

FIRST BANCORP /PR/
Form S-1/A
October 29, 2010

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As filed with the Securities and Exchange Commission on October 29, 2010

Registration No. 333-169399

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

**Amendment No. 2
to
Form S-1
REGISTRATION STATEMENT UNDER THE SECURITIES ACT OF 1933**

FIRST BANCORP.
(Exact name of registrant as specified in its charter)

Puerto Rico
*(State or other jurisdiction of
incorporation or organization)*

6022
*(Primary Standard Industrial
Classification Code Number)*

66-0561882
*(I.R.S. Employer
Identification Number)*

**1519 Ponce de León Avenue, Stop 23
Santurce, Puerto Rico 00908
(787) 729-8200**
(Address, including zip code and telephone number, including area code, of registrant's principal executive offices)

**Lawrence Odell
Executive Vice President and General Counsel
First BanCorp.
1519 Ponce de León Avenue, Stop 23
Santurce, Puerto Rico 00908
(787) 729-8109**
(Name, address, including zip code and telephone number, including area code, of agent for service)

Copies to:

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Approximate date of commencement of proposed sale to the public: As soon as practicable after the effective date of this registration statement.

If any of the securities being registered on this form are to be offered on a delayed or continuous basis pursuant to Rule 415 under the Securities Act of 1933, check the following box.

If this Form is filed to register additional securities for an offering pursuant to Rule 462(b) under the Securities Act, check the following box and list the Securities Act registration statement number of the earlier effective registration statement for the same offering.

If this Form is a post-effective amendment filed pursuant to Rule 462(c) under the Securities Act, check the following box and list the Securities Act registration statement number of the earlier effective registration statement for the same offering.

If this Form is a post-effective amendment filed pursuant to Rule 462(d) under the Securities Act, check the following box and list the Securities Act registration statement number of the earlier effective registration statement for the same offering.

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. (Check one):

Large accelerated filer Accelerated filer Non-accelerated filer Smaller reporting company
(Do not check if a smaller reporting company)

The registrant hereby amends this registration statement on such date or dates as may be necessary to delay its effective date until the registrant shall file a further amendment which specifically states that this registration statement shall thereafter become effective in accordance with Section 8(a) of the Securities Act of 1933 or until the registration statement shall become effective on such date as the Commission, acting pursuant to said Section 8(a), may determine.

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The information in this preliminary prospectus is not complete and may be changed. We may not sell these securities until the registration statement filed with the Securities and Exchange Commission is effective. This preliminary prospectus is not an offer to sell these securities and it is not soliciting an offer to buy these securities in any jurisdiction where the offer or sale is not permitted.

SUBJECT TO COMPLETION: DATED OCTOBER 29, 2010

PRELIMINARY PROSPECTUS

Shares

Common Stock

First BanCorp. is the holding company for FirstBank Puerto Rico, a Puerto Rico-chartered commercial bank headquartered in San Juan, Puerto Rico.

We are offering post-reverse stock split (as defined below) shares of our common stock representing an aggregate offering price of \$500,000,000. Our common stock is traded on the New York Stock Exchange under the symbol **FBP**. On October 28, 2010, the last reported sale price of our common stock on the New York Stock Exchange was \$0.29 per pre-reverse stock split share.

Before the registration statement of which this prospectus is a part is declared effective, we will effect a reverse stock split (the reverse stock split) in the range of between one new share of common stock for 10 old shares of common stock and one new share of common stock for 20 old shares of common stock, which is the range that our stockholders approved at our Special Meeting of Stockholders on August 24, 2010. The number of authorized shares of common stock will remain the same after the reverse stock split. Once the ratio for the reverse stock split is determined, except where we state otherwise, all of the numbers and prices of shares presented in this prospectus will be restated on a post-reverse stock split basis.

The public offering price for each share of our post-reverse stock split shares of common stock will be determined by a negotiation between us and the underwriters based upon market conditions, an estimate of the change in the market price of our common stock as a result of the reverse stock split and other factors on the day we price the shares. In the usual case, as a result of a reverse stock split (all other things being equal), the market price of common stock may not rise proportionally to the decrease in outstanding shares resulting from the reverse stock split. While it is not possible to predict the impact of the reverse stock split in our case, consideration of the impact of the reverse stock split will be necessary in determining the number of post-reverse stock split shares to include in this offering.

Although we want to receive gross proceeds of at least \$500 million in this offering, we may determine to complete an offering for a number of shares of common stock that results in a lower amount of gross proceeds.

Investing in our common stock involves risks. See Risk Factors beginning on page 24 to read about factors you should consider before you make your investment decision.

