

FIRST COMMONWEALTH FINANCIAL CORP /PA/  
Form 10-Q  
November 08, 2018  
UNITED STATES  
SECURITIES AND EXCHANGE COMMISSION  
Washington, D.C. 20549  
FORM 10-Q

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

For the quarterly period ended September 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 001-11138

First Commonwealth Financial Corporation

(Exact name of registrant as specified in its charter)

Pennsylvania

25-1428528

(State or other jurisdiction of

(I.R.S. Employer

incorporation or organization)

Identification No.)

601 Philadelphia Street, Indiana, PA 15701

(Address of principal executive offices) (Zip Code)

724-349-7220

(Registrant's telephone number, including area code)

N/A

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

Indicate by a check mark whether the registrant (1) has filed all reports required to be filed by Section 13 or 15(d) of the Securities Exchange Act of 1934 during the preceding 12 months (or for such shorter period that the registrant was required to file such reports), and (2) has been subject to such filing requirements for the past 90 days. Yes  No

Indicate by check mark whether the registrant has submitted electronically and posted on its corporate Web site, if any, every Interactive Data File required to be submitted and posted pursuant to Rule 405 of Regulation S-T (§232.405 of this chapter) during the preceding 12 months (or for such shorter period that the registrant was required to submit and post such files). Yes  No

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

Large accelerated filer  Accelerated filer  Smaller reporting company  Emerging growth company

Non-accelerated filer  (Do not check if a smaller reporting 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

The number of shares outstanding of issuer's common stock, \$1.00 par value, as of November 7, 2018, was 99,423,275.

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## ITEM 1. Financial Statements and Supplementary Data

## FIRST COMMONWEALTH FINANCIAL CORPORATION AND SUBSIDIARIES

## CONDENSED CONSOLIDATED STATEMENTS OF FINANCIAL CONDITION (Unaudited)

	September 30, 2018	December 31, 2017
	(dollars in thousands, except share data)	
<b>Assets</b>		
Cash and due from banks	\$93,162	\$ 98,624
Interest-bearing bank deposits	3,022	8,668
Securities available for sale, at fair value	889,056	731,358
Securities held to maturity, at amortized cost (Fair value of \$373,933 and \$418,249 at September 30, 2018 and December 31, 2017, respectively)	389,621	422,096
Other investments	25,029	29,837
Loans held for sale	8,287	14,850
Loans:		
Portfolio loans	5,662,782	5,407,376
Allowance for credit losses	(50,746 )	(48,298 )
Net loans	5,612,036	5,359,078
Premises and equipment, net	80,426	81,339
Other real estate owned	3,874	2,765
Goodwill	274,202	255,353
Amortizing intangibles, net	13,826	15,007
Bank owned life insurance	214,322	212,099
Other assets	79,482	77,465
<b>Total assets</b>	<b>\$7,686,345</b>	<b>\$ 7,308,539</b>
<b>Liabilities</b>		
Deposits (all domestic):		
Noninterest-bearing	\$1,451,284	\$ 1,416,771
Interest-bearing	4,443,859	4,163,934
<b>Total deposits</b>	<b>5,895,143</b>	<b>5,580,705</b>
Short-term borrowings	587,806	707,466
Subordinated debentures	170,249	72,167
Other long-term debt	7,706	8,161
Capital lease obligation	7,311	7,590
<b>Total long-term debt</b>	<b>185,266</b>	<b>87,918</b>
Other liabilities	45,199	44,323
<b>Total liabilities</b>	<b>6,713,414</b>	<b>6,420,412</b>
<b>Shareholders' Equity</b>		
Preferred stock, \$1 par value per share, 3,000,000 shares authorized, none issued	—	—
Common stock, \$1 par value per share, 200,000,000 shares authorized; 113,914,902 shares issued at September 30, 2018 and December 31, 2017, and 100,361,434 and 97,456,478 shares outstanding at September 30, 2018 and December 31, 2017, respectively	113,915	113,915
Additional paid-in capital	492,262	470,123
Retained earnings	493,392	437,416

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Accumulated other comprehensive loss, net	(20,657	)	(6,173	)
Treasury stock (13,553,468 and 16,458,424 shares at September 30, 2018 and December 31, 2017, respectively)	(105,981	)	(127,154	)
Total shareholders' equity	972,931		888,127	
Total liabilities and shareholders' equity	\$7,686,345		\$7,308,539	

The accompanying notes are an integral part of these unaudited condensed consolidated financial statements.

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## ITEM 1. Financial Statements and Supplementary Data (Continued)

