OFG BANCORP
Form 10-Q
August 03, 2018

UNITED STATES

SECURITIES AND EXCHANGE COMMISSION

Washington, D.C. 20549

FORM 10-Q

(Mark One)

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

For the quarterly period ended June 30, 2018

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 Accelerated Filer ý Non-Accelerated Filer Smaller Reporting Company

(Do not check if a smaller reporting company)

Emerging Growth Company

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

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

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

43,983,195 common shares ($1.00 par value per share) outstanding as of July 31, 2018

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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 "Oriental"), 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 Oriental'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 expr 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 Oriental'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 credit default by the municipalities of the government of Puerto Rico;
- amendments to the fiscal plan approved by the Financial Oversight and Management Board of Puerto Rico;
- determinations in the court-supervised debt-restructuring process under Title III of PROMESA for the Puerto Rico government and all of its agencies, including some of its public corporations;
- the impact of property, credit and other losses in Puerto Rico as a result of hurricanes, earthquakes and other natural disasters;
- the amount of government, private and philanthropic financial assistance for the reconstruction of Puerto Rico's critical infrastructure, which suffered catastrophic damages caused by hurricane Maria;
- the pace and magnitude of Puerto Rico's economic recovery;
- the fiscal and monetary policies of the federal government and its agencies;
- changes in federal bank regulatory and supervisory policies, including required levels of capital;
- the relative strength or weakness of the commercial and consumer credit sectors and the real estate market in Puerto Rico;

- the performance of the stock and bond markets;
- competition in the financial services industry; 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; Oriental’s ability to grow its core businesses; decisions to downsize, sell or close units or otherwise change Oriental’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 Oriental as of the date of this report, and other than as required by law, including the requirements of applicable securities laws, Oriental 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.

OFG BANCORP

UNAUDITED CONSOLIDATED STATEMENTS OF FINANCIAL CONDITION

AS OF JUNE 30, 2018 AND DECEMBER 31, 2017

		June 30, 2018		December 31, 2017
		(In thousands)		
ASSETS				
Cash and cash equivalents:				
Cash and due from banks	$	368,344	$	478,182
Money market investments		6,991		7,021
Total cash and cash equivalents		**375,335**		**485,203**
Restricted cash		3,030		3,030
Investments:				
Trading securities, at fair value, with amortized cost of $647 (December 31, 2017 - $647)		418		191
Investment securities available-for-sale, at fair value, with amortized cost of $890,308 (December 31, 2017 - $648,800)		872,341		645,797
Investment securities held-to-maturity, at amortized cost, with fair value of $447,947 (December 31, 2017 - $497,681)		465,427		506,064
Federal Home Loan Bank (FHLB) stock, at cost		14,919		13,995
Other investments		3		3
Total investments		**1,353,108**		**1,166,050**
Loans:				
Loans held-for-sale, at lower of cost or fair value		10,215		12,272
Loans held for investment, net of allowance for loan and lease losses of $165,434 (December 31, 2017 - $167,509)		4,305,651		4,044,057
Total loans		**4,315,866**		**4,056,329**
Other assets:				
Foreclosed real estate		40,551		44,174
Accrued interest receivable		34,476		49,969
Deferred tax asset, net		125,141		127,421
Premises and equipment, net		66,174		67,860
Customers' liability on acceptances		30,578		27,663
Servicing assets		10,829		9,821
Derivative assets		1,100		771
Goodwill		86,069		86,069
Other assets		59,305		64,693
Total assets	$	**6,501,562**	$	**6,189,053**

See notes to unaudited consolidated financial statements

OFG BANCORP

UNAUDITED CONSOLIDATED STATEMENTS OF FINANCIAL CONDITION

AS OF JUNE 30, 2018 AND DECEMBER 31, 2017 (CONTINUED)

		June 30, 2018		December 31, 2017
		(In thousands)		
LIABILITIES AND STOCKHOLDERS' EQUITY				
Deposits:				
Demand deposits	$	2,176,935	$	2,039,126
Savings accounts		1,253,451		1,251,398
Time deposits		1,449,815		1,508,958
Total deposits		**4,880,201**		**4,799,482**
Borrowings:				
Securities sold under agreements to repurchase		387,770		192,869
Advances from FHLB		128,114		99,643
Subordinated capital notes		36,083		36,083
Other borrowings		299		153
Total borrowings		**552,266**		**328,748**
Other liabilities:				
Derivative liabilities		679		1,281
Acceptances executed and outstanding		30,578		27,644
Accrued expenses and other liabilities		80,019		86,791
Total liabilities		**5,543,743**		**5,243,946**
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, 2017 - 1,340,000 shares; 1,380,000 shares; and 960,000 shares) $25 liquidation value		92,000		92,000
84,000 shares of Series C issued and outstanding (December 31, 2017 - 84,000 shares); $1,000 liquidation value		84,000		84,000
Common stock, $1 par value; 100,000,000 shares authorized; 52,625,869 shares issued: 43,983,195 shares outstanding (December 31, 2017 - 52,625,869; 43,947,442)		52,626		52,626
Additional paid-in capital		541,734		541,600

Legal surplus	85,249		81,454
Retained earnings	221,441		200,878
Treasury stock, at cost, 8,642,674 shares (December 31, 2017 - 8,678,427 shares)	(103,969)		(104,502)
Accumulated other comprehensive (loss), net of tax of $2,284 (December 31, 2017 $564)	(15,262)		(2,949)
Total stockholders' equity	**957,819**		**945,107**
Total liabilities and stockholders' equity	$ **6,501,562**		$ **6,189,053**

See notes to unaudited consolidated financial statements

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OFG BANCORP

UNAUDITED CONSOLIDATED STATEMENTS OF OPERATIONS

FOR THE QUARTERS AND SIX-MONTH PERIODS ENDED JUNE 30, 2018 AND 2017

	Quarter Ended June 30,		Six-Month Period Ended June 30,	
	2018	2017	2018	2017
	(In thousands, except per share data)			
Interest income:				
Loans	$ 78,429	$ 77,238	$ 153,041	$ 154,888
Mortgage-backed securities	8,034	7,276	15,085	14,482
Investment securities and other	1,543	1,426	3,050	2,748
Total interest income	**88,006**	**85,940**	**171,176**	**172,118**
Interest expense:				
Deposits	7,651	7,652	14,949	15,005
Securities sold under agreements to repurchase	1,840	1,734	2,918	4,979
Advances from FHLB and other borrowings	448	607	822	1,202
Subordinated capital notes	479	384	905	751
Total interest expense	**10,418**	**10,377**	**19,594**	**21,937**
Net interest income	**77,588**	**75,563**	**151,582**	**150,181**
Provision for loan and lease losses, net	14,747	26,536	30,207	44,190
Net interest income after provision for loan and lease losses	**62,841**	**49,027**	**121,375**	**105,991**
Non-interest income:				
Banking service revenue	11,144	10,458	21,607	21,084
Wealth management revenue	6,262	6,516	12,281	12,731
Mortgage banking activities	988	959	2,745	1,546
Total banking and financial service revenues	**18,394**	**17,933**	**36,633**	**35,361**
FDIC shared-loss benefit, net	-	-	-	1,403
Net gain on:				
Sale of securities	-	6,891	-	6,891
Derivatives	-	22	-	103
Early extinguishment of debt	-	(80)	-	(80)
Other non-interest income	309	120	584	282
Total non-interest income, net	**18,703**	**24,886**	**37,217**	**43,960**

See notes to unaudited consolidated financial statements

OFG BANCORP

UNAUDITED CONSOLIDATED STATEMENTS OF OPERATIONS

FOR THE QUARTERS AND SIX-MONTH PERIODS ENDED JUNE 30, 2018 AND 2017 (CONTINUED)

	Quarter Ended June 30,		Six-Month Period Ended June 30,	
	2018	2017	2018	2017
	(In thousands, except per share data)			
Non-interest expense:				
Compensation and employee benefits	18,099	19,317	38,707	39,664
Professional and service fees	3,146	3,225	5,840	6,462
Occupancy and equipment	9,166	8,538	16,934	15,735
Insurance	1,482	1,183	2,960	2,783
Electronic banking charges	5,415	5,450	10,382	10,352
Information technology expenses	2,000	2,069	4,009	4,068
Advertising, business promotion, and strategic initiatives	1,024	1,405	2,371	2,800
Loss on sale of foreclosed real estate and other repossessed assets	392	1,787	1,618	3,113
Loan servicing and clearing expenses	1,227	1,270	2,388	2,459
Taxes, other than payroll and income taxes	2,384	2,393	4,645	4,764
Communication	815	913	1,700	1,828
Printing, postage, stationary and supplies	605	665	1,249	1,303
Director and investor relations	337	274	577	554
Credit related expenses	1,897	2,217	4,316	4,843
Other	4,311	2,110	6,725	3,772
Total non-interest expense	**52,300**	**52,816**	**104,421**	**104,500**
Income before income taxes	**29,244**	**21,097**	**54,171**	**45,451**
Income tax expense	9,595	3,993	17,605	13,197
Net income	**19,649**	**17,104**	**36,566**	**32,254**
Less: dividends on preferred stock	(3,465)	(3,466)	(6,930)	(6,931)
Income available to common shareholders	**$ 16,184**	**$ 13,638**	**$ 29,636**	**$ 25,323**
Earnings per common share:				
Basic	**$ 0.36**	**$ 0.30**	**$ 0.67**	**$ 0.58**
Diluted	**$ 0.35**	**$ 0.30**	**$ 0.65**	**$ 0.57**
Average common shares outstanding and equivalents	**51,226**	**51,100**	**51,157**	**51,093**
Cash dividends per share of common stock	**$ 0.06**	**$ 0.06**	**$ 0.12**	**$ 0.12**

See notes to unaudited consolidated financial statements

OFG BANCORP

UNAUDITED CONSOLIDATED STATEMENTS OF COMPREHENSIVE INCOME

FOR THE QUARTERS AND SIX-MONTH PERIODS ENDED JUNE 30, 2018 AND 2017

	Quarter Ended June 30,		Six-Month Period Ended June 30,	
	2018	2017	2018	2017
	(In thousands)			
Net income	**$ 19,649**	**$ 17,104**	**$ 36,566**	**$ 32,254**
Other comprehensive loss before tax:				
Unrealized (loss) gain on securities available-for-sale	(3,638)	3,454	(14,964)	5,319
Realized gain on investment securities included in net income	-	(6,891)	-	(6,891)
Unrealized gain (loss) on cash flow hedges	275	(102)	931	81
Other comprehensive (loss) before taxes	**(3,363)**	**(3,539)**	**(14,033)**	**(1,491)**
Income tax effect	286	(116)	1,720	(412)
Other comprehensive (loss) after taxes	**(3,077)**	**(3,655)**	**(12,313)**	**(1,903)**
Comprehensive income	**$ 16,572**	**$ 13,449**	**$ 24,253**	**$ 30,351**

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, 2018 AND 2017

	Six-Month Period Ended June 30,			
	2018		2017	
	(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		52,626
Balance at end of period		**52,626**		**52,626**
Additional paid-in capital:				
Balance at beginning of period		541,600		540,948
Stock-based compensation expense		635		515
Stock-based compensation excess tax benefit recognized in income		(140)		(100)
Lapsed restricted stock units		(361)		(358)
Balance at end of period		**541,734**		**541,005**
Legal surplus:				
Balance at beginning of period		81,454		76,293
Transfer from retained earnings		3,795		3,167
Balance at end of period		**85,249**		**79,460**
Retained earnings:				
Balance at beginning of period		200,878		177,808
Net income		36,566		32,254
Cash dividends declared on common stock		(5,278)		(5,277)
Cash dividends declared on preferred stock		(6,930)		(6,931)
Transfer to legal surplus		(3,795)		(3,167)
Balance at end of period		**221,441**		**194,687**
Treasury stock:				
Balance at beginning of period		(104,502)		(104,860)
Lapsed restricted stock units		533		358
Balance at end of period		**(103,969)**		**(104,502)**
Accumulated other comprehensive (loss), net of tax:				
Balance at beginning of period		(2,949)		1,596
Other comprehensive (loss), net of tax		(12,313)		(1,903)
Balance at end of period		**(15,262)**		**(307)**
Total stockholders' equity	**$**	**957,819**	**$**	**938,969**

See notes to unaudited consolidated financial statements

OFG BANCORP

UNAUDITED CONSOLIDATED STATEMENTS OF CASH FLOWS

FOR THE SIX-MONTH PERIODS ENDED JUNE 30, 2018 AND 2017

	Six-Month Period Ended June 30,	
	2018	**2017**
	(In thousands)	
Cash flows from operating activities:		
Net income	$ **36,566**	$ **32,254**
Adjustments to reconcile net income to net cash provided by operating activities:		
Amortization of deferred loan origination fees and fair value premiums on acquired loans	2,296	1,457
Amortization of investment securities premiums, net of accretion of discounts	3,045	4,362
Amortization of core deposit and customer relationship intangibles	659	737
FDIC shared-loss benefit	-	(1,403)
Depreciation and amortization of premises and equipment	4,454	4,231
Deferred income tax expense, net	4,001	7,570
Provision for loan and lease losses	30,207	44,190
Stock-based compensation	635	515
Stock-based compensation excess tax benefit recognized in income	(140)	(100)
(Gain) loss on:		
Sale of mortgage loans held-for-sale	(185)	(517)
Derivatives	-	(103)
Sale of securities	-	(6,891)
Early extinguishment of debt	-	80
Foreclosed real estate	1,436	3,453
Sale of other repossessed assets	(9)	(153)
Sale of other assets	(44)	-
Originations of loans held-for-sale	(47,929)	(74,806)
Proceeds from sale of mortgage loans held-for-sale	11,306	24,020
Net (increase) decrease in:		
Trading securities	(227)	53
Accrued interest receivable	15,493	429
Servicing assets	(1,008)	(8)
Other assets	6,683	12,493
Net (decrease) in:		
Accrued interest on deposits and borrowings	(359)	(370)
Accrued expenses and other liabilities	(18,419)	(45,858)
Net cash provided by operating activities	**48,461**	**5,635**

See notes to unaudited consolidated financial statements

OFG BANCORP

UNAUDITED CONSOLIDATED STATEMENTS OF CASH FLOWS

FOR THE SIX-MONTH PERIODS ENDED JUNE 30, 2018 AND 2017 (CONTINUED)

	Six-Month Period Ended June 30, 2018	2017
	(In thousands)	
Cash flows from investing activities:		
Purchases of:		
Investment securities available-for-sale	(259,665)	(114,595)
FHLB stock	(99,365)	(26,730)
Maturities and redemptions of:		
Investment securities available-for-sale	54,727	57,714
Investment securities held-to-maturity	38,640	41,920
FHLB stock	98,441	20,907
Proceeds from sales of:		
Investment securities available-for-sale	-	212,203
Foreclosed real estate and other repossessed assets, including write-offs	25,059	21,754
Premises and equipment	873	-
Origination and purchase of loans, excluding loans held-for-sale	(693,586)	(384,211)
Principal repayment of loans	382,191	367,834
Repayments to FDIC on shared-loss agreements	-	(10,125)
Additions to premises and equipment	(3,597)	(3,660)
Net cash (used in) provided by investing activities	**(456,282)**	**183,011**
Cash flows from financing activities:		
Net increase (decrease) in:		
Deposits	86,293	(41,900)
Securities sold under agreements to repurchase	194,879	(199,466)
FHLB advances, federal funds purchased, and other borrowings	28,816	32,194
Restricted units lapsed	172	-
Dividends paid on preferred stock	(6,930)	(6,931)
Dividends paid on common stock	(5,277)	(5,674)
Net cash provided (used in) financing activities	**$ 297,953**	**$ (221,777)**
Net change in cash, cash equivalents and restricted cash	**(109,868)**	**(33,131)**
Cash, cash equivalents and restricted cash at beginning of period	**488,233**	**513,469**
Cash, cash equivalents and restricted cash at end of period	**$ 378,365**	**$ 480,338**
Supplemental Cash Flow Disclosure and Schedule of Non-cash Activities:		
Interest paid	$ 19,095	$ 21,386

Income taxes paid	$	8,890	$	15
Mortgage loans securitized into mortgage-backed securities	$	37,618	$	49,648
Transfer from loans to foreclosed real estate and other repossessed assets	$	25,465	$	28,293
Reclassification of loans held-for-investment portfolio to held-for-sale portfolio	$	-	$	33,647
Reclassification of loans held-for-sale portfolio to held-for-investment portfolio	$	1,247	$	112
Financed sales of foreclosed real estate	$	667	$	534
Loans booked under the GNMA buy-back option	$	14,521	$	9,229

See notes to unaudited consolidated financial statements

OFG BANCORP

UNAUDITED CONSOLIDATED STATEMENTS OF CASH FLOWS

FOR THE SIX-MONTH PERIODS ENDED JUNE 30, 2018 AND 2017 (CONTINUED)

OFG BANCORP

NOTES TO CONSOLIDATED FINANCIAL STATEMENTS

NOTE 1 – ORGANIZATION, CONSOLIDATION AND BASIS OF PRESENTATION

Nature of Operations

OFG Bancorp (“Oriental”) is a publicly-owned financial holding company incorporated under the laws of the Commonwealth of Puerto Rico. Oriental 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, LLC. (“Oriental Insurance”), a retirement plan administrator, Oriental Pension Consultants, Inc. (“OPC”), and two operating subsidiaries of the Bank, OFG USA, LLC ("OFG USA") and Oriental International Bank, Inc. Through these subsidiaries and their respective divisions, Oriental 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 February 6, 2017, the Bank and the FDIC agreed to terminate the shared-loss agreements related to the Eurobank Acquisition. On December 18, 2012, Oriental 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.” These acquired businesses have been integrated with Oriental’s existing business.

New Accounting Updates Not Yet Adopted

Premium Amortization on Purchased Callable Debt Securities Receivables. In March 2017, the FASB issued ASU No. 2017-08, which requires the amortization of the premium on callable debt securities to the earliest call date. The amortization period for callable debt securities purchased at a discount would not be impacted by the ASU. This ASU will be applied prospectively for annual and interim periods in fiscal years beginning after December 15, 2018. The ASU is not expected to have a material impact on Oriental's consolidated financial position or results of operations. At June 30, 2018, Oriental does not have callable debt securities.

Plan Accounting: Defined Benefit Pension Plans (Topic 960), Defined Contribution Pension Plans (Topic 962), Health and Welfare Benefit Plans (Topic 965): Employee Benefit Plan Master Trust Reporting (a consensus of the Emerging Issues Task Force). In February 2017, the FASB issued ASU No. 2017-06, which intended to reduce diversity and improve the usefulness of information provided by employee benefit plans that hold interests in master trusts. This ASU will be applied prospectively for annual and interim periods in fiscal years beginning after December 15, 2018. The ASU is not expected to have a material impact on Oriental's consolidated financial position or results of operations.

Simplifying the Test for Goodwill Impairment. In January 2017, the FASB issued ASU No. 2017-04, which simplifies the measurement of goodwill impairment. An entity will no longer perform a hypothetical purchase price allocation to measure goodwill impairment. Instead, impairment will be measured using the difference between the carrying amount and the fair value of the reporting unit. This ASU will be applied prospectively for annual and interim periods in fiscal years beginning after December 15, 2019. We will assess the impact that the adoption of ASU 2017-04 will have on our consolidated financial statements and related disclosures during this year.

Measurement of Credit Losses on Financial Instruments. In June 2016, the FASB issued ASU No. 2016-13, which includes an impairment model (known as the current expected credit loss (CECL) model) that is based on expected losses rather than incurred losses. Under the new guidance, an entity recognizes as an allowance its estimate of expected credit losses. ASU No. 2016-13 is effective for fiscal years, and interim periods, beginning after December 15, 2019. Oriental will implement ASU No. 2016-13 on January 1, 2020. While we continue to assess the impact of ASU No. 2016-13, we have developed a roadmap with time schedules in place from 2016 to implementation date. Oriental's cross-functional implementation team has developed a project plan to ensure we comply with all updates from this ASU at the time of adoption. We recently have selected the software and are in the process of assessing the methodology to be used in order to develop an acceptable model to estimate the expected credit losses. After the model has been developed, reviewed and validated in accordance with our governance policies, Oriental will keep disclosing relevant information of concerning implementation process and impact of ASU No. 2016-13, as well as the updating of policies, procedures and internal controls. Although Oriental expects the allowance for credit losses to increase upon adoption with a corresponding adjustment to retained earnings, the ultimate amount of the increase will depend on the portfolio composition, credit quality, economic conditions and reasonable and supportable forecasts at that time.

Leases. In February 2016, the FASB issued ASU No. 2016-02, the FASB issued ASU No. 2016-02, which requires lessees to recognize a right-of-use asset and related lease liability for leases classified as operating leases at the commencement date that have lease terms of more than 12 months. This ASU retains the classification distinction between finance leases and operating leases. ASU No. 2016-02 is effective for fiscal years, and interim periods, beginning after December 15, 2018. Oriental plans to adopt this guidance effective January 1, 2019 using the required modified retrospective approach, which includes presenting the cumulative effect of initial application along with supplementary disclosures. As a lessor and lessee, we do not anticipate the classification of our leases to change, but we expect to recognize right-of-use assets and lease liabilities for substantially all of our operating lease commitments for which we are the lessee as a lease liability and corresponding right-of-use asset on our consolidated financial statements. Oriental has made substantial progress in reviewing contractual arrangements for embedded leases in an effort to identify Oriental's full lease population and is presently evaluating all of its leases, as well as contracts that may contain embedded leases, for compliance with the new lease accounting rules. Oriental's leases primarily consist of leased office space, and information technology equipment. At June 30, 2018, Oriental had $33.7 million of minimum lease commitments from these operating leases (refer to Note 20). Although Oriental is still evaluating the impact that the adoption of this accounting pronouncement will have on its consolidated financial statements, preliminarily it expects that the amounts to be recognized as right-of-use assets and lease liabilities will be less than 1% of its total assets and is not expected to have a material impact on its regulatory capital.

New Accounting Updates Adopted During the Six-month Period Ended June 30, 2018

Restricted Cash. In November 2016, the FASB issued ASU No. 2016-18, which amends Topic 230 (Statement of Cash Flows) and requires that a statement of cash flows explain the change during the period in the total of cash, cash equivalents, and amounts generally described as restricted cash or restricted cash equivalents. ASU No. 2016-18 is intended to reduce diversity in practice in how restricted cash or restricted cash equivalents are presented and classified in the statement of cash flows. ASU No. 2016-18 is effective for fiscal years, and interim periods, beginning after December 15, 2017. The standard requires application using a retrospective transition method. The adoption of ASU No. 2016-18 on January 1, 2018, changed the presentation and classification of restricted cash and restricted cash equivalents in our consolidated statements of cash flows.

Revenue from Contracts with Customers. In May 2014, the FASB issued ASU No. 2014-09, which supersedes the revenue recognition requirements Topic 605 (Revenue Recognition), and most industry-specific guidance. ASU No. 2014-09 is based on the principle that revenue is recognized to depict the transfer of goods or services to customers in an amount that reflects the consideration to which the entity expects to be entitled in exchange for those goods or services. ASU No. 2014-09 also requires additional disclosure about the nature, amount, timing and uncertainty of revenue and cash flows arising from customer contracts, including significant judgments and changes in judgments and assets recognized from costs incurred to obtain or fulfill a contract. ASU No. 2014-09 permits two methods of adoption: retrospectively to each prior reporting period presented (full retrospective method), or retrospectively with the cumulative effect of initially applying the guidance recognized at the date of initial application (modified retrospective method). In August 2015, the FASB issued ASU No. 2015-14 to defer the effective date of ASU No.

2014-09 by one year to fiscal years beginning after December 15, 2017. Oriental has adopted this ASU on January 1, 2018 using the modified retrospective method. Oriental's implementation efforts included the identification of revenue streams that are within the scope of the new guidance and the review of related contracts with customers to determine their effect on certain non-interest income items presented in our consolidated statements of operations and the additional presentation disclosures required (refer to note 21). We concluded that substantially all of Oriental's revenues are generated from activities that are outside the scope of this ASU, and the adoption did not have a material impact on our consolidated financial statements. Therefore, there was no cumulative effect adjustment recorded.

NOTE 2 – SIGNIFICANT EVENTS

Hurricanes Irma and Maria

During 2017, Oriental was impacted by hurricanes Irma and Maria, which struck the Island on September 7, 2017 and September 20, 2017, respectively. Hurricane Maria caused catastrophic damages throughout Puerto Rico, including homes, businesses, roads, bridges, power lines, commercial establishments, and public facilities. It caused an unprecedented crisis when it ravaged the Island's electric power grid less than two weeks after hurricane Irma left over a million Puerto Rico residents without power. For several months after the hurricanes, a large part of Puerto Rico was and some areas still remain without electricity, many businesses were unable to operate, and government authorities struggled to deliver emergency supplies and clean drinking water to many communities outside the San Juan metropolitan area. Further, payment and delivery systems, including the U.S. Post Office, were unable to operate for weeks after hurricane Maria.

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NOTES TO CONSOLIDATED FINANCIAL STATEMENTS – (Continued)

Almost all of Oriental's operations and clients are located in Puerto Rico. Although Oriental's business operations were disrupted by major damages to Puerto Rico's critical infrastructure, including its electric power grid and telecommunications network, Oriental's digital channels, core banking and electronic funds transfer systems continued to function uninterrupted during and after the hurricanes. Within days after hurricane Maria, and upon securing a continuing supply of diesel fuel for its electric power generators, Oriental was able to open its main offices and many of its branches and ATMs in addition to its digital and phone trade channels.

As a result of this event, and based on current assessments of information available for the impact of the hurricanes on our credit portfolio, 2017 third and fourth quarter results included an additional loan loss provision of $27.0 million and $5.4 million, respectively.

Oriental implemented its disaster response plan as these storms approached its service areas. To operate in disaster response mode, Oriental incurred expenses for, among other things, buying diesel and generators for electric power, debris removal, security matters, property damages, and emergency communication with customers regarding the status of Bank operations. The estimated total non-credit operating costs as of December 31, 2017 amounted to $6.6 million. No additional losses have been incurred at June 30, 2018.

Oriental maintains insurance for casualty losses as well as for disaster response costs and certain revenue lost through business interruption. Management believes that recovery of $2.2 million incurred costs as of December 31, 2017 is probable. Oriental received a $1.0 million partial payment from the insurance company during the quarter ended December 2017 and a $0.7 million payment during the six-month period ended June 30, 2018. Accordingly, a receivable of $0.5 million and $1.2 million was included in other assets at June 30, 2018 and December 31, 2017, respectively, for the expected recovery.

NOTE 3 – RESTRICTED CASH

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

	June 30, 2018	December 31, 2017
	(In thousands)	
Cash pledged as collateral to other financial institutions to secure:		
Derivatives	$ 1,980	$ 1,980

Obligations under agreement of loans sold with recourse		1,050		1,050
	$	**3,030**	**$**	**3,030**

At both June 30, 2018 and December 31, 2017, the Bank's international banking entities, Oriental International Bank Inc. ("OIB") and Oriental Overseas, a division of the Bank, held an unencumbered certificate of deposit and other short-term highly liquid securities in the amount of $300 thousand and $325 thousand, respectively, as the legal reserve required for international banking entities under Puerto Rico law. These instruments cannot be withdrawn or transferred by OIB or Oriental Overseas without prior written approval of the Office of the Commissioner of Financial Institutions of Puerto Rico (the "OCFI").