	Per post-reverse stock split share	Total
Price to public	\$	\$

Underwriting discount	\$	\$
Proceeds, before expenses, to First BanCorp.	\$	\$

We have granted the underwriters a 30-day option to purchase up to _____ additional post-reverse stock split shares of common stock (equal to 15% of the total number of shares we are offering) solely to cover over-allotments, if any.

Neither the Securities and Exchange Commission nor any securities commission of any state or other jurisdiction has approved or disapproved of these securities or passed upon the accuracy or adequacy of this prospectus. Any representation to the contrary is a criminal offense.

These securities are not savings accounts, deposits, or other obligations of any bank and are not insured by the Federal Deposit Insurance Corporation or any other governmental agency.

The underwriters expect to deliver the common stock to purchasers on or about _____, 2010, subject to customary closing conditions.

Sole Book-Running Manager

Lead Manager

UBS Investment Bank

The date of this prospectus is _____, 2010

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We have not authorized anyone to provide any information other than that contained or incorporated by reference in this prospectus or in any free writing prospectus prepared by or on behalf of us or to which we have referred you. We take no responsibility for, and can provide no assurance as to the reliability of, any other information that others may give you.

This prospectus and any applicable prospectus supplement are not offers to sell nor are they seeking an offer to buy these securities in any jurisdiction where the offer or sale is not permitted. The information contained in this prospectus and any applicable prospectus supplement is complete and correct only as of the date on the front cover of such documents, regardless of the time of the delivery of such documents or any sale of these securities. In this prospectus, First BanCorp, we, us, and our refer to the consolidated operations of First BanCorp., and references to a company name refer solely to such company.

For investors outside the United States: Neither we nor any of the underwriters have taken any action to permit a public offering of the shares of our common stock or the possession or distribution of this prospectus in any jurisdiction where action for that purpose is required, other than the United States. You are required to inform yourselves about and to observe any restrictions relating to this offering and the distribution of this prospectus.

This prospectus includes statistical and other industry and market data that we obtained from industry publications and research, surveys and studies conducted by third parties. Industry publications and third party research, surveys and studies generally indicate that their information has been obtained from sources believed to be reliable, although they do not guarantee the accuracy or completeness of such information. While we believe these industry publications and third party research, surveys and studies are reliable, we have not independently verified such data.

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About This Prospectus

This prospectus is part of a registration statement that we filed with Securities and Exchange Commission (the SEC). When required, we will file prospectus supplements to update or change information contained in this prospectus. You should read both this prospectus and any prospectus supplement together with additional information described under the headings Additional Information and Incorporation By Reference.

Additional Information

As permitted by SEC rules, this prospectus omits certain information that is included in the registration statement and its exhibits. Since the prospectus may not contain all of the information that you may find important, you should review the full text of these documents. If we have filed a contract, agreement or other document as an exhibit to the registration statement, you should read the exhibit for a more complete understanding of the document or matter involved. Each statement in this prospectus, including statements incorporated by reference as discussed below, regarding a contract, agreement or other document is qualified in its entirety by reference to the actual document.

We file annual, quarterly and special reports and other information with the SEC. You may read and copy any document we file with the SEC at the SEC's public reference room located at 100 F Street, N.E., Washington, D.C. 20549. Please call the SEC at 1-800-SEC-0330 for further information on the public reference room. Our filings are also available to the public from the SEC's web site at <http://www.sec.gov>.

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Incorporation by Reference

The SEC allows us to incorporate by reference the information we file with the SEC, which means we can disclose important information to you by referring to these documents. The information included in the following documents is incorporated by reference and is considered a part of this prospectus. The most recent information that we file with the SEC automatically updates and supersedes previously filed information.

We hereby incorporate by reference into this prospectus the following documents that we have filed with the SEC:

Our Annual Report on Form 10-K for the year ended December 31, 2009 filed with the SEC on March 2, 2010;

Our Quarterly Reports on Form 10-Q for the quarter ended March 31, 2010 and June 30, 2010 filed with the SEC on May 10, 2010 and August 9, 2010, respectively;

Our Current Reports on Form 8-K filed with the SEC on February 3, 2010 (excluding Item 2.02 and Exhibit 99.2 of Item 9.01), April 29, 2010 (excluding Items 2.02 and 9.01, as amended by Form 8-K/A filed with the SEC on May 3, 2010), June 4, 2010, July 2, 2010, July 7, 2010, July 15, 2010, July 16, 2010, July 20, 2010, August 17, 2010, August 18, 2010, August 23, 2010, August 24, 2010, August 26, 2010 and October 26, 2010 (excluding the three paragraphs immediately following the bullets under the section heading Third Quarter Highlights beginning on the first page of Exhibit 99.1);

Our Proxy Statement for the Annual Meeting of Stockholders held on April 27, 2010 filed with the SEC on April 6, 2010; and

Our Proxy Statement for the August 24, 2010 Special Meeting of Stockholders filed with the SEC on August 2, 2010.