## FIRST COMMONWEALTH FINANCIAL CORPORATION AND SUBSIDIARIES

## CONDENSED CONSOLIDATED STATEMENTS OF INCOME (Unaudited)

	For the Three Months Ended September 30, 2018		For the Nine Months Ended September 30, 2018	
	2017	2018	2017	2018
	(dollars in thousands, except share data)			
Interest Income				
Interest and fees on loans	\$66,105	\$57,335	\$188,529	\$160,548
Interest and dividends on investments:				
Taxable interest	7,899	7,219	23,031	21,577
Interest exempt from federal income taxes	410	410	1,231	1,212
Dividends	420	417	1,412	1,276
Interest on bank deposits	39	30	109	97
Total interest income	74,873	65,411	214,312	184,710
Interest Expense				
Interest on deposits	6,006	2,491	14,639	6,511
Interest on short-term borrowings	2,603	2,427	7,387	6,373
Interest on subordinated debentures	2,302	772	4,664	2,215
Interest on other long-term debt	76	81	228	245
Interest on lease obligations	73	77	221	156
Total interest expense	11,060	5,848	27,139	15,500
Net Interest Income	63,813	59,563	187,173	169,210
Provision for credit losses	2,961	1,214	11,032	2,834
Net Interest Income after Provision for Credit Losses	60,852	58,349	176,141	166,376
Noninterest Income				
Net securities gains	—	92	8,102	695
Trust income	2,206	2,147	6,014	5,275
Service charges on deposit accounts	4,589	4,803	13,418	13,858
Insurance and retail brokerage commissions	1,872	2,128	5,560	6,652
Income from bank owned life insurance	1,579	1,472	5,241	4,213
Gain on sale of mortgage loans	1,542	1,418	4,267	3,710
Gain on sale of other loans and assets	643	503	3,548	1,267
Card-related interchange income	5,044	4,780	14,929	13,873
Derivatives mark to market	—	(14	) 789	(49
Swap fee income	528	217	1,115	458
Other income	1,754	2,244	5,125	5,674
Total noninterest income	19,757	19,790	68,108	55,626
Noninterest Expense				
Salaries and employee benefits	26,553	26,169	77,580	74,933
Net occupancy expense	4,341	3,715	12,932	11,597
Furniture and equipment expense	3,424	3,342	10,611	9,753
Data processing expense	2,853	2,229	7,764	6,659
Advertising and promotion expense	1,200	941	3,185	2,735
Pennsylvania shares tax expense	1,248	1,093	3,398	3,070
Intangible amortization	817	844	2,430	2,262

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Collection and repossession expense	630	402	2,060	1,342
Other professional fees and services	962	1,300	3,000	3,355
FDIC insurance	217	696	1,590	2,466
Loss on sale or write-down of assets	181	167	875	1,486
Litigation and operational losses	435	598	811	1,107
Merger and acquisition related	24	(69	) 1,634	10,412
Other operating expenses	6,645	5,934	17,662	17,212
Total noninterest expense	49,530	47,361	145,532	148,389
Income Before Income Taxes	31,079	30,778	98,717	73,613
Income tax provision	5,930	9,495	18,217	22,429
Net Income	\$25,149	\$ 21,283	\$80,500	\$ 51,184
Average Shares Outstanding	100,226,077	102,816	98,998,497	94,536,472
Average Shares Outstanding Assuming Dilution	100,490,807	102,457,470	99,197,568	94,578,490
Per Share Data:				
Basic Earnings per Share	\$0.25	\$ 0.22	\$0.81	\$ 0.54
Diluted Earnings per Share	\$0.25	\$ 0.22	\$0.81	\$ 0.54
Cash Dividends Declared per Common Share	\$0.09	\$ 0.08	\$0.26	\$ 0.24

The accompanying notes are an integral part of these unaudited condensed consolidated financial statements.

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## ITEM 1. Financial Statements and Supplementary Data (Continued)

## FIRST COMMONWEALTH FINANCIAL CORPORATION AND SUBSIDIARIES

## CONDENSED CONSOLIDATED STATEMENTS OF COMPREHENSIVE INCOME (Unaudited)

	For the Three Months Ended September 30, 2018		For the Nine Months Ended September 30, 2017	
	2018	2017	2018	2017
	(dollars in thousands)			
Net Income	\$25,149	\$21,283	\$80,500	\$51,184
Other comprehensive (loss) income, before tax benefit (expense):				
Unrealized holding (losses) gains on securities arising during the period	(5,382 )	1,690	(8,704 )	5,935
Less: reclassification adjustment for gains on securities included in net income	—	(92 )	(8,102 )	(695 )
Unrealized holding gains (losses) on derivatives arising during the period	198	(49 )	165	(631 )
Less: reclassification adjustment for losses on derivatives included in net income	—	20	10	93
Total other comprehensive (loss) income, before tax benefit (expense)	(5,184 )	1,569	(16,631 )	4,702
Income tax benefit (expense) related to items of other comprehensive (loss) income	1,088	(549 )	3,491	(1,646 )
Total other comprehensive (loss) income	(4,096 )	1,020	(13,140 )	3,056
Comprehensive Income	\$21,053	\$22,303	\$67,360	\$54,240

The accompanying notes are an integral part of these unaudited condensed consolidated financial statements.

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## ITEM 1. Financial Statements and Supplementary Data (Continued)

## FIRST COMMONWEALTH FINANCIAL CORPORATION AND SUBSIDIARIES

## CONDENSED CONSOLIDATED STATEMENTS OF CHANGES IN SHAREHOLDERS' EQUITY (Unaudited)

	Shares Outstanding	Common Stock	Additional Paid-in- Capital	Retained Earnings	Accumulated Other Comprehensive Income (Loss), net	Treasury Stock	Total Shareholders' Equity
(dollars in thousands, except share and per share data)							
Balance at December 31, 2017	97,456,478	\$ 113,915	\$ 470,123	\$ 437,416	\$ (6,173 )	\$ (127,154)	\$ 888,127
Cumulative effect of adoption of ASU 2018-02				1,344	(1,344 )		—
January 1, 2018	97,456,478	113,915	470,123	438,760	(7,517 )	(127,154 )	888,127
Net income				80,500			80,500
Other comprehensive loss					(13,140 )		(13,140 )
Cash dividends declared (\$0.26 per share)				(25,868 )			(25,868 )
Treasury stock acquired	(75,778 )					(1,136 )	(1,136 )
Treasury stock reissued	2,908,234		21,579	—		22,447	44,026
Restricted stock	72,500	—	560	—		(138 )	422
Balance at September 30, 2018	100,361,434	\$ 113,915	\$ 492,262	\$ 493,392	\$ (20,657 )	\$ (105,981)	\$ 972,931
	Shares Outstanding	Common Stock	Additional Paid-in- Capital	Retained Earnings	Accumulated Other Comprehensive Income (Loss), net	Treasury Stock	Total Shareholders' Equity
(dollars in thousands, except share and per share data)							
Balance at December 31, 2016	89,007,077	\$ 105,563	\$ 366,426	\$ 412,764	\$ (7,027 )	\$ (127,797)	\$ 749,929
Net income				51,184			51,184
Other comprehensive income					3,056		3,056
Cash dividends declared (\$0.24 per share)				(22,717 )			(22,717 )
Treasury stock acquired	(85,160 )					(1,187 )	(1,187 )
Treasury stock reissued	181,211		1,170	—		1,387	2,557
Restricted stock	21,000	—	138	—		600	738
Common stock issuance	8,351,447	8,352	102,389				110,741
Balance at September 30, 2017	97,475,575	\$ 113,915	\$ 470,123	\$ 441,231	\$ (3,971 )	\$ (126,997)	\$ 894,301

The accompanying notes are an integral part of these unaudited condensed consolidated financial statements.