As part of its derivative activities, Oriental has entered into collateral agreements with certain financial counterparties. At both June 30, 2018 and December 31, 2017, Oriental had delivered approximately $2.0 million of cash as collateral for such derivatives activities.

Oriental has a contract with FNMA which requires collateral to guarantee the repurchase, if necessary, of loans sold with recourse. At both June 30, 2018 and December 31, 2017, Oriental delivered as collateral cash amounting to approximately $1.1 million.

The Bank is required by Puerto Rico law to maintain average weekly reserve balances to cover demand deposits. The amount of those minimum average reserve balances for the week that covered June 30, 2018 was $219.7 million (December 31, 2017 - $189.2 million). At June 30, 2018 and December 31, 2017, 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.

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NOTES TO CONSOLIDATED FINANCIAL STATEMENTS – (Continued)

NOTE 4 – INVESTMENT SECURITIES

Money Market Investments

Oriental 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 both, June 30, 2018 and December 31, 2017, money market instruments included as part of cash and cash equivalents amounted to $7.0 million.

Investment Securities

The amortized cost, gross unrealized gains and losses, fair value, and weighted average yield of the securities owned by Oriental at June 30, 2018 and December 31, 2017 were as follows:

	June 30, 2018				
	Amortized Cost	**Gross Unrealized Gains**	**Gross Unrealized Losses**	**Fair Value**	**Weighted Average Yield**
			(In thousands)		
Available-for-sale					
Mortgage-backed securities					
FNMA and FHLMC certificates	$ 600,978	$ 266	$ 11,571	$ 589,673	2.58%
GNMA certificates	198,301	459	3,902	194,858	3.03%
CMOs issued by US government-sponsored agencies	74,147	-	2,992	71,155	1.90%
Total mortgage-backed securities	**873,426**	**725**	**18,465**	**855,686**	**2.62%**
Investment securities					
US Treasury securities	10,610	-	161	10,449	1.30%
Obligations of US government-sponsored agencies	2,622	-	81	2,541	1.38%

Obligations of Puerto Rico government and public instrumentalities		2,455		-		-		2,455	5.55%
Other debt securities		1,195		15		-		1,210	2.95%
Total investment securities		**16,882**		**15**		**242**		**16,655**	**2.05%**
Total securities available for sale	**$**	**890,308**	**$**	**740**	**$**	**18,707**	**$**	**872,341**	**2.61%**
Held-to-maturity									
Mortgage-backed securities									
FNMA and FHLMC certificates	**$**	**465,427**	**$**	**-**	**$**	**17,480**	**$**	**447,947**	**2.07%**

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NOTES TO CONSOLIDATED FINANCIAL STATEMENTS – (Continued)

	December 31, 2017				
	Amortized Cost	Gross Unrealized Gains	Gross Unrealized Losses	Fair Value	Weighted Average Yield
	(In thousands)				
Available-for-sale					
Mortgage-backed securities					
FNMA and FHLMC certificates	$ 383,194	$ 1,402	$ 2,881	$ 381,715	2.39%
GNMA certificates	166,436	1,486	584	167,338	2.94%
CMOs issued by US government-sponsored agencies	82,026	-	1,955	80,071	1.90%
Total mortgage-backed securities	**631,656**	**2,888**	**5,420**	**629,124**	**2.47%**
Investment securities					
US Treasury securities	10,276	-	113	10,163	1.25%
Obligations of US government-sponsored agencies	2,927	-	48	2,879	1.38%
Obligations of Puerto Rico government and public instrumentalities	2,455	-	362	2,093	5.55%
Other debt securities	1,486	52	-	1,538	2.97%
Total investment securities	**17,144**	**52**	**523**	**16,673**	**2.04%**
Total securities available-for-sale	**$ 648,800**	**$ 2,940**	**$ 5,943**	**$ 645,797**	**2.46%**
Held-to-maturity					
Mortgage-backed securities					
FNMA and FHLMC certificates	**$ 506,064**	**$ -**	**$ 8,383**	**$ 497,681**	**2.07%**

The amortized cost and fair value of Oriental's investment securities at June 30, 2018, 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.

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NOTES TO CONSOLIDATED FINANCIAL STATEMENTS – (Continued)

	June 30, 2018			
	Available-for-sale		Held-to-maturity	
	Amortized Cost	Fair Value	Amortized Cost	Fair Value
	(In thousands)			
Mortgage-backed securities				
Due from 1 to 5 years				
FNMA and FHLMC certificates	$ 4,907	$ 4,833	$ -	$ -
Total due from 1 to 5 years	**4,907**	**4,833**	-	-
Due after 5 to 10 years				
CMOs issued by US government-sponsored agencies	$ 65,480	$ 62,680	$ -	$ -
FNMA and FHLMC certificates	227,886	223,185	-	-
Total due after 5 to 10 years	**293,366**	**285,865**	**-**	**-**
Due after 10 years				
FNMA and FHLMC certificates	$ 368,185	$ 361,655	$ 465,427	$ 447,947
GNMA certificates	198,301	194,858	-	-
CMOs issued by US government-sponsored agencies	8,667	8,475	-	-
Total due after 10 years	**575,153**	**564,988**	**465,427**	**447,947**
Total mortgage-backed securities	**873,426**	**855,686**	**465,427**	**447,947**
Investment securities				
Due less than one year				
US Treasury securities	$ 646	$ 646	$ -	$ -
Obligations of Puerto Rico government and public instrumentalities	2,455	2,455	-	-
Total due in less than one year	**3,101**	**3,101**	**-**	**-**
Due from 1 to 5 years				
US Treasury securities	$ 9,964	$ 9,803	$ -	$ -
Obligations of US government and sponsored agencies	2,622	2,541	-	-
Total due from 1 to 5 years	**12,586**	**12,344**	**-**	**-**
Due from 5 to 10 years				
Other debt securities	1,195	1,210	-	-
Total due after 5 to 10 years	**1,195**	**1,210**	**-**	**-**
Total investment securities	**16,882**	**16,655**	**-**	**-**

Total	**$ 890,308**	**$ 872,341**	**$ 465,427**	**$ 447,947**

During the six-month period ended June 30, 2018, Oriental retained securitized GNMA pools totaling $37.6 million, amortized cost, at a yield of 3.45% from its own originations while, during the six-month period ended June 30, 2017, that amount totaled $49.8 million, amortized cost, at a yield of 3.15%.

During the six-month period ended June 30, 2017, Oriental sold $166.0 million of mortgage-backed securities and $39.3 million of US Treasury securities, and recorded a net gain on sale of securities of $6.9 million. During the six-month period ended June 30, 2018, Oriental did not sell any mortgage-backed securities or investment securities.

	Six-Month Period Ended June 30, 2017			
Description	**Sale Price**	**Book Value at Sale**	**Gross Gains**	**Gross Losses**
		(In thousands)		
Sale of securities available-for-sale				
Mortgage-backed securities				
FNMA and FHLMC certificates	$ 107,510	$ 102,311	$ 5,199	$ -
GNMA certificates	$ 65,284	$ 63,704	$ 1,580	$ -
Investment securities				
US Treasury securities	39,409	39,297	112	-
Total mortgage-backed securities	**$ 212,203**	**$ 205,312**	**$ 6,891**	**$ -**

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NOTES TO CONSOLIDATED FINANCIAL STATEMENTS – (Continued)

The following tables show Oriental'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, 2018 and December 31, 2017:

	June 30, 2018		
	12 months or more		
	Amortized Cost	Unrealized Loss	Fair Value
		(In thousands)	
Securities available-for-sale			
CMOs issued by US Government-sponsored agencies	$ 66,298	$ 2,822	$ 63,476
FNMA and FHLMC certificates	101,571	4,296	97,275
Obligations of US Government and sponsored agencies	2,622	81	2,541
GNMA certificates	20,388	1,055	19,333
US Treasury Securities	9,964	161	9,803
	$ 200,843	**$ 8,415**	**$ 192,428**
Securities held to maturity			
FNMA and FHLMC certificates	**$ 324,963**	**$ 13,594**	**$ 311,369**

	Less than 12 months		
	Amortized Cost	Unrealized Loss	Fair Value
		(In thousands)	
Securities available-for-sale			
CMOs issued by US government-sponsored agencies	$ 7,849	$ 170	$ 7,679
FNMA and FHLMC certificates	413,181	7,275	405,906
GNMA certificates	142,431	2,847	139,584
US Treasury Securities	324	-	324
	$ 563,785	**$ 10,292**	**$ 553,493**
Securities held-to-maturity			
FNMA and FHLMC Certificates	**$ 140,464**	**$ 3,886**	**$ 136,578**

	Total		
	Amortized Cost	Unrealized Loss	Fair Value
		(In thousands)	
Securities available-for-sale			
CMOs issued by US government-sponsored agencies	$ 74,147	$ 2,992	$ 71,155
FNMA and FHLMC certificates	514,752	11,571	503,181
Obligations of US government and sponsored agencies	2,622	81	2,541

GNMA certificates		162,819		3,902		158,917
US Treausury Securities		10,288		161		10,127
	$	**764,628**	**$**	**18,707**	**$**	**745,921**
Securities held-to-maturity						
FNMA and FHLMC certificates	**$**	**465,427**	**$**	**17,480**	**$**	**447,947**

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NOTES TO CONSOLIDATED FINANCIAL STATEMENTS – (Continued)

		December 31, 2017 12 months or more	
	Amortized Cost	Unrealized Loss (In thousands)	Fair Value
Securities available-for-sale			
CMOs issued by US Government-sponsored agencies	$ 72,562	$ 1,857	$ 70,705
FNMA and FHLMC certificates	111,635	2,122	109,513
Obligations of US Government and sponsored agencies	2,927	48	2,879
Obligations of Puerto Rico government and public instrumentalities	2,455	362	2,093
GNMA certificates	20,803	499	20,304
US Treasury Securities	9,952	113	9,839
	$ 220,334	**$ 5,001**	**$ 215,333**
Securities available-for-sale			
FNMA and FHLMC certificates	**$ 352,399**	**7,264**	**345,135**

		Less than 12 months	
	Amortized Cost	Unrealized Loss (In thousands)	Fair Value
Securities available-for-sale			
CMOs issued by US Government-sponsored agencies	9,464	98	9,366
FNMA and FHLMC certificates	125,107	759	124,348
GNMA certificates	14,001	85	13,916
US Treasury Securities	324	-	324
	$ 148,896	**$ 942**	**$ 147,954**
Securities held to maturity			
FNMA and FHLMC certificates	**$ 153,665**	**$ 1,119**	**$ 152,546**

		Total	
	Amortized Cost	Unrealized Loss (In thousands)	Fair Value
Securities available-for-sale			
CMOs issued by US Government-sponsored agencies	82,026	1,955	80,071
FNMA and FHLMC certificates	236,742	2,881	233,861
Obligations of Puerto Rico government and public instrumentalities	2,455	362	2,093
	2,927	48	2,879

Obligations of US government and sponsored agencies						
GNMA certificates		34,804		584		34,220
US Treausury Securities		10,276		113		10,163
	$	**369,230**	**$**	**5,943**	**$**	**363,287**
Securities held to maturity						
FNMA and FHLMC certificates	**$**	**506,064**	**$**	**8,383**	**$**	**497,681**

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NOTES TO CONSOLIDATED FINANCIAL STATEMENTS – (Continued)

Oriental performs valuations of the investment securities on a monthly basis. Moreover, Oriental 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 Oriental believes that the methodology used to value these exposures is reasonable, the methodology is subject to continuing improvement, 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.

All of the investments ($1.2 billion, amortized cost) with an unrealized loss position at June 30, 2018 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 sole exposure to a Puerto Rico government bond ($2.5 million, amortized cost) at June 30, 2018, consists of an obligation issued by the Puerto Rico Highways and Transportation Authority ("PRHTA") secured by a pledge of toll revenues from the Teodoro Moscoso Bridge operated through a public-private partnership. The PRHTA bond had an aggregate fair value of $2.5 million at June 30, 2018 and matured on July 1, 2018. The full payment was received on July 2, 2018.

NOTE 5 - LOANS

Oriental’s loan portfolio is composed of two segments, loans initially accounted for under the amortized cost method (referred to as "originated and other" loans) and loans acquired (referred to as "acquired" loans). Acquired loans are further segregated between acquired BBVAPR loans and acquired Eurobank loans.

The composition of Oriental’s loan portfolio at June 30, 2018 and December 31, 2017 was as follows:

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NOTES TO CONSOLIDATED FINANCIAL STATEMENTS – (Continued)

	June 30, 2018	December 31, 2017
	(In thousands)	
Originated and other loans and leases held for investment:		
Mortgage	$ 678,259	$ 683,607
Commercial	1,507,368	1,307,261
Consumer	339,341	330,039
Auto and leasing	1,014,664	883,985
	3,539,632	**3,204,892**
Allowance for loan and lease losses on originated and other loans and leases	(94,218)	(92,718)
	3,445,414	**3,112,174**
Deferred loan costs, net	7,028	6,695
Total originated and other loans held for investment, net	**3,452,442**	**3,118,869**
Acquired loans:		
Acquired BBVAPR loans:		
Accounted for under ASC 310-20 (Loans with revolving feature and/or acquired at a premium)		
Commercial	2,909	4,380
Consumer	25,736	28,915
Auto	11,283	21,969
	39,928	**55,264**
Allowance for loan and lease losses on acquired BBVAPR loans accounted for under ASC 310-20	(2,726)	(3,862)
	37,202	**51,402**
Accounted for under ASC 310-30 (Loans acquired with deteriorated credit quality, including those by analogy)		
Mortgage	516,934	532,053
Commercial	223,853	243,092
Consumer	495	1,431
Auto	26,937	43,696
	768,219	**820,272**
Allowance for loan and lease losses on acquired BBVAPR loans accounted for under ASC 310-30	(44,176)	(45,755)
	724,043	**774,517**
Total acquired BBVAPR loans, net	**761,245**	**825,919**
Acquired Eurobank loans:		
Loans secured by 1-4 family residential properties	65,637	69,538
Commercial	49,706	53,793
Consumer	935	1,112
Total acquired Eurobank loans	**116,278**	**124,443**
Allowance for loan and lease losses on Eurobank loans	(24,314)	(25,174)
Total acquired Eurobank loans, net	**91,964**	**99,269**

Total acquired loans, net		**853,209**		**925,188**
Total held for investment, net		**4,305,651**		**4,044,057**
Mortgage loans held-for-sale		10,215		12,272
Total loans, net	**$**	**4,315,866**	**$**	**4,056,329**

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NOTES TO CONSOLIDATED FINANCIAL STATEMENTS – (Continued)

As a result of the devastation caused by hurricanes Irma and Maria, Oriental offered an automatic three-month moratorium for the payment due on certain loans. The level of delinquencies for mortgage and auto loans as of December 31, 2017 was impacted by the loan moratorium. Aging of current and early delinquent loans in moratorium were frozen at September 30, 2017, throughout the moratorium period. In addition, although the repayment schedule was modified as part of the moratorium, certain borrowers continued to make payments shortly after the moratorium, having an impact on the respective delinquency status at December 31, 2017. At June 30, 2018, most of the loan moratoriums have expired, and total delinquency levels are returning to pre-hurricane levels.

Originated and Other Loans and Leases Held for Investment

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

The tables below present the aging of the recorded investment in gross originated and other loans held for investment at June 30, 2018 and December 31, 2017, by class of loans. Mortgage loans past due include 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.

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NOTES TO CONSOLIDATED FINANCIAL STATEMENTS – (Continued)

	June 30, 2018						
	30-59 Days Past Due	**60-89 Days Past Due**	**90+ Days Past Due**	**Total Past Due**	**Current**	**Total Loans**	**Loans 90+ Days Past Due and Still Accruing**
	(In thousands)						
Mortgage							
Traditional (by origination year):							
Up to the year 2002	$ 165	$ 1,397	$ 3,539	$ 5,101	$ 38,932	$ 44,033	$ 242
Years 2003 and 2004	83	1,624	5,907	7,614	71,750	79,364	-
Year 2005	-	831	4,125	4,956	37,488	42,444	68
Year 2006	350	1,603	4,783	6,736	52,292	59,028	-
Years 2007, 2008 and 2009	112	1,360	7,443	8,915	56,154	65,069	57
Years 2010, 2011, 2012, 2013	350	719	8,638	9,707	111,791	121,498	366
Years 2014, 2015, 2016, 2017 and 2018	-	132	1,593	1,725	128,731	130,456	-
	1,060	7,666	36,028	44,754	497,138	541,892	733
Non-traditional	-	-	3,131	3,131	12,363	15,494	-
Loss mitigation program	12,147	5,135	18,539	35,821	70,274	106,095	2,726
	13,207	12,801	57,698	83,706	579,775	663,481	3,459
Home equity secured personal loans	-	-	-	-	257	257	-
GNMA's buy-back option program	-	-	14,521	14,521	-	14,521	-
	13,207	**12,801**	**72,219**	**98,227**	**580,032**	**678,259**	**3,459**
Commercial							
Commercial secured by real estate:							

Corporate	-	-	-	-	274,435	274,435	-
Institutional	-	-	-	-	81,019	81,019	-
Middle market	-	-	5,602	5,602	188,671	194,273	-
Retail	1,240	473	9,327	11,040	205,450	216,490	-
Floor plan	-	-	-	-	4,017	4,017	-
Real estate	-	-	-	-	15,157	15,157	-
	1,240	473	14,929	16,642	768,749	785,391	-
Other commercial and industrial:							
Corporate	-	-	-	-	190,414	190,414	-
Institutional	-	-	-	-	113,810	113,810	-
Middle market	7,233	174	881	8,288	86,691	94,979	-
Retail	341	212	709	1,262	283,334	284,596	-
Floor plan	26	-	51	77	38,101	38,178	-
	7,600	386	1,641	9,627	712,350	721,977	-
	8,840	**859**	**16,570**	**26,269**	**1,481,099**	**1,507,368**	**-**

OFG BANCORP

NOTES TO CONSOLIDATED FINANCIAL STATEMENTS – (Continued)

	June 30, 2018						
	30-59 Days Past Due	60-89 Days Past Due	90+ Days Past Due	Total Past Due	Current	Total Loans	Loans 90+ Days Past Due and Still Accruing
	(In thousands)						
Consumer							
Credit cards	$ 701	$ 274	$ 875	$ 1,850	$ 26,009	$ 27,859	$ -
Overdrafts	12	1	-	13	145	158	-
Personal lines of credit	72	30	40	142	1,789	1,931	-
Personal loans	4,045	1,704	1,100	6,849	287,099	293,948	-
Cash collateral personal loans	137	87	17	241	15,204	15,445	-
	4,967	2,096	2,032	9,095	330,246	339,341	-
Auto and leasing	45,953	19,870	11,101	76,924	937,740	1,014,664	-
Total	**$ 72,967**	**$ 35,626**	**$ 101,922**	**$ 210,515**	**$ 3,329,117**	**$ 3,539,632**	**$ 3,459**

OFG BANCORP

NOTES TO CONSOLIDATED FINANCIAL STATEMENTS – (Continued)

	December 31, 2017						
	30-59 Days Past Due	**60-89 Days Past Due**	**90+ Days Past Due**	**Total Past Due**	**Current**	**Total Loans**	**Loans 90+ Days Past Due and Still Accruing**
			(In thousands)				
Mortgage							
Traditional (by origination year):							
Up to the year 2002	$ 86	$ 938	$ 3,537	$ 4,561	$ 41,579	$ 46,140	$ 467
Years 2003 and 2004	92	1,077	6,304	7,473	75,758	83,231	-
Year 2005	101	383	3,348	3,832	40,669	44,501	68
Year 2006	242	604	5,971	6,817	55,966	62,783	66
Years 2007, 2008 and 2009	358	1,258	8,561	10,177	58,505	68,682	577
Years 2010, 2011, 2012, 2013	233	978	7,393	8,604	116,674	125,278	1,202
Years 2014, 2015, 2016 and 2017	-	75	1,649	1,724	121,194	122,918	-
	1,112	5,313	36,763	43,188	510,345	553,533	2,380
Non-traditional	-	326	3,543	3,869	14,401	18,270	-
Loss mitigation program	7,233	3,331	18,923	29,487	73,793	103,280	4,981
	8,345	8,970	59,229	76,544	598,539	675,083	7,361
Home equity secured personal loans	-	-	-	-	256	256	-
GNMA's buy-back option program	-	-	8,268	8,268	-	8,268	-
	8,345	**8,970**	**67,497**	**84,812**	**598,795**	**683,607**	**7,361**
Commercial							
Commercial secured by real estate:							

Corporate	-	-	-	-	235,426	235,426	-
Institutional	-	-	118	118	44,648	44,766	-
Middle market	765	-	3,527	4,292	225,649	229,941	-
Retail	352	936	9,695	10,983	235,084	246,067	-
Floor plan	-	-	-	-	3,998	3,998	-
Real estate	-	-	-	-	17,556	17,556	-
	1,117	936	13,340	15,393	762,361	777,754	-
Other commercial and industrial:							
Corporate	-	-	-	-	170,015	170,015	-
Institutional	-	-	-	-	125,591	125,591	-
Middle market	-	-	881	881	84,482	85,363	-
Retail	455	103	1,616	2,174	111,078	113,252	-
Floor plan	9	-	51	60	35,226	35,286	-
	464	103	2,548	3,115	526,392	529,507	-
	1,581	**1,039**	**15,888**	**18,508**	**1,288,753**	**1,307,261**	**-**

OFG BANCORP

NOTES TO CONSOLIDATED FINANCIAL STATEMENTS – (Continued)

	December 31, 2017						
	30-59 Days Past Due	60-89 Days Past Due	90+ Days Past Due	Total Past Due	Current	Total Loans	Loans 90+ Days Past Due and Still Accruing
	(In thousands)						
Consumer							
Credit cards	$ 246	$ 130	$ 1,227	$ 1,603	$ 26,827	$ 28,430	$ -
Overdrafts	20	6	31	57	157	214	-
Personal lines of credit	259	54	87	400	1,820	2,220	-
Personal loans	3,778	1,494	223	5,495	278,982	284,477	-
Cash collateral personal loans	103	59	312	474	14,224	14,698	-
	4,406	**1,743**	**1,880**	**8,029**	**322,010**	**330,039**	**-**
Auto and leasing	**21,760**	**10,399**	**4,232**	**36,391**	**847,594**	**883,985**	**-**
Total	**$ 36,092**	**$ 22,151**	**$ 89,497**	**$ 147,740**	**$ 3,057,152**	**$ 3,204,892**	**$ 7,361**

At both June 30, 2018 and December 31, 2017, Oriental had a carrying balance of $94.9 million in originated and other loans held for investment granted to the Puerto Rico government, including its instrumentalities, public corporations and municipalities as part of the institutional commercial loan segment. All originated and other loans granted to the Puerto Rico government are general obligations 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.

Acquired Loans

Acquired loans were initially measured at fair value and subsequently accounted for under either ASC 310-30 or ASC 310-20 (Non-refundable fees and Other Costs). We have acquired loans in the acquisitions of BBVAPR and Eurobank.

Acquired BBVAPR 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 are accounted for under the guidance of ASC 310-20, which requires that any contractually required loan payment receivable in excess of Oriental’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 Oriental’s non-accrual policy, and any accretion of discount or amortization of premium is discontinued. Acquired BBVAPR loans 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.

OFG BANCORP

NOTES TO CONSOLIDATED FINANCIAL STATEMENTS – (Continued)

The following tables present the aging of the recorded investment in gross acquired BBVAPR loans accounted for under ASC 310-20 as of June 30, 2018 and December 31, 2017, by class of loans:

	June 30, 2018						
	30-59 Days Past Due	60-89 Days Past Due	90+ Days Past Due	Total Past Due	Current	Total Loans	Loans 90+ Days Past Due and Still Accruing
	(In thousands)						
Commercial							
Commercial secured by real estate							
Retail	$ -	$ -	$ 54	$ 54	$ -	$ 54	$ -
Floor plan	-	-	917	917	332	1,249	-
	-	-	971	971	332	1,303	-
Other commercial and industrial							
Retail	22	13	42	77	1,527	1,604	-
Floor plan	-	-	2	2	-	2	-
	22	13	44	79	1,527	1,606	-
	22	**13**	**1,015**	**1,050**	**1,859**	**2,909**	**-**
Consumer							
Credit cards	516	196	584	1,296	22,185	23,481	-
Personal loans	73	8	14	95	2,160	2,255	-
	589	**204**	**598**	**1,391**	**24,345**	**25,736**	**-**
Auto	**726**	**475**	**139**	**1,340**	**9,943**	**11,283**	**-**
Total	**$ 1,337**	**$ 692**	**$ 1,752**	**$ 3,781**	**$ 36,147**	**$ 39,928**	**$ -**

OFG BANCORP

NOTES TO CONSOLIDATED FINANCIAL STATEMENTS – (Continued)

	December 31, 2017						
	30-59 Days Past Due	60-89 Days Past Due	90+ Days Past Due	Total Past Due	Current	Total Loans	Loans 90+ Days Past Due and Still Accruing
	(In thousands)						
Commercial							
Commercial secured by real estate							
Retail	$ -	$ -	$ 119	$ 119	$ -	$ 119	$ -
Floor plan	-	-	928	928	393	1,321	-
	-	-	1,047	1,047	393	1,440	-
Other commercial and industrial							
Retail	36	-	221	257	2,681	2,938	-
Floor plan	-	-	2	2	-	2	-
	36	-	223	259	2,681	2,940	-
	36	**-**	**1,270**	**1,306**	**3,074**	**4,380**	**-**
Consumer							
Credit cards	208	127	1,310	1,645	24,822	26,467	-
Personal loans	139	61	45	245	2,203	2,448	-
	347	**188**	**1,355**	**1,890**	**27,025**	**28,915**	**-**
Auto	**602**	**248**	**179**	**1,029**	**20,940**	**21,969**	**-**
Total	**$ 985**	**$ 436**	**$ 2,804**	**$ 4,225**	**$ 51,039**	**$ 55,264**	**$ -**

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

Acquired BBVAPR loans, 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 Oriental in accordance with ASC 310-30.

The carrying amount corresponding to acquired BBVAPR loans with deteriorated credit quality, including those accounted under ASC 310-30 by analogy, in the statements of financial condition at June 30, 2018 and December 31, 2017 is as follows:

		June 30, 2018		December 31, 2017
		(In thousands)		
Contractual required payments receivable:	$	1,406,468	$	1,481,616
Less: Non-accretable discount		350,257		352,431
Cash expected to be collected		1,056,211		1,129,185
Less: Accretable yield		287,992		308,913
Carrying amount, gross		768,219		820,272
Less: allowance for loan and lease losses		44,176		45,755
Carrying amount, net	**$**	**724,043**	**$**	**774,517**

OFG BANCORP

NOTES TO CONSOLIDATED FINANCIAL STATEMENTS – (Continued)

At June 30, 2018 and December 31, 2017, Oriental had $50.8 million and $50.3 million, respectively, in loans granted to Puerto Rico municipalities as part of its acquired BBVAPR loans accounted for under ASC 310-30. These loans are primarily secured municipal general obligations.