You may request a copy of these filings, other than an exhibit to a filing (unless that exhibit is specifically incorporated by reference into that filing), at no cost, by writing to us at the following address: First BanCorp., Attention: Lawrence Odell, Secretary, P.O. Box 9146, San Juan, Puerto Rico, 00908-0146. Telephone requests may be directed to: (787) 729-8109. E-mail requests may be directed to lawrence.odell@firstbankpr.com. You may also access this information at our website at www.firstbankpr.com by viewing the SEC Filings subsection of the Investor Relations menu. No additional information on our website is deemed to be part of or incorporated by reference into this prospectus. We have included our website address in this prospectus solely as an inactive textual reference.

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PROSPECTUS SUMMARY

This summary does not contain all of the information you should consider before investing in our common stock. This prospectus includes or incorporates by reference information about the shares we are offering as well as information regarding our business and detailed financial data. Before you decide to invest in our common stock, you should read the entire prospectus carefully, including the Risk Factors section and any information incorporated by reference herein.

First BanCorp

OUR COMPANY

Founded in 1948, First BanCorp is the second-largest publicly owned financial holding company in Puerto Rico as measured by total assets as of June 30, 2010. We are subject to regulation, supervision and examination by the Federal Reserve Bank of New York (the Federal Reserve) and the Board of Governors of the Federal Reserve System. First BanCorp was incorporated under the laws of the Commonwealth of Puerto Rico to serve as the bank holding company for FirstBank Puerto Rico (FirstBank). We are a full-service provider of financial services and products with operations in Puerto Rico, the mainland United States (the U.S.), the United States Virgin Islands (the USVI) and the British Virgin Islands (the BVI and together with the USVI, the Virgin Islands). As of June 30, 2010, we had total assets of \$18.1 billion, total deposits of \$12.7 billion and total stockholders equity of \$1.4 billion.

We provide a wide range of financial services for retail, commercial and institutional clients. We control two wholly owned subsidiaries: FirstBank, a Puerto Rico-chartered commercial bank, and FirstBank Insurance Agency, Inc., a Puerto Rico-chartered insurance agency (FirstBank Insurance Agency).

FirstBank is subject to the supervision, examination and regulation of both the Office of the Commissioner of Financial Institutions of the Commonwealth of Puerto Rico (the OCIF) and the Federal Deposit Insurance Corporation (the FDIC). Deposits are insured through the FDIC Deposit Insurance Fund. In addition, within FirstBank, the operations in the USVI are subject to regulation and examination by the United States Virgin Islands Banking Board and, in the BVI, operations are subject to regulation by the British Virgin Islands Financial Services Commission. FirstBank Insurance Agency is subject to the supervision, examination and regulation of the Office of the Insurance Commissioner of the Commonwealth of Puerto Rico and operates six offices in Puerto Rico.

FirstBank conducts its business through its main office located in San Juan, Puerto Rico, forty-eight full service banking branches in Puerto Rico, fourteen branches in the USVI and the BVI and ten branches in the State of Florida.

In addition to the banking operations of FirstBank, we provide, through directly or indirectly owned subsidiaries, small loan origination services in Puerto Rico and the USVI, residential mortgage loan origination services, local municipal bond underwriting services and insurance services in Puerto Rico and the USVI.

BUSINESS SEGMENTS

We have six operating segments: Commercial and Corporate Banking, Mortgage Banking, Consumer (Retail) Banking and Treasury and Investments in Puerto Rico; United States Operations; and Virgin Islands Operations. Each of our six operating segments is described below:

Commercial and Corporate Banking

The Commercial and Corporate Banking segment consists of our lending and other services across a broad spectrum of industries ranging from small businesses to large corporate clients. FirstBank has developed expertise in industries including healthcare, tourism, financial institutions, food and beverage, income-producing real estate

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and the public sector. The Commercial and Corporate Banking segment offers commercial loans, including commercial real estate (CRE) and construction loans, and other products such as cash management and business management services. A substantial portion of this portfolio is secured by the underlying value of the real estate collateral and personal guarantees of the borrowers.

Mortgage Banking

The Mortgage Banking segment conducts its operations mainly through FirstBank and its mortgage origination subsidiary, FirstMortgage, Inc (FirstMortgage). These operations consist of the origination, sale and servicing of a variety of residential mortgage loans products. Originations are sourced through different channels such as FirstBank branches, mortgage bankers and in association with new project developers. FirstMortgage focuses on originating residential real estate loans, some of which conform to Federal Housing Administration (FHA), Veterans Administration (VA) and Rural Development (RD) standards. Loans originated that meet FHA standards qualify for FHA s insurance program whereas loans that meet VA and RD standards are guaranteed by their respective federal agencies.