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## ITEM 1. Financial Statements and Supplementary Data (Continued)

## FIRST COMMONWEALTH FINANCIAL CORPORATION AND SUBSIDIARIES

## CONDENSED CONSOLIDATED STATEMENTS OF CASH FLOWS (Unaudited)

	For the Nine Months Ended September 30,	
	2018	2017
	(dollars in thousands)	
Operating Activities		
Net income	\$80,500	\$51,184
Adjustment to reconcile net income to net cash provided by operating activities:		
Provision for credit losses	11,032	2,834
Deferred tax expense	2,969	3,411
Depreciation and amortization	5,620	6,711
Net gains on securities and other assets	(15,816 )	(3,821 )
Net amortization of premiums and discounts on securities	2,343	2,685
Income from increase in cash surrender value of bank owned life insurance	(4,364 )	(4,213 )
Increase in interest receivable	(2,483 )	(588 )
Mortgage loans originated for sale	(129,552)	(116,699 )
Proceeds from sale of mortgage loans	139,685	114,819
Increase in interest payable	1,672	678
(Decrease) increase in income taxes payable	(3,412 )	3,288
Distribution from unconsolidated subsidiary	9,000	—
Other-net	(3,655 )	2,963
Net cash provided by operating activities	93,539	63,252
Investing Activities		
Transactions with securities held to maturity:		
Proceeds from maturities and redemptions	37,007	36,620
Purchases	(5,506 )	(101,372 )
Transactions with securities available for sale:		
Proceeds from sales	15,939	143,660
Proceeds from maturities and redemptions	111,800	100,620
Purchases	(292,249)	(150,892 )
Purchases of FHLB stock	(38,947 )	(35,346 )
Proceeds from the redemption of FHLB stock	43,754	42,791
Proceeds from bank owned life insurance	2,140	—
Proceeds from sale of loans	32,745	9,986
Proceeds from sale of other assets	2,486	3,835
Acquisition, net of cash acquired	705	3,188
Net increase in loans	(109,060)	(132,079 )
Purchases of premises and equipment and other assets	(6,862 )	(8,960 )
Net cash used in investing activities	(206,048)	(87,949 )
Financing Activities		
Net increase in federal funds purchased	6,500	—
Net decrease in other short-term borrowings	(126,160)	(62,118 )
Net increase in deposits	173,553	123,455
Repayments of other long-term debt	(23,443 )	(440 )

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Repayments of capital lease obligation	(279 )	(173 )
Proceeds from issuance of other long-term debt	98,026	—
Dividends paid	(25,868 )	(22,717 )
Proceeds from reissuance of treasury stock	208	228
Purchase of treasury stock	(1,136 )	(1,187 )
Net cash provided by financing activities	101,401	37,048
Net (decrease) increase in cash and cash equivalents	(11,108 )	12,351
Cash and cash equivalents at January 1	107,292	115,677
Cash and cash equivalents at September 30	\$96,184	\$128,028

The accompanying notes are an integral part of these unaudited condensed consolidated financial statements.

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ITEM 1. Financial Statements and Supplementary Data

FIRST COMMONWEALTH FINANCIAL CORPORATION AND SUBSIDIARIES

NOTES TO THE UNAUDITED CONDENSED CONSOLIDATED FINANCIAL STATEMENTS (Continued)

ITEM 1. Financial Statements and Supplementary Data

FIRST COMMONWEALTH FINANCIAL CORPORATION AND SUBSIDIARIES

NOTES TO THE UNAUDITED CONDENSED CONSOLIDATED FINANCIAL STATEMENTS

Note 1 Basis of Presentation

The accounting and reporting policies of First Commonwealth Financial Corporation and its subsidiaries ("First Commonwealth" or the "Company") conform with generally accepted accounting principles in the United States of America ("GAAP"). The preparation of financial statements in conformity with GAAP requires management to make estimates, assumptions and judgments that affect the amounts reported in the financial statements and accompanying notes. Actual realized amounts could differ from those estimates. In the opinion of management, the unaudited interim condensed consolidated financial statements include all adjustments (consisting of only normal recurring adjustments) necessary for a fair presentation of First Commonwealth's financial position, results of operations, comprehensive income, cash flows and changes in shareholders' equity as of and for the periods presented.

The results of operations for the nine months ended September 30, 2018 are not necessarily indicative of the results that may be expected for the full year of 2018. These interim financial statements should be read in conjunction with First Commonwealth's 2017 Annual Report on Form 10-K.