The following tables describe the accretable yield and non-accretable discount activity of acquired BBVAPR loans accounted for under ASC 310-30 for the quarters and six-month periods ended June 30, 2018 and 2017:

	Quarter Ended June 30, 2018				
	Mortgage	Commercial	Auto	Consumer	Total
			(In thousands)		
Accretable Yield Activity:					
Balance at beginning of period	$ 248,379	$ 45,711	$ 1,726	$ 649	$ 296,465
Accretion	(6,915)	(3,597)	(656)	(194)	(11,362)
Change in expected cash flows	-	2,775	400	73	3,248
Transfer from (to) non-accretable discount	2,439	(2,368)	(399)	(31)	(359)
Balance at end of period	**$ 243,903**	**$ 42,521**	**$ 1,071**	**$ 497**	**$ 287,992**
Non-Accretable Discount Activity:					
Balance at beginning of period	$ 301,107	$ 10,731	$ 23,443	$ 19,309	$ 354,590
Change in actual and expected losses	(2,531)	(1,956)	(197)	(8)	(4,692)
Transfer from accretable yield	(2,439)	2,368	399	31	359
Balance at end of period	**$ 296,137**	**$ 11,143**	**$ 23,645**	**$ 19,332**	**$ 350,257**

	Six-Month Period Ended June 30, 2018				
	Mortgage	Commercial	Auto	Consumer	Total
			(In thousands)		
Accretable Yield Activity:					
Balance at beginning of period	$ 258,498	$ 46,764	$ 2,766	$ 885	$ 308,913
Accretion	(13,988)	(7,282)	(1,525)	(450)	(23,245)
Change in expected cash flows	-	5,931	826	131	6,888

Transfer (to) non-accretable discount		(607)		(2,892)		(996)		(69)		(4,564)
Balance at end of period	**$**	**243,903**	**$**	**42,521**	**$**	**1,071**	**$**	**497**	**$**	**287,992**
Non-Accretable Discount Activity:										
Balance at beginning of period	$	299,501	$	10,596	$	23,050	$	19,284	$	352,431
Change in actual and expected losses		(3,971)		(2,345)		(401)		(21)		(6,738)
Transfer from accretable yield		607		2,892		996		69		4,564
Balance at end of period	**$**	**296,137**	**$**	**11,143**	**$**	**23,645**	**$**	**19,332**	**$**	**350,257**

OFG BANCORP

NOTES TO CONSOLIDATED FINANCIAL STATEMENTS – (Continued)

	Quarter Ended June 30, 2017				
	Mortgage	Commercial	Auto (In thousands)	Consumer	Total
Accretable Yield Activity:					
Balance at beginning of period	$ 276,817	$ 46,902	$ 6,583	$ 3,058	$ 333,360
Accretion	(7,694)	(4,513)	(1,776)	(556)	(14,539)
Change in actual and expected losses	1	15,993	98	50	16,142
Transfer (to) from non-accretable discount	1,024	(2,344)	(52)	(1,066)	(2,438)
Balance at end of period	**$ 270,148**	**$ 56,038**	**$ 4,853**	**$ 1,486**	**$ 332,525**
Non-Accretable Discount Activity:					
Balance at beginning of period	$ 309,993	$ 14,803	$ 22,564	$ 18,159	$ 365,519
Change in actual and expected losses	(2,465)	(280)	1,344	206	(1,195)
Transfer from (to) accretable yield	(1,024)	2,344	52	1,066	2,438
Balance at end of period	**$ 306,504**	**$ 16,867**	**$ 23,960**	**$ 19,431**	**$ 366,762**

	Six-Month Period Ended June 30, 2017				
	Mortgage	Commercial	Auto (In thousands)	Consumer	Total
Accretable Yield Activity:					
Balance at beginning of period	$ 292,115	$ 50,366	$ 8,538	$ 3,682	$ 354,701
Accretion	(15,584)	(9,494)	(3,923)	(1,158)	(30,159)
Change in actual and expected losses	2	16,191	150	86	16,429
Transfer (to) from non-accretable discount	(6,385)	(1,025)	88	(1,124)	(8,446)
Balance at end of period	**$ 270,148**	**$ 56,038**	**$ 4,853**	**$ 1,486**	**$ 332,525**
Non-Accretable Discount Activity:					
Balance at beginning of period	$ 305,615	$ 16,965	$ 22,407	$ 18,120	$ 363,107
Change in actual and expected losses	(5,496)	(1,123)	1,641	187	(4,791)
Transfer from (to) accretable yield	6,385	1,025	(88)	1,124	8,446

Balance at end of period	**$**	**306,504**	**$**	**16,867**	**$**	**23,960**	**$**	**19,431**	**$**	**366,762**

OFG BANCORP

NOTES TO CONSOLIDATED FINANCIAL STATEMENTS – (Continued)

Acquired Eurobank Loans

The carrying amount of acquired Eurobank loans at June 30, 2018 and December 31, 2017 is as follows:

		June 30 2018		December 31 2017
		(In thousands)		
Contractual required payments receivable:	$	165,175	$	179,960
Less: Non-accretable discount		3,819		5,845
Cash expected to be collected		161,356		174,115
Less: Accretable yield		45,078		49,672
Carrying amount, gross		116,278		124,443
Less: Allowance for loan and lease losses		24,314		25,174
Carrying amount, net	**$**	**91,964**	**$**	**99,269**

The following tables describe the accretable yield and non-accretable discount activity of acquired Eurobank loans for the quarters and six-month periods ended June 30, 2018 and 2017:

	Quarter Ended June 30, 2018					
	Loans Secured by 1-4 Family Residential Properties	**Commercial**	**Construction & Development Secured by 1-4 Family Residential Properties**	**Leasing**	**Consumer**	**Total**
			(In thousands)			
Accretable Yield Activity:						
Balance at beginning of period	$ 39,622	5,616	1,356	-	-	46,594
Accretion	(1,538)	(1,706)	-	(4)	(118)	(3,366)
Change in expected cash flows	(836)	1,832	-	(111)	236	1,121
Transfer (to) from non-accretable discount	2,021	(1,157)	(132)	115	(118)	729
	$ 39,269	**$ 4,585**	**$ 1,224**	**$ -**	**$ -**	**$ 45,078**

Balance at end of period												
Non-Accretable Discount Activity:												
Balance at beginning of period	$	4,479		-		849		-		219		5,547
Change in actual and expected losses		180		(1,157)		-		115		(137)		(999)
Transfer from (to) accretable yield		(2,021)		1,157		132		(115)		118		(729)
Balance at end of period	**$**	**2,638**	**$**	**-**	**$**	**981**	**$**	**-**	**$**	**200**	**$**	**3,819**

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NOTES TO CONSOLIDATED FINANCIAL STATEMENTS – (Continued)

	Six-Month Period Ended June 30, 2018					
	Loans Secured by 1-4 Family Residential Properties	Commercial	Construction & Development Secured by 1-4 Family Residential Properties	Leasing	Consumer	Total
	(In thousands)					
Accretable Yield Activity:						
Balance at beginning of year	$ 41,474	$ 6,751	$ 1,447	$ -	$ -	$ 49,672
Accretion	(3,143)	(3,312)	-	(38)	(214)	(6,707)
Change in expected cash flows	(980)	2,730	-	(174)	414	1,990
Transfer from (to) non-accretable discount	1,918	(1,584)	(223)	212	(200)	123
Balance at end of period	**$ 39,269**	**$ 4,585**	**$ 1,224**	**$ -**	**$ -**	**$ 45,078**
Non-Accretable Discount Activity:						
Balance at beginning of year	$ 4,576	$ 276	$ 758	$ -	$ 235	$ 5,845
Change in actual and expected losses	(20)	(1,860)	-	212	(235)	(1,903)
Transfer from (to) accretable yield	(1,918)	1,584	223	(212)	200	(123)
Balance at end of period	**$ 2,638**	**$ -**	**$ 981**	**$ -**	**$ 200**	**$ 3,819**

OFG BANCORP

NOTES TO CONSOLIDATED FINANCIAL STATEMENTS – (Continued)

	Quarter Ended June 30, 2017					
	Loans Secured by 1-4 Family Residential Properties	Commercial	Construction & Development Secured by 1-4 Family Residential Properties	Leasing	Consumer	Total
			(In thousands)			
Accretable Yield Activity:						
Balance at beginning of period	$ 44,697	$ 12,743	$ 1,871	-	$ -	$ 59,311
Accretion	(1,923)	(4,061)	(5)	(11)	(37)	(6,037)
Change in actual and expected losses	19	543	6	(22)	74	620
Transfer from (to) non-accretable discount	219	(68)	34	33	(37)	181
Balance at end of period	**$ 43,012**	**$ 9,157**	**$ 1,906**	**$ -**	**$ -**	**$ 54,075**
Non-Accretable Discount Activity:						
Balance at beginning of period	$ 7,426	$ 2,471	$ 333	$ -	$ 6	$ 10,236
Change in actual and expected losses	(520)	(529)	-	33	(29)	(1,045)
Transfer (to) from accretable yield	(219)	68	(34)	(33)	37	(181)
Balance at end of period	**$ 6,687**	**$ 2,010**	**$ 299**	**$ -**	**$ 14**	**$ 9,010**

OFG BANCORP

NOTES TO CONSOLIDATED FINANCIAL STATEMENTS – (Continued)

	Six-Month Period Ended June 30, 2017					
	Loans Secured by 1-4 Family Residential Properties	Commercial	Construction & Development Secured by 1-4 Family Residential Properties	Leasing	Consumer	Total
	(In thousands)					
Accretable Yield Activity:						
Balance at beginning of period	$ 45,839	$ 16,475	$ 2,194	$ -	$ -	$ 64,508
Accretion	(3,827)	(8,571)	(43)	(11)	(195)	(12,647)
Change in expected cash flows	100	1,321	43	(165)	384	1,683
Transfer from (to) non-accretable discount	900	(68)	(288)	176	(189)	531
Balance at end of period	**$ 43,012**	**$ 9,157**	**$ 1,906**	**$ -**	**$ -**	**$ 54,075**
Non-Accretable Discount Activity:						
Balance at beginning of period	$ 8,441	$ 3,880	$ 11	$ -	$ 8	$ 12,340
Change in actual and expected cash flows	(854)	(1,938)	-	176	(183)	(2,799)
Transfer (to) from accretable yield	(900)	68	288	(176)	189	(531)
Balance at end of period	**$ 6,687**	**$ 2,010**	**$ 299**	**$ -**	**$ 14**	**$ 9,010**

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NOTES TO 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, 2018 and December 31, 2017:

	June 30, 2018	December 31, 2017
	(In thousands)	
Originated and other loans and leases held for investment		
Mortgage		
Traditional (by origination year):		
Up to the year 2002	$ 3,616	$ 3,070
Years 2003 and 2004	6,082	6,380
Year 2005	4,108	3,280
Year 2006	5,004	5,905
Years 2007, 2008 and 2009	7,454	7,984
Years 2010, 2011, 2012, 2013	8,272	6,259
Years 2014, 2015, 2016 and 2017	1,593	1,649
	36,129	34,527
Non-traditional	3,131	3,543
Loss mitigation program	19,675	16,783
	58,935	54,853
Commercial		
Commercial secured by real estate		
Institutional	10,352	118
Middle market	8,533	11,394
Retail	15,906	14,438
	34,791	25,950
Other commercial and industrial		
Middle market	9,781	6,323
Retail	2,828	2,929
Floor plan	51	51
	12,660	9,303
	47,451	**35,253**
Consumer		
Credit cards	875	1,227
Overdrafts	-	31
Personal lines of credit	50	102
Personal loans	1,884	900
Cash collateral personal loans	17	312

		2,826		**2,572**
Auto and leasing		**11,141**		**4,232**
Total non-accrual originated loans	$	**120,353**	$	**96,910**

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NOTES TO CONSOLIDATED FINANCIAL STATEMENTS – (Continued)

	June 30, 2018	December 31, 2017
	(In thousands)	
Acquired BBVAPR loans accounted for under ASC 310-20		
Commercial		
Commercial secured by real estate		
Retail	$ 54	$ 119
Floor plan	917	928
	971	1,047
Other commercial and industrial		
Retail	42	221
Floor plan	2	2
	44	223
	1,015	**1,270**
Consumer		
Credit cards	584	1,310
Personal loans	14	45
	598	**1,355**
Auto	**139**	**179**
Total non-accrual acquired BBVAPR loans accounted for under ASC 310-20	**1,752**	**2,804**
Total non-accrual loans	**$ 122,105**	**$ 99,714**

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 or are accounted under the cost recovery method.

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 12 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. In addition, these loans are excluded from the impairment analysis.

At June 30, 2018 and December 31, 2017, loans whose terms have been extended and which are classified as troubled-debt restructurings that are not included in non-accrual loans amounted to $100.5 million and $109.2 million, respectively, as they are performing under their new terms.

At June 30, 2018 and December 31, 2017, loans that are current in their monthly payments, but placed in non-accrual due to credit deterioration amounted to $21.8 million and $20.1 million, respectively.

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NOTES TO CONSOLIDATED FINANCIAL STATEMENTS – (Continued)

Impaired Loans

Oriental evaluates all loans, some individually and others as homogeneous groups, for purposes of determining impairment. The total investment in impaired commercial loans that were individually evaluated for impairment was $69.8 million and $72.3 million at June 30, 2018 and December 31, 2017, respectively. The impairments on these 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 allowance for loan and lease losses for these impaired commercial loans amounted to $10.0 million and $10.6 million at June 30, 2018 and December 31, 2017, respectively. The total investment in impaired mortgage loans that were individually evaluated for impairment was $84.5 million and $85.4 million at June 30, 2018 and December 31, 2017, respectively. Impairment on mortgage loans assessed as troubled-debt restructurings was measured using the present value of cash flows. The allowance for loan losses for these impaired mortgage loans amounted to $9.9 million and $9.1 million at June 30, 2018 and December 31, 2017, respectively.

Originated and Other Loans and Leases Held for Investment

Oriental's recorded investment in 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, 2018 and 2017 are as follows:

	June 30, 2018			
	Unpaid Principal	**Recorded Investment**	**Related Allowance**	**Coverage**
		(In thousands)		
Impaired loans with specific allowance:				
Commercial	$ 47,346	$ 43,363	$ 9,906	23%
Residential impaired and troubled-debt restructuring	95,121	84,520	9,862	12%
Impaired loans with no specific allowance:				
Commercial	30,916	25,689	N/A	0%
Total investment in impaired loans	**$ 173,383**	**$ 153,572**	**$ 19,768**	**13%**

	December 31, 2017			
	Unpaid Principal	Recorded Investment	Related Allowance	Coverage
	(In thousands)			
Impaired loans with specific allowance:				
Commercial	$ 57,922	$ 52,585	$ 10,573	20%
Residential impaired and troubled-debt restructuring	94,971	85,403	9,121	11%
Impaired loans with no specific allowance				
Commercial	22,022	18,953	N/A	0%
Total investment in impaired loans	**$ 174,915**	**$ 156,941**	**$ 19,694**	**13%**

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NOTES TO CONSOLIDATED FINANCIAL STATEMENTS – (Continued)

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

Oriental’s recorded investment in acquired BBVAPR commercial 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, 2018 and December 31, 2017 are as follows:

	June 30, 2018			
	Unpaid Principal	Recorded Investment	Related Allowance	Coverage
	(In thousands)			
Impaired loans with specific allowance				
Commercial	$ 926	$ 747	$ 68	9%
Impaired loans with no specific allowance				
Commercial	$ -	$ -	N/A	0%
Total investment in impaired loans	**$ 926**	**$ 747**	**$ 68**	**9%**

	December 31, 2017			
	Unpaid Principal	Recorded Investment	Specific Allowance	Coverage
	(In thousands)			
Impaired loans with specific allowance				
Commercial	$ 926	$ 747	$ 20	3%
Impaired loans with no specific allowance				
Commercial	$ -	$ -	N/A	0%
Total investment in impaired loans	**$ 926**	**$ 747**	**$ 20**	**3%**

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

Oriental’s recorded investment in acquired BBVAPR loan pools accounted for under ASC 310-30 that have recorded impairments and their related allowance for loan and lease losses at June 30, 2018 and December 31, 2017 are as follows:

	June 30, 2018			
	Unpaid Principal	Recorded Investment	Allowance	Coverage to Recorded Investment
		(In thousands)		
Impaired loan pools with specific allowance:				
Mortgage	$ 525,230	$ 516,934	$ 14,567	3%
Commercial	230,905	222,202	23,019	10%
Consumer	1,400	495	18	4%
Auto	28,086	26,937	6,572	24%
Total investment in impaired loan pools	**$ 785,621**	**$ 766,568**	**$ 44,176**	6%

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NOTES TO CONSOLIDATED FINANCIAL STATEMENTS – (Continued)

	December 31 , 2017			
	Unpaid Principal	Recorded Investment	Allowance	Coverage to Recorded Investment
		(In thousands)		
Impaired loan pools with specific allowance:				
Mortgage	$ 547,064	$ 532,052	$ 14,085	3%
Commercial	250,451	241,124	23,691	10%
Consumer	2,468	1,431	18	1%
Auto	43,440	43,696	7,961	18%
Total investment in impaired loan pools	**$ 843,423**	**$ 818,303**	**$ 45,755**	6%

The tables above only present information with respect to acquired BBVAPR loan pools accounted for under ASC 310-30 if there is a recorded impairment to such loan pools and a specific allowance for loan losses.

Acquired Eurobank Loans

Oriental's recorded investment in acquired Eurobank loan pools that have recorded impairments and their related allowance for loan and lease losses as of June 30, 2018 and December 31, 2017 are as follows:

	June 30, 2018			
	Unpaid Principal	Recorded Investment	Allowance	Coverage to Recorded Investment
		(In thousands)		
Impaired loan pools with specific allowance:				
Loans secured by 1-4 family residential properties	$ 74,185	$ 65,584	$ 15,170	23%
Commercial	51,865	49,758	9,140	18%
Consumer	14	4	4	100%
Total investment in impaired loan pools	**$ 126,064**	**$ 115,346**	**$ 24,314**	21%

	December 31, 2017			
	Unpaid Principal	**Recorded Investment**	**Specific Allowance**	**Coverage to Recorded Investment**
		(In thousands)		
Impaired loan pools with specific allowance				
Loans secured by 1-4 family residential properties	$ 81,132	$ 69,538	$ 15,187	22%
Commercial	58,099	53,793	9,982	19%
Consumer	15	4	5	125%
Total investment in impaired loan pools	**$ 139,246**	**$ 123,335**	**$ 25,174**	20%

The tables above only present information with respect to acquired Eurobank loan pools accounted for under ASC 310-30 if there is a recorded impairment to such loan pools and a specific allowance for loan losses.

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NOTES TO CONSOLIDATED FINANCIAL STATEMENTS – (Continued)

The following table presents the interest recognized in commercial and mortgage loans that were individually evaluated for impairment, which excludes loans accounted for under ASC 310-30, for the quarters and six-month periods ended June 30, 2018 and 2017:

	Quarter Ended June 30,			
	2018		2017	
	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	$ 129	$ 46,976	$ 193	$ 14,908
Residential troubled-debt restructuring	705	84,473	723	87,615
Impaired loans with no specific allowance				
Commercial	131	22,129	383	44,528
	965	**153,578**	**1,299**	**147,051**
Acquired loans accounted for under ASC 310-20:				
Impaired loans with specific allowance				
Commercial	-	747	-	-
Impaired loans with no specific allowance				
Commercial	-	-	-	763
Total interest income from impaired loans	**$ 965**	**$ 154,325**	**$ 1,299**	**$ 147,814**

	Six-Month Period Ended June 30,			
	2018		2017	
	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	$	250	$	49,154	$	385	$	13,859
Residential troubled-debt restructuring		1,384		84,613		1,427		88,579
Impaired loans with no specific allowance								
Commercial		262		19,946		766		44,211
Total interest income from impaired loans	**$**	**1,896**	**$**	**153,713**	**$**	**2,578**	**$**	**146,649**
Acquired loans accounted for under ASC 310-20:								
Impaired loans with specific allowance								
Commercial	$	-	$	747	$	-	$	-
Impaired loans with no specific allowance								
Commercial		-		-		-		840
Total interest income from impaired loans	**$**	**1,896**	**$**	**154,460**	**$**	**2,578**	**$**	**147,489**

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NOTES TO CONSOLIDATED FINANCIAL STATEMENTS – (Continued)

Modifications

The following tables present the troubled-debt restructurings in all loan portfolios during the quarters and six-month periods ended June 30, 2018 and 2017.

	Quarter Ended June 30, 2018						
	Number of contracts	Pre-Modification Outstanding Recorded Investment	Pre-Modification Weighted Average Rate	Pre-Modification Weighted Average Term (in Months)	Post-Modification Outstanding Recorded Investment	Post-Modification Weighted Average Rate	Post-Modification Weighted Average Term (in Months)
	(Dollars in thousands)						
Mortgage	45	$ 5,718	5.63%	371	$ 5,679	4.85%	325
Commercial	5	5,775	5.55%	39	5,775	6.34%	45
Consumer	21	357	16.49%	56	357	10.26%	72

	Six-Month Period Ended June 30, 2018						
	Number of contracts	Pre-Modification Outstanding Recorded Investment	Pre-Modification Weighted Average Rate	Pre-Modification Weighted Average Term (in Months)	Post-Modification Outstanding Recorded Investment	Post-Modification Weighted Average Rate	Post-Modification Weighted Average Term (in Months)
	(Dollars in thousands)						
Mortgage	83	$ 11,466	5.66%	384	$ 11,019	4.96%	344
Commercial	8	7,334	5.38%	46	7,330	6.00%	50
Consumer	49	711	16.12%	51	712	10.93%	70

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NOTES TO CONSOLIDATED FINANCIAL STATEMENTS – (Continued)

	Quarter Ended June 30, 2017						
	Number of contracts	Pre-Modification Outstanding Recorded Investment	Pre-Modification Weighted Average Rate	Pre-Modification Weighted Average Term (in Months)	Post-Modification Outstanding Recorded Investment	Post-Modification Weighted Average Rate	Post-Modification Weighted Average Term (in Months)
	(Dollars in thousands)						
Mortgage	27	$ 3,349	6.00%	382	$ 3,313	4.21%	367
Commercial	9	2,155	5.96%	55	2,155	5.12%	68
Consumer	37	477	12.83%	65	477	10.87%	68
Auto	4	66	6.39%	61	66	12.91%	37

	Six-Month Period Ended June 30, 2017						
	Number of contracts	Pre-Modification Outstanding Recorded Investment	Pre-Modification Weighted Average Rate	Pre-Modification Weighted Average Term (in Months)	Post-Modification Outstanding Recorded Investment	Post-Modification Weighted Average Rate	Post-Modification Weighted Average Term (in Months)
	(Dollars in thousands)						
Mortgage	59	$ 7,353	6.29%	387	$ 7,328	4.26%	378
Commercial	18	3,373	6.44%	55	3,374	5.41%	67
Consumer	62	869	11.98%	65	907	10.62%	70
Auto	7	111	7.41%	67	113	12.48%	38

The following table presents troubled-debt restructurings for which there was a payment default during the twelve month periods ended June 30, 2018 and 2017:

	Twelve Month Period Ended June 30,			
	2018		2017	
	Number of Contracts	Recorded Investment	Number of Contracts	Recorded Investment
	(Dollars in thousands)			
Mortgage	12	$ 1,718	22	$ 2,293
Commercial	1	$ 235	5	$ 563
Consumer	15	$ 141	17	$ 156

Credit Quality Indicators

Oriental categorizes originated and other loans and acquired loans accounted for under ASC 310-20 into risk categories based on relevant information about the ability of borrowers to service their debt, such as economic conditions, portfolio risk characteristics, prior loss experience, and the results of periodic credit reviews of individual loans.

Oriental uses the following definitions for risk ratings:

Pass: Loans classified as "pass" have a well-defined primary source of repayment very likely to be sufficient, with no apparent risk, strong financial position, minimal operating risk, profitability, liquidity and capitalization better than industry standards.

Special Mention: Loans classified as "special mention" have a potential weakness that deserves management's close attention. If left uncorrected, these potential weaknesses may result in deterioration of the repayment prospects for the loan or of the institution's credit position at some future date.

Substandard: Loans classified as "substandard" are inadequately protected by the current net worth and paying capacity of the obligor or of the collateral pledged, if any. Loans so classified have a well-defined weakness or weaknesses that jeopardize the liquidation of the debt. They are characterized by the distinct possibility that the institution will sustain some loss if the deficiencies are not corrected.