The Mortgage Banking segment also acquires and sells mortgages in the secondary markets. More than 90% of FirstBank s residential mortgage loan portfolio consists of fixed-rate, fully amortizing, full documentation loans. FirstBank is not actively engaged in offering negative amortization loans or option adjustable rate mortgage loans.

Consumer (Retail) Banking

The Consumer (Retail) Banking segment consists of our consumer lending and deposit-taking activities conducted mainly through FirstBank s branch network and loan centers in Puerto Rico. Loans to consumers include auto, boat and personal loans and lines of credit. Deposit products include interest bearing and non-interest bearing checking and savings accounts, individual retirement accounts and retail certificates of deposit (CDs). Retail deposits gathered through each branch of FirstBank s retail network serve as one of the funding sources for its lending and investment activities. Credit card accounts are issued under FirstBank s name through an alliance with a nationally recognized financial institution, which bears the credit risk.

Treasury and Investments

The Treasury and Investments segment is responsible for our treasury and investment management functions. In the treasury function, which includes funding and liquidity management, the Treasury and Investments segment sells funds to the Commercial and Corporate Banking segment, the Mortgage Banking segment and the Consumer (Retail) Banking segment to finance their respective lending activities and purchases funds gathered by those segments.

United States Operations

The United States Operations segment consists of all banking activities conducted by FirstBank in the U.S. mainland. FirstBank provides a wide range of banking services to individual and corporate customers primarily in southern Florida through its ten branches and two specialized lending centers. Our success in attracting core deposits in Florida has enabled us to become less dependent on brokered deposits. The United States Operations segment offers an array of both retail and commercial banking products and services. Consumer banking products include checking, savings and money market accounts, retail CDs, internet banking services, residential mortgages, home equity loans and lines of credit, automobile loans and credit cards through an alliance with a nationally recognized financial institution, which bears the credit risk.

The commercial banking services include checking, savings and money market accounts, CDs, internet banking services, cash management services, remote data capture and automated clearing house, or ACH, transactions. Loan products include the traditional commercial and industrial (C&I) and CRE products, such as lines of credit, term loans and construction loans.

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Virgin Islands Operations

The Virgin Islands Operations segment consists of all banking activities conducted by FirstBank in the USVI and BVI, including retail and commercial banking services, with a total of fourteen branches serving St. Thomas, St. Croix, St. John, Tortola and Virgin Gorda. The Virgin Islands Operations segment is driven by its consumer, commercial lending and deposit-taking activities. Since 2005, FirstBank has been the largest bank in the USVI as measured by total assets.

CURRENT SITUATION

Like many financial institutions across the U.S., our operations have been adversely affected by sustained adverse economic conditions that have affected Puerto Rico and the U.S. The economy in Puerto Rico continues to be challenging, although the year-over-year economic activity and recent employment increases in the services, financial activities and tourism industries suggest some improvement. The Government Development Bank for Puerto Rico Economic Activity Index (GDB-EAI), which is a coincident index consisting of four major monthly economic indicators, namely total payroll employment, total electric power consumption, cement sales and gas consumption, monitors the actual trend of Puerto Rico's economy. The GDB-EAI showed a slowing of the rate of contraction of Puerto Rico's economy in the six-month period ended June 30, 2010 as compared to the six-month period ended June 30, 2009, but the results for July 2010 showed a decline in the year-over-year growth rate after five consecutive months of improvement. These results are similar to the trend observed in the national economy for the month of July 2010.

The adverse economic conditions have negatively affected our capital position and reduced our profitability, particularly as a result of the dramatic reductions in the underlying collateral values of real estate for our secured loans. Since the beginning of 2009, we have taken a number of steps to enable us to emerge from the current adverse economic conditions as a stronger organization:

Capital Ratios. As of June 30, 2010, FirstBank's capital ratios exceeded the minimum established capital ratios required for a well-capitalized depository institution, with approximately \$355 million and \$695 million of capital in excess of that required to satisfy the minimum ratios for total capital to risk-weighted assets and Tier 1 capital to risk-weighted assets, respectively. We recently completed an offer to exchange newly issued shares of our common stock for any and all of the issued and outstanding shares of Noncumulative Perpetual Monthly Income Preferred Stock, Series A through E, and an exchange of shares of our Series F Preferred Stock (as defined below) that we previously had sold to the United States Department of the Treasury (the U.S. Treasury), plus dividends accrued thereon, for shares of Series G Preferred Stock (as defined below). See Our Strategy Strengthen our Capital Position. The exchange offer improved the quality of our capital position by substantially increasing tangible common equity and enhanced our ability to meet any new capital requirements. As of June 30, 2010, on a pro forma basis after giving effect to the exchange offer and the exchange of Series F Preferred Stock for Series G Preferred Stock, our Tier 1 common equity to risk-weighted assets ratio would increase from 2.86% as of June 30, 2010 on an as reported basis to 6.93% and our tangible common equity to tangible assets ratio would increase from 2.57% as of June 30, 2010 on an as reported basis to 5.40%. See Regulatory and Other Capital Ratios and Non-GAAP Data. Further, we believe the completion of the exchange offer improves our ability to operate in the current economic environment, access the capital markets to fund strategic initiatives or other business needs and absorb any future credit losses.

Regulatory Agreements. On June 4, 2010, we announced that FirstBank had agreed to a Consent Order (the Order) issued by the FDIC and OCIF, dated as of June 2, 2010, and we had entered into a Written Agreement with the Federal Reserve, dated as of June 3, 2010 (the Written Agreement and collectively with the Order, the Agreements). The Agreements require us and FirstBank to take certain actions to, among other things,

develop and adopt plans to attain certain capital levels and reduce non-performing and classified assets that have impacted FirstBank's financial condition and performance. We have submitted our capital plan setting forth how we plan to improve our capital positions to comply with the above mentioned Agreements over time. Specifically, the capital plan

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details how we will achieve a total capital to risk-weighted assets ratio of at least 12%, a Tier 1 capital to risk-weighted assets ratio of at least 10% and a leverage ratio of at least 8%. In addition to the capital plan, we have submitted to our regulators a liquidity and brokered deposit plan, including a contingency funding plan, a non-performing asset reduction plan, a budget and profit plan, a strategic plan and a plan for the reduction of classified and special mention assets. Further, we have reviewed and enhanced our loan review program, various credit policies, our treasury and investments policy, our asset classification and allowance for loan and lease losses and non-accrual policies, our charge-off policy and our appraisal program. The Agreements also require the submission to the regulators of quarterly progress reports.

Deleverage. We have deleveraged our balance sheet in order to preserve capital, principally by selling investments and reducing the size of the loan portfolio. Significant decreases in assets have been achieved mainly through the non-renewal of matured commercial loans, such as temporary loan facilities to the Puerto Rico government, and through the charge-off of portions of loans deemed uncollectible. In addition, a reduced volume of loan originations has contributed to this deleveraging strategy.

During the first half of 2010, we reduced our investment portfolio by approximately \$284 million, while our loan portfolio decreased by \$1.3 billion. The net reduction in securities and loans has reduced our total assets to \$18.1 billion as of June 30, 2010, a decrease of \$1.5 billion from December 31, 2009. This decrease in securities and loans allowed a reduction of \$1.9 billion in wholesale funding as of June 30, 2010, including repurchase agreements, advances, and brokered CDs.

Furthermore, during July and August of 2010, we achieved an additional reduction of \$1.3 billion in investment securities mostly as a result of a balance sheet repositioning strategy that resulted in the sale during August of \$1.2 billion in investment securities combined with the early termination of repurchase agreements, which, given the yield and cost combination of the instruments, eliminated assets that were providing no positive marginal contribution to earnings.

Asset Quality. We have strengthened our processes to enhance asset quality through the implementation of stricter loan approval processes. In addition, the responsibilities of our Special Assets Group, which reports directly to our chief executive officer, have been expanded to include management of all activities related to our classified credits and non-performing assets for the commercial business with the purpose of improving their quality or disposing of the assets. See Our Strategy Improve our Profitability. Our Special Assets Group focuses on strategies for the accelerated reduction of non-performing assets through note sales, troubled debt restructurings, loss mitigation programs, sales of real estate owned and sales of loans through special purpose vehicles. In addition to the management of the resolution process for problem loans, the Special Assets Group oversees collection efforts for all loans to prevent migration to the non-performing and or classified status. Therefore, the Special Assets Group not only implements a remediation strategy, but also provides preventive oversight at a corporate level to reduce non-performing migration trends within the commercial loan portfolio.

As a result of these strategies, FirstBank has reduced delinquencies within the 30 to 89 days past due range and the level of non-performing loans as of June 30, 2010, when compared to the first quarter of 2010. Total non-performing loans decreased by \$88.7 million to \$1.55 billion when compared to \$1.64 billion as of March 31, 2010. This decrease resulted from the sale of non-performing loans, charge-off activity and a reduction in the migration of loans to non-accrual status. This decrease was reflected in all three geographic areas in which FirstBank operates. During the first half of 2010, we sold non-performing assets totaling approximately \$115.5 million, which includes \$88.4 million of non-performing loans, and \$27.1 million of real estate owned properties.