Adoption of New Accounting Standards

On January 1, 2018, First Commonwealth adopted ASU 2014-09, "Revenue from Contracts with Customers" ("ASC 606") and all subsequent amendments to the ASU, which creates a single framework for recognizing revenue from contracts with customers that fall within its scope and revises when it is appropriate to recognize a gain(loss) from the transfer of nonfinancial assets, such as OREO. The majority of the Company's revenues come from interest income and other sources, including loans and securities, that are outside the scope of ASC 606. The Company's services that fall within the scope of ASC 606 are presented within non-interest income and are recognized as revenue as the Company satisfies its obligation to the customer. Services within the scope of ASC 606 include trust income, service charges on deposits, insurance and retail brokerage commissions, interchange fees and gain(loss) on other real estate owned ("OREO"). Refer to Note 15, "Revenue Recognition" for further discussion on the Company's accounting policies for revenue sources within the scope of ASC 606. The Company adopted ASC 606 using the modified retrospective method applied to all contracts not completed as of January 1, 2018. Results for reporting periods beginning after January 1, 2018 are presented under ASC 606 while prior period amounts continue to be reported in accordance with legacy GAAP. The adoption of ASC 606 did not result in a significant change to the accounting for any of the in-scope revenue streams; as such, no cumulative effect adjustment was recorded.

On January 1, 2018, First Commonwealth elected to adopt ASU 2018-02, "Income Statement - Reporting Comprehensive Income (Topic 220)." As part of this adoption, First Commonwealth has elected to reclassify the income tax effects resulting from tax reform from accumulated other comprehensive income to retained earnings on a portfolio basis. ASU 2018-02 provides for the reclassification of the stranded tax effects resulting from the Tax Cuts and Jobs Act. As of January 1, 2018, First Commonwealth reclassified \$1.3 million from accumulated other comprehensive income to retained earnings in relation to the stranded tax effect which included accumulated other comprehensive income recognized on available-for-sale investment securities, interest rate swaps and other post-retirement benefits. This reclassification is shown as an adjustment to the beginning of the year balances and can be seen in the Condensed Consolidated Statements of Changes in Shareholders' Equity.

In January 2016, the FASB issued ASU No. 2016-01, "Recognition and Measurement of Financial Assets and Financial Liabilities." This ASU addresses certain aspects of recognition, measurement, presentation, and disclosure of financial instruments by making targeted improvements to GAAP as follows: (1) require equity investments (except those accounted for under the equity method of accounting or those that result in consolidation of the investee) to be measured at fair value with changes in fair value recognized in net income; (2) simplify the impairment assessment of equity investments without readily determinable fair values by requiring a qualitative assessment to identify impairment, and when that assessment indicates that impairment exists, requiring the entity to measure the investment

at fair value; (3) eliminate the requirement to disclose the fair value of financial instruments measured at amortized cost for entities that are not public business entities; (4) eliminate the requirement for public business entities to disclose the method(s) and significant assumptions used to estimate the fair value that is required to be disclosed for financial instruments measured at amortized cost on the balance sheet; (5) require public business entities to use the exit price notion when measuring the fair value of financial instruments for disclosure purposes; (6) require an entity to present separately in other comprehensive income the portion of the total change in the fair value of a liability resulting from a change in the instrument-specific credit risk when the entity has elected to measure the liability at fair value in accordance with the fair value option for financial instruments; (7) require separate presentation of financial assets and financial liabilities by measurement category and form of financial asset (that is, securities or loans and receivables) on the balance sheet or the accompanying notes to the financial statements; and (8) clarify that an entity should evaluate the need for a

## ITEM 1. Financial Statements and Supplementary Data

## FIRST COMMONWEALTH FINANCIAL CORPORATION AND SUBSIDIARIES

## NOTES TO THE UNAUDITED CONDENSED CONSOLIDATED FINANCIAL STATEMENTS (Continued)

valuation allowance on a deferred tax asset related to available-for-sale securities in combination with the entity's other deferred tax assets. The adoption of ASU No. 2016-01 on January 1, 2018 did not have a material impact on the Company's Consolidated Financial Statements. In accordance with this ASU, and as reflected in Note 11, "Fair Values of Assets and Liabilities," the Company measured the fair value of its loan portfolio as of September 30, 2018 using an exit price notion.

For purposes of reporting cash flows, cash and cash equivalents include cash on hand, amounts due from banks, federal funds sold and interest-bearing bank deposits. Generally, federal funds are sold for one-day periods.

## Note 2 Acquisition

On May 1, 2018, the Company completed its acquisition of Garfield Acquisition Corporation ("Garfield") and its banking subsidiary, Foundation Bank, for consideration of \$17.4 million in cash and 2.7 million shares of the Company's common stock. Through the acquisition, the Company obtained five full-service banking offices which are operating under the First Commonwealth name. This acquisition expands the Company's presence into the Cincinnati, Ohio market and added \$184.5 million in loans and \$141.3 million in deposits to the Company's balance sheet.

The table below summarizes the net assets acquired (at fair value) and consideration transferred in connection with the Garfield acquisition (dollars in thousands):

## Consideration Paid

Cash paid to shareholders	\$ 17,400	
Shares issued to shareholders (2,745,098 shares)	41,561	
Total consideration paid		\$ 58,961

## Fair Value of Assets Acquired

Cash and cash equivalents	18,105
FHLB Stock	3,261
Loans	184,506
Premises and other equipment	409
Intangible assets	1,248
Other assets	1,747
Total assets acquired	209,276

## Fair Value of Liabilities Assumed

Deposits	141,281
Federal Home Loan Bank borrowings	22,988
Other liabilities	5,068
Total liabilities assumed	169,337

Total Fair Value of Identifiable Net Assets	39,939
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Goodwill	\$ 19,022
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The goodwill of \$19.0 million arising from the acquisition represents the value of synergies and economies of scale expected from combining the operations of the Company with Garfield Acquisition Corporation.

