

POPULAR INC
Form 10-Q
November 08, 2018
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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**

Commission File Number: 001-34084

POPULAR, INC.

(Exact name of registrant as specified in its charter)

Puerto Rico
(State or other jurisdiction of
Incorporation or organization)

66-0667416
(IRS Employer
Identification Number)

Popular Center Building

209 Muñoz Rivera Avenue

Hato Rey, Puerto Rico
(Address of principal executive offices)

00918
(Zip code)

(787) 765-9800

(Registrant's telephone number, including area code)

NOT APPLICABLE

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

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

Indicate by check mark whether the registrant has submitted electronically every Interactive Data File required to be submitted 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 such files). Yes No

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

Large accelerated filer

Accelerated filer

Non-accelerated filer

Smaller reporting company

Emerging growth company

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

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

Indicate the number of shares outstanding of each of the issuer's classes of common stock, as of the latest practicable date: Common Stock, \$0.01 par value, 100,352,514 shares outstanding as of November 5, 2018.

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Forward-Looking Information

This Form 10-Q contains forward-looking statements within the meaning of the U.S. Private Securities Litigation Reform Act of 1995, including, without limitation, statements about Popular Inc.'s (the Corporation, Popular, we, our) business, financial condition, results of operations, plans, objectives and future performance. These statements are not guarantees of future performance, are based on management's current expectations and, by their nature, involve risks, uncertainties, estimates and assumptions. Potential factors, some of which are beyond the Corporation's control, could cause actual results to differ materially from those expressed in, or implied by, such forward-looking statements. Risks and uncertainties include without limitation the effect of competitive and economic factors, and our reaction to those factors, the adequacy of the allowance for loan losses, delinquency trends, market risk and the impact of interest rate changes, capital markets conditions, capital adequacy and liquidity, the effect of legal proceedings and new accounting standards on the Corporation's financial condition and results of operations, and the impact of Hurricanes Irma and María on the Corporation. All statements contained herein that are not clearly historical in nature are forward-looking, and the words anticipate, believe, continues, expect, estimate, intend, project and similar and future or conditional verbs such as will, would, should, could, might, can, may or similar expressions generally intended to identify forward-looking statements.

Various factors, some of which are beyond Popular's control, could cause actual results to differ materially from those expressed in, or implied by, such forward-looking statements. Factors that might cause such a difference include, but are not limited to:

the rate of growth in the economy and employment levels, as well as general business and economic conditions in the geographic areas we serve;

the impact of the current fiscal and economic crisis of the Commonwealth of Puerto Rico (the Commonwealth or Puerto Rico) and the measures taken and to be taken by the Puerto Rico Government and the Federally-appointed oversight board on the economy, our customers and our business;

the impact of the pending debt restructuring proceedings under Title III of the Puerto Rico Oversight, Management and Economic Stability Act (PROMESA) and of other actions taken or to be taken to address Puerto Rico's fiscal crisis on the value of our portfolio of Puerto Rico government securities and loans to governmental entities and private borrowers that have relationships with the government, and the possibility that these actions may result in credit losses that are higher than currently expected;

the impact of Hurricanes Irma and Maria, and the measures taken to recover from these hurricanes (including the availability of relief funds and insurance proceeds), on the economy of Puerto Rico, the U.S. Virgin Islands and the British Virgin Islands, and on our customers and our business;

changes in interest rates and market liquidity, which may reduce interest margins, impact funding sources and affect our ability to originate and distribute financial products in the primary and secondary markets;

the fiscal and monetary policies of the federal government and its agencies;

changes in federal bank regulatory and supervisory policies, including required levels of capital and the impact of proposed capital standards on our capital ratios;

the impact of the Dodd-Frank Wall Street Reform and Consumer Protection Act (the Dodd-Frank Act) on our businesses, business practices and cost of operations;

regulatory approvals that may be necessary to undertake certain actions or consummate strategic transactions such as acquisitions and dispositions;

the ability to successfully integrate the auto finance business acquired from Wells Fargo & Company, as well as unexpected costs, including, without limitation, costs due to exposure to any unrecorded liabilities or issues not identified during the due diligence investigation of the business or that are not subject to indemnification or reimbursement, and risks that the business may suffer as a result of the transaction, including due to adverse effects on relationships with customers, employees and service providers;

the relative strength or weakness of the consumer and commercial credit sectors and of the real estate markets in Puerto Rico and the other markets in which borrowers are located;

the performance of the stock and bond markets;