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 CONSOLIDATED FINANCIAL STATEMENTS – (Continued)

As of June 30, 2018 and December 31, 2017, and based on the most recent analysis performed, the risk category of gross originated and other loans and BBVAPR acquired loans accounted for under ASC 310-20 subject to risk rating by class of loans is as follows:

	June 30, 2018					
		Risk Ratings				
	Balance Outstanding	Pass	Special Mention	Substandard	Doubtful	Loss
	(In thousands)					
Commercial - originated and other loans held for investment						
Commercial secured by real estate:						
Corporate	$ 274,435	$ 240,118	$ 32,480	$ 1,837	$ -	$ -
Institutional	81,019	70,468	-	10,551	-	-
Middle market	194,273	150,675	32,987	10,611	-	-
Retail	216,490	189,366	4,079	23,045	-	-
Floor plan	4,017	2,714	-	1,303	-	-
Real estate	15,157	15,157	-	-	-	-
	785,391	668,498	69,546	47,347	-	-
Other commercial and industrial:						
Corporate	190,414	179,117	11,297	-	-	-
Institutional	113,810	113,810	-	-	-	-
Middle market	94,979	67,804	3,470	23,705	-	-
Retail	284,596	280,653	229	3,714	-	-
Floor plan	38,178	35,105	3,022	51	-	-
	721,977	676,489	18,018	27,470	-	-
Total	1,507,368	1,344,987	87,564	74,817	-	-
Commercial - acquired loans						
(under ASC 310-20)						
Commercial secured by real estate:						

Retail	54	-	-	54	-	-
Floor plan	1,249	332	-	917	-	-
	1,303	332	-	971	-	-
Other commercial and industrial:						
Retail	1,604	1,603	-	1	-	-
Floor plan	2	-	-	2	-	-
	1,606	1,603	-	3	-	-
Total	2,909	1,935	-	974	-	-

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NOTES TO CONSOLIDATED FINANCIAL STATEMENTS – (Continued)

	June 30, 2018 Risk Ratings					
	Balance Outstanding	**Pass**	**Special Mention**	**Substandard**	**Doubtful**	**Loss**
			(In thousands)			
Retail - originated and other loans held for investment						
Mortgage:						
Traditional	541,892	505,864	-	36,028	-	-
Non-traditional	15,494	12,363	-	3,131	-	-
Loss mitigation program	106,095	87,556	-	18,539	-	-
Home equity secured personal loans	257	257	-	-	-	-
GNMA's buy-back option program	14,521	-	-	14,521	-	-
	678,259	606,040	-	72,219	-	-
Consumer:						
Credit cards	27,859	26,984	-	875	-	-
Overdrafts	158	145	-	13	-	-
Unsecured personal lines of credit	1,931	1,891	-	40	-	-
Unsecured personal loans	293,948	292,848	-	1,100	-	-
Cash collateral personal loans	15,445	15,428	-	17	-	-
	339,341	337,296	-	2,045	-	-
Auto and Leasing	1,014,664	1,003,563	-	11,101	-	-
Total	2,032,264	1,946,899	-	85,365	-	-
Retail - acquired loans (accounted for under ASC 310-20)						
Consumer:						
Credit cards	23,481	22,897	-	584	-	-
Personal loans	2,255	2,241	-	14	-	-
	25,736	25,138	-	598	-	-
Auto	11,283	11,144	-	139	-	-
	37,019	36,282	-	737	-	-
	$ 3,579,560	**$ 3,330,103**	**$ 87,564**	**$ 161,893**	**$ -**	**$ -**

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NOTES TO CONSOLIDATED FINANCIAL STATEMENTS – (Continued)

	December 31, 2017					
		Risk Ratings				
	Balance Outstanding	Pass	Special Mention	Substandard	Doubtful	Loss
			(In thousands)			
Commercial - originated and other loans held for investment						
Commercial secured by real estate:						
Corporate	$ 235,426	$ 200,395	$ 33,094	$ 1,937	$ -	$ -
Institutional	44,766	33,856	-	10,910	-	-
Middle market	229,941	196,058	4,749	29,134	-	-
Retail	246,067	215,121	8,058	22,888	-	-
Floor plan	3,998	2,678	1,320	-	-	-
Real estate	17,556	17,556	-	-	-	-
	777,754	665,664	47,221	64,869	-	-
Other commercial and industrial:						
Corporate	170,015	157,683	12,332	-	-	-
Institutional	125,591	125,591	-	-	-	-
Middle market	85,363	71,222	6,386	7,755	-	-
Retail	113,252	109,477	562	3,213	-	-
Floor plan	35,286	32,165	3,070	51	-	-
	529,507	496,138	22,350	11,019	-	-
Total	1,307,261	1,161,802	69,571	75,888	-	-
Commercial - acquired loans (under ASC 310-20)						
Commercial secured by real estate:						
Retail	119	-	-	119	-	-
Floor plan	1,321	393	-	928	-	-
	1,440	393	-	1,047	-	-
Other commercial and industrial:						

Retail	2,938	2,933	-	5	-	-
Floor plan	2	-	-	2	-	-
	2,940	2,933	-	7	-	-
Total	4,380	3,326	-	1,054	-	-

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NOTES TO CONSOLIDATED FINANCIAL STATEMENTS – (Continued)

	December 31, 2017 Risk Ratings					
	Balance Outstanding	**Pass**	**Special Mention**	**Substandard**	**Doubtful**	**Loss**
			(In thousands)			
Retail - originated and other loans held for investment						
Mortgage:						
Traditional	553,533	516,770	-	36,763	-	-
Non-traditional	18,270	14,727	-	3,543	-	-
Loss mitigation program	103,280	84,357	-	18,923	-	-
Home equity secured personal loans	256	256	-	-	-	-
GNMA's buy-back option program	8,268	-	-	8,268	-	-
	683,607	616,110	-	67,497	-	-
Consumer:						
Credit cards	28,430	27,203	-	1,227	-	-
Overdrafts	214	158	-	56	-	-
Unsecured personal lines of credit	2,220	2,133	-	87	-	-
Unsecured personal loans	284,477	284,255	-	222	-	-
Cash collateral personal loans	14,698	14,386	-	312	-	-
	330,039	328,135	-	1,904	-	-
Auto and Leasing	883,985	879,753	-	4,232	-	-
Total	1,897,631	1,823,998	-	73,633	-	-
Retail - acquired loans						
(under ASC 310-20)						
Consumer:						
Credit cards	26,467	25,156	-	1,311	-	-
Personal loans	2,448	2,402	-	46	-	-
	28,915	27,558	-	1,357	-	-
Auto	21,969	21,790	-	179	-	-
Total	50,884	49,348	-	1,536	-	-
	$ 3,260,156	**$ 3,038,474**	**$ 69,571**	**$ 152,111**	**$ -**	**$ -**

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NOTES TO CONSOLIDATED FINANCIAL STATEMENTS – (Continued)

NOTE 6 – ALLOWANCE FOR LOAN AND LEASE LOSSES

The composition of Oriental's allowance for loan and lease losses at June 30, 2018 and December 31, 2017 was as follows:

	June 30, 2018	December 31, 2017
	(In thousands)	
Allowance for loans and lease losses:		
Originated and other loans and leases held for investment:		
Mortgage	$ 19,323	$ 20,439
Commercial	31,480	30,258
Consumer	16,192	16,454
Auto and leasing	27,223	25,567
Total allowance for originated and other loans and lease losses	**94,218**	**92,718**
Acquired BBVAPR loans:		
Accounted for under ASC 310-20 (Loans with revolving feature and/or acquired at a premium)		
Commercial	86	42
Consumer	2,357	3,225
Auto	283	595
	2,726	**3,862**
Accounted for under ASC 310-30 (Loans acquired with deteriorated credit quality, including those by analogy)		
Mortgage	14,567	14,085
Commercial	23,019	23,691
Consumer	18	18
Auto	6,572	7,961
	44,176	**45,755**
Total allowance for acquired BBVAPR loans and lease losses	**46,902**	**49,617**
Acquired Eurobank loans:		
Loans secured by 1-4 family residential properties	15,170	15,187
Commercial	9,140	9,982
Consumer	4	5
Total allowance for acquired Eurobank loan and lease losses	**24,314**	**25,174**
Total allowance for loan and lease losses	**$ 165,434**	**$ 167,509**

Oriental 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. Oriental'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 Oriental'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.

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NOTES TO CONSOLIDATED FINANCIAL STATEMENTS – (Continued)

As discussed in Note 2, during 2017, hurricanes Irma and Maria caused catastrophic damages throughout Puerto Rico. Management performed an evaluation of the loan portfolios to assess the impact on repayment sources and underlying collateral that could result in additional losses.

For the commercial portfolio, the framework for the analysis was based on our current ALLL methodology with additional considerations according to the estimated impact categorized as low, medium or high. From this impact assessment, additional reserve levels were estimated by increasing default probabilities (“PD”) and loss given default expectations (“LGD”) of each allowance segment.

As part of the process, Oriental contacted its clients to evaluate the impact of the hurricanes on their business operations and collateral. The impact was then categorized as follows: (i) low risk, for clients that had no business impact or relatively insignificant impact; (ii) medium risk, for clients that had a business impact on their primary or secondary sources of repayment, but still had adequate cash flow to cover operations and to satisfy their obligations; or (iii) high risk, for clients that had potentially significant problems that affected primary, secondary and tertiary (collateral) sources of repayment. This criterion was used to model adjusted PDs and LGDs considering internal and external sources of information available to support our estimation process and output.

During the fourth quarter, Oriental performed an update of the initial estimate, taking into consideration the most recent available information gathered through additional visits and interviews with clients and the economic environment in Puerto Rico.

For the retail portfolios, mortgage, consumer and auto, the assumptions established in the initial estimate were based on the historical losses of each ALLL segment and then further adjusted based on parameters used as key risk indicators, such as the industry of employment for all portfolios and the location of the collateral for mortgage loans. During the fourth quarter of 2017, Oriental performed additional procedures to evaluate the reasonability of the initial estimate based on the payment experience percentage of borrowers for which the deferral period expired. The analysis took into consideration historical payment behavior and loss experience of borrowers (PDs and LGDs) of each portfolio segment to develop a range of estimated potential losses. Management understands that this approach is reasonable given the lack of historical information related to the behavior of local borrowers in such an unprecedented event. The amount used in the analysis represents the average of potential outcomes of expected losses.

During the first quarter of 2018, Oriental updated the previous performed analysis to estimate probable losses related to the hurricanes. Analyses were based on the payment experience percentage of borrowers for which the deferral period expired in retail portfolios. For commercial portfolio, no changes in the level of impact assessed were identified based on communications with credit officers. During the second quarter of 2018, Oriental continued its monitoring process of the performance of those affected borrowers. As information became available, it was incorporated into the allowance framework.

At June 30, 2018 and December 31, 2017, Oriental's allowance for loan and lease losses incorporated all risks associated to our loan portfolio, including the impact of hurricanes Irma and Maria.

As part of Oriental's continuous enhancement to the allowance for loan and lease losses methodology, during the second quarter of 2018 the following assumptions were reviewed:

- An assessment of the look-back period and historical loss factor was performed for auto and leasing, 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, 2018. As a result, for the commercial portfolio, the look-back period was revised to 40 months from 36 months. Also, for auto and consumer portfolios, a look back period of 24 months was maintained. For the residential mortgages portfolio, the factor was reviewed to 24 months from 12 months.

- 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, credit quality, expected impact due to recent economic developments, and changes in values of collateral, among others.

- The loss realization period was revised to 2.38 years from 2.13 years in 2017 for the commercial real estate portfolio, and other portfolios remained at one year.

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.

Allowance for Originated and Other Loan and Lease Losses Held for Investment

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

	Quarter Ended June 30, 2018				
	Mortgage	**Commercial**	**Consumer**	**Auto and Leasing**	**Total**

			(In thousands)		
Allowance for loan and lease losses for originated and other loans:					
Balance at beginning of period	$ 18,983	$ 33,174	$ 18,023	$ 26,652	$ 96,832
Charge-offs	(1,328)	(1,998)	(4,588)	(13,748)	(21,662)
Recoveries	466	227	240	5,280	6,213
Provision for loan and lease losses	1,202	77	2,517	9,039	12,835
Balance at end of period	**$ 19,323**	**$ 31,480**	**$ 16,192**	**$ 27,223**	**$ 94,218**

	Six-Month Period Ended June 30, 2018				
	Mortgage	**Commercial**	**Consumer**	**Auto and Leasing**	**Total**
			(In thousands)		
Allowance for loan and lease losses for originated and other loans:					
Balance at beginning of period	$ 20,439	$ 30,258	$ 16,454	$ 25,567	$ 92,718
Charge-offs	(2,298)	(3,147)	(8,847)	(22,731)	(37,023)
Recoveries	786	409	479	9,056	10,730
Provision for loan and lease losses	396	3,960	8,106	15,331	27,793
Balance at end of period	**$ 19,323**	**$ 31,480**	**$ 16,192**	**$ 27,223**	**$ 94,218**

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NOTES TO CONSOLIDATED FINANCIAL STATEMENTS – (Continued)

	June 30, 2018				
	Mortgage	**Commercial**	**Consumer**	**Auto and Leasing**	**Total**
			(In thousands)		
Allowance for loan and lease losses on originated and other loans:					
Ending allowance balance attributable to loans:					
Individually evaluated for impairment	$ 9,862	$ 9,906	$ -	$ -	$ 19,768
Collectively evaluated for impairment	9,461	21,574	16,192	27,223	74,450
Total ending allowance balance	**$ 19,323**	**$ 31,480**	**$ 16,192**	**$ 27,223**	**$ 94,218**
Loans:					
Individually evaluated for impairment	$ 84,520	$ 69,052	$ -	$ -	$ 153,572
Collectively evaluated for impairment	593,739	1,438,316	339,341	1,014,664	3,386,060
Total ending loan balance	**$ 678,259**	**$ 1,507,368**	**$ 339,341**	**$ 1,014,664**	**$ 3,539,632**

	Quarter Ended June 30, 2017					
	Mortgage	**Commercial**	**Consumer**	**Auto and Leasing**	**Unallocated**	**Total**
			(In thousands)			
Allowance for loan and lease losses for originated and other loans:						
Balance at beginning of period	$ 18,578	$ 9,888	$ 13,394	$ 18,621	$ 2	$ 60,483
Charge-offs	(2,162)	(4,841)	(4,012)	(7,775)	-	(18,790)
Recoveries	63	136	780	4,176	-	5,155
Provision (recapture) for originated and other loan and lease losses	2,185	12,096	4,819	3,720	(2)	22,818
Balance at end of period	**$ 18,664**	**$ 17,279**	**$ 14,981**	**$ 18,742**	**$ -**	**$ 69,666**

	Six-Month Period Ended June 30, 2017					
	Mortgage	**Commercial**	**Consumer**	**Auto and Leasing**	**Unallocated**	**Total**
			(In thousands)			
Allowance for loan and lease losses for originated and other loans:						
Balance at beginning of period	$ 17,344	$ 8,995	$ 13,067	$ 19,463	$ 431	$ 59,300
Charge-offs	(4,541)	(5,697)	(7,368)	(15,339)	-	(32,945)
Recoveries	119	226	945	7,470	-	8,760
Provision (recapture) for originated and other loan and lease losses	5,742	13,755	8,337	7,148	(431)	34,551
Balance at end of period	**$ 18,664**	**$ 17,279**	**$ 14,981**	**$ 18,742**	**$ -**	**$ 69,666**

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NOTES TO CONSOLIDATED FINANCIAL STATEMENTS – (Continued)

	December 31, 2017					
	Mortgage	Commercial	Consumer	Auto and Leasing	Unallocated	Total
	(In thousands)					
Allowance for loan and lease losses on originated and other loans:						
Ending allowance balance attributable to loans:						
Individually evaluated for impairment	$ 9,121	$ 10,573	$ -	$ -	$ -	$ 19,694
Collectively evaluated for impairment	11,318	19,685	16,454	25,567	-	73,024
Total ending allowance balance	**$ 20,439**	**$ 30,258**	**$ 16,454**	**$ 25,567**	**$ -**	**$ 92,718**
Loans:						
Individually evaluated for impairment	$ 85,403	$ 71,538	$ -	$ -	$ -	$ 156,941
Collectively evaluated for impairment	598,204	1,235,723	330,039	883,985	-	3,047,951
Total ending loan balance	**$ 683,607**	**$ 1,307,261**	**$ 330,039**	**$ 883,985**	**$ -**	**$ 3,204,892**

Allowance for BBVAPR Acquired Loan Losses

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 BBVAPR acquired loan portfolio accounted for under ASC 310-20, for the periods indicated:

	Quarter Ended June 30, 2018			
	Commercial	Consumer	Auto	Total
	(In thousands)			
Allowance for loan and lease losses				

for acquired BBVAPR loans accounted for under ASC 310-20:								
Balance at beginning of period	$	37	$	2,659	$	488	$	3,184
Charge-offs		(5)		(420)		(88)		(513)
Recoveries		12		94		244		350
Provision (recapture) for acquired BBVAPR loan and lease losses accounted for under ASC 310-20		42		24		(361)		(295)
Balance at end of period	**$**	**86**	**$**	**2,357**	**$**	**283**	**$**	**2,726**

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NOTES TO CONSOLIDATED FINANCIAL STATEMENTS – (Continued)

	Six-Month Period Ended June 30, 2018			
	Commercial	Consumer	Auto	Total
	(In thousands)			
Allowance for loan and lease losses for acquired BBVAPR loans accounted for under ASC 310-20:				
Balance at beginning of period	$ 42	$ 3,225	$ 595	$ 3,862
Charge-offs	(5)	(1,442)	(213)	(1,660)
Recoveries	15	148	472	635
Provision (recapture) for acquired BBVAPR loan and lease losses accounted for under ASC 310-20	34	426	(571)	(111)
Balance at end of period	**$ 86**	**$ 2,357**	**$ 283**	**$ 2,726**

	June 30, 2018			
	Commercial	Consumer	Auto	Total
	(In thousands)			
Allowance for loan and lease losses for acquired BBVAPR loans accounted for under ASC 310-20:				
Ending allowance balance attributable to loans:				
Individually evaluated for impairment	$ 68	$ -	$ -	$ 68
Collectively evaluated for impairment	18	2,357	283	2,658
Total ending allowance balance	**$ 86**	**$ 2,357**	**$ 283**	**$ 2,726**
Loans:				
Individually evaluated for impairment	$ 747	$ -	$ -	$ 747
	2,162	25,736	11,283	39,181

Collectively evaluated for impairment								
Total ending loan balance	**$**	**2,909**	**$**	**25,736**	**$**	**11,283**	**$**	**39,928**

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NOTES TO CONSOLIDATED FINANCIAL STATEMENTS – (Continued)

	Quarter Ended June 30, 2017			
	Commercial	Consumer	Auto	Total
	(In thousands)			
Allowance for loan and lease losses for acquired BBVAPR loans accounted for under ASC 310-20:				
Balance at beginning of period	$ 183	$ 2,591	$ 841	$ 3,615
Charge-offs	(126)	(771)	(205)	(1,102)
Recoveries	2	295	597	894
Provision (recapture) for acquired loan and lease losses accounted for under ASC 310-20	(18)	508	(549)	(59)
Balance at end of period	**$ 41**	**$ 2,623**	**$ 684**	**$ 3,348**

	Six-Month Period Ended June 30, 2017			
	Commercial	Consumer	Auto	Total
	(In thousands)			
Allowance for loan and lease losses for acquired BBVAPR loans accounted for under ASC 310-20:				
Balance at beginning of year	$ 169	$ 3,028	$ 1,103	$ 4,300
Charge-offs	(132)	(1,656)	(483)	(2,271)
Recoveries	3	359	1,049	1,411
Provision (recapture) for acquired loan and lease losses accounted for under ASC 310-20	1	892	(985)	(92)
Balance at end of period	**$ 41**	**$ 2,623**	**$ 684**	**$ 3,348**

	December 31, 2017			
	Commercial	Consumer	Auto	Total
	(In thousands)			
Allowance for loan and lease losses for acquired BBVAPR loans accounted for under ASC 310-20:				
Ending allowance balance attributable to loans:				
Individually evaluated for impairment	$ 20	$ -	$ -	$ 20
Collectively evaluated for impairment	22	3,225	595	3,842
Total ending allowance balance	**$ 42**	**$ 3,225**	**$ 595**	**$ 3,862**
Loans:				
Individually evaluated for impairment	$ 747	$ -	$ -	$ 747
Collectively evaluated for impairment	3,633	28,915	21,969	54,517
Total ending loan balance	**$ 4,380**	**$ 28,915**	**$ 21,969**	**$ 55,264**

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NOTES TO CONSOLIDATED FINANCIAL STATEMENTS – (Continued)

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

For loans accounted for under ASC 310- 30, as part of the evaluation of actual versus expected cash flows, Oriental 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 following tables present the activity in our allowance for loan losses and related recorded investment of the acquired BBVAPR loan portfolio accounted for under ASC 310-30 for the periods indicated:

	Quarter Ended June 30, 2018				
	Mortgage	Commercial	Consumer	Auto	Total
		(In thousands)			
Allowance for loan and lease losses for acquired BBVAPR loans accounted for under ASC 310-30:					
Balance at beginning of period	$ 14,331	$ 22,047	$ 18	$ 6,770	43,166
Provision for acquired BBVAPR loans and lease losses accounted for under ASC 310-30	236	1,306	-	-	1,542
Allowance de-recognition	-	(334)	-	(198)	(532)
Balance at end of period	**$ 14,567**	**$ 23,019**	**$ 18**	**$ 6,572**	**44,176**

	Six-Month Period Ended June 30, 2018				
	Mortgage	Commercial	Consumer	Auto	Total
		(In thousands)			
Allowance for loan and lease losses for acquired BBVAPR loans accounted for under ASC 310-30:					
Balance at beginning of period	$ 14,085	$ 23,691	$ 18	$ 7,961	45,755
Provision (recapture) for acquired BBVAPR loans and	550	2,058	-	(887)	1,721

lease losses accounted for under ASC 310-30								
Allowance de-recogntion		(68)		(2,730)		-		(502)	(3,300)
Balance at end of period	**$**	**14,567**	**$**	**23,019**	**$**	**18**	**$**	**6,572**	**44,176**

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NOTES TO CONSOLIDATED FINANCIAL STATEMENTS – (Continued)

	Quarter Ended June 30, 2017			
	Mortgage	Commercial	Auto	Total
	(In thousands)			
Allowance for loan and lease losses for acquired BBVAPR loans accounted for under ASC 310-30:				
Balance at beginning of period	$ 3,573	$ 23,528	$ 7,829	$ 34,930
Provision (recapture) for acquired BBVAPR loans and lease losses accounted for under ASC 310-30	630	2,735	-	3,365
Allowance de-recognition	(62)	(649)	(90)	(801)
Balance at end of period	**$ 4,141**	**$ 25,614**	**$ 7,739**	**$ 37,494**

	Six-Month Period Ended June 30, 2017			
	Mortgage	Commercial	Auto	Total
	(In thousands)			
Allowance for loan and lease losses for acquired BBVAPR loans accounted for under ASC 310-30:				
Balance at beginning of period	$ 2,682	$ 23,452	$ 4,922	$ 31,056
Provision for acquired BBVAPR loans and lease losses accounted for under ASC 310-30	1,552	2,958	3,186	7,696
Allowance de-recogntion	(93)	(796)	(369)	(1,258)
Balance at end of period	**$ 4,141**	**$ 25,614**	**$ 7,739**	**$ 37,494**

Allowance for Acquired Eurobank Loan Losses

The changes in the allowance for loan and lease losses on acquired Eurobank loans for the quarters and six-month periods ended June 30, 2018 and 2017 were as follows:

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NOTES TO CONSOLIDATED FINANCIAL STATEMENTS – (Continued)

	Quarter Ended June 30, 2018			
	Loans Secured by 1-4 Family Residential Properties	Commercial	Consumer	Total
	(In thousands)			
Allowance for loan and lease losses for acquired Eurobank loans:				
Balance at beginning of period	$ 15,414	$ 9,992	$ 5	$ 25,411
Provision for loan and lease losses, net	605	60	-	665
Allowance de-recognition	(849)	(912)	(1)	(1,762)
Balance at end of period	**$ 15,170**	**$ 9,140**	**$ 4**	**$ 24,314**

	Six-Month Period Ended June 30, 2018			
	Loans Secured by 1-4 Family Residential Properties	Commercial	Consumer	Total
	(In thousands)			
Allowance for loan and lease losses for acquired Eurobank loans:				
Balance at beginning of period	$ 15,187	$ 9,982	$ 5	$ 25,174
Provision for loan and lease losses, net	784	21	-	805
Allowance de-recognition	(801)	(863)	(1)	(1,665)
Balance at end of period	**$ 15,170**	**$ 9,140**	**$ 4**	**$ 24,314**

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NOTES TO CONSOLIDATED FINANCIAL STATEMENTS – (Continued)

	Quarter Ended June 30, 2017			
	Loans secured by 1-4 Family Residential Properties	**Commercial**	**Consumer**	**Total**
		(In thousands)		
Allowance for loan and lease losses for acquired Eurobank loans:				
Balance at beginning of period	$ 14,168	$ 7,833	$ 5	$ 22,006
Provision for (recapture) acquired Eurobank loan and lease losses, net	474	(62)	-	412
Allowance de-recognition	(991)	360	-	(631)
Balance at end of period	**$ 13,651**	**$ 8,131**	**$ 5**	**$ 21,787**

	Six-Month Period Ended June 30, 2017			
	Loans secured by 1-4 Family Residential Properties	**Commercial**	**Consumer**	**Total**
		(In thousands)		
Allowance for loan and lease losses for Eurobank loans:				
Balance at beginning of period	$ 11,947	$ 9,328	$ 6	$ 21,281
Provision for (recapture) acquired Eurobank loan and lease losses, net	2,872	(840)	-	2,032
Allowance de-recognition	(1,168)	(357)	(1)	(1,526)
Balance at end of period	**$ 13,651**	**$ 8,131**	**$ 5**	**$ 21,787**

NOTE 7- FDIC SHARED-LOSS AGREEMENTS

On February 6, 2017, the Bank and the FDIC agreed to terminate the single family and commercial shared-loss agreements related to the FDIC assisted acquisition of Eurobank on April 30, 2010. As part of the loss share termination transaction, the Bank made a payment of $10.1 million to the FDIC and recorded a net benefit of $1.4 million. Such termination payment took into account the anticipated reimbursements over the life of the shared-loss agreements and the true-up payment liability of the Bank anticipated at the end of the ten-year term of the single family shared-loss agreement. All rights and obligations of the parties under the shared-loss agreements terminated as of the closing date of the agreement.

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NOTES TO CONSOLIDATED FINANCIAL STATEMENTS – (Continued)

NOTE 8 — FORECLOSED REAL ESTATE

The following tables present the activity related to foreclosed real estate for the quarters and six-months periods ended June 30, 2018 and 2017:

	Quarter Ended June 30, 2018			
	Originated and other loans and leases held for investment	Acquired BBVAPR loans	Acquired Eurobank loans	Total
	(In thousands)			
Balance at beginning of period	**$ 13,365**	**$ 16,495**	**$ 10,454**	**$ 40,314**
Decline in value	(170)	(478)	(290)	(938)
Additions	1,782	3,275	1,828	6,885
Sales	(2,791)	(1,800)	(1,119)	(5,710)
Other adjustments	-	-	-	-
Balance at end of period	**$ 12,186**	**$ 17,492**	**$ 10,873**	**$ 40,551**

	Quarter Ended June 30, 2017			
	Originated and other loans and leases held for investment	Acquired BBVAPR loans	Acquired Eurobank loans	Total
	(In thousands)			
Balance at beginning of period	**$ 13,468**	**$ 21,534**	**$ 12,549**	**$ 47,551**
Decline in value	(844)	(936)	(522)	(2,302)
Additions	4,445	3,553	1,493	9,491
Sales	(1,228)	(2,367)	(810)	(4,405)
Other adjustments	-	(113)	-	(113)
Balance at end of period	**$ 15,841**	**$ 21,671**	**$ 12,710**	**$ 50,222**

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NOTES TO CONSOLIDATED FINANCIAL STATEMENTS – (Continued)

	Six-Month Period Ended June 30, 2018			
	Originated and other loans and leases held for investment	Acquired BBVAPR loans	Acquired Eurobank loans	Total
	(In thousands)			
Balance at beginning of period	**$ 14,283**	**$ 18,347**	**$ 11,544**	**$ 44,174**
Decline in value	(658)	(1,514)	(752)	(2,924)
Additions	3,269	4,925	1,941	10,135
Sales	(4,708)	(4,266)	(1,860)	(10,834)
Balance at end of period	**$ 12,186**	**$ 17,492**	**$ 10,873**	**$ 40,551**

	Six-Month Period Ended June 30, 2017			
	Originated and other loans and leases held for investment	Acquired BBVAPR loans	Acquired Eurobank loans	Total
	(In thousands)			
Balance at beginning of period	**$ 12,390**	**$ 21,379**	**$ 13,751**	**$ 47,520**
Decline in value	(1,081)	(1,628)	(1,270)	(3,979)
Additions	7,856	7,087	1,932	16,875
Sales	(3,239)	(5,054)	(1,703)	(9,996)
Other adjustments	(85)	(113)	-	(198)
Balance at end of period	**$ 15,841**	**$ 21,671**	**$ 12,710**	**$ 50,222**

After hurricanes Irma and Maria in September 2017, management evaluated the potential impact these events brought to Oriental's foreclosed real estate, considering the related underlying insurance coverage. Oriental has performed property inspections and taking into consideration all available information, the fair value of these properties was not materially impacted.

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NOTES TO CONSOLIDATED FINANCIAL STATEMENTS – (Continued)

NOTE 9 — DERIVATIVES

The following table presents Oriental’s derivative assets and liabilities at June 30, 2018 and December 31, 2017:

	June 30, 2018	December 31, 2017
	(In thousands)	
Derivative assets:		
Interest rate swaps designated as cash flow hedges	$ 421	$ -
Interest rate swaps not designated as hedges	335	618
Interest rate caps	344	153
	$ 1,100	**$ 771**
Derivative liabilities:		
Interest rate swaps designated as cash flow hedges	-	510
Interest rate swaps not designated as hedges	335	618
Interest rate caps	344	153
	$ 679	**$ 1,281**

Interest Rate Swaps

Oriental 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 Oriental’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 (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, Oriental does not expect to reclassify any amount included in other comprehensive (loss) related to these interest rate swaps to operations in the next twelve months.