The Company determined that this acquisition constitutes a business combination as defined in FASB ASC Topic 805, "Business Combinations." Accordingly, as of the date of the acquisition, the Company recorded the assets acquired and liabilities assumed at fair value. The Company determined fair values in accordance with the guidance provided in FASB ASC Topic 820, "Fair Value Measurements and Disclosures." Acquired loans were recorded at fair value with no

carryover of the related allowance for loan losses. Fair value is established by discounting the expected future cash flows with a market discount

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## ITEM 1. Financial Statements and Supplementary Data

## FIRST COMMONWEALTH FINANCIAL CORPORATION AND SUBSIDIARIES

## NOTES TO THE UNAUDITED CONDENSED CONSOLIDATED FINANCIAL STATEMENTS (Continued)

rate for like maturities and risk instruments. At the date of acquisition, none of the loans were accounted for under the guidance of ASC Topic 310-30, "Receivables-Loans and Debt Securities Acquired with Deteriorated Credit Quality." The \$184.5 million fair value of acquired loans is the result of \$183.7 million in net loans acquired from Garfield, the recognition of a net combined yield and credit mark adjustment of \$4.3 million and the \$5.1 million reversal of Garfield's allowance as well as prior fair value marks recorded by Garfield.

The fair value of the 2,745,098 common shares issued was determined based on the market price of the Company's common shares on the acquisition date.

Costs related to the acquisition totaled \$1.6 million. These amounts were expensed as incurred and are recorded as a merger and acquisition related expense in the Condensed Consolidated Statements of Income.

As a result of the full integration of the operations of Garfield, it is not practicable to determine revenue or net income included in the Company's operating results relating to Garfield since the date of acquisition as Garfield's results cannot be separately identified.

## Note 3 Supplemental Comprehensive Income Disclosures

The following table identifies the related tax effects allocated to each component of other comprehensive income ("OCI") in the Condensed Consolidated Statements of Comprehensive Income. Reclassification adjustments related to securities available for sale are included in the "Net securities gains" line and reclassification adjustments related to losses on derivatives are included in the "Other operating expenses" line in the Condensed Consolidated Statements of Income.

	For the Nine Months Ended September 30,					
	2018			2017		
	Pretax Amount	Tax (Expense) Benefit	Net of Tax Amount	Pretax Amount	Tax (Expense) Benefit	Net of Tax Amount
	(dollars in thousands)					
Unrealized (losses) gains on securities:						
Unrealized holding (losses) gains on securities arising during the period	\$(8,704 )	\$ 1,828	\$(6,876 )	\$5,935	\$(2,077 )	\$3,858
Reclassification adjustment for gains on securities included in net income	(8,102 )	1,701	(6,401 )	(695 )	243	(452 )
Total unrealized (losses) gains on securities	(16,806 )	3,529	(13,277 )	5,240	(1,834 )	3,406
Unrealized gains (losses) on derivatives:						
Unrealized holding gains (losses) on derivatives arising during the period	165	(35 )	130	(631 )	221	(410 )
Reclassification adjustment for losses on derivatives included in net income	10	(3 )	7	93	(33 )	60
Total unrealized gains (losses) on derivatives	175	(38 )	137	(538 )	188	(350 )
Total other comprehensive (loss) income	\$(16,631 )	\$ 3,491	\$(13,140 )	\$4,702	\$(1,646 )	\$3,056

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FIRST COMMONWEALTH FINANCIAL CORPORATION AND SUBSIDIARIES

NOTES TO THE UNAUDITED CONDENSED CONSOLIDATED FINANCIAL STATEMENTS (Continued)

	For the Three Months Ended September 30,					
	2018			2017		
	Pretax Amount	Tax (Expense) Benefit	Net of Tax Amount	Pretax Amount	Tax (Expense) Benefit	Net of Tax Amount
	(dollars in thousands)					
Unrealized (losses) gains on securities:						
Unrealized holding (losses) gains on securities arising during the period	\$ (5,382 )	\$ 1,130	\$ (4,252 )	\$ 1,690	\$ (591 )	\$ 1,099
Reclassification adjustment for gains on securities included in net income	—	—	—	(92 )	32	(60 )
Total unrealized (losses) gains on securities	(5,382 )	1,130	(4,252 )	1,598	(559 )	1,039
Unrealized gains (losses) on derivatives:						
Unrealized holding gains (losses) on derivatives arising during the period	198	(42 )	156	(49 )	17	(32 )
Reclassification adjustment for losses on derivatives included in net income	—	—	—	20	(7 )	13
Total unrealized gains (losses) on derivatives	198	(42 )	156	(29 )	10	(19 )
Total other comprehensive (loss) income	\$ (5,184 )	\$ 1,088	\$ (4,096 )	\$ 1,569	\$ (549 )	\$ 1,020

The following table details the change in components of OCI for the nine months ended September 30:

	2018			2017				
	Securities Available for Sale	Post-Retirement Obligation	Derivatives	Accumulated Other Comprehensive Income (Loss)	Securities Available for Sale	Post-Retirement Obligation	Derivatives	Accumulated Other Comprehensive Income (Loss)
	(dollars in thousands)							
Balance at December 31	\$ (6,166 )	\$ 299	\$ (306 )	\$ (6,173 )	\$ (7,455 )	\$ 225	\$ 203	\$ (7,027 )
Cumulative effect of adoption of ASU 2018-02	(1,344 )	—	—	(1,344 )	—	—	—	—
Balance at January 1	(7,510 )	299	(306 )	(7,517 )	(7,455 )	225	203	(7,027 )
Other comprehensive (loss) income before reclassification adjustment	(6,876 )	—	130	(6,746 )	3,858	—	(410 )	3,448
Amounts reclassified from accumulated other comprehensive (loss) income	(6,401 )	—	7	(6,394 )	(452 )	—	60	(392 )
Net other comprehensive (loss) income during the period	(13,277 )	—	137	(13,140 )	3,406	—	(350 )	3,056
Balance at September 30	\$ (20,787 )	\$ 299	\$ (169 )	\$ (20,657 )	\$ (4,049 )	\$ 225	\$ (147 )	\$ (3,971 )