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competition in the financial services industry;

additional Federal Deposit Insurance Corporation (FDIC) assessments;

possible legislative, tax or regulatory changes; and

a failure in or breach of our operational or security systems or infrastructure or those of EVERTEC, Inc., our provider of core financial transaction processing and information technology services, as a result of cyberattacks, including e-fraud, denial-of-services and computer intrusion, that might result in loss or breach of customer data, disruption of services, reputational damage or additional costs to Popular.

Other possible events or factors that could cause results or performance to differ materially from those expressed in these forward-looking statements include the following:

negative economic conditions, including as a result of Hurricanes Irma and Maria, that adversely affect housing prices, the job market, consumer confidence and spending habits which may affect, among other things, the level of non-performing assets, charge-offs and provision expense;

changes in market rates and prices which may adversely impact the value of financial assets and liabilities;

liabilities resulting from litigation and regulatory investigations;

changes in accounting standards, rules and interpretations;

our ability to grow our core businesses;

decisions to downsize, sell or close units or otherwise change our business mix; and

management's ability to identify and manage these and other risks.

Moreover, the outcome of legal proceedings, as discussed in Part II, Item I. Legal Proceedings, is inherently uncertain and depends on judicial interpretations of law and the findings of regulators, judges and/or juries. Investors should refer to the Corporation's Annual Report on Form 10-K for the year ended December 31, 2017 as well as Part II, Item 1A of this Form 10-Q for a discussion of such factors and certain risks and uncertainties to which the Corporation is subject.

All forward-looking statements included in this Form 10-Q are based upon information available to Popular as of the date of this Form 10-Q and, other than as required by law, including the requirements of applicable securities laws, we assume no obligation to update or revise any such forward-looking statements or information which speak as of their

respective dates.

Table of Contents**POPULAR, INC.****CONSOLIDATED STATEMENTS OF FINANCIAL CONDITION****(UNAUDITED)**

(In thousands, except share information)	September 30, 2018	December 31, 2017
Assets:		
Cash and due from banks	\$ 400,949	\$ 402,857
Money market investments:		
Time deposits with other banks	4,609,061	5,255,119
Total money market investments	4,609,061	5,255,119
Trading account debt securities, at fair value:		
Pledged securities with creditors right to repledge	600	625
Other trading securities	37,131	33,301
Debt securities available-for-sale, at fair value:		
Pledged securities with creditors right to repledge	295,437	393,634
Other investment securities available-for-sale	12,752,180	9,783,289
Debt securities held-to-maturity, at amortized cost (fair value 2018 - \$105,074; 2017 - \$97,501)	101,238	107,019
Equity securities (realizable value 2018 -\$162,741); (2017 - \$168,417)	157,962	165,103
Loans held-for-sale, at lower of cost or fair value	51,742	132,395
Loans held-in-portfolio:		
Loans not covered under loss-sharing agreements with the FDIC	26,661,951	24,423,427
Loans covered under loss-sharing agreements with the FDIC		517,274
Less Unearned income	149,783	130,633
Allowance for loan losses	633,718	623,426
Total loans held-in-portfolio, net	25,878,450	24,186,642
FDIC loss-share asset		45,192
Premises and equipment, net	557,104	547,142
Other real estate not covered under loss-sharing agreements with the FDIC	133,780	169,260
Other real estate covered under loss-sharing agreements with the FDIC		19,595
Accrued income receivable	163,443	213,844
Mortgage servicing assets, at fair value	162,779	168,031
Other assets	1,900,850	1,991,323
Goodwill	687,536	627,294
Other intangible assets	29,186	35,672
Total assets	\$ 47,919,428	\$ 44,277,337