Our entire construction portfolio has been transferred to the Special Assets Group and is in the workout phase. Strategies are being implemented to expedite the resolution of problem loans through restructurings, note sales and

short sales, among others. The portfolio is increasingly moving

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into the project completion phase. During July and August of 2010, \$84.4 million of construction loans were converted to CRE loans, of which \$78 million have Puerto Rico government guarantees. We expect additional conversions of construction loans to commercial loans or CRE loans in the amounts of \$9.8 million in the fourth quarter of 2010 and \$133.1 million in 2011. Absorption rates on residential construction projects in Puerto Rico, that is, the rates at which newly constructed units are sold, have increased for the third consecutive quarter from 6% in the third quarter of 2009 to 11% in the fourth quarter of 2009 to 17% in the first quarter of 2010 and to 18% in the second quarter of 2010. As a key initiative to increase the absorption rate in residential construction projects, we have engaged in discussions with developers to review the sales strategies and to reduce the sale price per unit. In addition, we believe that absorption rate may increase as a result of recent legislation enacted in Puerto Rico. In September, the Puerto Rico government enacted a housing stimulus package that provides various incentives to buyers of residences in Puerto Rico. See Recent Developments. With respect to non-performing residential construction loans, we are providing mortgage financing incentives for buyers of the units.

The United States Operations segment has also had success in substantially reducing its construction loan portfolio and the level of non-performing assets. The construction portfolio in Florida has been reduced to \$192 million as of June 30, 2010 from \$981 million as of June 30, 2006 when construction lending in this segment was halted. Non-performing assets in Florida decreased by \$99 million, or 26%, from \$384 million as of December 31, 2009 to \$285 million as of June 30, 2010.

With respect to the residential mortgage portfolio, delinquencies appear to be stabilizing. Residential mortgages originated during 2004 through 2008 are starting to reflect a reduction in delinquencies that are 30 days past due. As part of its asset quality initiatives for the residential mortgage portfolio, FirstBank developed a loss mitigation program in 2007 focused on providing homeownership preservation assistance. In 2010, FirstBank expanded the loss mitigation program, dedicated additional personnel and engaged a third party to further expand our resources in this area.

With respect to the consumer loan portfolio, performance of the portfolio has been stable since 2008. We continue to believe that this portfolio will remain stable.

Corporate Governance. We reorganized our management structure to better implement and execute our business strategies. In addition, since September of 2009 we have an independent chairman who is separate from the chief executive officer. Two new committees at the board level, a Strategic Planning Committee and a Compliance Committee, were established to provide ongoing monitoring of business strategies, financial targets and corporate objectives as well as compliance with regulatory Agreements.

We believe that these steps, together with our established, integrated and geographically diverse network, position us to emerge from the current adverse economic conditions as a stronger organization.

QUALITY OF LOAN PORTFOLIO

Loan Reviews

We regularly perform internal assessments of all loan portfolios. Our internal loan review unit (Loan Review) assesses a variety of factors, including the soundness of the loan structure, the value of the underlying collateral, the ability of the primary borrower to repay the debt as contracted, the accuracy of the risk ratings and the adherence to FirstBank's policies. Loan Review is an independent function and, as such, reports to the audit committee of our board of directors. Loan Review applies a risk-based approach in selecting commercial loans for review purposes. The scope of our annual plan to internally review loans, which is designed to include a representative mix of our commercial loan portfolio, encompasses nearly 65% of our total commercial loan portfolio as measured in dollars. The annual plan

contemplates the quarterly review of those loans classified as special mention or worse and/or in non-accrual status and an annual review. The review of the retail credit portfolio (consumer, auto and mortgage loan portfolios) is accomplished

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through assessments performed by the Quality Assurance units (Quality Assurance) over a sample of loans. Quality Assurance assesses compliance with FirstBank's retail credit policies and procedures, including documentation, and applicable laws and regulations. We believe that our loan review process is consistent with the requirement in the Order that FirstBank operate under an adequate and effective program of independent loan review.

In addition to our ongoing internal assessment of our loan portfolio, since October 2007 we have engaged an external loan review firm to review our Florida loan portfolio on a semi-annual basis. This firm typically reviews approximately 60% to 75% of our commercial loan portfolio in Florida, which includes construction, C&I and CRE loans and was \$688 million in size at June 30, 2010. These loan reviews are designed to verify the accuracy of our internal risk-grading process and compliance with our loan policy and regulatory and accounting guidelines.

