOR rate. Once the forecasted wholesale borrowings transactions occurred, the interest rate swap effectively fixes the Company's interest payments on an amount of forecasted interest expense attributable to the one-month LIBOR rate corresponding to the swap notional stated rate. A derivative liability of \$6.5 million (notional amount of \$263.7 million) was recognized at June 30, 2015 related to the valuation of these swaps.

In addition, the Company has certain derivative contracts, including interest rate swaps not designated as hedging instruments, which are utilized to convert certain variable rate loans to fixed-rate loans, and the mirror-images of these interest rate swaps in which the Company enters into to minimize its interest rate risk exposure that results from offering the derivatives to clients. These interest rate swaps are marked to market through earnings. At June 30, 2015, interest rate swaps offered to clients not designated as hedging instruments represented a derivative asset of \$2.2 million (notional amounts of \$16.4 million), and the mirror-image interest rate swaps in which BBVAPR entered into represented a derivative liability of \$2.2 million (notional amounts of \$16.4 million).

S&P options — The Company has offered its customers certificates of deposit with an option tied to the performance of the S&P 500 Index. At the end of five years, the depositor receives a minimum return or a specified percentage of the average increase of the month-end value of the S&P 500 Index. The Company uses option agreements with major money center banks and major broker-dealer companies to manage its exposure to changes in that index. Under the terms of the option agreements, the Company receives the average increase in the month-end value of the S&P 500 Index in exchange for a fixed premium. The changes in fair value of the options purchased and the options embedded in the certificates of deposit are recorded in earnings.

At June 30, 2015, the fair value of the purchased options used to manage the exposure to the S&P 500 Index on stock-indexed certificates of deposit represented an asset of \$2.1 million (notional amounts of \$5.0 million) and the options sold to customers embedded in the certificates of deposit represented a liability of \$2.0 million (notional amount of \$4.8 million).

Wholesale borrowings — The Company uses interest rate swaps to hedge the variability of interest cash flows of certain advances from the FHLB-NY that are tied to a variable rate index. The interest rate swaps effectively fix the Company's interest payments on these borrowings. As of June 30, 2015, the Company had \$263.7 million in interest rate swaps at an average rate of 2.6% designated as cash flow hedges for \$263.7 million in advances from the FHLB-NY that repriced or are being rolled over on a monthly basis.

Credit Risk

Credit risk is the possibility of loss arising from a borrower or counterparty in a credit-related contract failing to perform in accordance with its terms. The principal source of credit risk for the Company is its lending activities. In Puerto Rico, the Company's principal market, economic conditions are challenging, as they have been for the last eight years, due to a shrinking population, a protracted economic recession, a housing sector that remains under pressure, the Puerto Rico government's large indebtedness and structural budget deficit, and the recent rating downgrades of Puerto Rico general obligations and other government bonds to levels that are below investment grade.

The Company manages its credit risk through a comprehensive credit policy which establishes sound underwriting standards by monitoring and evaluating loan portfolio quality, and by the constant assessment of reserves and loan concentrations. The Company also employs proactive collection and loss mitigation practices.

The Company may also encounter risk of default in relation to its securities portfolio. The securities held by the Company are principally agency mortgage-backed securities. Thus, a substantial portion of these instruments are guaranteed by mortgages, a U.S. government-sponsored entity, or the full faith and credit of the U.S. government.

The Company's Executive Credit Committee, composed of its Chief Executive Officer, Chief Credit Risk Officer and other senior executives, has primary responsibility for setting strategies to achieve the Company's credit risk goals and objectives. Those goals and objectives are set forth in the Company's Credit Policy as approved by the Board.

Liquidity Risk

Liquidity risk is the risk of the Company not being able to generate sufficient cash from either assets or liabilities to meet obligations as they become due without incurring substantial losses. The Board has established a policy to manage this risk. The Company's cash requirements principally consist of deposit withdrawals, contractual loan funding, repayment of borrowings as these mature, and funding of new and existing investments as required.