The following table shows a summary of these swaps and their terms at June 30, 2018:

Type		Notional Amount (In thousands)	Fixed Rate	Variable Rate Index	Trade Date	Settlement Date	Maturity Date
Interest Rate Swaps	$	34,352	2.4210%	1-Month LIBOR	07/03/13	07/03/13	08/01/23
	$	**34,352**					

An accumulated unrealized gain of $421 thousand and a loss of $510 thousand were recognized in accumulated other comprehensive income related to the valuation of these swaps at June 30, 2018 and December 31, 2017, respectively, and the related asset or liability is being reflected in the consolidated statements of financial condition.

At June 30, 2018 and December 31, 2017, interest rate swaps not designated as hedging instruments that were offered to clients represented an asset of $335 thousand and $618 thousand, respectively, and were included as part of derivative assets in the consolidated statements of financial position. The credit risk to these clients stemming from these derivatives, if any, is not material. At June 30, 2018 and December 31, 2017, interest rate swaps not designated as hedging instruments that are the mirror-images of the derivatives offered to clients represented a liability of $335 thousand and $618 thousand, respectively, and were included as part of derivative liabilities in the consolidated statements of financial condition.

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NOTES TO CONSOLIDATED FINANCIAL STATEMENTS – (Continued)

The following table shows a summary of these interest rate swaps not designated as hedging instruments and their terms at June 30, 2018:

Type	Notional Amount (In thousands)	Fixed Rate	Variable Rate Index	Settlement Date	Maturity Date
Interest Rate Swaps - Derivatives Offered to Clients	$ 12,500	5.5050%	1-Month LIBOR	04/11/09	04/11/19
	$ 12,500				
Interest Rate Swaps - Mirror Image Derivatives	$ 12,500	5.5050%	1-Month LIBOR	04/11/09	04/11/19
	$ 12,500				

Interest Rate Caps

Oriental 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, Oriental 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. As of June 30, 2018 and December 31, 2017, the outstanding total notional amount of interest rate caps was $151.8 million and $152.6 million, respectively. At June 30, 2018 and December 31, 2017, the interest rate caps sold to clients represented a liability of $344 thousand and $153 thousand, respectively, and were included as part of derivative liabilities in the consolidated statements of financial condition. At June 30, 2018 and December 31, 2017, the interest rate caps purchased as mirror-images represented an asset of $344 thousand and $153 thousand, respectively, and were included as part of derivative assets in the consolidated statements of financial condition.

NOTE 10 — ACCRUED INTEREST RECEIVABLE AND OTHER ASSETS

Accrued interest receivable at June 30, 2018 and December 31, 2017 consists of the following:

	June 30, 2018	December 31, 2017
	(In thousands)	
Loans, excluding acquired loans	$ 30,944	$ 46,936
Investments	3,532	3,033
	$ 34,476	**$ 49,969**

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NOTES TO CONSOLIDATED FINANCIAL STATEMENTS – (Continued)

Accrued interest receivable at December 31, 2017, included $39.7 million, resulting from the loan payment moratorium. Accrued interest receivable resulting from the loan payment moratorium has been decreasing, as most moratoriums have expired. Some of these accrued interests are payable at the end of the loan term.

Other assets at June 30, 2018 and December 31, 2017 consist of the following:

		June 30, 2018		December 31, 2017
		(In thousands)		
Prepaid expenses	$	10,742	$	9,200
Other repossessed assets		5,483		3,548
Core deposit and customer relationship intangibles		4,027		4,687
Tax credits		2,277		4,277
Investment in Statutory Trust		1,083		1,083
Accounts receivable and other assets		35,693		41,898
	$	**59,305**	**$**	**64,693**

Prepaid expenses amounting to $10.7 million and $9.2 million at June 30, 2018 and December 31, 2017, respectively, include prepaid municipal, property and income taxes aggregating to $8.5 million and $5.7 million, respectively.

In connection with the FDIC-assisted acquisition and the BBVAPR Acquisition, Oriental recorded a core deposit intangible representing the value of checking and savings deposits acquired. At June 30, 2018 and December 31, 2017 this core deposit intangible amounted to $2.9 million and $3.3 million, respectively. In addition, Oriental recorded a customer relationship intangible representing the value of customer relationships acquired with the acquisition of the securities broker-dealer and insurance agency in the BBVAPR Acquisition. At June 30, 2018 and December 31, 2017, this customer relationship intangible amounted to $1.1 million and $1.4 million, respectively.

Other repossessed assets totaled $5.5 million and $3.5 million at June 30, 2018 and December 31, 2017, respectively, that consist mainly of repossessed automobiles, which are recorded at their net realizable value.

At June 30, 2018 and December 31, 2017, tax credits for Oriental totaled $2.3 million and $4.3 million, respectively. These tax credits do not have an expiration date.

NOTE 11— DEPOSITS AND RELATED INTEREST

Total deposits, including related accrued interest payable, as of June 30, 2018 and December 31, 2017 consist of the following:

	June 30, 2018	December 31, 2017
	(In thousands)	
Non-interest bearing demand deposits	$ 1,110,738	$ 969,525
Interest-bearing savings and demand deposits	2,285,357	2,274,116
Individual retirement accounts	208,807	231,376
Retail certificates of deposit	601,687	595,983
Institutional certificates of deposit	212,187	209,951
Total core deposits	**4,418,776**	**4,280,951**
Brokered deposits	461,425	518,531
Total deposits	$ **4,880,201**	$ **4,799,482**

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NOTES TO CONSOLIDATED FINANCIAL STATEMENTS – (Continued)

Brokered deposits include $427.1 million in certificates of deposits and $34.3 million in money market accounts at June 30, 2018, and $471.6 million in certificates of deposits and $46.9 million in money market accounts at December 31, 2017.

The weighted average interest rate of Oriental's deposits was 0.63% and 0.65% at June 30, 2018 and December 31, 2017, respectively. Interest expense for the quarters and six-month periods ended June 30, 2018 and 2017 was as follows:

	Quarter Ended June 30,		Six-Month Period Ended June 30,	
	2018	2017	2018	2017
	(In thousands)			
Demand and savings deposits	$ 2,956	$ 2,939	$ 5,768	$ 5,848
Certificates of deposit	4,695	4,713	9,181	9,157
	$ 7,651	**$ 7,652**	**$ 14,949**	**$ 15,005**

At June 30, 2018 and December 31, 2017, time deposits in denominations of $250 thousand or higher, excluding accrued interest and unamortized discounts, amounted to $363.4 million and $359.6 million, respectively. Such amounts include public funds time deposits from various Puerto Rico government municipalities, agencies, and corporations of $33.2 million and $3.5 million at a weighted average rate of 0.93% and 0.28% at June 30, 2018 and December 31, 2017, respectively.

At June 30, 2018 and December 31, 2017, total public fund deposits from various Puerto Rico government municipalities, agencies, and corporations amounted to $156.9 million and $153.1 million, respectively. These public funds were collateralized with commercial loans amounting to $201.2 million and $173.0 million at June 30, 2018 and December 31, 2017, respectively.

Excluding accrued interest of approximately $1.7 million, the scheduled maturities of certificates of deposit at June 30, 2018 and 2017 are as follows:

	June 30, 2018	December 31, 2017
	(In thousands)	

Within one year:				
Three (3) months or less	$	286,623	$	316,382
Over 3 months through 1 year		505,206		508,285
		791,829		**824,667**
Over 1 through 2 years		468,489		470,670
Over 2 through 3 years		111,344		137,016
Over 3 through 4 years		30,850		36,125
Over 4 through 5 years		45,630		38,623
	$	**1,448,142**	**$**	**1,507,101**

The table of scheduled maturities of certificates of deposits above includes brokered-deposits and individual retirement accounts.

The aggregate amount of overdrafts in demand deposit accounts that were reclassified to loans amounted to $367 thousand and $2.2 million as of June 30, 2018 and December 31, 2017, respectively.

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NOTES TO CONSOLIDATED FINANCIAL STATEMENTS – (Continued)

NOTE 12 — BORROWINGS AND RELATED INTEREST

Securities Sold under Agreements to Repurchase

At June 30, 2018, 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 Oriental the same or similar securities at the maturity of these agreements. The purpose of these transactions is to provide financing for Oriental's securities portfolio.

At June 30, 2018 and December 31, 2017, securities sold under agreements to repurchase (classified by counterparty), excluding accrued interest in the amount of $391 thousand and $369 thousand, respectively, were as follows:

	June 30, 2018		December 31, 2017	
	Borrowing Balance	Fair Value of Underlying Collateral	Borrowing Balance	Fair Value of Underlying Collateral
	(In thousands)			
KGS Alpha	12,460	13,855	-	-
Amherst Pierpont	46,427	48,966	-	-
JP Morgan Chase Bank NA	80,000	86,252	82,500	88,974
Nomura	60,000	63,464	-	-
JVB Financial	28,522	30,561	-	-
Federal Home Loan Bank	110,000	116,330	110,000	116,509
Citigroup	49,970	53,249	-	-
Total	**$ 387,379**	**$ 412,677**	**$ 192,500**	**$ 205,483**

The following table shows a summary of Oriental's repurchase agreements and their terms, excluding accrued interest in the amount of $391 thousand, at June 30, 2018:

Weighted-

Year of Maturity	Borrowing Balance (In thousands)	Average Coupon	Settlement Date	Maturity Date
2018	60,000	2.26%	6/8/2018	7/3/2018
	46,427	2.32%	6/26/2018	7/3/2018
	28,522	2.16%	6/15/2018	7/12/2018
	49,970	2.22%	6/22/2018	7/20/2018
	12,460	2.18%	6/25/2018	7/25/2018
2019	50,000	1.72%	3/2/2017	9/3/2019
2020	60,000	1.85%	3/2/2017	3/2/2020
	50,000	2.61%	3/15/2018	3/15/2020
	30,000	2.70%	3/23/2018	3/23/2020
	$ 387,379	**2.20%**		

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

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NOTES TO 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, 2018 and December 31, 2017. There was no cash collateral at June 30, 2018 and December 31, 2017.

	June 30, 2018			December 31, 2017		
	Repurchase Liability	Weighted Average Rate	Market Value of Underlying Collateral FNMA and FHLMC Certificates	Repurchase Liability	Weighted Average Rate	Market Value of Underlying Collateral FNMA and FHLMC Certificates
	(Dollars in thousands)					
Less than 90 days	$ 197,379	2.24%	$ 210,095	$ -	-	$ -
Over 90 days	190,000	2.15%	202,582	192,500	1.63%	205,483
Total	**$ 387,379**	**2.20%**	**$ 412,677**	**$ 192,500**	**1.63%**	**$ 205,483**

Advances from the Federal Home Loan Bank of New York

Advances are received from the FHLB-NY under an agreement whereby Oriental 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, 2018 and December 31, 2017, these advances were secured by mortgage and commercial loans amounting to $910.7 million and $1.3 billion, respectively. Also, at June 30, 2018 and December 31, 2017, Oriental had an additional borrowing capacity with the FHLB-NY of $775.6 million and $920.0 million, respectively. At June 30, 2018 and December 31, 2017, the weighted average remaining maturity of FHLB's advances was 8.4 months and 3.2 months, respectively. The original terms of these advances range between one month 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, 2018.

The following table shows a summary of these advances and their terms, excluding accrued interest in the amount of $123 thousand, at June 30, 2018:

Year of Maturity	Borrowing Balance	Weighted-Average Coupon	Settlement Date	Maturity Date
	(In thousands)			

2018		34,352	2.14%	6/1/2018	7/2/2018
		70,000	2.08%	6/29/2018	7/2/2018
2020		9,039	2.59%	7/19/2013	7/20/2020
2023		12,500	2.94%	5/9/2018	5/9/2023
		2,100	2.92%	6/8/2018	6/8/2023
	$	**127,991**	**2.23%**		

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 $36.1 million at June 30, 2018 and December 31, 2017, for both periods.

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NOTES TO CONSOLIDATED FINANCIAL STATEMENTS – (Continued)

NOTE 13 – OFFSETTING OF FINANCIAL ASSETS AND LIABILITIES

Oriental’s derivatives are subject to agreements which allow a right of set-off with each respective counterparty. In addition, Oriental’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 an account control agreement.

The following table presents the potential effect of rights of set-off associated with Oriental’s recognized financial assets and liabilities at June 30, 2018 and December 31, 2017:

	June 30, 2018					
				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	Financial Instruments	Cash Collateral Received	Net Amount
	(In thousands)					
Derivatives	$ 1,100	$ -	$ 1,100	$ 2,013	$ -	$ (913)

	December 31, 2017				
			Gross Amounts Not Offset in the Statement of Financial Condition		
	Gross Amounts Offset in the	Net amount of Assets Presented in Statement		Cash	

	Gross Amount of Recognized Assets	Statement of Financial Condition	of Financial Condition	Financial Instruments	Collateral Received	Net Amount
			(In thousands)			
Derivatives	$ 771	$ -	$ 771	$ 2,010	$ -	$ (1,239)

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NOTES TO CONSOLIDATED FINANCIAL STATEMENTS – (Continued)

June 30, 2018

	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: Financial Instruments	Cash Collateral Provided	Net Amount
	(In thousands)					
Derivatives	$ 679	$ -	$ 679	$ -	$ 1,980	$ (1,301)
Securities sold under agreements to repurchase	387,379	-	387,379	412,677	-	(25,298)
Total	**$ 388,058**	**$ -**	**$ 388,058**	**$ 412,677**	**$ 1,980**	**$ (26,599)**

December 31, 2017

	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: Financial Instruments	Cash Collateral Provided	Net Amount
	(In thousands)					
Derivatives	$ 1,281	$ -	$ 1,281	$ -	$ 1,980	$ (699)
Securities sold under agreements to repurchase	192,500	-	192,500	205,483	-	(12,983)
Total	**$ 193,781**	**$ -**	**$ 193,781**	**$ 205,483**	**$ 1,980**	**$ (13,682)**

NOTE 14 — INCOME TAXES

At June 30, 2018 and December 31, 2017, Oriental's net deferred tax asset amounted to $125.1 million and $127.4 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 Oriental will realize the deferred tax asset, net of the existing valuation allowances recorded at June 30, 2018 and December 31, 2017. 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.

Oriental classifies unrecognized tax benefits in other liabilities. These gross unrecognized tax benefits would affect the effective tax rate if realized. At June 30, 2018 the amount of unrecognized tax benefits remained at $1.3 million when compared to December 31, 2017. Oriental had accrued $48 thousand at June 30, 2018 (December 31, 2017 - $97 thousand) for the payment of interest and penalties relating to unrecognized tax benefits.

Oriental is subject to the dispositions of the 2011 Puerto Rico Internal Revenue Code, as amended (the "Code"). The Code imposes a maximum corporate tax rate of 39%. Oriental maintained a lower effective tax rate for the six-month periods ended June 30, 2018 and 2017 of 32.4% and 29.0%, respectively.

Oriental has operations in U.S. through its wholly owned subsidiary OPC, a retirement plan administration based in Florida. Also, in October 2017, Oriental expanded its operations in U.S. through the Bank's wholly owned subsidiary OFG USA LLC. Both subsidiaries are subject to state and federal taxes. OPC is subject to Florida state taxes and OFG USA is subject to North Carolina state taxes. OPC is a corporation and OFG USA elected to be classified as a corporation.

Income tax expense for the quarters ended June 30, 2018 and 2017 was $9.6 million and $4.0 million, respectively. Income tax expense for the six-month periods ended June 30, 2018 and 2017 was $17.6 million and $13.2 million, respectively.

NOTE 15 — REGULATORY CAPITAL REQUIREMENTS

Regulatory Capital Requirements

OFG Bancorp (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 Oriental's financial statements. Under capital adequacy guidelines and the regulatory framework for prompt corrective action, Oriental 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 adopted capital rules that became effective January 1, 2015 for Oriental 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 current capital rules prescribe a new standardized approach for risk weightings that expand the risk-weighting categories from the previous 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 current capital rules, the minimum capital ratios requirements 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, 2018 and December 31, 2017, OFG Bancorp and the Bank met all capital adequacy requirements to which they are subject. As of June 30, 2018 and December 31, 2017, 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 CONSOLIDATED FINANCIAL STATEMENTS – (Continued)

OFG Bancorp's and the Bank's actual capital amounts and ratios as of June 30, 2018 and December 31, 2017 are as follows:

	Actual		Minimum Capital Requirement		Minimum to be Well Capitalized	
	Amount	Ratio	Amount	Ratio	Amount	Ratio
			(Dollars in thousands)			
OFG Bancorp Ratios						
As of June 30, 2018						
Total capital to risk-weighted assets	$ 931,717	**19.67%**	$ 379,002	**8.00%**	$ 473,753	**10.00%**
Tier 1 capital to risk-weighted assets	$ 870,792	**18.38%**	$ 284,252	**6.00%**	$ 379,002	**8.00%**
Common equity tier 1 capital to risk-weighted assets	$ 669,922	**14.14%**	$ 213,189	**4.50%**	$ 307,939	**6.50%**
Tier 1 capital to average total assets	$ 870,792	**13.92%**	$ 250,165	**4.00%**	$ 312,706	**5.00%**
As of December 31, 2017						
Total capital to risk-weighted assets	$ 899,258	**20.34%**	$ 353,653	**8.00%**	$ 442,067	**10.00%**
Tier 1 capital to risk-weighted assets	$ 842,133	**19.05%**	$ 265,240	**6.00%**	$ 353,653	**8.00%**
Common equity tier 1 capital to risk-weighted assets	$ 644,804	**14.59%**	$ 198,930	**4.50%**	$ 287,343	**6.50%**
Tier 1 capital to average total assets	$ 842,133	**13.92%**	$ 242,057	**4.00%**	$ 302,571	**5.00%**

	Actual		Minimum Capital Requirement		Minimum to be Well Capitalized	
	Amount	Ratio	Amount	Ratio	Amount	Ratio
			(Dollars in thousands)			
Bank Ratios						
As of June 30, 2018						
Total capital to risk-weighted assets	$ 907,578	**19.18%**	$ 378,612	**8.00%**	$ 473,265	**10.00%**
Tier 1 capital to risk-weighted assets	$ 846,903	**17.89%**	$ 283,959	**6.00%**	$ 378,612	**8.00%**
	$ 846,903	**17.89%**	$ 212,969	**4.50%**	$ 307,622	**6.50%**

Common equity tier 1 capital to risk-weighted assets									
Tier 1 capital to average total assets	$	846,903	**13.59%**	$	249,314	**4.00%**	$	311,643	**5.00%**
As of December 31, 2017									
Total capital to risk-weighted assets	$	879,648	**19.92%**	$	353,265	**8.00%**	$	441,581	**10.00%**
Tier 1 capital to risk-weighted assets	$	822,776	**18.63%**	$	264,949	**6.00%**	$	353,265	**8.00%**
Common equity tier 1 capital to risk-weighted assets	$	822,776	**18.63%**	$	198,712	**4.50%**	$	287,028	**6.50%**
Tier 1 capital to average total assets	$	822,776	**13.63%**	$	241,417	**4.00%**	$	301,771	**5.00%**

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 both June 30, 2018 and December 31, 2017, accumulated issuance costs charged against additional paid-in capital amounted to $13.6 million and $10.1 million for preferred and common stock, respectively.

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NOTES TO CONSOLIDATED FINANCIAL STATEMENTS – (Continued)

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, 2018 and December 31, 2017, the Bank's legal surplus amounted to $85.2 million and $81.5 million, respectively. The amount transferred to the legal surplus account is not available for the payment of dividends to shareholders.

Treasury Stock

Under Oriental's current stock repurchase program it is authorized to purchase in the open market up to $7.7 million of its outstanding shares of common stock. The shares of common stock repurchased are to be held by Oriental as treasury shares. During the six-month periods ended June 30, 2018 and 2017, Oriental did not purchase any shares under the program.

At June 30, 2018 the number of shares that may yet be purchased under the $70 million program is estimated at 550,239 and was calculated by dividing the remaining balance of $7.7 million by $14.05 (closing price of Oriental's common stock at June 30, 2018).

The activity in connection with common shares held in treasury by Oriental for the six-month periods ended June 30, 2018 and 2017 is set forth below:

	Six-Month Period Ended June 30,			
	2018		2017	
	Shares	Dollar Amount	Shares	Dollar Amount
	(In thousands, except shares data)			
Beginning of period	8,678,427	$ 104,502	8,711,025	$ 104,860
Common shares used upon lapse of restricted stock units	(35,753)	(533)	(32,598)	(358)
End of period	**8,642,674**	**$ 103,969**	**8,678,427**	**$ 104,502**

NOTE 17 - ACCUMULATED OTHER COMPREHENSIVE INCOME

Accumulated other comprehensive income, net of income taxes, as of June 30, 2018 and December 31, 2017 consisted of:

		June 30, 2018		December 31, 2017
		(In thousands)		
Unrealized loss on securities available-for-sale which are not other-than-temporarily impaired	$	(17,967)	$	(3,003)
Income tax effect of unrealized loss on securities available-for-sale		2,449		365
Net unrealized gain on securities available-for-sale which are not other-than-temporarily impaired		(15,518)		(2,638)
Unrealized gain (loss) on cash flow hedges		421		(510)
Income tax effect of unrealized (gain) loss on cash flow hedges		(165)		199
Net unrealized gain (loss) on cash flow hedges		256		(311)
Accumulated other comprehensive (loss), net of income taxes	$	**(15,262)**	**$**	**(2,949)**

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NOTES TO CONSOLIDATED FINANCIAL STATEMENTS – (Continued)

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, 2018 and 2017:

	Quarter Ended June 30,					
	2018			2017		
	Net unrealized gains on securities available-for-sale	Net unrealized loss on cash flow hedges	Accumulated other comprehensive (loss) income	Net unrealized gains on securities available-for-sale	Net unrealized loss on cash flow hedges	Accumulated other comprehensive (loss) income
	(In thousands)					
Beginning balance	$ (12,274)	$ 89	$ (12,185)	$ 3,850	$ (502)	$ 3,348
Other comprehensive loss before reclassifications	(3,178)	(281)	(3,459)	(3,618)	(189)	(3,807)
Amounts reclassified out of accumulated other comprehensive income (loss)	(66)	448	382	24	128	152
Other comprehensive income (loss)	(3,244)	167	(3,077)	(3,594)	(61)	(3,655)
Ending balance	**$ (15,518)**	**$ 256**	**$ (15,262)**	**$ 256**	**$ (563)**	**$ (307)**

	Six-Month Period Ended June 30,					
	2018			2017		
	Net unrealized gains on securities available-for-sale	Net unrealized loss on cash flow hedges	Accumulated other comprehensive (loss) income	Net unrealized gains on securities available-for-sale	Net unrealized loss on cash flow hedges	Accumulated other comprehensive (loss) income
	(In thousands)					
Beginning balance	$ (2,638)	$ (311)	$ (2,949)	$ 2,209	$ (613)	$ 1,596
Other comprehensive loss before reclassifications	(12,754)	(255)	(13,009)	(1,911)	(227)	(2,138)
Amounts reclassified out of accumulated other comprehensive income (loss)	(126)	822	696	(42)	277	235
Other comprehensive income (loss)	(12,880)	567	(12,313)	(1,953)	50	(1,903)
Ending balance	**$ (15,518)**	**$ 256**	**$ (15,262)**	**$ 256**	**$ (563)**	**$ (307)**

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NOTES TO 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, 2018 and 2017:

	Amount reclassified out of accumulated other comprehensive income Quarter Ended June 30,		Affected Line Item in Consolidated Statement of Operations
	2018	2017	
	(In thousands)		
Cash flow hedges:			
Interest-rate contracts	$ 448	$ 128	Net interest expense
Available-for-sale securities:			
Gain on sale of investments	-	6,891	Income tax expense
Residual tax effect from OIB's change in applicable tax rate	-	95	Income tax expense
Tax effect from changes in tax rates	(66)	(71)	Income tax expense
	$ 382	**$ 7,043**	

	Amount reclassified out of accumulated other comprehensive income Six-Month Period Ended June 30,		Affected Line Item in Consolidated Statement of Operations
	2018	2017	
	(In thousands)		
Cash flow hedges:			
Interest-rate contracts	$ 822	$ 277	Net interest expense
Available-for-sale securities:			
Gain on sale of investments	-	6,891	Income tax expense
Residual tax effect from OIB's change in applicable tax rate	5	103	Income tax expense
Tax effect from changes in tax rates	(131)	(145)	Income tax expense
	$ 696	**$ 7,126**	

NOTE 18 – EARNINGS PER COMMON SHARE

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

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NOTES TO CONSOLIDATED FINANCIAL STATEMENTS – (Continued)

	Quarter Ended June 30, 2018	Quarter Ended June 30, 2017	Six-Month Period Ended June 30, 2018	Six-Month Period Ended June 30, 2017
	(In thousands, except per share data)			
Net income	$ 19,649	$ 17,104	$ 36,566	$ 32,254
Less: Dividends on preferred stock				
Non-convertible preferred stock (Series A, B, and D)	(1,628)	(1,629)	(3,255)	(3,256)
Convertible preferred stock (Series C)	(1,837)	(1,837)	(3,675)	(3,675)
Income available to common shareholders	**$ 16,184**	**$ 13,638**	**$ 29,636**	**$ 25,323**
Effect of assumed conversion of the convertible preferred stock	1,837	1,837	3,675	3,675
Income available to common shareholders assuming conversion	$ **18,021**	$ **15,475**	$ **33,311**	$ **28,998**
Weighted average common shares and share equivalents:				
Average common shares outstanding	43,975	43,947	43,965	43,931
Effect of dilutive securities:				
Average potential common shares-options	113	15	54	24
Average potential common shares-assuming conversion of convertible preferred stock	7,138	7,138	7,138	7,138
Total weighted average common shares outstanding and equivalents	**51,226**	**51,100**	**51,157**	**51,093**
Earnings per common share - basic	**$ 0.36**	**$ 0.30**	**$ 0.67**	**$ 0.58**
Earnings per common share - diluted	**$ 0.35**	**$ 0.30**	**$ 0.65**	**$ 0.57**

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NOTES TO CONSOLIDATED FINANCIAL STATEMENTS – (Continued)

In computing diluted earnings per common share, the 84,000 shares of convertible preferred stock, which remain outstanding at June 30, 2018, with a conversion rate, subject to certain conditions, of 86.4225 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 and six-month periods ended June 30, 2018 and 2017 on the convertible preferred stock were added back as income available to common shareholders.

For the quarters ended June 30, 2018 and 2017, weighted-average stock options with an anti-dilutive effect on earnings per share not included in the calculation amounted to 433,493 and 967,041, respectively. For the six-month period ended June 30, 2018 and 2017, weighted-average stock options with an anti-dilutive effect on earnings per share not included in the calculation amounted to 442,221 and 890,472, respectively.

NOTE 19 – GUARANTEES

At June 30, 2018 and December 31, 2017 , the unamortized balance of the obligations undertaken in issuing the guarantees under standby letters of credit represented a liability of $21.3 million and $21.1 million, respectively.

Oriental has 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, 2018 and December 31, 2017, the unpaid principal balance of residential mortgage loans sold subject to credit recourse was $5.9 million and $6.4 million, respectively.

The following table shows the changes in Oriental's liability for estimated losses from these credit recourse agreements, included in the consolidated statements of financial condition during the quarters and six-month periods ended June 30, 2018 and 2017.

	Quarter Ended June 30,		Six-Month Period Ended June 30,	
	2018	**2017**	**2018**	**2017**
	(In thousands)			
Balance at beginning of period	$ 264	$ 570	$ 358	$ 710
Net (charge-offs/terminations) recoveries	(75)	(111)	(169)	(251)
Balance at end of period	**$ 189**	**$ 459**	**$ 189**	**$ 459**

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 Oriental is obligated to repurchase the loan.