## ITEM 1. Financial Statements and Supplementary Data

## FIRST COMMONWEALTH FINANCIAL CORPORATION AND SUBSIDIARIES

## NOTES TO THE UNAUDITED CONDENSED CONSOLIDATED FINANCIAL STATEMENTS (Continued)

## Note 4 Supplemental Cash Flow Disclosures

The following table presents information related to cash paid during the period for interest and income taxes, as well as detail on non-cash investing and financing activities for the nine months ended September 30:

	2018	2017
	(dollars in thousands)	
Cash paid during the period for:		
Interest	\$25,780	\$14,995
Income taxes	18,750	17,394
Non-cash investing and financing activities:		
Loans transferred to other real estate owned and repossessed assets	3,346	2,154
Loans transferred from held to maturity to held for sale	29,765	13,292
Gross (decrease) increase in market value adjustment to securities available for sale	(16,806 )	5,240
Gross increase (decrease) in market value adjustment to derivatives	175	(538 )
Noncash treasury stock reissuance	2,257	2,258
Net assets acquired through acquisition	21,834	36,926
Proceeds from death benefit on bank-owned life insurance not received	—	897

## Note 5 Earnings per Share

The following table summarizes the composition of the weighted-average common shares (denominator) used in the basic and diluted earnings per share computations:

	For the Three Months Ended September 30,		For the Nine Months Ended September 30,	
	2018	2017	2018	2017
Weighted average common shares issued	113,914,902	113,914,902	113,914,902	111,100,495
Average treasury stock shares	(13,550,710 )	(16,436,228 )	(14,783,078 )	(16,465,984 )
Average deferred compensation shares	(37,411 )	—	(37,411 )	—
Average unearned nonvested shares	(100,134 )	(75,858 )	(95,916 )	(98,039 )
Weighted average common shares and common stock equivalents used to calculate basic earnings per share	100,226,647	97,402,816	98,998,497	94,536,472
Additional common stock equivalents (nonvested stock) used to calculate diluted earnings per share	226,754	54,654	161,660	42,018
Additional common stock equivalents (deferred compensation) used to calculate diluted earnings per share	37,411	—	37,411	—
Weighted average common shares and common stock equivalents used to calculate diluted earnings per share	100,490,812	97,457,470	99,197,568	94,578,490

The following table shows the number of shares and the price per share related to common stock equivalents that were not included in the computation of diluted earnings per share for the nine months ended September 30 because to do so would have been antidilutive.

	2018			2017		
	Shares	Price Range		Shares	Price Range	
		From	To		From	To
Restricted Stock	66,332	\$8.84	\$14.49	22,802	\$8.55	\$13.96
Restricted Stock Units	—	\$—	\$—	22,750	\$15.09	\$15.09



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## FIRST COMMONWEALTH FINANCIAL CORPORATION AND SUBSIDIARIES

## NOTES TO THE UNAUDITED CONDENSED CONSOLIDATED FINANCIAL STATEMENTS (Continued)

## Note 6 Commitments and Contingent Liabilities

## Commitments and Letters of Credit

Standby letters of credit and commercial letters of credit are conditional commitments issued by First Commonwealth to guarantee the performance of a customer to a third party. The contract or notional amount of these instruments reflects the maximum amount of future payments that First Commonwealth could be required to pay under the guarantees if there were a total default by the guaranteed parties, without consideration of possible recoveries under recourse provisions or from collateral held or pledged. In addition, many of these commitments are expected to expire without being drawn upon; therefore, the total commitment amounts do not necessarily represent future cash requirements.

The following table identifies the notional amount of those instruments at:

	September 30, 2018	December 31, 2017
	(dollars in thousands)	
Financial instruments whose contract amounts represent credit risk:		
Commitments to extend credit	\$1,846,575	\$1,840,180
Financial standby letters of credit	18,486	17,946
Performance standby letters of credit	21,460	20,472
Commercial letters of credit	927	1,149

The notional amounts outstanding as of September 30, 2018 include amounts issued in 2018 of \$1.1 million in financial standby letters of credit and \$0.7 million in performance standby letters of credit. There were no commercial letters of credit issued in 2018. A liability of \$0.2 million has been recorded as of September 30, 2018 and December 31, 2017, which represents the estimated fair value of letters of credit issued. The fair value of letters of credit is estimated based on the unrecognized portion of fees received at the time the commitment was issued. Unused commitments and letters of credit provide exposure to future credit loss in the event of nonperformance by the borrower or guaranteed parties. Management's evaluation of the credit risk related to these commitments resulted in the recording of a liability of \$5.2 million as of both September 30, 2018 and December 31, 2017. This liability is reflected in "Other liabilities" in the Condensed Consolidated Statements of Financial Condition. The credit risk evaluation incorporated probability of default, loss given default and estimated utilization for the next twelve months for each loan category and the letters of credit.

## Legal Proceedings

First Commonwealth and its subsidiaries are subject in the normal course of business to various pending and threatened legal proceedings in which claims for monetary damages are asserted. As of September 30, 2018, management, after consultation with legal counsel, does not anticipate that the aggregate ultimate liability arising out of litigation pending or threatened against First Commonwealth or its subsidiaries will be material to First Commonwealth's consolidated financial position. On at least a quarterly basis, First Commonwealth assesses its liabilities and contingencies in connection with such legal proceedings. For those matters where it is probable that First Commonwealth will incur losses and the amounts of the losses can be reasonably estimated, First Commonwealth records an expense and corresponding liability in its consolidated financial statements. To the extent the pending or threatened litigation could result in exposure in excess of that liability, the amount of such excess is not currently estimable. Although not considered probable, the range of reasonably possible losses for such matters in the aggregate, beyond the existing recorded liability (if any), is between \$0 and \$1 million. Although First Commonwealth does not believe that the outcome of pending litigation will be material to First Commonwealth's consolidated financial position, it cannot rule out the possibility that such outcomes will be material to the consolidated results of operations and cash flows for a particular reporting period in the future.