The Company's business requires continuous access to various funding sources. While the Company is able to fund its operations through deposits as well as through advances from the FHLB-NY and other alternative sources, the Company's business is dependent upon other wholesale funding sources. Although the Company has selectively reduced its use of wholesale funding sources, such as repurchase agreements and brokered deposits, it is still dependent on wholesale funding sources. As of June 30, 2015, the Company had \$1.159 billion in repurchase agreements, excluding accrued interests, and \$605.4 million in brokered deposits.

Brokered deposits are typically offered through an intermediary to small retail investors. The Company's ability to continue to attract brokered deposits is subject to variability based upon a number of factors, including volume and volatility in the global securities markets, the Company's credit rating, and the relative interest rates that it is prepared to pay for these liabilities. Brokered deposits are generally considered a less stable source of funding than core deposits obtained through retail bank branches. Investors in brokered deposits are generally more sensitive to interest rates and will generally move funds from one depository institution to another based on small differences in interest rates offered on deposits.

The Company participates in the Federal Reserve Bank's Borrower-In Custody Program which allows it to pledge certain type of loans while keeping physical control of the collateral.

Although the Company expects to have continued access to credit from the foregoing sources of funds, there can be no assurance that such financing sources will continue to be available or will be available on favorable terms. In a period of financial disruption or if negative developments occur with respect to the Company, the availability and cost of the Company's funding sources could be adversely affected. In that event, the Company's cost of funds may increase, thereby reducing its net interest income, or the Company may need to dispose of a portion of its investment portfolio, which depending upon market conditions, could result in realizing a loss or experiencing other adverse accounting consequences upon any such dispositions. The Company's efforts to monitor and manage liquidity risk may not be successful to deal with dramatic or unanticipated changes in the global securities markets or other reductions in liquidity driven by the Company or market-related events. In the event that such sources of funds are reduced or eliminated and the Company is not able to replace these on a cost-effective basis, the Company may be forced to curtail or cease its loan origination business and treasury activities, which would have a material adverse effect on its operations and financial condition.

As of June 30, 2015, the Company had approximately \$553.5 million in unrestricted cash and cash equivalents, \$221.7 million in investment securities that are not pledged as collateral, \$620.0 million in borrowing capacity at the FHLB-NY and \$699.1 million in borrowing capacity at the Federal Reserve's discount window available to cover liquidity needs.

Operational Risk

Operational risk is the risk of loss from inadequate or failed internal processes, personnel and systems or from external events. All functions, products and services of the Company are susceptible to operational risk.

The Company faces ongoing and emerging risk and regulatory pressure related to the activities that surround the delivery of banking and financial products and services. Coupled with external influences such as market conditions, security risks, and legal risk, the potential for operational and reputational loss has increased. In order to mitigate and control operational risk, the Company has developed, and continues to enhance, specific internal controls, policies and procedures that are designed to identify and manage operational risk at appropriate levels throughout the organization. The purpose of these policies and procedures is to provide reasonable assurance that the Company's business operations are functioning within established limits.

The Company classifies operational risk into two major categories: business specific and corporate-wide affecting all business lines. For business specific risks, a risk assessment group works with the various business units to ensure consistency in policies, processes and assessments. With respect to corporate-wide risks, such as information security, business recovery, legal and compliance, the Company has specialized groups, such as Information Security, Enterprise Risk Management, Corporate Compliance, Information Technology, Legal and Operations. These groups assist the lines of business in the development and implementation of risk management practices specific to the needs of the business groups. All these matters are reviewed and discussed in the Information Technology Steering Committee, and the Executive Risk and Compliance Committee.

The Company is subject to extensive United States federal and Puerto Rico regulations, and this regulatory scrutiny has been significantly increasing over the last several years. The Company has established and continues to enhance procedures based on legal and regulatory requirements that are reasonably designed to ensure compliance with all applicable statutory and regulatory requirements. The Company has a corporate compliance function headed by a Regulatory Compliance Director who reports to the Deputy General Counsel and the BSA Officer who reports to the Chief Risk Officer. The Regulatory Compliance Director is responsible for the oversight of regulatory compliance and implementation of a company-wide compliance program, except for the Bank Secrecy Act/ Anti-Money Laundering compliance program, which is overseen and implemented by the BSA Officer.