If a borrower defaults, pursuant to the credit recourse provided, Oriental is required to repurchase the loan or reimburse the third party investor for the incurred loss. The maximum potential amount of future payments that Oriental 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 ended June 30, 2018, Oriental did not repurchase any mortgage loans subject to credit recourse provisions. During the quarter ended June 30, 2017, Oriental repurchased approximately $66 thousand of unpaid principal balance in mortgage loans subject to the credit recourse provisions. During the six-month periods ended June 30, 2018, Oriental did not repurchase any mortgage loans subject to credit recourse provisions. During the six-month periods ended June 30, 2017, Oriental repurchased approximately $107 thousand of unpaid principal balance in mortgage loans subject to the credit recourse provisions. If a borrower defaults, Oriental has rights to the underlying collateral securing the mortgage loan. Oriental 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, 2018, Oriental’s liability for estimated credit losses related to loans sold with credit recourse amounted to $189 thousand (December 31, 2017– $358 thousand).

When Oriental sells or securitizes mortgage loans, it generally makes customary representations and warranties regarding the characteristics of the loans sold. Oriental'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 Oriental to ensure that asset guideline qualifications are met. To the extent the loans do not meet specified characteristics, Oriental may be required to repurchase such loans or indemnify for losses and bear any subsequent loss related to the loans. During the quarter ended June 30, 2018, Oriental repurchased $2.4 million (June 30, 2017 – $1.4 million) of unpaid principal balance in mortgage loans, excluding mortgage loans subject to credit recourse provision referred above. During the six-month periods ended June 30, 2018, Oriental repurchased $4.7 million (June 30, 2017 – $2.3 million) of unpaid principal balance in mortgage loans, excluding mortgage loans subject to credit recourse provision referred above.

During the quarters ended June 30, 2018 and 2017, Oriental recognized $375 thousand and $254 thousand, respectively, in losses from the repurchase of residential mortgage loans sold subject to credit recourse, and $31 thousand and $283 thousand, respectively, in losses from the repurchase of residential mortgage loans as a result of breaches of the customary representations and warranties. During the six-month periods ended June 30, 2018 and 2017, Oriental recognized $375 thousand and $354 thousand, respectively, in losses from the repurchase of residential mortgage loans sold subject to credit recourse, and $30 thousand and $590 thousand, respectively, 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 FHLMC, require Oriental 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, 2018, Oriental serviced $880.4 million (December 31, 2017 - $864.9 million) in mortgage loans for third-parties. Oriental 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, Oriental must absorb the cost of the funds it advances during the time the advance is outstanding. Oriental 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 Oriental would not receive any future servicing income with respect to that loan. At June 30, 2018, the outstanding balance of funds advanced by Oriental under such mortgage loan servicing agreements was approximately $651 thousand (December 31, 2017 - $440 thousand). To the extent the mortgage loans underlying Oriental's servicing portfolio experience increased delinquencies, Oriental 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.

NOTE 20— COMMITMENTS AND CONTINGENCIES

Loan Commitments

In the normal course of business, Oriental 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 Oriental's involvement in particular types of financial instruments.

Oriental'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. Oriental 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, 2018 and December 31, 2017 were as follows:

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NOTES TO CONSOLIDATED FINANCIAL STATEMENTS – (Continued)

	June 30, 2018	December 31, 2017
	(In thousands)	
Commitments to extend credit	$ 539,661	$ 485,019
Commercial letters of credit	1,735	494

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NOTES TO CONSOLIDATED FINANCIAL STATEMENTS – (Continued)

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. Oriental evaluates each customer's creditworthiness on a case-by-case basis. The amount of collateral obtained, if it is deemed necessary by Oriental upon the extension of credit, is based on management's credit evaluation of the counterparty.

At June 30, 2018 and December 31, 2017, 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 $567 thousand at both June 30, 2018 and December 31, 2017.

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.

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, 2018 and December 31, 2017, is as follows:

		June 30, 2018		December 31, 2017
		(In thousands)		
Standby letters of credit and financial guarantees	$	21,343	$	21,107
Loans sold with recourse		5,917		6,420

Standby letters of credit and financial guarantees are written conditional commitments issued by Oriental 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 Oriental upon extension of credit, is based on management's credit evaluation of the customer.

Lease Commitments

Oriental has entered into various operating lease agreements for branch facilities and administrative offices. Rent expense for the quarters ended June 30, 2018 and 2017, amounted to $3.2 million and $2.5 million, respectively. For the six-month periods ended June 30, 2018 and 2017, rent expense amounted to $5.4 million and $4.5 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, 2018, exclusive of taxes, insurance, and maintenance expenses payable by Oriental, are summarized as follows:

Year Ending December 31,		Minimum Rent (In thousands)
2018	$	4,995
2019		5,542
2020		4,000
2021		3,127
2022		2,485
Thereafter		6,880
	$	**27,029**

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NOTES TO CONSOLIDATED FINANCIAL STATEMENTS – (Continued)

Contingencies

Oriental and its subsidiaries are defendants in a number of legal proceedings incidental to their business. In the ordinary course of business, Oriental and its subsidiaries are also subject to governmental and regulatory examinations. Certain subsidiaries of Oriental, 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.

Oriental seeks to resolve all litigation and regulatory matters in the manner management believes is in the best interests of Oriental 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 Oriental'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 Oriental. 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 Oriental's consolidated results of operations or cash flows in particular quarterly or annual periods. Oriental has evaluated all litigation and regulatory matters where the likelihood of a potential loss is deemed reasonably possible. Oriental has determined that the estimate of the reasonably possible loss is not significant.

NOTE 21 - FAIR VALUE OF FINANCIAL INSTRUMENTS

Oriental follows the fair value measurement framework under U.S. Generally Accepted Accounting Principles ("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 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 Interactive Data Corporation ("IDC"), an independent, well-recognized pricing company. 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, 2018 and December 31, 2017, Oriental did not have investment securities classified as Level 3.

Securities purchased under agreements to resell

The fair value of securities purchased under agreements to resell 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 instruments.

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 Oriental. 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.

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.

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NOTES TO CONSOLIDATED FINANCIAL STATEMENTS – (Continued)

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 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 automobiles. 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.

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

	June 30, 2018 Fair Value Measurements			
	Level 1	**Level 2**	**Level 3**	**Total**
	(In thousands)			

Recurring fair value measurements:								
Investment securities available-for-sale	$	-	$	872,341	$	-	$	872,341
Trading securities		-		418		-		418
Money market investments		6,991		-		-		6,991
Derivative assets		-		1,100		-		1,100
Servicing assets		-		-		10,829		10,829
Derivative liabilities		-		(679)		-		(679)
	$	**6,991**	**$**	**873,180**	**$**	**10,829**	**$**	**891,000**
Non-recurring fair value measurements:								
Impaired commercial loans	$	-	$	-	$	69,799	$	69,799
Foreclosed real estate		-		-		40,551		40,551
Other repossessed assets		-		-		5,483		5,483
	$	**-**	**$**	**-**	**$**	**115,833**	**$**	**115,833**

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NOTES TO CONSOLIDATED FINANCIAL STATEMENTS – (Continued)

	December 31, 2017 Fair Value Measurements			
	Level 1	Level 2	Level 3	Total
	(In thousands)			
Recurring fair value measurements:				
Investment securities available-for-sale	$ -	$ 645,797	$ -	$ 645,797
Trading securities	-	191	-	191
Money market investments	7,021	-	-	7,021
Derivative assets	-	771	-	771
Servicing assets	-	-	9,821	9,821
Derivative liabilities	-	(1,281)	-	(1,281)
	$ 7,021	**$ 645,478**	**$ 9,821**	**$ 662,320**
Non-recurring fair value measurements:				
Impaired commercial loans	$ -	$ -	$ 72,285	$ 72,285
Foreclosed real estate	-	-	44,174	44,174
Other repossessed assets	-	-	3,548	3,548
	$ -	**$ -**	**$ 120,007**	**$ 120,007**

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, 2018 and 2017:

	Servicing assets Quarter Ended June 30,	
Level 3 Instruments Only	**2018**	**2017**
	(In thousands)	
Balance at beginning of period	$ 10,533	$ 9,688
New instruments acquired	389	540
Principal repayments	(210)	(164)
Changes in fair value of servicing assets	117	(198)
Balance at end of period	**$ 10,829**	**$ 9,866**

	Servicing assets Six-Month Period Ended June 30,	
Level 3 Instruments Only	**2018**	**2017**
	(In thousands)	
Balance at beginning of period	$ 9,821	$ 9,858
New instruments acquired	741	1,074
Principal repayments	(409)	(326)

Changes in fair value of servicing assets		676		(740)
Balance at end of period	**$**	**10,829**	**$**	**9,866**

During the quarters and six-month periods ended June 30, 2018 and 2017, 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 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, 2018:

	June 30, 2018				
	Fair Value (In thousands)		Valuation Technique	Unobservable Input	Range
Servicing assets	$	10,829	Cash flow valuation	Constant prepayment rate	4.66% -8.64%
				Discount rate	10.00% - 12.00%
Collateral dependent impaired loans	$	35,131	Fair value of property or collateral	Appraised value less disposition costs	17.20% - 34.20%
Other non-collateral dependent impaired loans	$	34,668	Cash flow valuation	Discount rate	4.25% - 10.50%
Foreclosed real estate	$	40,551	Fair value of property or collateral	Appraised value less disposition costs	17.20% - 34.20%
Other repossessed assets	$	5,483	Fair value of property or collateral	Estimated net realizable value less disposition costs	36.00% - 64.00%

Information about Sensitivity to Changes in Significant Unobservable Inputs

Servicing assets – The significant unobservable inputs used in the fair value measurement of Oriental'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.

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 Oriental.

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 CONSOLIDATED FINANCIAL STATEMENTS – (Continued)

The estimated fair value and carrying value of Oriental's financial instruments at June 30, 2018 and December 31, 2017 is as follows:

	June 30, 2018		December 31, 2017	
	Fair Value	Carrying Value	Fair Value	Carrying Value
	(In thousands)			
Level 1				
Financial Assets:				
Cash and cash equivalents	$ 375,335	$ 375,335	$ 485,203	$ 485,203
Restricted cash	$ 3,030	$ 3,030	$ 3,030	$ 3,030
Level 2				
Financial Assets:				
Trading securities	$ 418	$ 418	$ 191	$ 191
Investment securities available-for-sale	$ 872,341	$ 872,341	$ 645,797	$ 645,797
Investment securities held-to-maturity	$ 447,947	$ 465,427	$ 497,681	$ 506,064
Federal Home Loan Bank (FHLB) stock	$ 14,919	$ 14,919	$ 13,995	$ 13,995
Other investments	$ 3	$ 3	$ 3	$ 3
Derivative assets	$ 1,100	$ 1,100	$ 771	$ 771
Financial Liabilities:				
Derivative liabilities	$ 679	$ 679	$ 1,281	$ 1,281
Level 3				
Financial Assets:				
Total loans (including loans held-for-sale)	$ 3,897,042	$ 4,315,866	$ 3,842,907	$ 4,056,329
Accrued interest receivable	$ 34,476	$ 34,476	$ 49,969	$ 49,969
Servicing assets	$ 10,829	$ 10,829	$ 9,821	$ 9,821
Accounts receivable and other assets	$ 35,693	$ 35,693	$ 41,898	$ 41,898
Financial Liabilities:				
Deposits	$ 4,850,971	$ 4,880,201	$ 4,782,197	$ 4,799,482
Securities sold under agreements to repurchase	$ 385,430	$ 387,770	$ 191,104	$ 192,869
Advances from FHLB	$ 127,994	$ 128,114	$ 99,509	$ 99,643
Other borrowings	$ 299	$ 299	$ 153	$ 153
Subordinated capital notes	$ 33,784	$ 36,083	$ 33,080	$ 36,083
Accrued expenses and other liabilities	$ 80,019	$ 80,019	$ 86,791	$ 86,791

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NOTES TO CONSOLIDATED FINANCIAL STATEMENTS – (Continued)

The following methods and assumptions were used to estimate the fair values of significant financial instruments at June 30, 2018 and December 31, 2017:

- Cash and cash equivalents (including money market investments and time deposits with other banks), restricted cash, accrued interest receivable, accounts receivable and other assets 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 prices provided from contracted pricing providers, 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 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.

- 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 loan portfolio (including loans held-for-sale and non-performing loans) is based on the exit market price, which 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. The fair value 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.

- 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, 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 – BANKING AND FINANCIAL SERVICE REVENUES

The following table presents the major categories of banking and financial service revenues for the quarters and six-month periods ended June 30, 2018 and 2017:

	Quarter Ended June 30,		Six-Month Period Ended June 30,	
	2018	2017	2018	2017
	(In thousands)			
Banking service revenues:				
Checking accounts fees	$ 1,365	$ 1,852	$ 2,884	$ 3,703
Savings accounts fees	157	162	312	317
Electronic banking fees	8,286	7,676	15,856	15,360
Credit life commissions	139	154	258	304
Branch service commissions	396	104	723	251
Servicing and other loan fees	618	305	1,220	789
International fees	179	202	349	349
Miscellaneous income	4	3	5	11
Total banking service revenues	**11,144**	**10,458**	**21,607**	**21,084**
Wealth management revenue:				
Insurance income	1,405	1,551	2,644	3,101
Broker fees	1,657	1,795	3,447	3,670
Trust fees	2,902	2,799	5,597	5,347
Retirement plan and administration fees	298	342	584	584
Investment banking fees	-	29	9	29
Total wealth management revenue	**6,262**	**6,516**	**12,281**	**12,731**
Mortgage banking activities:				
Net servicing fees	1,318	1,185	3,072	2,006
Net gains on sale of mortgage loans and valuation	77	310	80	484
Other	(407)	(536)	(407)	(944)
Total mortgage banking activities	**988**	**959**	**2,745**	**1,546**
Total banking and financial service revenues	**$ 18,394**	**$ 17,933**	**$ 36,633**	**$ 35,361**

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NOTES TO CONSOLIDATED FINANCIAL STATEMENTS – (Continued)

NOTE 23 – BUSINESS SEGMENTS

Oriental 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 Oriental's organization, nature of its products, distribution channels and economic characteristics of the products were also considered in the determination of the reportable segments. Oriental 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. Oriental'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 Oriental's own portfolio. As part of its mortgage banking activities, Oriental 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 Oriental'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 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, 2018 and 2017:

	Quarter Ended June 30, 2018					
	Banking	**Wealth Management**	**Treasury**	**Total Major Segments**	**Eliminations**	**Consolidated Total**
			(In thousands)			
Interest income	$ 78,133	$ 14	$ 9,859	$ 88,006	$ -	$ **88,006**
Interest expense	(7,132)	-	(3,286)	(10,418)	-	**(10,418)**
Net interest income	71,001	14	6,573	77,588	-	77,588
Provision for loan and lease losses	(14,744)	-	(3)	(14,747)	-	**(14,747)**
Non-interest income	12,240	6,448	15	18,703	-	**18,703**
Non-interest expenses	(46,109)	(5,282)	(909)	(52,300)	-	**(52,300)**
Intersegment revenue	542	-	-	542	(542)	**-**
Intersegment expenses	-	(208)	(334)	(542)	542	**-**
Income before income taxes	$ 22,930	$ 972	$ 5,342	$ 29,244	$ -	$ **29,244**
Income tax expense	8,943	379	273	9,595	-	**9,595**
Net income	**$ 13,987**	**$ 593**	**$ 5,069**	**$ 19,649**	**$ -**	**$ 19,649**
Total assets	**$ 6,006,889**	**$ 29,253**	**$ 1,447,949**	**$ 7,484,091**	**$ (982,529)**	**$ 6,501,562**

	Quarter Ended June 30, 2017					
	Banking	**Wealth Management**	**Treasury**	**Total Major Segments**	**Eliminations**	**Consolidated Total**
			(In thousands)			
Interest income	$ 77,019	$ 18	$ 8,903	$ 85,940	$ -	$ **85,940**
Interest expense	(6,820)	-	(3,557)	(10,377)	-	**(10,377)**
Net interest income	70,199	18	5,346	75,563	**-**	**75,563**

Provision for loan and lease losses	(26,526)	-	(10)	(26,536)	-	**(26,536)**
Non-interest income	11,776	6,329	6,781	24,886	-	**24,886**
Non-interest expenses	(47,402)	(4,100)	(1,314)	(52,816)	-	**(52,816)**
Intersegment revenue	346	-	71	417	(417)	-
Intersegment expenses	(71)	(254)	(92)	(417)	417	**-**
Income before income taxes	$ 8,322	$ 1,993	$ 10,782	$ 21,097	$ -	$ 21,097
Income tax expense (benefit)	3,246	777	(30)	3,993	-	3,993
Net income	**$ 5,076**	**$ 1,216**	**$ 10,812**	**$ 17,104**	**$ -**	**$ 17,104**
Total assets	**$ 5,490,287**	**$ 22,531**	**$ 1,692,603**	**$ 7,205,421**	**$ (969,595)**	**$ 6,235,826**

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NOTES TO CONSOLIDATED FINANCIAL STATEMENTS – (Continued)

	Six-Month Period Ended June 30, 2018					
	Banking	Wealth Management	Treasury	Total Major Segments	Eliminations	Consolidated Total
	(In thousands)					
Interest income	$ 152,507	$ 26	$ 18,643	$ 171,176	$ -	**$ 171,176**
Interest expense	(13,422)	-	(6,172)	(19,594)	-	**(19,594)**
Net interest income	139,085	26	12,471	151,582	-	**151,582**
Provision for loan and lease losses, net	(30,199)	-	(8)	(30,207)	-	**(30,207)**
Non-interest income	24,433	12,756	28	37,217	-	**37,217**
Non-interest expenses	(94,190)	(8,568)	(1,663)	(104,421)	-	**(104,421)**
Intersegment revenue	903	-	-	903	(903)	**-**
Intersegment expenses	-	(387)	(516)	(903)	903	**-**
Income before income taxes	$ 40,032	$ 3,827	$ 10,312	$ 54,171	$ -	**$ 54,171**
Income tax expense	15,612	1,493	500	17,605	-	**17,605**
Net income	**$ 24,420**	**$ 2,334**	**$ 9,812**	**$ 36,566**	**$ -**	**$ 36,566**
Total assets	**$ 6,006,889**	**$ 29,253**	**$ 1,447,949**	**$ 7,484,091**	**$ (982,529)**	**$ 6,501,562**

	Six-Month Period Ended June 30, 2017					
	Banking	Wealth Management	Treasury	Total Major Segments	Eliminations	Consolidated Total
	(In thousands)					
Interest income	$ 154,592	$ 30	$ 17,496	$ 172,118	$ -	**$ 172,118**
Interest expense	(13,634)	-	(8,303)	(21,937)	-	**(21,937)**
Net interest income	140,958	30	9,193	150,181	-	**150,181**
Provision for loan and lease losses, net	(44,168)	-	(22)	(44,190)	-	**(44,190)**
Non-interest income	25,003	12,257	6,700	43,960	-	**43,960**
Non-interest expenses	(93,456)	(8,320)	(2,724)	(104,500)	-	**(104,500)**
Intersegment revenue	810	-	142	952	(952)	**-**
Intersegment expenses	(142)	(565)	(245)	(952)	952	**-**
Income before income taxes	$ 29,005	$ 3,402	$ 13,044	$ 45,451	$ -	**$ 45,451**
Income tax expense	11,312	1,327	558	13,197	-	**13,197**
Net income	**$ 17,693**	**$ 2,075**	**$ 12,486**	**$ 32,254**	**$ -**	**$ 32,254**
Total assets	**$ 5,490,287**	**$ 22,531**	**$ 1,692,603**	**$ 7,205,421**	**$ (969,595)**	**$ 6,235,826**

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

INTRODUCTION

The following discussion of Oriental's financial condition and results of operations should be read in conjunction with the "Selected Financial Data" and Oriental's 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, 2017 (the "2017 Form 10-K"), for discussion of the uncertainties, risks and assumptions associated with these statements.

Oriental 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. Oriental operates through three major business segments: Banking, Wealth Management, and Treasury, and distinguishes itself based on quality service. Oriental has 39 branches in Puerto Rico and a subsidiary in Boca Raton, Florida, and a non-bank operating subsidiary in Cornelius, North Carolina. Oriental'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.

Oriental'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, Oriental'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 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 2017 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 2017 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:

- Fair value measurements of financial instruments
- Interest on loans and allowance for loan losses
- Acquisition accounting for loans
- Income taxes
- Goodwill

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 Oriental's continuous enhancement to the allowance for loan and lease losses methodology, during the quarter ended June 30, 2018, 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, 2018. As a result, for the commercial portfolio, the look-back period was extended to 40 months from 36 months. For auto and consumer portfolios, a look back period of 24 months was maintained, and for the residential mortgage portfolio, the period was extended to 24 from 12 months. In addition, during the quarter ended June 30, 2018, 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. Apart 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 2017 Form 10-K.

OVERVIEW OF FINANCIAL PERFORMANCE

SELECTED FINANCIAL DATA

	Quarter Ended June 30,			Six-Month Period Ended June 30,		
	2018	2017	Variance %	2018	2017	Variance %
EARNINGS DATA:	(In thousands, except per share data)					
Interest income	$ 88,006	$ 85,940	2.4%	$ 171,176	$ 172,118	-0.5%
Interest expense	10,418	10,377	0.4%	19,594	21,937	-10.7%
Net interest income	**77,588**	**75,563**	**2.7%**	**151,582**	**150,181**	**0.9%**
Provision for loan and lease losses, net	14,747	26,536	-44.4%	30,207	44,190	-31.6%
Net interest income after provision for loan and lease losses	**62,841**	**49,027**	**28.2%**	**121,375**	**105,991**	**14.5%**
Non-interest income	18,703	24,886	-24.8%	37,217	43,960	-15.3%
Non-interest expenses	52,300	52,816	-1.0%	104,421	104,500	-0.1%
Income before taxes	**29,244**	**21,097**	**38.6%**	**54,171**	**45,451**	**19.2%**
Income tax expense	9,595	3,993	140.3%	17,605	13,197	33.4%
Net income	**19,649**	**17,104**	**14.9%**	**36,566**	**32,254**	**13.4%**
Less: dividends on preferred stock	(3,465)	(3,466)	0.0%	(6,930)	(6,931)	**0.0%**
Income available to common shareholders	**$ 16,184**	**$ 13,638**	**18.7%**	**$ 29,636**	**$ 25,323**	**17.0%**
PER SHARE DATA:						
Basic	**$ 0.36**	**$ 0.30**	**20.0%**	**$ 0.67**	**$ 0.58**	**15.5%**
Diluted	**$ 0.35**	**$ 0.30**	**16.7%**	**$ 0.65**	**$ 0.57**	**14.0%**
Average common shares outstanding	**43,975**	**43,947**	**0.1%**	**43,965**	**43,931**	**0.1%**
Average common shares outstanding and equivalents	**51,226**	**51,100**	**0.2%**	**51,157**	**51,093**	**0.1%**
Cash dividends declared per common share	**$ 0.06**	**$ 0.06**	**0.0%**	**$ 0.12**	**$ 0.12**	**0.0%**
Cash dividends declared on common shares	**$ 2,640**	**$ 2,640**	**0.0%**	**$ 5,278**	**$ 5,277**	**0.0%**
PERFORMANCE RATIOS:						
Return on average assets (ROA)	**1.23%**	**1.09%**	**12.8%**	**1.16%**	**1.02%**	**13.7%**
Return on average tangible common equity	**9.20%**	**8.01%**	**14.9%**	**8.47%**	**7.51%**	**12.8%**
Return on average common equity (ROE)	**8.15%**	**7.06%**	**15.4%**	**7.50%**	**6.61%**	**13.5%**
Efficiency ratio	**5.16%**	**5.10%**	**1.2%**	**5.15%**	**5.07%**	**1.6%**

Interest rate spread	**5.24%**	**5.18%**	**1.2%**	**5.23%**	**5.14%**	**1.8%**

SELECTED FINANCIAL DATA - (Continued)

		June 30, 2018		December 31, 2017	Variance %
PERIOD END BALANCES AND CAPITAL RATIOS:		**(In thousands, except per share data)**			
Investments and loans					
Investment securities	$	1,353,108	$	1,166,050	16.0%
Loans and leases, net		4,315,866		4,056,329	6.4%
Total investments and loans	**$**	**5,668,974**	**$**	**5,222,379**	**8.6%**
Deposits and borrowings					
Deposits	$	4,880,201	$	4,799,482	1.7%
Securities sold under agreements to repurchase		387,770		192,869	101.1%
Other borrowings		164,496		135,879	21.1%
Total deposits and borrowings	**$**	**5,432,467**	**$**	**5,128,230**	**5.9%**
Stockholders' equity					
Preferred stock	$	176,000	$	176,000	0.0%
Common stock		52,626		52,626	0.0%
Additional paid-in capital		541,734		541,600	0.0%
Legal surplus		85,249		81,454	4.7%
Retained earnings		221,441		200,878	10.2%
Treasury stock, at cost		(103,969)		(104,502)	0.5%
Accumulated other comprehensive (loss)		(15,262)		(2,949)	-417.5%
Total stockholders' equity	**$**	**957,819**	**$**	**945,107**	**1.3%**
Per share data					
Book value per common share	**$**	**18.01**	**$**	**17.73**	**1.6%**
Tangible book value per common share	**$**	**15.96**	**$**	**15.67**	**1.8%**
Market price at end of period	**$**	**14.05**	**$**	**9.40**	**49.5%**
Capital ratios					
Leverage capital		**13.92%**		**13.92%**	**0.0%**
Common equity Tier 1 capital ratio		**14.14%**		**14.59%**	**-3.1%**
Tier 1 risk-based capital		**18.38%**		**19.05%**	**-3.5%**
Total risk-based capital		**19.67%**		**20.34%**	**-3.3%**
Equity to assets ratio		**14.73%**		**15.27%**	**-3.5%**
Financial assets managed					
Trust assets managed	$	2,953,335	$	3,039,998	-2.9%
Broker-dealer assets gathered	$	2,262,454	$	2,250,460	0.5%

FINANCIAL HIGHLIGHTS

Our earnings per share in the second quarter increased more than 17% from the first quarter and more than 16% year over year. Virtually every one of our financial performance metrics confirms the success of our strategies, people and technology.

For the third quarter in a row, loan growth, new loan production, and return on average tangible common stockholders' equity are up, while credit quality remained stable. For two quarters in a row, customer count, banking and financial service revenues, core retail deposits and NIM increased, and delinquency rates remained below pre-hurricane levels.

Our efforts to differentiate Oriental through superior service and technology is working. During the second quarter of 2018, we launched *Oriental SmallBiz,* another banking first for Puerto Rico, where new and existing customers can apply online for commercial credit. Services like these enable us to step up our ability to reach out to customers and clients *fácil, rápido, hecho* (easy, fast, done).

We are also encouraged as OFG continues to build solid capital, with tangible book value per common share at $15.96, up from the prior quarter more than 6% on an annualized basis. All indicators are positive, positioning us well to continue this trend for the rest of 2018.

While Puerto Rico faces similar challenges as before, now that insurance and federal funds are flowing, economic activity and optimism are gaining momentum. Based on what we have seen to date, we are confident about Oriental’s ability to continue to grow, deliver great customer experience and performance, and help Puerto Rico recover.