First Commonwealth Financial Corporation and First Commonwealth Bank were named defendants in an action commenced August 27, 2015 by eight named plaintiffs that filed in the Court of Common Pleas of Jefferson County, Pennsylvania. The plaintiffs alleged that the Bank repossessed motor vehicles, sold the vehicles and sought to collect deficiency balances in a manner that did not comply with the notice requirements of the Pennsylvania Uniform Commercial Code (UCC), charged inappropriate costs and fees, including storage costs for dates that a repossessed vehicle was not in storage, and wrongly filed forms with the Department of Motor Vehicles asserting that the Bank had complied with applicable laws relating to the repossession of the vehicles. First Commonwealth Financial Corporation, First Commonwealth Bank, the plaintiffs, the plaintiffs' counsel and First Commonwealth's liability insurer entered into a Class Action Settlement Agreement and Release in

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## FIRST COMMONWEALTH FINANCIAL CORPORATION AND SUBSIDIARIES

## NOTES TO THE UNAUDITED CONDENSED CONSOLIDATED FINANCIAL STATEMENTS (Continued)

which, among other things, First Commonwealth and its insurer agreed to pay certain amounts into a settlement fund to be distributed among the class members and class counsel, First Commonwealth agreed to satisfy the remaining deficiency balances of the class members and request that credit reporting agencies delete the tradeline relating to the repossession from each class member's credit report, and the class members released all claims against First Commonwealth and its insurer. At a hearing on July 23, 2018, the Court granted final approval of the settlement and dismissed all claims against First Commonwealth. In August 2018, this settlement was completed. The cost of the settlement to First Commonwealth was recorded as a liability in the second quarter of 2016.

## Note 7 Investment Securities

## Securities Available for Sale

Below is an analysis of the amortized cost and estimated fair values of securities available for sale at:

	September 30, 2018				December 31, 2017			
	Amortized Cost	Gross Unrealized Gains	Gross Unrealized Losses	Estimated Fair Value	Amortized Cost	Gross Unrealized Gains	Gross Unrealized Losses	Estimated Fair Value
(dollars in thousands)								
Obligations of U.S. Government Agencies:								
Mortgage-Backed Securities – Residential	\$9,276	\$ 484	\$(132 )	\$9,628	\$10,556	\$ 789	\$(7 )	\$11,338
Mortgage-Backed Securities – Commercial	170,086	—	(2,675 )	167,411	24,611	—	(462 )	24,149
Obligations of U.S. Government-Sponsored Enterprises:								
Mortgage-Backed Securities – Residential	685,721	987	(25,079 )	661,629	632,422	2,622	(9,489 )	625,555
Other Government-Sponsored Enterprises	100	—	—	100	1,098	—	(1 )	1,097
Obligations of States and Political Subdivisions	27,590	56	(129 )	27,517	27,083	327	—	27,410
Corporate Securities	20,907	473	(279 )	21,101	15,907	590	(4 )	16,493
Pooled Trust Preferred Collateralized Debt Obligations	—	—	—	—	27,499	526	(4,379 )	23,646
Total Debt Securities	913,680	2,000	(28,294 )	887,386	739,176	4,854	(14,342 )	729,688
Equities	1,670	—	—	1,670	1,670	—	—	1,670
Total Securities Available for Sale	\$915,350	\$ 2,000	\$(28,294 )	\$889,056	\$740,846	\$ 4,854	\$(14,342 )	\$731,358

Mortgage-backed securities include mortgage-backed obligations of U.S. Government agencies and obligations of U.S. Government-sponsored enterprises. These obligations have contractual maturities ranging from less than one year to approximately 30 years with lower anticipated lives to maturity due to prepayments. All mortgage-backed securities contain a certain amount of risk related to the uncertainty of prepayments of the underlying mortgages. Interest rate changes have a direct impact upon prepayment speeds; therefore, First Commonwealth uses computer simulation models to test the average life and yield volatility of all mortgage-backed securities under various interest rate scenarios to monitor the potential impact on earnings and interest rate risk positions.

Expected maturities will differ from contractual maturities because issuers may have the right to call or repay obligations with or without call or prepayment penalties. Other fixed income securities within the portfolio also contain prepayment risk.

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## FIRST COMMONWEALTH FINANCIAL CORPORATION AND SUBSIDIARIES

## NOTES TO THE UNAUDITED CONDENSED CONSOLIDATED FINANCIAL STATEMENTS (Continued)

The amortized cost and estimated fair value of debt securities available for sale at September 30, 2018, by contractual maturity, are shown below.

	Amortized Cost	Estimated Fair Value
	(dollars in thousands)	
Due within 1 year	\$4,099	\$4,089
Due after 1 but within 5 years	15,730	15,464
Due after 5 but within 10 years	26,342	26,269
Due after 10 years	2,426	2,896
	48,597	48,718
Mortgage-Backed Securities (a)	865,083	838,668
Total Debt Securities	\$913,680	\$887,386

Mortgage-Backed Securities include an amortized cost of \$179.4 million and a fair value of \$177.0 million for Obligations of U.S. Government agencies issued by Ginnie Mae and an amortized cost of \$685.7 million and a fair value of \$661.6 million for Obligations of U.S. Government-sponsored enterprises issued by Fannie Mae and Freddie Mac.