Liabilities and Stockholders Equity		
Liabilities:		
Deposits:		
Non-interest bearing	\$ 8,803,752	\$ 8,490,945
Interest bearing	30,845,075	26,962,563
Total deposits	39,648,827	35,453,508
Assets sold under agreements to repurchase	300,116	390,921
Other short-term borrowings	1,200	96,208
Notes payable	1,744,687	1,536,356
Other liabilities	980,249	1,696,439
Total liabilities	42,675,079	39,173,432
Commitments and contingencies (Refer to Note 22)		
Stockholders equity:		
Preferred stock, 30,000,000 shares authorized; 2,006,391 shares issued and outstanding	50,160	50,160
Common stock, \$0.01 par value; 170,000,000 shares authorized; 104,304,529 shares issued (2017 - 104,238,159) and 100,336,341 shares outstanding (2017 - 102,068,981)	1,043	1,042
Surplus	4,281,515	4,298,503
Retained earnings	1,629,692	1,194,994
Treasury stock - at cost, 3,968,188 shares (2017 - 2,169,178)	(183,872)	(90,142)
Accumulated other comprehensive loss, net of tax	(534,189)	(350,652)
Total stockholders equity	5,244,349	5,103,905
Total liabilities and stockholders equity	\$ 47,919,428	\$ 44,277,337

The accompanying notes are an integral part of these Consolidated Financial Statements.

Table of Contents**POPULAR, INC.****CONSOLIDATED STATEMENTS OF OPERATIONS****(UNAUDITED)**

(In thousands, except per share information)	Quarters ended September 30,		Nine months ended September 30,	
	2018	2017	2018	2017
Interest income:				
Loans	\$ 430,637	\$ 371,979	\$ 1,190,498	\$ 1,102,784
Money market investments	27,581	15,529	86,258	33,233
Investment securities	70,147	48,375	185,537	144,594
Total interest income	528,365	435,883	1,462,293	1,280,611
Interest expense:				
Deposits	55,134	37,058	139,050	104,907
Short-term borrowings	1,622	1,524	5,387	3,734
Long-term debt	20,140	19,130	59,204	57,222
Total interest expense	76,896	57,712	203,641	165,863
Net interest income	451,469	378,171	1,258,652	1,114,748
Provision for loan losses - non-covered loans	54,387	157,659	183,774	249,681
Provision for loan losses - covered loans		3,100	1,730	4,255
Net interest income after provision for loan losses	397,082	217,412	1,073,148	860,812
Service charges on deposit accounts	38,147	39,273	111,704	119,882
Other service fees	64,316	53,481	187,794	168,824
Mortgage banking activities (Refer to Note 11)	11,269	5,239	33,408	27,349
Net gain on sale of debt securities		83		83
Other-than-temporary impairment losses on debt securities				(8,299)
Net gain (loss), including impairment on equity securities	370	20	(42)	201
Net (loss) profit on trading account debt securities	(122)	253	(299)	(680)
Net loss on sale of loans, including valuation adjustments on loans held-for-sale		(420)		(420)
Adjustments (expense) to indemnity reserves on loans sold	(3,029)	(6,406)	(6,482)	(11,302)
FDIC loss-share (expense) income (Refer to Note 29)		(3,948)	94,725	(12,680)
Other operating income	40,070	12,799	78,519	50,078
Total non-interest income	151,021	100,374	499,327	333,036

Operating expenses:

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Personnel costs	139,757	117,769	389,941	358,457
Net occupancy expenses	18,602	22,254	63,829	65,295
Equipment expenses	18,303	16,457	53,284	48,677
Other taxes	11,923	10,858	33,701	32,567
Professional fees	83,860	70,772	260,748	212,956
Communications	6,054	5,394	17,342	17,242
Business promotion	15,478	15,216	44,265	40,158
FDIC deposit insurance	8,610	6,271	22,534	18,936
Other real estate owned (OREO) expenses	7,950	11,724	21,028	41,212
Other operating expenses	52,576	38,028	111,462	92,707
Amortization of intangibles	2,324	2,345	6,973	7,034
Total operating expenses	365,437	317,088	1,025,107	935,241
Income before income tax	182,666	698	547,368	258,607
Income tax expense (benefit)	42,018	(19,966)	35,613	48,772
Net Income	\$ 140,648	\$ 20,664	\$ 511,755	\$ 209,835
Net Income Applicable to Common Stock	\$ 139,718	\$ 19,734	\$ 508,963	\$ 207,043
Net Income per Common Share Basic	\$ 1.38	\$ 0.19	\$ 5.01	\$ 2.03
Net Income per Common Share Diluted	\$ 1.38	\$ 0.19	\$ 5.00	\$ 2.03

The accompanying notes are an integral part of these Consolidated Financial Statements.