Concentration Risk

Substantially all of the Company's business activities and a significant portion of its credit exposure are concentrated in Puerto Rico. As a consequence, the Company's profitability and financial condition may be adversely affected by an extended economic slowdown, adverse political or economic developments in Puerto Rico or the effects of a natural disaster, all of which could result in a reduction in loan originations, an increase in non-performing assets, an increase in foreclosure losses on mortgage loans, and a reduction in the value of its loans and loan servicing portfolio.

ITEM 4. CONTROLS AND PROCEDURES

Disclosure Controls and Procedures

As of the end of the period covered by this quarterly report on Form 10-Q, an evaluation was carried out under the supervision and with the participation of the Company's management, including the Chief Executive Officer ("CEO") and the Chief Financial Officer ("CFO"), of the effectiveness of the design and operation of the Company's disclosure controls and procedures (as such term is defined in Rules 13a-15(e) and 15d-15(e) under the Exchange Act). Based upon such evaluation, the CEO and the CFO have concluded that, as of the end of such period, the Company's disclosure controls and procedures provided reasonable assurance of effectiveness in recording, processing, summarizing and reporting, on a timely basis, information required to be disclosed by the Company in the reports that

it files or submits under the Exchange Act. Notwithstanding the foregoing, a control system, no matter how well designed and operated, can provide only reasonable, not absolute assurance that it will detect or uncover failures within the Company to disclose material information otherwise required to be set forth in the Company's periodic reports.

Internal Control over Financial Reporting

There have not been any changes in the Company's internal control over financial reporting (as such term is defined in Rules 13a-15(f) and 15d-15(f) under the Exchange Act) during the quarter ended June 30, 2015, that has materially affected, or is reasonably likely to materially affect, the Company's internal control over financial reporting.

PART - II OTHER INFORMATION

ITEM 1. LEGAL PROCEEDINGS

The Company and its subsidiaries are defendants in a number of legal proceedings incidental to their business. The Company is vigorously contesting such claims. Based upon a review by legal counsel and the development of these matters to date, management is of the opinion that the ultimate aggregate liability, if any, resulting from these claims will not have a material adverse effect on the Company's financial condition or results of operations.

ITEM 1A. RISK FACTORS

Except as set forth below, there have been no material changes to the risk factors previously disclosed in the Company's annual report on Form 10-K for the year ended December 31, 2014. In addition to other information set forth in this report, you should carefully consider the risk factors included in the Company's annual report on Form 10-K, as updated by this report or other filings the Company makes with the SEC under the Exchange Act. Additional risks and uncertainties not presently known to the Company at this time or that the Company currently deems immaterial may also adversely affect the Company's business, financial condition or results of operations.

We are exposed to credit and concentration risks in connection with our credit facilities to the government of Puerto Rico, including some of its public corporations, instrumentalities and municipalities, and any credit default on their debt obligations or a further deterioration of the Puerto Rico economy could adversely and materially affect our financial condition and results of operations.

The Commonwealth of Puerto Rico and its instrumentalities, municipalities and public corporations face severe economic and fiscal challenges that, either individually or in the aggregate, could adversely affect the Commonwealth's ability to fund or otherwise maintain all necessary government programs and services, and have already caused one of its public corporations, the Public Finance Corporation, to default on a payment due to its bondholders. Further, the Commonwealth's liquidity has been significantly reduced and it no longer has access to capital markets. In June 2015, the Governor issued a public announcement that the Commonwealth will be unable to pay its debts absent a restructuring. Moreover, the government has enacted legislation that casts significant doubt with respect to whether it will continue making debt payments throughout fiscal year 2016, including a budget that does not appropriate funds needed for debt service payments by certain public corporations and a law that allows the Puerto Rico Treasury Secretary to discontinue funding the debt service reserve for the Commonwealth's general obligation debt unless the Commonwealth or Government Development Bank for Puerto Rico obtain financing from the capital markets in the current fiscal year ending June 30, 2016.