Proceeds from sales, gross gains (losses) realized on sales, maturities and other-than-temporary impairment charges related to securities available for sale were as follows for the nine months ended September 30:

	2018	2017
	(dollars in thousands)	
Proceeds from sales	\$ 15,939	\$ 143,660
Gross gains (losses) realized:		
Sales Transactions:		
Gross gains	\$4,719	\$ 359
Gross losses	—	(316 )
	4,719	43
Maturities and impairment		
Gross gains	3,383	712
Gross losses	—	(60 )
	3,383	652
Net gains and impairment	\$ 8,102	\$ 695

Gross gains from sales transactions of \$4.7 million were recognized in 2018 as a result of the sale of the remaining pooled trust preferred security portfolio. Gross gains from maturities and impairment of \$3.4 million were recognized in 2018 as a result of successful auction calls on PreSTL XIV and PreSTL IX, two of our pooled trust preferred securities. Gross gains of \$0.7 million were recognized in 2017 due to the early redemption of another of our trust preferred securities, PreSTL VII.

Securities available for sale with an estimated fair value of \$680.9 million and \$569.0 million were pledged as of September 30, 2018 and December 31, 2017, respectively, to secure public deposits and for other purposes required or permitted by law.

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## FIRST COMMONWEALTH FINANCIAL CORPORATION AND SUBSIDIARIES

## NOTES TO THE UNAUDITED CONDENSED CONSOLIDATED FINANCIAL STATEMENTS (Continued)

## Securities Held to Maturity

Below is an analysis of the amortized cost and fair values of debt securities held to maturity at:

	September 30, 2018				December 31, 2017			
	Amortized Cost	Gross Unrealized Gains	Gross Unrealized Losses	Estimated Fair Value	Amortized Cost	Gross Unrealized Gains	Gross Unrealized Losses	Estimated Fair Value
(dollars in thousands)								
Obligations of U.S. Government Agencies:								
Mortgage-Backed Securities – Residential	\$3,663	\$ —	\$(156)	\$3,507	\$3,925	\$ —	\$(14)	\$3,911
Mortgage-Backed Securities-Commercial	55,726	—	(2,742)	52,984	58,249	—	(1,394)	56,855
Obligations of U.S. Government-Sponsored Enterprises:								
Mortgage-Backed Securities – Residential	273,972	—	(11,468)	262,504	305,126	10	(2,552)	302,584
Mortgage-Backed Securities – Commercial	13,413	—	(427)	12,986	14,056	—	(71)	13,985
Obligations of States and Political Subdivisions	42,447	5	(895)	41,557	40,540	335	(161)	40,714
Debt Securities Issued by Foreign Governments	400	—	(5)	395	200	—	—	200
Total Securities Held to Maturity	\$389,621	\$ 5	\$(15,693)	\$373,933	\$422,096	\$ 345	\$(4,192)	\$418,249

The amortized cost and estimated fair value of debt securities held to maturity at September 30, 2018, by contractual maturity, are shown below. Expected maturities will differ from contractual maturities because borrowers may have the right to call or repay obligations with or without call or prepayment penalties.

	Amortized Cost	Estimated Fair Value
(dollars in thousands)		
Due within 1 year	\$85	\$85
Due after 1 but within 5 years	3,814	3,778
Due after 5 but within 10 years	37,329	36,491
Due after 10 years	1,619	1,598
	42,847	41,952
Mortgage-Backed Securities (a)	346,774	331,981
Total Debt Securities	\$389,621	\$373,933

Mortgage-Backed Securities include an amortized cost of \$59.4 million and a fair value of \$56.5 million for Obligations of U.S. Government agencies issued by Ginnie Mae and an amortized cost of \$287.4 million and a fair value of \$275.5 million for Obligations of U.S. Government-sponsored enterprises issued by Fannie Mae and Freddie Mac.

Securities held to maturity with an amortized cost of \$298.9 million and \$338.3 million were pledged as of September 30, 2018 and December 31, 2017, respectively, to secure public deposits and for other purposes required or



permitted by law.

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FIRST COMMONWEALTH FINANCIAL CORPORATION AND SUBSIDIARIES

NOTES TO THE UNAUDITED CONDENSED CONSOLIDATED FINANCIAL STATEMENTS (Continued)

Note 8 Impairment of Investment Securities

Securities Available for Sale and Held to Maturity

As required by FASB ASC Topic 320, "Investments – Debt and Equity Securities," credit-related other-than-temporary impairment on debt securities is recognized in earnings, while non-credit related other-than-temporary impairment on debt securities not expected to be sold is recognized in OCI. During the nine months ended September 30, 2018 and 2017, no other-than-temporary impairment charges were recognized.

First Commonwealth utilizes the specific identification method to determine the net gain or loss on debt securities and the average cost method to determine the net gain or loss on equity securities.

We review our investment portfolio on a quarterly basis for indications of impairment. This review includes analyzing the length of time and the extent to which the fair value has been lower than the cost, the financial condition and near-term prospects of the issuer, including any specific events which may influence the operations of the issuer and whether we are more likely than not to sell, or be required to sell, the security. We evaluate whether we are more likely than not to sell debt securities based upon our investment strategy for the particular type of security, our cash flow needs, liquidity position, capital adequacy, tax position and interest rate risk position. In addition, the risk of future other-than-temporary impairment may be influenced by weakness in the U.S. economy or changes in real estate values.

The following table presents the gross unrealized losses and estimated fair values at September 30, 2018 for both available for sale and held to maturity securities by investment category and time frame for which securities have been in a continuous unrealized loss position:

	Less Than 12 Months	12 Months or More	Total
	Estimated Fair Value	Estimated Fair Value	Estimated Fair Value
	Gross Unrealized Losses	Gross Unrealized Losses	Gross Unrealized Losses
(dollars in thousands)			
Obligations of U.S. Government Agencies:			
Mortgage-Backed Securities – Residential	\$7,267	\$ (288 )	\$ —
			—\$7,267 \$ (288