Table of Contents**POPULAR, INC.****CONSOLIDATED STATEMENTS OF COMPREHENSIVE INCOME****(UNAUDITED)**

(In thousands)	Quarters ended, September 30,		Nine months ended, September 30,	
	2018	2017	2018	2017
Net income	\$ 140,648	\$ 20,664	\$ 511,755	\$ 209,835
Reclassification to retained earnings due to cumulative effect of accounting change			(605)	
Other comprehensive (loss) income before tax:				
Foreign currency translation adjustment	(605)	(390)	(3,968)	(1,839)
Amortization of net losses of pension and postretirement benefit plans	5,386	5,606	16,157	16,819
Amortization of prior service credit of pension and postretirement benefit plans	(868)	(950)	(2,603)	(2,850)
Unrealized holding (losses) gains on debt securities arising during the period	(43,781)	9,180	(201,193)	14,912
Other-than-temporary impairment included in net income				8,299
Reclassification adjustment for gains included in net income		(83)		(83)
Unrealized holding gains on equity securities arising during the period		60		225
Reclassification adjustment for gains included in net income		(20)		(201)
Unrealized net gains (losses) on cash flow hedges	341	(410)	1,296	(1,424)
Reclassification adjustment for net losses (gains) included in net income	147	232	(870)	2,122
Other comprehensive (loss) income before tax	(39,380)	13,225	(191,786)	35,980
Income tax benefit (expense)	1,983	(1,614)	8,249	(7,026)
Total other comprehensive (loss) income, net of tax	(37,397)	11,611	(183,537)	28,954
Comprehensive income, net of tax	\$ 103,251	\$ 32,275	\$ 328,218	\$ 238,789

Tax effect allocated to each component of other comprehensive (loss) income:

(In thousands)	Quarters ended September 30,		Nine months ended, September 30,	
	2018	2017	2018	2017
Amortization of net losses of pension and postretirement benefit plans	\$ (2,101)	\$ (2,185)	\$ (6,301)	\$ (6,556)

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Amortization of prior service credit of pension and postretirement benefit plans	339	370	1,016	1,110
Unrealized holding (losses) gains on debt securities arising during the period	3,936	122	13,701	239
Other-than-temporary impairment included in net income				(1,559)
Reclassification adjustment for gains included in net income		17		17
Unrealized holding gains on equity securities arising during the period		(12)		(45)
Reclassification adjustment for gains included in net income		4		40
Unrealized net gains (losses) on cash flow hedges	(133)	160	(506)	555
Reclassification adjustment for net losses (gains) included in net income	(58)	(90)	339	(827)
Income tax benefit (expense)	\$ 1,983	\$ (1,614)	\$ 8,249	\$ (7,026)

The accompanying notes are an integral part of the Consolidated Financial Statements.