Stress Testing Analysis

For the last four years, FirstBank's operations have been adversely affected by sustained adverse economic conditions as a result of the recessionary environment in Puerto Rico, the Virgin Islands and the mainland U.S. During this period, FirstBank's loan portfolios have deteriorated as reflected in the significant reductions in collateral values and the higher delinquencies resulting from the reduced income generation capacity of its borrowers. We have conducted a detailed portfolio level credit stress test that assumes an economic outlook that is more adverse than the current environment, adjusted for the particular characteristics of our loan portfolio and markets in which we operate. Our analysis was generally consistent with the guidelines utilized for the Supervisory Capital Assessment Program (SCAP) analysis, which was intended to measure the financial strength of the nation's 19 largest financial institutions on a going forward basis. The 19 financial institutions were asked to project potential losses over a two-year period, however, our analysis projected losses over longer periods, as described below.

With respect to the residential mortgage portfolio, the analysis was performed by a third party consulting firm based on market information from such firm's database and FirstBank's portfolio specific information provided by management. With our concurrence, the consultants used risk characteristics of the portfolio such as historical loss migration by region, vintage, rank and credit scores to analyze the performance of the portfolio at the individual loan level. These factors were analyzed under the assumption of a continued recessionary environment where there is a prolonged decline in the House Price Index (HPI) and foreclosures are approximately 5% compared to the current 3.1% level. HPI was stressed by applying an additional reduction from current price levels of 20% in year one, 10% in year two and 5% in year three, leveling off in year four and with a 3% recovery in year five. The model also provided for risk adjusted prepayment curves, default curves and loss severity curves. Management believes that the cumulative effect of the additional reduction in HPI in addition to the reductions that have already been experienced in our markets applied a significant level of stress to the portfolio.

With respect to the construction, CRE and C&I portfolios, we performed a stress test with the assistance of a consultant by applying stress factors, as described below, to a representative sample of loans from FirstBank's respective loan portfolios in Puerto Rico. The statistical sample selection achieved a 95% confidence level with a 5% margin of error. The resulting coverage of the sample, measured in dollars, was 34% of the construction portfolio, 43% of the CRE portfolio and 15% of the C&I portfolio. The results obtained on the tested samples were then applied by FirstBank's credit risk group to the overall loan portfolios.

For the construction portfolio, severity was measured by reducing absorption rates by 50% and property selling prices by 40% from those reflected on recent appraisals. For land loans, recent appraised collateral values were reduced by 35%. In the case of CRE loans secured by income producing properties, vacancy rates were increased to 25% coupled with the loss of the anchor tenant, and, for owner occupied properties, net operating income was reduced by 25%. For C&I loans, the severity factor was applied by reducing borrowers' current net operating income by 25% and applying haircuts to existing collateral values between 10% and

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50%, depending on the type of collateral. In the event the collateral on the loans included real estate properties, we applied a haircut of 20% to the appraised value with respect to appraisals older than two years at the time of the analysis. Loss factors were computed based on the deficiency reflected on all sampled loans where debt service coverage fell below 1.15x under the above stressed conditions. For the loan portfolios described herein, the appraisal, net operating income and vacancy rates information used for the stress analysis consisted of the most recent information available as of the third quarter of 2009 when the detailed testing of the sample was performed.

With respect to the consumer portfolio, which consists mostly of personal and auto loans, the stress analysis was performed internally by increasing the current loss rates by the worst percentage loss rate change experienced by FirstBank on each product type between 2005 through 2009 and generally an additional 20% related to bankruptcy increases. FirstBank does not have any credit card receivables and home equity loans amounted to only \$29 million, or less than 2% of the consumer loan portfolio, as of June 30, 2010.

Presented below is a comparison of FirstBank's stress test loss factors on the more adverse loss scenario described above as compared to the average of the highest and lowest SCAP factors of the institutions tested:

	FirstBank's more adverse loss factor	Average of SCAP loss factor range on the more adverse⁽¹⁾
Residential Mortgage	9.51%	11.51%
Construction	51.28%	16.50%
CRE	19.09%	8.00%
C&I	7.35%	6.50%
Consumer	10.23%	10.00%

(1) Average of high/low cumulative two-year loss factors

The application of FirstBank's more adverse loss factors to the gross outstanding loan portfolios as of June 30, 2010 would represent additional losses of approximately \$1.5 billion over the next two to five years, in excess of the charge-offs we have already taken. Losses on the residential mortgage portfolio were estimated over five years while consumer losses were based on the average life of the portfolio, which approximates two and a half years. Construction, CRE and C&I losses are mostly expected to occur over two years. These losses are not considered forecasts of expected losses but a calculation of the loss impact on the loan portfolio based on a hypothetical exercise which assumes that market financial conditions deteriorate to the levels considered in the more adverse stress factors.