The Commonwealth's ability to finance its budget deficits is very limited. If the government is unable to access the capital markets to place new debt or refinance its upcoming maturities, the government may have to continue implementing additional austerity measures, including reducing spending, imposing new taxes, and taking emergency or extraordinary actions, including a debt restructuring or a default or moratorium on debt-service payments, which would slow Puerto Rico's weak economy even further. The Commonwealth may also have to reduce or eliminate important government programs and services in order to attempt to balance its budget and comply with its debt obligations.

It is uncertain how Puerto Rico's business, political and social sectors would react to a significant reduction or elimination of such programs and services. It is also uncertain whether Puerto Rico's government, including some of its municipalities, instrumentalities and public corporations, will be able to continue to service their debts as they become due. Any further deterioration of economic or fiscal conditions in Puerto Rico could adversely and materially affect the value of our credit facilities to the government of Puerto Rico and our investment portfolio of Puerto Rico

government bonds.

On February 5, 2015, Dr. Anne O. Krueger, Dr. Ranjit S. Teja and Dr. Andrew Wolfe (the “Former IMF economists”), each of whom has previously occupied senior executive positions at the International Monetary Fund (“IMF”), were engaged to analyze the Commonwealth’s economic and financial stability and growth prospects.

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Their final report was delivered to the Governor of Puerto Rico on June 28, 2015 and was made public on that date.

The report from the Former IMF economists (the “Krueger Report”) states that Puerto Rico faces an acute crisis in the face of faltering economic activity, fiscal solvency and debt sustainability, and institutional credibility.

At June 30, 2015, we had approximately \$515.3 million of outstanding credit facilities to the government of Puerto Rico, including its instrumentalities, municipalities and public corporations. We do not have any credit facilities to the Public Finance Corporation. A substantial portion of our credit exposure to Puerto Rico’s government consists of collateralized loans or obligations that have a specific source of income or revenues identified for their repayment. Approximately \$214 million of these loans are general obligation debt of municipalities secured by *ad valorem* taxation, without limitation as to rate or amount, on all taxable property within the issuing municipalities. The good faith, credit and unlimited taxing power of each issuing municipality are pledged for the payment of its general obligation debt.

In addition, some of these obligations consist of senior and subordinated loans to public corporations that obtain revenues from rates charged for services or products, such as the Puerto Rico Electric Power Authority (“PREPA”) and the State Insurance Fund Corporation. The Commonwealth’s instrumentalities or public corporations have varying degrees of independence from the central government. Some instrumentalities or public corporations that provide essential or important government services, such as the University of Puerto Rico, the Puerto Rico Medical Services Administration and the Puerto Rico Metropolitan Bus Authority, are supported by the Commonwealth through budget appropriations, while others, such as PREPA, are owed substantial amounts for utility services rendered to the Commonwealth. It is uncertain whether any such instrumentalities or public corporations will continue to receive government support or whether they will be able to collect amounts owed by the Commonwealth or its instrumentalities.

At June 30, 2015, we had approximately \$301.3 million of credit facilities to public corporations of the Commonwealth, including:

- PREPA with an outstanding balance of \$197.6 million;
- The State Insurance Fund Corporation with an outstanding balance of \$77.6 million, which is approximately 130% collateralized by a portfolio of A-plus rated securities; and
- The Puerto Rico Housing Finance Authority with an outstanding balance of \$25.2 million to be repaid from abandoned or unclaimed funds at financial institutions that revert to the government under a Puerto Rico escheat law.

The outstanding balance of credit facilities to public corporations decreased during the second quarter as a result of a repayment in full by the Puerto Rico Aqueduct and Sewer Authority of a \$75 million loan.