Summary of second quarter of 2018

- Net income available to shareholders was $16.2 million, or $0.35 per fully diluted share, compared to the first quarter of 2018 $13.5 million and the second quarter of 2017 $13.6 million, equal to $0.30 per share, respectively.

- Average loan balances of $4.3 billion increased 3.0% from the preceding quarter as growth of originated loans is outpacing the anticipated runoff of acquired loans.

- New loan production of $432.1 million grew 39.7% from the first quarter of 2018 with increases in production across the board in all categories.

- Average core deposit balances of $4.4 billion rose 1.6% from the first quarter of 2018 with a 6.2% increase in non-interest bearing accounts to a record high $1.1 billion.

- Customer count grew 1% from the first quarter of 2018 and 3% year over year as our strategy of differentiation, delivering superior customer convenience with innovative technology solutions, continues to be successful.

- Total provision for loan and lease losses of $14.7 million dropped 4.6% from the preceding quarter as credit quality remains stable.

- All key performance metrics improved from the first quarter of 2018 with net interest margin at 5.24%, return on average assets at 1.23%, return on average tangible common stockholders’ equity at 9.20%, and the efficiency ratio at 54.49%.

- Tangible book value per common share of $15.96 at June 30, 2018 increased 6.4% annualized from March 31, 2018.

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, 2018 and 2017:

TABLE 1 - ANALYSIS OF NET INTEREST INCOME AND CHANGES DUE TO VOLUME/RATE FOR THE QUARTERS ENDED JUNE 30, 2018 AND 2017

	Interest		Average rate		Average balance	
	June 2018	June 2017	June 2018	June 2017	June 2018	June 2017
			(Dollars in thousands)			
A - TAX EQUIVALENT SPREAD						
Interest-earning assets	**$ 88,006**	**$ 85,940**	**5.95%**	**5.89%**	**$ 5,933,775**	**$ 5,848,525**
Tax equivalent adjustment	1,218	1,302	0.08%	0.09%	-	-
Interest-earning assets - tax equivalent	**89,224**	**87,242**	**6.03%**	**5.98%**	**5,933,775**	**5,848,525**
Interest-bearing liabilities	10,418	10,377	0.78%	0.79%	5,311,070	5,293,848
Tax equivalent net interest income / spread	**78,806**	**76,865**	**5.24%**	**5.19%**	**622,705**	**554,677**
Tax equivalent interest rate margin			**5.33%**	**5.27%**		
B - NORMAL SPREAD						
Interest-earning assets:						
Investments:						
Investment securities	8,335	7,746	2.51%	2.33%	1,330,138	1,334,938
Interest bearing cash and money market investments	1,242	956	1.70%	1.00%	293,431	384,037
Total investments	**9,577**	**8,702**	**2.37%**	**2.03%**	**1,623,569**	**1,718,975**
Non-acquired loans						
Mortgage	8,752	9,411	5.17%	5.40%	679,133	698,782
Commercial	20,518	16,688	5.83%	5.33%	1,411,177	1,256,827
Consumer	8,833	8,075	11.05%	11.06%	320,687	292,739
Auto and leasing	23,080	19,275	9.27%	9.63%	999,047	803,201
Total non-acquired loans	**61,183**	**53,449**	**7.20%**	**7.03%**	**3,410,044**	**3,051,549**
Acquired loans:						
Acquired BBVAPR						
Mortgage	6,916	7,694	5.49%	5.66%	505,384	545,490
Commercial	3,601	4,517	7.13%	7.31%	202,530	247,815
Consumer	2,336	2,847	17.11%	18.93%	54,763	60,317

Auto	1,027	2,694	9.33%	11.27%	44,153	95,857
Total acquired BBVAPR loans	**13,880**	**17,752**	**6.90%**	**7.50%**	**806,830**	**949,479**
Acquired Eurobank	**3,366**	**6,037**	**14.47%**	**18.84%**	**93,332**	**128,522**
Total loans	**78,429**	**77,238**	**7.30%**	**7.50%**	**4,310,206**	**4,129,550**
Total interest-earning assets	**88,006**	**85,940**	**5.95%**	**5.89%**	**5,933,775**	**5,848,525**

	Interest		Average rate		Average balance	
	June 2018	June 2017	June 2018	June 2017	June 2018	June 2017
	(Dollars in thousands)					
Interest-bearing liabilities:						
Deposits:						
NOW Accounts	966	1,051	0.37%	0.39%	1,052,465	1,080,135
Savings and money market	1,555	1,485	0.51%	0.52%	1,230,741	1,151,650
Individual retirement accounts	299	380	0.56%	0.63%	213,750	242,009
Retail certificates of deposits	2,406	1,769	1.63%	1.24%	591,885	571,266
Total core deposits	**5,226**	**4,685**	**0.69%**	**0.63%**	**3,088,841**	**3,045,060**
Institutional deposits	76	653	0.15%	1.17%	206,695	223,788
Brokered deposits	2,134	2,084	1.82%	1.45%	470,775	575,642
Total wholesale deposits	**2,210**	**2,737**	**1.32%**	**1.39%**	**677,470**	**799,430**
	7,436	**7,422**	**0.79%**	**0.77%**	**3,766,311**	**3,844,490**
Non-interest bearing deposits	-	-	0.00%	0.00%	1,082,145	835,026
Core deposit intangible amortization	215	230	0.00%	0.00%	-	-
Total deposits	**7,651**	**7,652**	**0.63%**	**0.66%**	**4,848,456**	**4,679,516**
Borrowings:						
Securities sold under agreements to repurchase	1,840	1,734	2.09%	1.47%	353,313	472,338
Advances from FHLB and other borrowings	448	607	2.45%	2.30%	73,218	105,911
Subordinated capital notes	479	384	5.29%	4.27%	36,083	36,083
Total borrowings	**2,767**	**2,725**	**2.40%**	**1.78%**	**462,614**	**614,332**
Total interest bearing liabilities	**10,418**	**10,377**	**0.79%**	**0.79%**	**5,311,070**	**5,293,848**
Net interest income / spread	**$ 77,588**	**$ 75,563**	**5.16%**	**5.10%**		
Interest rate margin			**5.24%**	**5.18%**		
Excess of average interest-earning assets over average interest-bearing liabilities					**$ 622,705**	**$ 554,677**
Average interest-earning assets to average interest-bearing liabilities ratio					**111.72%**	**110.48%**

C - CHANGES IN NET INTEREST INCOME DUE TO:

	Volume	Rate	Total
		(In thousands)	
Interest Income:			
Investments	$ (483)	$ 1,358	$ 875
Loans	1,959	(768)	1,191
Total interest income	**1,476**	**590**	**2,066**
Interest Expense:			
Deposits	276	(277)	(1)
Repurchase agreements	(437)	546	109
Other borrowings	(228)	161	(67)
Total interest expense	**(389)**	**430**	**41**
Net Interest Income	**$ 1,865**	**$ 160**	**$ 2,025**

TABLE 1A - ANALYSIS OF NET INTEREST INCOME AND CHANGES DUE TO VOLUME/RATE FOR THE SIX-MONTH PERIODS ENDED JUNE 30, 2018 AND 2017

	Interest		Average rate		Average balance	
	June 2018	June 2017	June 2018	June 2017	June 2018	June 2017
	(Dollars in thousands)					
A - TAX EQUIVALENT SPREAD						
Interest-earning assets	**$ 171,176**	**$ 172,118**	5.91%	5.90%	**$ 5,842,933**	**$ 5,887,428**
Tax equivalent adjustment	2,380	2,577	0.08%	0.09%	-	-
Interest-earning assets - tax equivalent	**173,556**	**174,695**	5.99%	5.99%	**5,842,933**	**5,887,428**
Interest-bearing liabilities	19,594	21,937	0.76%	0.83%	5,219,637	5,346,194
Tax equivalent net interest income / spread	**153,962**	**152,758**	5.23%	5.16%	**623,296**	**541,234**
Tax equivalent interest rate margin			5.31%	5.23%		
B - NORMAL SPREAD						
Interest-earning assets:						
Investments:						
Investment securities	15,686	15,429	2.46%	2.31%	1,285,215	1,347,492
Interest bearing cash and money market investments	2,449	1,801	1.59%	0.89%	310,726	407,442
Total investments	**18,135**	**17,230**	**2.29%**	**1.98%**	**1,595,941**	**1,754,934**
Non-acquired loans						
Mortgage	17,757	18,932	5.26%	5.41%	681,265	705,167
Commercial	38,793	32,685	5.75%	5.27%	1,360,811	1,251,179
Consumer	17,265	15,722	10.91%	11.08%	318,991	286,149
Auto and leasing	44,149	38,065	9.21%	9.70%	966,251	791,008
Total non-acquired loans	**117,964**	**105,404**	7.15%	7.01%	**3,327,318**	**3,033,503**
Acquired loans:						
Acquired BBVAPR						
Mortgage	13,988	15,585	5.54%	5.69%	509,626	552,177
Commercial	7,290	9,500	7.07%	7.56%	207,975	253,286
Consumer	4,724	5,779	16.96%	19.04%	56,156	61,207
Auto	2,367	5,973	9.46%	11.27%	50,478	106,895
Total acquired BBVAPR loans	**28,369**	**36,837**	6.94%	7.63%	**824,235**	**973,566**
Acquired Eurobank	**6,708**	**12,647**	14.17%	20.33%	**95,438**	**125,425**
Total loans	**153,041**	**154,888**	**7.27%**	7.56%	**4,246,991**	**4,132,494**
Total interest-earning assets	**171,176**	**172,118**	**5.91%**	5.90%	**5,842,932**	**5,887,428**

	Interest		Average rate		Average balance	
	June 2018	June 2017	June 2018	June 2017	June 2018	June 2017
			(Dollars in thousands)			
Interest-bearing liabilities:						
Deposits:						
NOW Accounts	$ 1,864	$ 2,092	0.36%	0.39%	$ 1,055,779	$ 1,086,228
Savings and money market	3,052	2,966	0.51%	0.52%	1,218,488	1,157,811
Individual retirement accounts	635	806	0.58%	0.66%	218,996	247,785
Retail certificates of deposits	4,866	3,418	1.65%	1.24%	594,169	556,568
Total core deposits	**10,417**	**9,282**	**0.64%**	**0.65%**	**3,087,432**	**3,048,392**
Institutional deposits	82	1,294	0.08%	1.16%	205,336	223,991
Brokered deposits	4,020	3,969	1.73%	1.39%	468,718	575,098
Total wholesale deposits	**4,102**	**5,263**	**0.61%**	**0.66%**	**674,054**	**799,089**
	14,519	**14,545**	**0.78%**	**0.76%**	**3,761,486**	**3,847,481**
Non-interest bearing deposits	-	-	0.00%	-0.01%	1,050,642	$ 833,852
Core deposit intangible amortization	430	460	0.00%	0.00%	-	-
Total deposits	**14,949**	**15,005**	**0.63%**	**0.65%**	**4,812,128**	**4,681,333**
Borrowings:						
Securities sold under agreements to repurchase	2,918	4,979	1.94%	1.92%	302,728	523,272
Advances from FHLB and other borrowings	822	1,202	2.41%	2.30%	68,698	105,506
Subordinated capital notes	905	751	5.05%	4.20%	36,083	36,083
Total borrowings	**4,645**	**6,932**	**2.30%**	**2.10%**	**407,509**	**664,861**
Total interest-bearing liabilities	**19,594**	**21,937**	**0.76%**	**0.83%**	**5,219,637**	**5,346,194**
Net interest income / spread	**$ 151,582**	**$ 150,181**	**5.15%**	**5.07%**		
Interest rate margin			**5.23%**	**5.14%**		
Excess of average interest-earning assets over average interest-bearing liabilities					**$ 623,296**	**$ 541,234**
Average interest-earning assets to average interest-bearing liabilities ratio					**111.94%**	**110.12%**

C - CHANGES IN NET INTEREST INCOME DUE TO:

	Volume	Rate	Total
		(In thousands)	
Interest Income:			
Investments	$ (1,561)	$ 2,466	$ 905
Loans	2,107	(3,952)	(1,845)
Total interest income	546	(1,486)	(940)
Interest Expense:			
Deposits	419	(475)	(56)
Repurchase agreements	(2,099)	39	(2,060)
Other borrowings	(508)	281	(227)
Total interest expense	(2,188)	(155)	(2,343)
Net Interest Income	**$** 2,734	**$** (1,331)	**$** 1,403

Net Interest Income

Net interest income is a function of the difference between rates earned on Oriental's interest-earning assets and rates paid on its interest-bearing liabilities (interest rate spread) and the relative amounts of its interest earning assets and interest-bearing liabilities (interest rate margin). Oriental constantly monitors the composition and re-pricing of its assets and liabilities to maintain its net interest income at adequate levels.

Comparison for the quarters ended June 30, 2018 and 2017

Net interest income of $77.6 million increased $2.0 million from $75.6 million. Interest rate spread increased 6 basis points to 5.16% from 5.10% and net interest margin increased 6 basis points to 5.24% from 5.18%. These increases are mainly due to the net effect of an increase of 6 basis points in the average yield of total interest earning assets.

Net interest income increased as a result of:

- Higher interest income from originated loans of $7.7 million, reflecting higher balances in the commercial and auto portfolios; and

- Higher interest income from investment of $875 thousand, reflecting an increase in interest rates of $1.4 million, partially offset by a decrease in volume of $483 thousand.

Such increases in net interest income were partially offset by:

- A decrease of $6.5 million in the interest income from acquired loans as such loans continue to be repaid.

Comparison of six-month periods ended June 30, 2018 and 2017

Net interest income of $151.6 million increased $1.4 million compared with $150.2 million. Interest rate spread increased 8 basis points from 5.07% to 5.15% and net interest margin increased 9 basis points to 5.23% from 5.14%.

These increases are mainly due to the net effect of 1 basis points increase in the average yield of interest-earning assets from 5.90% to 5.91% and to 7 basis points decrease in average costs of interest-bearing liabilities from 0.83% to 0.76%

Net interest income increased as a result of:

- Higher interest income from originated loans of $12.6 million, reflecting higher balances in the commercial, auto and consumer portfolios;

- Higher interest income from investment of $905 thousand, reflecting an increase in interest rates of $2.5 million, partially offset by a decrease in volume of $1.6 million; and

- Lower interest expenses on repurchase agreements and other borrowings of $2.3 million as a result of the repayment of high cost repurchase agreements and FHLB advances.

Such increases in net interest income were partially offset by:

- A decrease of $14.4 million in the interest income from acquired loans as such loans continue to be repaid.

TABLE 2 - NON-INTEREST INCOME SUMMARY

	Quarter Ended June 30,			Six-Month Period Ended June 30,		
	2018	**2017**	**Variance**	**2018**	**2017**	**Variance**
			(Dollars in thousands)			
Banking service revenue	$ 11,144	$ 10,458	6.6%	$ 21,607	$ 21,084	2.5%
Wealth management revenue	6,262	6,516	-3.9%	12,281	12,731	-3.5%
Mortgage banking activities	988	959	3.0%	2,745	1,546	77.6%
Total banking and financial service revenue	**18,394**	**17,933**	**2.6%**	**36,633**	**35,361**	**3.6%**
FDIC shared-loss benefit	-	-	0.0%	-	1,403	-100.0%
Net gain on:						
Sale of securities available for sale	-	6,891	-100.0%	-	6,891	-100.0%
Derivatives	-	22	-100.0%	-	103	-100.0%
Early extinguishment of debt	-	(80)	100.0%	-	(80)	100.0%
Other non-interest income	309	120	157.5%	584	282	107.1%
	309	6,953	-95.6%	584	8,599	-93.2%
Total non-interest income, net	**$ 18,703**	**$ 24,886**	**-24.8%**	**$ 37,217**	**$ 43,960**	**-15.3%**

Non-Interest Income

Non-interest income is affected by the amount of the trust department 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, fees generated from loans and deposit accounts, and gains on sales of assets.

Comparison of quarters ended June 30, 2018 and 2017

Oriental recorded non-interest income, net, in the amount of $18.7 million, compared to $24.9 million, a decrease of 24.8%, or $6.2 million. The decrease in non-interest income was mainly due to:

- The sale of $166.0 million in mortgage-backed securities during the second quarter of 2017, which generated a gain of $6.9 million.

Comparison of six-month periods ended June 30, 2018 and 2017

Oriental recorded non-interest income, net, in the amount of $37.2 million, compared to $44.0 million, a decrease of 15.3%, or $6.7 million. The decrease in non-interest income was mainly due to:

- The sale of $166.0 million in mortgage-backed securities during the second quarter of 2017, which generated a gain of $6.9 million; and

- The termination of the FDIC shared-loss agreement during the first quarter of 2017 resulting in the recognition of a $1.4 million gain.

The decrease was partially offset by:

- An increase of $1.2 million in mortgage banking activities which included $1.0 million in other income from servicing assets due to higher book balances of mortgage loans, mainly attributed to the hurricane related moratorim.

TABLE 3 - NON-INTEREST EXPENSES SUMMARY

	Quarter Ended June 30,			Six-Month Period Ended June 30,		
	2018	**2017**	**Variance %**	**2018**	**2017**	**Variance %**
	(Dollars in thousands)					
Compensation and employee benefits	$ 18,099	$ 19,317	-6.3%	$ 38,707	$ 39,664	-2.4%
Professional and service fees	3,146	3,225	-2.4%	5,840	6,462	-9.6%
Occupancy and equipment	9,166	8,538	7.4%	16,934	15,735	7.6%
Insurance	1,482	1,183	25.3%	2,960	2,783	6.4%
Electronic banking charges	5,415	5,450	-0.6%	10,382	10,352	0.3%
Information technology expenses	2,000	2,069	-3.3%	4,009	4,068	-1.5%
Advertising, business promotion, and strategic initiatives	1,024	1,405	-27.1%	2,371	2,800	-15.3%
Loss on sale of foreclosed real estate and other repossessed assets	392	1,787	-78.1%	1,618	3,113	-48.0%
Loan servicing and clearing expenses	1,227	1,270	-3.4%	2,388	2,459	-2.9%
Taxes, other than payroll and income taxes	2,384	2,393	-0.4%	4,645	4,764	-2.5%
Communication	815	913	-10.7%	1,700	1,828	-7.0%
Printing, postage, stationery and supplies	605	665	-9.0%	1,249	1,303	-4.1%
Director and investor relations	337	274	23.0%	577	554	4.2%
Credit related expenses	1,897	2,217	-14.4%	4,316	4,843	-10.9%
Other operating expenses	4,311	2,110	104.3%	6,725	3,772	78.3%
Total non-interest expenses	**$ 52,300**	**$ 52,816**	**-1.0%**	**$ 104,421**	**$ 104,500**	**-0.1%**
Relevant ratios and data:						
Efficiency ratio	**54.49%**	**56.49%**		**55.48%**	**56.32%**	
Compensation and benefits to non-interest expense	**34.61%**	**36.57%**		**37.07%**	**37.96%**	
Compensation to average total assets owned	**1.11%**	**1.23%**		**1.19%**	**1.25%**	
Average number of employees	**1,354**	**1,462**		**1,354**	**1,449**	
Average compensation per employee	**$ 13.37**	**$ 13.21**		**$ 28.59**	**$ 27.37**	
Average loans per average employee	**$ 3,183**	**$ 2,825**		**$ 3,137**	**$ 2,854**	

Non-Interest Expenses

Comparison of quarters ended June 30, 2018 and 2017

Non-interest expense was $52.3 million, representing a slight decrease of 1.0% compared to $52.8 million.

The decrease in non-interest expenses was driven by:

- Lower loss on sale of foreclosed real estate and other repossessed assets by $1.4 million in the second quarter of 2018; and

- Lower compensation and employee benefits by $1.2 million, mainly due to a decrease in the average number of employees.

The decreases in the foregoing non-interest expenses were offset by:

- Higher other operating expenses by $2.2 million, mainly attributed to an increase in claims and settlements accruals and other losses, and to minor repairs to physical assets related to the impact of hurricanes.

The efficiency ratio improved to 54.49% from 56.49%. The efficiency ratio measures how much of Oriental’s revenues is used to pay operating expenses. Oriental 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, FDIC shared-loss benefit, 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 income that are excluded from efficiency ratio computation for the quarters ended June 30, 2018 and 2017 amounted to $309 thousand and $7.0 million, respectively.

Oriental implemented its disaster response plan as hurricanes Irma and Maria approached its service areas. To operate in disaster response mode, Oriental incurred expenses for, among other things, buying diesel and generators for electric power, debris removal, security services, property damages, and emergency communication with customers regarding the status of Bank operations. Estimated losses at December 31, 2017 amounted to $6.6 million. No additional losses have been incurred at June 30, 2018.

Oriental maintains insurance for casualty losses as well as for disaster response costs and certain revenue lost through business interruption. Management believes that recovery of $2.2 million incurred costs as of December 31, 2017 is probable. Oriental received a $1.0 million partial payment from the insurance company in December 2017 and a $0.7 million payment during the six-month period ended June 30, 2018. Accordingly, a receivable of $0.5 million and $1.2 million was included in other assets at June 30, 2018 and December 31, 2017, respectively, for the expected recovery.

Comparison of six-month periods ended June 30, 2018 and 2017

Non-interest expense was $104.4 million, representing a slight decrease of 0.1% compared to $104.5 million.

The decrease in non-interest expenses for the six-month period ended June 30, 2018 was driven by:

- Lower loss on sale of foreclosed real estate and other repossessed assets by $1.5 million, particularly attributed to an increase in gain on sales of $762 thousand and other repossessed assets markdowns of $1.1 million;

- Lower compensation and employee benefits by $1.0 million, mainly due to a decrease in the average number of employees;

- Lower professional and services fees by $622 thousand, mainly due to a decrease in consulting and advisory expenses of $777 thousand;

- Lower credit related expenses by $527 thousand related to a decrease in foreclosure legal fees of $281 thousand; and

- Lower marketing expenses by $429 thousand.

The decreases in the foregoing non-interest expenses were offset by:

- Higher other operating expenses by $3.0 million, mainly attributed to an increase in claims and settlements accruals and other losses, and to minor repairs to physical assets related to the impact of hurricanes.

- Higher occupancy and equipment expenses by $1.2 million, particularly attributed to a lease cancellation fee of $1.5 million to bring more of our offices into the Oriental Center building.

The efficiency ratio improved to 55.48% from 56.32% for the same period in 2017. Amounts presented as part of non-interest income that are excluded from efficiency ratio computation for the six-month periods ended June 30, 2018 and 2017 amounted to $584 thousand and $8.6 million, respectively.

Provision for Loan and Lease Losses

Comparison of quarters ended June 30, 2018 and 2017

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

Provision for loan and lease losses decreased 44.4%, or $11.8 million, to $14.7 million. The decrease in the provision was mostly due to:

- A $4.3 million provision in the second quarter of 2017 to charge-off the loss on sale of a loan to a Puerto Rico government municipality and a $5.9 million provision to increase the general allowance on the remaining municipal loan portfolio; and

- Most of the incremental commercial, consumer and auto charge-offs during the quarter ended June 30, 2018 were previously reserved.

Comparison of six-month periods ended June 30, 2018 and 2017

Provision for loan and lease losses decreased 31.6%, or $14.0 million, to $30.2 million. The decrease in the provision was mostly due to:

- The additional provisions placed during the second quarter of 2017 described above; and

- Most of the incremental commercial, consumer and auto charge-offs during the quarter ended June 30, 2018 were previously reserved.

Please refer to the "Allowance for Loan and Lease Losses" in the "Credit Risk Management" section of this MD&A for a more detailed analysis of the allowance for loan and lease losses.

Income Taxes

Comparison of quarters ended June 30, 2018 and 2017

Income tax expense was $9.6 million, compared to $4.0 million, reflecting the effective income tax rate of 32.6% and the net income before income taxes of $29.2 million for 2018.

Comparison of six-month periods ended June 30, 2018 and 2017

Income tax expense was $17.6 million, compared to $13.2 million, reflecting the effective income tax rate of 32.4% and the net income before income taxes of $54.2 million for 2018.

Business Segments

Oriental 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 Oriental's organization, nature of its products, distribution channels and economic characteristics of the products were also considered in the determination of the reportable segments. Oriental 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. Oriental'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, 2018 and 2017.

	Quarter Ended June 30, 2018					
	Banking	Wealth Management	Treasury	Total Major Segments	Eliminations	Consolidated Total
	(In thousands)					
Interest income	$ 78,133	$ 14	$ 9,859	$ 88,006	$ -	$ **88,006**
Interest expense	(7,132)	-	(3,286)	(10,418)	-	**(10,418)**
Net interest income	71,001	14	6,573	77,588	-	**77,588**
Provision for loan and lease losses	(14,744)	-	(3)	(14,747)	-	**(14,747)**
Non-interest income	12,240	6,448	15	18,703	-	**18,703**
Non-interest expenses	(46,109)	(5,282)	(909)	(52,300)	-	**(52,300)**
Intersegment revenue	542	-	-	542	(542)	**-**
Intersegment expenses	-	(208)	(334)	(542)	542	**-**
Income before income taxes	$ 22,930	$ 972	$ 5,342	$ 29,244	$ -	$ **29,244**
Income tax expense	8,943	379	273	9,595	-	**9,595**
Net income	**$ 13,987**	**$ 593**	**$ 5,069**	**$ 19,649**	**$ -**	**$ 19,649**
Total assets	**$ 6,006,889**	**$ 29,253**	**$ 1,447,949**	**$ 7,484,091**	**$ (982,529)**	**$ 6,501,562**

	Quarter Ended June 30, 2017					
	Banking	Wealth Management	Treasury	Total Major Segments	Eliminations	Consolidated Total
	(In thousands)					
Interest income	$ 77,019	$ 18	$ 8,903	$ 85,940	$ -	$ **85,940**
Interest expense	(6,820)	-	(3,557)	(10,377)	-	**(10,377)**
Net interest income	70,199	18	5,346	75,563	-	**75,563**
Provision for loan and lease losses	(26,526)	-	(10)	(26,536)	-	**(26,536)**
Non-interest income	11,776	6,329	6,781	24,886	-	**24,886**
Non-interest expenses	(47,402)	(4,100)	(1,314)	(52,816)	-	**(52,816)**
Intersegment revenue	346	-	71	417	(417)	**-**
Intersegment expenses	(71)	(254)	(92)	(417)	417	**-**
Income before income taxes	$ 8,322	$ 1,993	10,782	$ 21,097	$ -	$ **21,097**
Income tax expense (benefit)	3,246	777	(30)	3,993	-	**3,993**

Net income	**$ 5,076**	**$ 1,216**	**$ 10,812**	**$ 17,104**	**$ -**	**$ 17,104**
Total assets	**$ 5,490,287**	**$ 22,531**	**$ 1,692,603**	**$ 7,205,421**	**$ (969,595)**	**$ 6,235,826**

	Six-Month Period Ended June 30, 2018					
	Banking	Wealth Management	Treasury	Total Major Segments	Eliminations	Consolidated Total
	(In thousands)					
Interest income	$ 152,507	$ 26	$ 18,643	$ 171,176	$ -	$ **171,176**
Interest expense	(13,422)	-	(6,172)	(19,594)	-	**(19,594)**
Net interest income	139,085	26	12,471	151,582	-	**151,582**
Provision for loan and lease losses	(30,199)	-	(8)	(30,207)	-	**(30,207)**
Non-interest income	24,433	12,756	28	37,217	-	**37,217**
Non-interest expenses	(94,190)	(8,568)	(1,663)	(104,421)	-	**(104,421)**
Intersegment revenue	903	-	-	903	(903)	**-**
Intersegment expenses	-	(387)	(516)	(903)	903	**-**
Income before income taxes	$ 40,032	$ 3,827	$ 10,312	$ 54,171	$ -	$ **54,171**
Income tax expense	15,612	1,493	500	17,605	-	**17,605**
Net income	**$ 24,420**	**$ 2,334**	**$ 9,812**	**$ 36,566**	**$ -**	**$ 36,566**
Total assets	**$ 6,006,889**	**$ 29,253**	**$ 1,447,949**	**$ 7,484,091**	**$ (982,529)**	**$ 6,501,562**

	Six-Month Period Ended June 30, 2017					
	Banking	Wealth Management	Treasury	Total Major Segments	Eliminations	Consolidated Total
	(In thousands)					
Interest income	$ 154,592	$ 30	$ 17,496	$ 172,118	$ -	$ **172,118**
Interest expense	(13,634)	-	(8,303)	(21,937)	-	**(21,937)**
Net interest income	140,958	30	9,193	150,181	-	**150,181**
Provision for loan and lease losses	(44,168)	-	(22)	(44,190)	-	**(44,190)**
Non-interest income	25,003	12,257	6,700	43,960	-	**43,960**
Non-interest expenses	(93,456)	(8,320)	(2,724)	(104,500)	-	**(104,500)**
Intersegment revenue	810	-	142	952	(952)	**-**
Intersegment expenses	(142)	(565)	(245)	(952)	952	**-**
Income before income taxes	$ 29,005	$ 3,402	$ 13,044	$ 45,451	$ -	$ **45,451**
Income tax expense	11,312	1,327	558	13,197	-	**13,197**

Net income	**$**	**17,693**	**$**	**2,075**	**$**	**12,486**	**$**	**32,254**	**$**	**-**	**$**	**32,254**
Total assets	**$**	**5,490,287**	**$**	**22,531**	**$**	**1,692,603**	**$**	**7,205,421**	**$**	**(969,595)**	**$**	**6,235,826**

Comparison of quarters ended June 30, 2018 and 2017

Banking

Oriental's banking segment net income before taxes increased $14.6 million to $22.9 million, reflecting that:

- The provision for loan and lease losses in the second quarter of 2017 included $4.3 million to charge-off the loss on sale of a loan to a Puerto Rico government municipality and a $5.9 million provision for loan and lease losses to increase the general allowance on the municipal loan portfolio, and most of the incremental commercial, consumer and auto charge-offs during the quarter ended June 30, 2018 were previously reserved;

- Higher interest income by $1.1 million, reflecting more interest income from originated loans due to higher balances in the commercial and auto portfolios; and

- Lower non-interest expenses by $1.3 million, mainly from lower losses on sale of foreclosed real estate and other repossessed assets by $1.4 million.