Table of Contents**POPULAR, INC.****CONSOLIDATED STATEMENTS OF CHANGES IN STOCKHOLDERS EQUITY****(UNAUDITED)**

(In thousands)	Common stock	Preferred stock	Surplus	Retained earnings	Treasury stock	Accumulated other comprehensive loss	Total
Balance at							
December 31, 2016	\$ 1,040	\$ 50,160	\$ 4,255,022	\$ 1,220,307	\$ (8,286)	\$ (320,286)	\$ 5,197,957
Net income				209,835			209,835
Issuance of stock	2		5,513				5,515
Dividends declared:							
Common stock				(76,620)			(76,620)
Preferred stock				(2,792)			(2,792)
Common stock purchases			4,518		(81,936)		(77,418)
Other comprehensive income, net of tax						28,954	28,954
Balance at							
September 30, 2017	\$ 1,042	\$ 50,160	\$ 4,265,053	\$ 1,350,730	\$ (90,222)	\$ (291,332)	\$ 5,285,431
Balance at							
December 31, 2017	\$ 1,042	\$ 50,160	\$ 4,298,503	\$ 1,194,994	\$ (90,142)	\$ (350,652)	\$ 5,103,905
Cumulative effect of accounting change				1,935			1,935
Net income				511,755			511,755
Issuance of stock	1		2,564				2,565
Dividends declared:							
Common stock				(76,200)			(76,200)
Preferred stock				(2,792)			(2,792)
Common stock purchases			(23,020)		(104,423)		(127,443)
Common stock reissuance			143		2,008		2,151
Stock based compensation			3,325		8,685		12,010
Other comprehensive income, net of tax						(183,537)	(183,537)
Balance at							
September 30, 2018	\$ 1,043	\$ 50,160	\$ 4,281,515	\$ 1,629,692	\$ (183,872)	\$ (534,189)	\$ 5,244,349

	September 30, 2018	September 30, 2017
Disclosure of changes in number of shares:		
Preferred Stock:		
Balance at beginning and end of period	2,006,391	2,006,391
Common Stock Issued:		
Balance at beginning of period	104,238,159	104,058,684
Issuance of stock	66,370	138,840
Balance at end of period	104,304,529	104,197,524
Treasury stock	(3,968,188)	(2,171,107)
Common Stock Outstanding	100,336,341	102,026,417

The accompanying notes are an integral part of these Consolidated Financial Statements.

Table of Contents**POPULAR, INC.****CONSOLIDATED STATEMENTS OF CASH FLOWS****(UNAUDITED)**

(In thousands)	Nine months ended September 30,	
	2018	2017
Cash flows from operating activities:		
Net income	\$ 511,755	\$ 209,835
Adjustments to reconcile net income to net cash provided by operating activities:		
Provision for loan losses	185,504	253,936
Amortization of intangibles	6,973	7,034
Depreciation and amortization of premises and equipment	39,083	35,966
Net accretion of discounts and amortization of premiums and deferred fees	(43,533)	(17,371)
Share-based compensation	5,962	
Impairment losses on long-lived assets	272	11,286
Other-than-temporary impairment on debt securities		8,299
Fair value adjustments on mortgage servicing rights	13,123	24,262
FDIC loss share (income) expense	(94,725)	12,680
Adjustments (expense) to indemnity reserves on loans sold	6,482	11,302
Earnings from investments under the equity method, net of dividends or distributions	(14,772)	(11,514)
Deferred income tax (benefit) expense	(97,708)	30,471
Loss (gain) on:		
Disposition of premises and equipment and other productive assets	17,694	5,018
Proceeds from insurance claims	(14,411)	
Sale and valuation adjustments of debt securities		(83)
Sale of loans, including valuation adjustments on loans held-for-sale and mortgage banking activities	(6,734)	(16,455)
Sale of foreclosed assets, including write-downs	(638)	19,228
Acquisitions of loans held-for-sale	(173,644)	(204,813)
Proceeds from sale of loans held-for-sale	51,131	68,326
Net originations on loans held-for-sale	(186,063)	(283,709)
Net decrease (increase) in:		
Trading debt securities	346,455	499,714
Equity securities	(2,480)	(613)
Accrued income receivable	51,868	(8,297)
Other assets	234,836	(1,882)
Net (decrease) increase in:		
Interest payable	(9,933)	(9,299)
Pension and other postretirement benefits obligation	3,392	(13,760)
Other liabilities	(197,035)	15,178

Total adjustments	121,099	434,904
Net cash provided by operating activities	632,854	644,739
Cash flows from investing activities:		
Net increase (decrease) in money market investments	647,519	(2,600,853)
Purchases of investment securities:		
Available-for-sale	(6,968,920)	(2,356,385)
Equity	(11,304)	(23,822)
Proceeds from calls, paydowns, maturities and redemptions of investment securities:		
Available-for-sale	3,925,362	1,225,915
Held-to-maturity	7,184	