Our banking subsidiary, Oriental Bank, is part of a four bank syndicate providing a \$550 million revolving line of credit to finance the purchase of fuel for PREPA's day-to-day power generation activities. Our participation in the line of credit has an unpaid principal balance of \$197.6 million as of June 30, 2015. We, as part of the bank syndicate, entered into a forbearance agreement with PREPA, which has been extended several times, most recently until September 15, 2015. In connection with such extensions, PREPA appointed a Chief Restructuring Officer to work alongside the Executive Director to develop, organize and manage a financial and operational restructuring of PREPA subject to the approval of PREPA's Board of Directors. PREPA also has been in negotiations with its forbearing creditors to restructure its debts and obtain financing for capital improvements needed to its infrastructure. There can be no assurance that PREPA and its forbearing creditors will agree on any restructuring. As previously disclosed, we have classified our credit facility to PREPA as substandard and on non-accrual status. We also took a \$24 million provision for loan and lease losses against such credit during the first quarter of 2015.

PREPA's enabling act provides for local receivership upon request to any Puerto Rico court of competent jurisdiction in the event of a default in debt-service payments or other obligations in connection with PREPA's bonds. The receiver so appointed would be empowered, directly or through its agents and attorneys, to take possession of the undertakings, income and revenues pledged to the payment of the bonds in default; to have, hold, use, operate, manage and control the same; and to exercise all of PREPA's rights and powers with respect to such undertakings. However, any such receiver would not have the power to sell, assign, mortgage or otherwise dispose of PREPA's assets, and its powers would be limited to the operation and maintenance of such undertakings and the

collection and application of the income and revenues therefrom. These provisions have not been tested in the courts, and it is not clear if and how they would apply in connection with other debts and obligations of PREPA upon an event of default.

In June 2014, Puerto Rico enacted the Puerto Rico Public Corporation Debt Enforcement and Recovery Act (the “Recovery Act”), which established procedures for the adjustment of debts of certain public corporations of the Commonwealth, which, as Puerto Rico governmental instrumentalities, are not currently eligible for federal bankruptcy relief under any chapter of the U.S. Bankruptcy Code. The Recovery Act states in its preamble that it further promotes the government’s public policy of no longer providing financial support to such public corporations, such as PREPA and PRASA, and promoting their economic independence. In February 2015, the U.S. District Court for the District of Puerto Rico held that the Recovery Act is preempted by the U.S. Bankruptcy Code and is therefore void pursuant to the Supremacy Clause of the United States Constitution. It also permanently enjoined the Commonwealth from enforcing the Recovery Act. Such decision was confirmed by the U.S. Circuit Court of Appeals for the First Circuit on July 6, 2015. However, the Commonwealth has declared its intent to file an appeal before the U.S. Supreme Court.

On February 11, 2015, Puerto Rico’s non-voting representative to the U.S. House of Representatives introduced a bill (H.R. 870) that would empower the government of Puerto Rico to authorize its municipalities and public corporations to restructure their debts under Chapter 9 of the U.S. Bankruptcy Code. Such bill has been referred to the Subcommittee on Regulatory Reform, Commercial and Antitrust Law. On July 15, 2015, an identical companion bill (S. 1774) was filed by 12 senators in the U.S. Senate. It is unclear if and when any of these bills will be approved and, if approved, whether they will have retroactive effect for debts that are currently outstanding.

If the Bank’s Puerto Rico government debtors are unable to pay their obligations as they become due, or under certain other circumstances, including, for example, a debt restructuring or a moratorium on debt-service payments by such debtors, we may be required to adversely classify additional credit facilities to such Puerto Rico government debtors and provision for additional losses in connection therewith. Any such additional adverse classification or provision may significantly affect our financial condition and regulatory capital ratios.

We are subject to extensive regulatory oversight by federal and local banking authorities.

We are subject to extensive supervision, regulation and examination by the FDIC, the Federal Reserve Board and the Office of the Commissioner of Financial Institutions of Puerto Rico. As a result, we are limited in the manner in which we conduct our business, undertake new investments and activities, and obtain financing. This regulatory structure is designed primarily for the protection of the Deposit Insurance Fund and our depositors, and not to benefit our stockholders. This regulatory structure also gives the regulatory authorities extensive discretion in connection with their supervisory and enforcement actions and examination policies, including policies with respect to capital levels, the timing and amount of dividend payments, the classification of assets, the establishment of adequate loan loss reserves for regulatory purposes, and the timing and amounts of assessments and fees. Also, any changes to such regulatory structure, including changes in interpretation or implementation of laws, regulations or policies, could affect us in substantial and unpredictable ways.