As of June 30, 2010, we had a total capital ratio of 13.35%, a Tier I capital ratio of 12.05% and a leverage ratio of 8.14%. We believe that the likelihood of the level of loan losses projected in the more adverse economic scenario is remote. Notwithstanding this view, we used stress testing to gauge the amount of regulatory capital that would be required in the event that the more adverse conditions were to prevail. In performing this analysis, we considered the current level of pre-tax, pre-provision earnings, the portion of the \$604 million in allowance for loan losses as of June 30, 2010 available to absorb losses after allocating a normalized reserve level to the remaining loan portfolio, the time it would take for the losses to occur and the current level of capital. If we adjust our pro forma and as adjusted capital ratios as of June 30, 2010 disclosed in the section Regulatory and Other Capital Ratios, which give effect to the additional \$500 million in capital from this offering, to reflect three years of the annualized 2010 level of pre-tax,

pre-provision earnings, the assumed additional \$1.5 billion of losses and the allocation of a portion of our allowance, our adjusted pro forma and as adjusted capital ratios would exceed currently established regulatory well-capitalized capital ratio requirements.

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OUR STRATEGY

We developed and have been implementing a strategy to strengthen our capital position and improve our profitability, which have been adversely affected over the past few years as a result of the sustained adverse economic conditions that have affected Puerto Rico and the U.S. To implement this strategy, we have modified our business model to respond to economic conditions and to maintain our business on a sound course. We have undergone an extensive strategic exercise that has enabled us to identify opportunities to stabilize portfolios and increase revenues. The challenges ahead and current economic conditions mandate this new focus.

Since late 2009, we have developed and pursued a strategic plan that includes the following key features:

capital preservation and optimization through the implementation of capital restructuring initiatives;

enhanced and proactive management action plans on all loan portfolios across the entire credit cycle to improve asset quality, with the expectation of increased spreads and reduced portfolio risk;

heightened efforts to grow core deposits and reduce dependency on brokered deposits, including increasing deposit growth through network optimization and core deposit penetration in commercial loan and government customers and in Florida and the Virgin Islands, which provide an additional source of funds to increase core deposits;

initiatives to increase non-interest income through insurance fees and transaction banking services, among other things;

initiatives to increase margins and loan yields through pricing rationalization; and

continued operating efficiency improvements and expense reduction by expanding the specific initiatives and enhancing our technological infrastructure through targeted investments.

We believe that the recent consolidation of the Puerto Rico banking market provides a significant opportunity for us to grow organically and to capture market share as a wide gap currently exists between the market share leader and other banks in Puerto Rico. Given our franchise strengths and proven track record of growing organically, we are confident that we will capitalize on these opportunities and solidify our position in Puerto Rico. Our competitive strengths, which we believe will enable us to successfully implement our strategic plan and to accomplish these goals, and further details about our strategy are set forth below.

Our competitive strengths have enabled us to deliver positive pre-tax, pre-provision earnings during the past five years although we have had GAAP losses since 2009. See Non-GAAP Data. These strengths include:

our position as the second largest financial holding company in Puerto Rico and as the largest bank in the USVI as measured by total assets as of June 30, 2010;

FirstBank's recognized brand in Puerto Rico and the Virgin Islands, with consistent execution of a banking strategy focused on customer satisfaction and personalized service in both retail and commercial operations;

a well-diversified operation with a wide range of financial services, including a diversified portfolio of products and services and over 630,000 retail and commercial customers who enable FirstBank to continue to grow and who provide FirstBank with opportunities to cross-sell its products;

an ability to attract new customers and to cross-sell products due to its strong market share in retail deposits, commercial lending, automobile lending, finance leasing, personal loans and small loans;

a high-quality technology and operating infrastructure that supports our customer focus while maintaining non-interest expenses at an efficient level;

an experienced management team; and

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FirstBank's established, integrated and geographically diverse network of branches, offices and service centers that are located in Puerto Rico, the Virgin Islands and Florida.

Our specific strengths as of June 30, 2010 by geographic area are described below in further detail:

Puerto Rico

a strong diversified franchise with 48 bank branches located throughout much of the island of Puerto Rico;

an attractive business mix with substantial market share, ranking second in total loans and third in total deposits net of brokered CDs;

a proven track record of organic growth and a core deposit growth strategy that has driven a \$888.9 million, or 38%, increase in core deposits since December 31, 2007; and

assets of \$15.2 billion representing 84% of our total assets.

Virgin Islands

a strong market position with market share in excess of 40% and limited competition;

14 branches serving St. Thomas, St. Croix, St. John, Tortola and Virgin Gorda;

an attractive customer and business segment mix, skewed more towards mass affluent retail customers and retail-oriented businesses; and

asset