Wealth Management

Wealth management segment revenue, which consists of commissions and fees from fiduciary activities, and securities brokerage and insurance activities, decreased $1.0 million to $972 thousand due to higher expenses by $1.2 million, mainly related to an increase in claims and settlements accruals.

Treasury

Treasury segment net income before taxes, which consists of Oriental's asset/liability management activities, such as purchase and sale of investment securities, interest rate risk management, derivatives, and borrowings, decreased to $5.3 million, compared to $10.8 million, reflecting the sale of $166.0 million in mortgage-backed securities during the second quarter of 2017, which generated a gain of $6.9 million.

Comparison of six-month periods ended June 30, 2018 and 2017

Banking

Oriental's banking segment net income before taxes increased $11.0 million to $40.0 million, reflecting:

- The lower provision for loan and lease losses by $14.0 million to $30.2 million related to the additional provisions placed during the second quarter of 2017;

Such decrease in the provision was partially offset by:

- Lower interest income by $2.1 million reflecting a decrease in the interest income from acquired loans as such loans continue to be repaid.

Wealth Management

Wealth management revenue, which consists of commissions and fees from fiduciary activities, and securities brokerage and insurance activities, increased $425 thousand to $3.8 million, mainly from changes in volume and market rates.

Treasury

Treasury segment net income before taxes decreased to $10.3 million, compared to $13.0 million, reflecting:

- The sale of $166.0 million in mortgage-backed securities during the second quarter of 2017, which generated a gain of $6.9 million.

Such decrease was partially offset by:

- Higher interest income from investment of $1.1 million, reflecting an increase in interest rates; and

- Lower interest expenses on repurchase agreements and other borrowings of $2.1 million as a result of the repayment of high cost repurchase agreements and FHLB advances.

ANALYSIS OF FINANCIAL CONDITION

Assets Owned

At June 30, 2018, Oriental’s total assets amounted to $6.502 billion representing an increase of 5.05% when compared to $6.189 billion at December 31, 2017. This increase is attributable to an increase in the loans portfolio and investments portfolios of $259.5 million and $187.1 million, respectively, partially offset by a decrease in cash and cash equivalents of $109.9 million.

Oriental’s loan portfolio is comprised of residential mortgage loans, commercial loans collateralized by mortgages on real estate, other commercial and industrial loans, consumer loans, and auto loans. At June 30, 2018, Oriental’s loan portfolio increased 6.4%. Loan production during the six-month period ended June 30, 2018, reached $741.5 million compared to $473.3 million in the year ago period, a 56.7% increase. The non-acquired loan portfolio increased $334.7 million from December 31, 2017 to $3.540 billion at June 30, 2018. The BBVAPR acquired loan portfolio decreased $64.7 million from December 31, 2017 to $761.2 million at June 30, 2018. The Eurobank acquired loan portfolio decreased $7.3 million from December 31, 2017 to $92.0 million at June 30, 2018.

Oriental's investment portfolio increased 16.0% to $1.353 billion at June 30, 2018, mainly attributed to the purchase of $260.0 million mortgage-backed securities available-for-sale and retained securitized GNMA pools totaling $37.6 million, partially offset by paydowns in the investment available-for-sale portfolio of $54.4 million and in the investment securities held-to-maturity portfolio of $38.6 million during the six-month period ended June 30, 2018.

Cash and cash equivalents decreased 22.6% to $375.3 million, mainly attributed to the funding of new loan growth and purchases of investments, partially offset by repurchase agreements and Federal Home Loan Bank advances.

Accrued interest receivable resulting from the loan payment moratorium has been decreasing from December 31, 2017, as most moratoriums have expired. Some of these accrued interests are payable at the end of the loan term.

Financial Assets Managed

Oriental’s financial assets include those managed by Oriental’s trust division, retirement plan administration subsidiary, and assets gathered by its broker-dealer and insurance subsidiaries. Oriental’s trust division offers various types of individual retirement accounts ("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, 2018, total assets managed by Oriental’s trust division and OPC amounted to $2.953 billion, compared to $3.040 billion at December 31, 2017. 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, 2018, total assets gathered by Oriental Financial Services and Oriental Insurance from its customer investment accounts amounted to $2.262 billion, compared to $2.250 billion at December 31, 2017. Changes in trust and broker-dealer related assets primarily reflect changes in portfolio balances and differences in market values.

Goodwill

Goodwill recorded in connection with the BBVAPR Acquisition and the FDIC-assisted Eurobank acquisition is not amortized to expense but is tested at least annually for impairment. A quantitative annual impairment test is not required if, based on a qualitative analysis, Oriental determines that the existence of events and circumstances indicate that it is more likely than not that goodwill is not impaired. Oriental completes its annual goodwill impairment test as of October 31 of each year. Oriental tests for impairment by first allocating its goodwill and other assets and liabilities, as necessary, to defined reporting units. A fair value is then determined for each reporting unit. If the fair values of the reporting units exceed their book values, no write-down of the recorded goodwill is necessary. If the fair values are less than the book values, an additional valuation procedure is necessary to assess the proper carrying value of the goodwill.

Reporting unit valuation is inherently subjective, with a number of factors based on assumptions and management judgments or estimates. Actual values may differ significantly from such estimates. Among these are future growth rates for the reporting units, selection of comparable market transactions, discount rates and earnings capitalization rates. Changes in assumptions and results due to economic conditions, industry factors, and reporting unit performance and cash flow projections could result in different assessments of the fair values of reporting units and could result in impairment charges. If an event occurs or circumstances change that would more likely than not reduce the fair value of a reporting unit below its carrying amount, an interim impairment test is required.

Relevant events and circumstances for evaluating whether it is more likely than not that the fair value of a reporting unit is less than its carrying amount may include macroeconomic conditions (such as a further deterioration of the Puerto Rico economy or the liquidity for Puerto Rico securities or loans secured by assets in Puerto Rico), adverse changes in legal factors or in the business climate, adverse actions by a regulator, unanticipated competition, the loss of key employees, or similar events. Oriental's loan portfolio, which is the largest component of its interest-earning assets, is concentrated in Puerto Rico and is directly affected by adverse local economic and fiscal conditions. Such conditions have generally affected the market demand for non-conforming loans secured by assets in Puerto Rico and, therefore, affect the valuation of Oriental's assets.

As of June 30, 2018, Oriental had $86.1 million of goodwill allocated as follows: $84.1 million to the Banking unit and $2.0 million to the Wealth Management unit. During the last quarter of 2017, based on its annual goodwill impairment test, Oriental determined that the Banking unit failed step one of the two-step impairment test and that the Wealth Management unit passed such step. As a result of step one, the Banking unit's adjusted net book value exceeded its fair value by approximately $236.4 million, or 26%. Accordingly, Oriental proceeded to perform step two of the analysis. Based on the results of step two, Oriental determined that the carrying value of the goodwill allocated to the Banking unit was not impaired as of the valuation date. During the six-month period ended June 30, 2018, Oriental performed an assessment of events or circumstances that could trigger reductions in the book value of the goodwill. Based on this assessment, no events were identified that triggered changes in the book value of goodwill at June 30, 2018.

FDIC Indemnification Asset

On February 6, 2017, the Bank and the FDIC agreed to terminate the single family and commercial shared-loss agreements related to the FDIC assisted acquisition of Eurobank on April 30, 2010. As part of the loss share termination transaction, the Bank made a payment of $10.1 million to the FDIC and recorded a net benefit of $1.4 million. Such termination payment took into account the anticipated reimbursements over the life of the shared-loss agreements and the true-up payment liability of the Bank anticipated at the end of the ten-year term of the single family shared-loss agreement. All rights and obligations of the parties under the shared-loss agreements terminated as of the closing date of the agreement.

TABLE 4 - ASSETS SUMMARY AND COMPOSITION

	June 30 2018	December 31 2017	Variance %
	(Dollars in thousands)		
Investments:			
FNMA and FHLMC certificates	$ 1,055,100	$ 887,779	18.8%
Obligations of US government-sponsored agencies	2,541	2,879	-11.7%
US Treasury securities	10,450	10,163	2.8%
CMOs issued by US government-sponsored agencies	71,154	80,071	-11.1%
GNMA certificates	194,858	167,338	16.4%
Puerto Rico government and public instrumentalities	2,455	2,093	17.3%
FHLB stock	14,919	13,995	6.6%
Other debt securities	1,210	1,538	-21.3%
Other investments	421	194	117.0%
Total investments	**1,353,108**	**1,166,050**	**16.0%**
Loans	**4,315,866**	**4,056,329**	**6.4%**
Total investments and loans	**5,668,974**	**5,222,379**	**8.6%**
Other assets:			
Cash and due from banks (including restricted cash)	371,374	481,212	-22.8%
Money market investments	6,991	7,021	-0.4%
Foreclosed real estate	40,551	44,174	-8.2%
Accrued interest receivable	34,476	49,969	-31.0%
Deferred tax asset, net	125,141	127,421	-1.8%
Premises and equipment, net	66,174	67,860	-2.5%
Servicing assets	10,829	9,821	10.3%
Derivative assets	1,100	771	42.7%
Goodwill	86,069	86,069	0.0%
Other assets and customers' liability on acceptances	89,883	92,356	-2.7%
Total other assets	**832,588**	**966,674**	**-13.9%**
Total assets	**$ 6,501,562**	**$ 6,189,053**	**5.0%**
Investment portfolio composition:			
FNMA and FHLMC certificates	77.9%	76.1%	
Obligations of US government-sponsored agencies	0.2%	0.2%	
US Treasury securities	0.8%	0.9%	
CMOs issued by US government-sponsored agencies	5.3%	6.9%	
GNMA certificates	14.4%	14.4%	
Puerto Rico government and public instrumentalities	0.2%	0.2%	
FHLB stock	1.1%	1.2%	
Other debt securities and other investments	0.1%	0.1%	
	100.0%	**100.0%**	

TABLE 5 — LOANS RECEIVABLE COMPOSITION

	June 30 2018	December 31 2017	Variance %
	(In thousands)		
Originated and other loans and leases held for investment:			
Mortgage	$ 678,259	$ 683,607	-0.8%
Commercial	1,507,368	1,307,261	15.3%
Consumer	339,341	330,039	2.8%
Auto and leasing	1,014,664	883,985	14.8%
	3,539,632	**3,204,892**	**10.4%**
Allowance for loan and lease losses on originated and other loans and leases	(94,218)	(92,718)	1.6%
	3,445,414	**3,112,174**	**10.7%**
Deferred loan costs, net	7,028	6,695	5.0%
Total originated and other loans held for investment, net	**3,452,442**	**3,118,869**	**10.7%**
Acquired loans:			
Acquired BBVAPR loans:			
Accounted for under ASC 310-20 (Loans with revolving feature and/or acquired at a premium)			
Commercial	2,909	4,380	-33.6%
Consumer	25,736	28,915	-11.0%
Auto	11,283	21,969	-48.6%
	39,928	**55,264**	**-27.8%**
Allowance for loan and lease losses on acquired BBVAPR loans accounted for under ASC 310-20	(2,726)	(3,862)	-29.4%
	37,202	**51,402**	**-27.6%**
Accounted for under ASC 310-30 (Loans acquired with deteriorated credit quality, including those by analogy)			
Mortgage	516,934	532,053	-2.8%
Commercial	223,853	243,092	-7.9%
Consumer	495	1,431	-65.4%
Auto	26,937	43,696	-38.4%
	768,219	**820,272**	**-6.3%**
Allowance for loan and lease losses on acquired BBVAPR loans accounted for under ASC 310-30	(44,176)	(45,755)	-3.5%
	724,043	**774,517**	**-6.5%**
Total acquired BBVAPR loans, net	**761,245**	**825,919**	**-7.8%**
Acquired Eurobank loans:			
Loans secured by 1-4 family residential properties	65,637	69,538	-5.6%
Commercial	49,706	53,793	-7.6%
Consumer	935	1,112	-15.9%

	116,278	**124,443**	**-6.6%**
Allowance for loan and lease losses on Eurobank loans	(24,314)	(25,174)	-3.4%
Total acquired Eurobank loans, net	**91,964**	**99,269**	**-7.4%**
Total acquired loans, net	**853,209**	**925,188**	**-7.8%**
Total held for investment, net	**4,305,651**	**4,044,057**	**6.5%**
Mortgage loans held for sale	**10,215**	**12,272**	**-16.8%**
Total loans, net	**$ 4,315,866**	**$ 4,056,329**	**6.4%**

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Oriental’s loan portfolio is composed of two segments, loans initially accounted for under the amortized cost method (referred to as "originated and other" loans) and loans acquired (referred to as "acquired" loans). Acquired loans are further segregated between acquired BBVAPR loans and acquired Eurobank loans. Acquired Eurobank loans were purchased subject to loss-sharing agreements with the FDIC, which were terminated on February 6, 2017.

As shown in Table 5 above, total loans, net, amounted to $4.316 billion at June 30, 2018 and $4.056 billion at December 31, 2017. Oriental’s originated and other loans held-for-investment portfolio composition and trends were as follows:

- Mortgage loan portfolio amounted to $678.3 million (19.2% of the gross originated loan portfolio) compared to $683.6 million (21.3% of the gross originated loan portfolio) at December 31, 2017. Mortgage loan production totaled $31.8 million and $58.5 million, for the quarter and six-month period ended June 30, 2018, which represents a decrease of 30.7% and 34.6% from $45.9 million and $89.4 million, respectively, for the same periods in 2017. Mortgage loans included delinquent loans in the GNMA buy-back option program amounting to $14.5 million and $8.3 million at June 30, 2018 and December 31, 2017, 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.

- Commercial loan portfolio amounted to $1.507 billion (42.6% of the gross originated loan portfolio) compared to $1.307 billion (40.8% of the gross originated loan portfolio) at December 31, 2017. Commercial loan production, including the U.S. loan program production of $99.7 million and $174.0 million, respectively, increased 182.3% and 171.3% to $226.9 million and $344.0 million, respectively, for the quarter and six-month period ended June 30, 2018, from $80.4 million and $126.8 million for the same periods in 2017.

- Consumer loan portfolio amounted to $339.3 million (9.6% of the gross originated loan portfolio) compared to $330.0 million (10.3% of the gross originated loan portfolio) at December 31, 2017. Consumer loan production decreased 14.8% and 13.1% to $42.3 million and $79.8 million, respectively, for the quarter and six-month period ended June 30, 2018 from $49.7 million and $91.8 million, respectively, for the same periods in 2017.

- Auto and leasing portfolio amounted to $1.015 billion (28.6% of the gross originated loan portfolio) compared to $884.0 million (27.6% of the gross originated loan portfolio) at December 31, 2017. Auto production increased by 66.8% and 56.8%, respectively, to $131.1 million and $259.2 million, respectively, for the quarter and six-month period ended June 30, 2018 compared to $78.6 million and $165.4 million, respectively, for the same periods in 2017.

TABLE 6 — HIGHER RISK RESIDENTIAL MORTGAGE LOANS

	June 30, 2018 Higher-Risk Residential Mortgage Loans*								
	Junior Lien Mortgages			Interest Only Loans			High Loan-to-Value Ratio Mortgages LTV 90% and over		
	Carrying Value	Allowance	Coverage	Carrying Value	Allowance	Coverage	Carrying Value	Allowance	Coverage
	(In thousands)								
Delinquency:									
0 - 89 days	$ 9,116	$ 276	3.03%	$ 8,110	$ 404	4.98%	$ 65,447	$ 1,393	2.13%
90 - 119 days	252	19	7.54%	433	23	5.31%	1,328	44	3.31%
120 - 179 days	81	2	2.47%	130	22	16.92%	1,550	140	9.03%
180 - 364 days	55	7	12.73%	314	53	16.88%	1,559	77	4.94%
365+ days	249	34	13.65%	1,279	221	17.28%	8,068	556	6.89%
Total	$ 9,753	$ 338	3.47%	$ 10,266	$ 723	7.04%	$ 77,952	$ 2,210	2.84%
Percentage of total loans excluding acquired loans accounted for under ASC 310-30	0.27%			0.29%			2.18%		
Refinanced or Modified Loans:									
Amount	$ 1,897	$ 225	11.86%	$ 523	$ 62	11.85%	$ 17,397	$ 1,350	7.76%
Percentage of Higher-Risk Loan Category	19.45%			5.09%			22.32%		
Loan-to-Value Ratio:									
Under 70%	$ 6,488	$ 235	3.62%	$ 828	$ 37	4.47%	$ -	$ -	-
70% - 79%	1,495	84	5.62%	2,588	119	4.60%	-	-	-
80% - 89%	1,051	6	0.57%	2,835	212	7.48%	-	-	-
90% and over	719	13	1.81%	4,015	355	8.84%	77,952	2,210	2.84%
	$ 9,753	$ 338	3.47%	$ 10,266	$ 723	7.04%	$ 77,952	$ 2,210	2.84%

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

Deposits from the Puerto Rico government totaled $156.9 million at June 30, 2018. The following table includes the maturities Oriental's lending and investment exposure to the Puerto Rico government, which is limited solely to loans to 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.

TABLE 7 - PUERTO RICO GOVERNMENT RELATED LOANS AND SECURITIES

	June 30, 2018			
			Maturity	
Loans and Securities:	**Carrying Value**	**Less than 1 Year**	**1 to 3 Years**	**More than 3 Years**
		(In thousands)		
Municipalities	**$ 145,637**	**$ 5,273**	**$ 95,641**	**$ 44,723**

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Credit Risk Management

Allowance for Loan and Lease Losses

Oriental 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. Oriental’s allowance for loan and lease losses ("ALLL") 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 Oriental’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 discussed in Note 2, during 2017, hurricanes Irma and Maria caused catastrophic damages throughout Puerto Rico. Management performed an evaluation of the loan portfolios in order to assess the impact on repayment sources and underlying collateral that could result in additional losses.

At June 30, 2018, Oriental’s allowance for loan and lease losses amounted to $165.4 million, a $2.1 million decrease from $167.5 million at December 31, 2017.

For the commercial portfolio, the framework for the analysis was based on our current ALLL methodology with additional considerations according to the estimated impact categorized as low, medium or high. From this impact assessment, additional reserve levels were estimated by increasing default probabilities (“PD”) and loss given default expectations (“LGD”) of each allowance segment.

As part of the process, Oriental contacted its clients to evaluate the impact of the hurricanes on their business operations and collateral. The impact was then categorized as follows: (i) low risk, for clients that had no business impact or relatively insignificant impact; (ii) medium risk, for clients that had a business impact on their primary or secondary sources of repayment, but had adequate cash flow to cover operations and to satisfy their obligations; or (iii) high risk, for clients that had potentially significant problems that affected primary, secondary and tertiary (collateral) sources of repayment. This criterion was used to model adjusted PDs and LGDs considering internal and external sources of information available to support our estimation process and output.

During the fourth quarter of 2017, Oriental performed an update of the initial estimate, taking into consideration the most recent available information gathered through additional visits and interviews with clients and the economic environment in Puerto Rico.

For the retail portfolios, mortgage, consumer and auto, the assumptions established in the initial estimate were based on the historical losses of each ALLL segment and then further adjusted based on parameters used as key risk indicators, such as the industry of employment for all portfolios and the location of the collateral for mortgage loans. During the fourth quarter of 2017, Oriental performed additional procedures to evaluate the reasonability of the initial estimate based on the payment experience percentage of borrowers for which the deferral period expired. The analysis took into consideration historical payment behavior and loss experience of borrowers (PDs and LGDs) of each portfolio segment to develop a range of estimated potential losses. Management understands that this approach is reasonable given the lack of historical information related to the behavior of local borrowers in such an unprecedented event. The amount used in the analysis represents the average of potential outcomes of expected losses.

During the first quarter of 2018, Oriental updated the previously performed analysis to estimate probable losses related to the hurricanes. Analyses were based on the payment experience percentage of borrowers for which the deferral period expired in retail portfolios. For the commercial portfolio, no changes in the level of impact assessed were identified based on communications with credit officers. During the second quarter of 2018, Oriental continued its monitoring process of the performance of those affected borrowers. As additional information became available, it was incorporated into the allowance framework.

At June 30, 2018 and December 31, 2017, Oriental's allowance for loan and lease losses incorporated all risks associated to our loan portfolio, including the impact of hurricanes Irma and Maria.

Tables 8 through 10 set forth an analysis of activity in the ALLL and present selected loan loss statistics. In addition, Table 5 sets forth the composition of the loan portfolio.

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

Oriental’s non-performing assets include non-performing loans and foreclosed real estate (see Tables 11 and 12). At June 30, 2018 and December 31, 2017, Oriental had $122.1 million and $99.7 million, respectively, of non-accrual loans, including acquired BBVAPR loans accounted for under ASC 310-20 (loans with revolving feature and/or acquired at a premium).

At June 30, 2018 and December 31, 2017, loans whose terms have been extended and which are classified as troubled-debt restructuring that are not included in non-performing assets amounted to $100.5 million and $109.2 million, respectively.

At June 30, 2018 and December 31, 2017, loans that are current in their monthly payments, but placed in non-accrual amounted to $21.8 million and $20.1 million, respectively. During the six-month period ended June 30, 2018, a $10.4 million loan that is current in its monthly payments was placed in non-accrual due to credit deterioration after the hurricanes.

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 12 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.

Acquired loans 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 these loans when it is probable that all cash flows expected at acquisition will not be collected.

Following hurricanes Irma and Maria, Oriental offered automatic payment deferrals and 90-day extensions for most loan categories. Most of these payment moratoriums ended during the six-month period ended June 30, 2018 with most credit metrics better than, or returned to, pre-hurricanes levels.

At June 30, 2018, Oriental’s non-performing assets increased by 12.5% to $176.2 million (2.82% of total assets, excluding acquired loans with deteriorated credit quality) from $156.7 million (2.95% of total assets, excluding acquired loans with deteriorated credit quality) at December 31, 2017. Foreclosed real estate and other repossessed assets amounting to $40.6 million and $5.5 million, respectively at June 30, 2018. and $44.2 million and $3.5 million, respectively, at December 31, 2017, were recorded at fair value. Oriental does not expect non-performing loans to result in significantly higher losses. At June 30, 2018, the allowance for originated loan and lease losses to non-performing loans coverage ratio was 73.37% (87.35% at December 31, 2017).

Oriental 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, Oriental 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:

Residential 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 12 months or more past due. At June 30, 2018, Oriental's originated non-performing mortgage loans totaled $67.0 million (51.3% of Oriental's non-performing loans), a 4.6% increase from $64.1 million (58.7% of Oriental's non-performing loans) at December 31, 2017.

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, 2018, Oriental's originated non-performing commercial loans amounted to $47.5 million (36.5% of Oriental's non-performing loans), a 34.6% increase from $35.3 million at December 31, 2017 (32.4% of Oriental's non-performing loans). This increase is mainly from a $10.4 million loan that is current in its monthly payments but was placed in non-accrual during the six-month period ended June 30, 2018 due to credit deterioration after the hurricanes.

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, 2018, Oriental's originated non-performing consumer loans amounted to $2.8 million (2.2% of Oriental's non-performing loans), a 9.9% increase from $2.6 million at December 31, 2017 (2.4% of Oriental's non-performing loans).

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, 2018, Oriental's originated non-performing auto loans and leases amounted to $11.1 million (8.6% of Oriental's total non-performing loans), an increase of 163.3% from $4.2 million at December 31, 2017 (3.9% of Oriental's total non-performing loans).

Oriental 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 Oriental'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, RURAL, PRHFA, conventional loans guaranteed by Mortgage Guaranty Insurance Corporation (MGIC), conventional loans sold to FNMA and FHLMC, and conventional loans retained by Oriental. 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/interest 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 pursuant Oriental's current credit and underwriting guidelines. Oriental 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.

In order to apply for any of the loan modification programs, if the borrower is active in Chapter 13 bankruptcy, it must request an authorization from the bankruptcy trustee to allow for the loan modification. Borrowers with discharged Chapter 7 bankruptcies may also apply. Loans in these programs are evaluated by designated underwriters for troubled-debt restructuring classification if Oriental grants a concession for legal or economic reasons due to the debtor's financial difficulties.

TABLE 8 — ALLOWANCE FOR LOAN AND LEASE LOSSES BREAKDOWN

	June 30, 2018	December 31, 2017	Variance %
	(Dollars in thousands)		
Originated and other loans held for investment			
Allowance balance:			
Mortgage	$ 19,323	$ 20,439	-5.5%
Commercial	31,480	30,258	4.0%
Consumer	16,192	16,454	-1.6%
Auto and leasing	27,223	25,567	6.5%
Total allowance balance	**$ 94,218**	**$ 92,718**	**1.6%**
Allowance composition:			
Mortgage	20.5%		