In addition, we must comply with significant anti-money laundering and anti-terrorism laws and regulations, Community Reinvestment Act laws and regulations, and consumer financial protection laws and regulations. Government agencies have the authority to impose monetary penalties and other sanctions or restrictions on institutions that fail to comply with these laws and regulations, which could significantly affect our business activities, including our ability to acquire other financial institutions or expand our branch network.

ITEM 2. UNREGISTERED SALES OF EQUITY SECURITIES AND USE OF PROCEEDS

On June 29, 2011, the Company announced the approval by the Board of Directors of a stock repurchase program to purchase an additional \$70 million of the Company's common stock in the open market.

Any shares of common stock repurchased are held by the Company as treasury shares. The Company records treasury stock purchases under the cost method whereby the entire cost of the acquired stock is recorded as treasury stock. During the quarter ended June 30, 2015, the Company purchased 303,985 additional shares under this program for a total of \$4.2 million, at an average price of \$13.9 per share.

The following table presents the shares repurchased for each month during the quarter ended June 30, 2015:

| <u>Period</u> | Total number of shares purchased | Average price paid per share | Total number of shares purchased as part of publicly announced programs | Maximum approximate dollar value of shares that may yet be purchased under the programs (In thousands) |
|------------------------------------|---|-------------------------------------|--|---|
| April 1-30, 2015 | 204,338 | \$ 14.38 | 204,338 | \$ 13,717 |
| May 1-31, 2015 | 48,200 | 13.09 | 48,200 | 13,086 |
| June 1-30, 2015 | 51,447 | 12.81 | 51,447 | 12,427 |
| Quarter ended June 30, 2015 | 303,985 | \$ 13.90 | 303,985 | \$ 12,427 |

The number of shares that may yet be purchased under the current \$70 million program is estimated at 1,164,671 and was calculated by dividing the remaining balance of \$12.4 million by \$10.67 (closing price of the Company's common stock at June 30, 2015). The Company did not purchase any shares of its common stock other than through its publicly announced stock repurchase program during the quarter ended June 30, 2015.

ITEM 3. DEFAULTS UPON SENIOR SECURITIES

None.

ITEM 4. MINE SAFETY DISCLOSURES

Not applicable.

ITEM 5. *OTHER INFORMATION*

None.

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ITEM 6. EXHIBITS

Exhibit No.

Description of Document:

31.1 Certification of Chief Executive Officer pursuant to Section 302 of the Sarbanes-Oxley Act of 2002.

31.2 Certification of Chief Financial Officer pursuant to Section 302 of the Sarbanes-Oxley Act of 2002.

32.1 Certification of Chief Executive Officer pursuant to Section 906 of the Sarbanes-Oxley Act of 2002.

32.2 Certification of Chief Financial Officer pursuant to Section 906 of the Sarbanes-Oxley Act of 2002.

101 The following materials from OFG Bancorp's Quarterly Report on Form 10-Q for the quarter ended June 30, 2015, formatted in XBRL (eXtensible Business Reporting Language): (i) Unaudited Consolidated Statements of Financial Condition, (ii) Unaudited Consolidated Statements of Operations, (iii) Unaudited Consolidated Statements of Comprehensive Income, (iv) Unaudited Consolidated Statements of Changes in Stockholders' Equity, (v) Unaudited Consolidated Statements of Cash Flows, and (vi) Notes to Unaudited Consolidated Financial Statements.

Signatures

Pursuant to the requirements of the Securities Exchange Act of 1934, the registrant has duly caused this report to be signed on its behalf by the undersigned, thereunto duly authorized.

OFG Bancorp

(Registrant)

By: /s/ José Rafael Fernández

Date: August 10, 2015

José Rafael Fernández
President and Chief Executive Officer

By: /s/ Ganesh Kumar

Date: August 10, 2015

Ganesh Kumar
Executive Vice President and Chief Financial
Officer

By: /s/ Maritza Arizmendi

Date: August 10, 2015

Maritza Arizmendi
Senior Vice President and Chief Accounting
Officer