CIT Group, Inc.

Q2 2019 CIT Group, Inc. Earnings Conference Call

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CORPORATE PARTICIPANTS

Ellen Alemany - *Chairwoman, Chief Executive Officer*

John Fawcett - *Chief Financial Officer*

Barbara Callahan - *Head of Investor Relations*

PRESENTATION

Operator
Good morning and welcome to CIT's second quarter earnings conference call. My name is Nicole and I will be your operator today. At this time, all participants are in a listen-only mode. There will be a question and answer session later in the call.

To ask a question, you may press Star, then 1 on your telephone keypad. To withdraw your question, please press Star, then 2. If at any time during the call, you require assistance, please press Star 0 and an operator will be happy to assist you.

As a reminder, this conference call is being recorded. I would now like to turn the call over to Barbara Callahan, Head of Investor Relations. Please proceed, ma'am.

Barbara Callahan
Good morning, and welcome to CIT's SECOND QUARTER 2019 earnings conference call. Our call today will be hosted by Ellen Alemany, Chairwoman and CEO; and John Fawcett, our CFO. During this call, we will be referencing a presentation that is available in the Investor Relations section of our website at cit.com.

Our forward-looking statements disclosure and non-GAAP reconciliations are included in today's earnings materials and within our SEC filings. These cover our presentation materials, prepared comments, and the question and answer segment of today's call.

I'll now turn the call over to Ellen Alemany.

Ellen Alemany
Thanks, Barbara. Welcome and thank you for joining the call. I'm pleased to report that we had a solid second quarter. We're making steady progress on the next phase of our strategic plan and delivered $128 million of net income in the second quarter, or $1.33 per share. Tangible book value per share also increased by 3.6 percent as we work to create long term value in CIT.

Let me touch on a few highlights related to our strategic plan that helped to drive performance, which you can see on Slide 2. We continued to grow our core business with average loans and leases up 1 percent compared to last quarter and 8 percent compared to the prior year.

Origination volume was solid across the division with commercial finance and business capital driving overall asset growth. We made continued progress in optimizing our balance sheet through deposit growth, a reduction in wholesale funded debt, and returning additional capital to shareholders.

We grew average consumer deposits in the online bank by more than $2 billion, reduced average secured debt by $1.7 billion, and repurchased $158 million of common shares. As a result, deposits now comprise 85 percent of our total funding, up from 77 percent a year ago. And, 95 percent of our funding in the bank is from deposits.

Our operating efficiency also continued to improve and we achieved a 56 percent efficiency ratio, which is in line with our target. We continued to reduce operating expenses while also balancing investment and technology, which is critical to future marketplace success and our ability to streamline processes and get more efficient scale in the business. Lastly, credit remains strong and we remain disciplined in our underwriting.

We ended the second quarter with a 10.3 percent return on tangible common equity. Let me share a few highlights in the business.

The lending market remains competitive, as it has been for a while now, and we are still being disciplined and winning business. Average loans and leases in the commercial finance division were up 2 percent from last quarter and 10 percent from last year.

We've continued to grow in collateral base lending, where we have strong expertise and can be more selective in the type of deals we do. We also announced an expansion in our asset management capabilities through a managed financing vehicle with an A rated insurance company.

This, like the Northbridge structure, allows us to leverage our origination expertise without committing significant capital and serve a broader network of clients and create fee income. It will take some time to fully ramp up, but we expect the asset management business to be a source of revenue growth for us over time.

CIT Northbridge just completed their largest deal yet earlier this month, where they led a $100 million revolving credit line for an offshore services company that was a referral from our capital equipment business. We see a lot of deals in the market and these new structures allow us to serve a broader range of clients, including those that may not be a fit for our balance sheet.

The business capital division continued to post solid growth in the second quarter, with average loans and leases up 1 percent from the prior quarter and 8 percent from the prior year. There were strong volumes in the equipment financing space, and our differentiated technology offering is a competitive advantage.

Factoring volume is down modestly from last year, but core volumes are up. Across our commercial businesses, customer sentiment generally still feels cautiously optimistic, but it's starting to soften in certain markets, as businesses contemplate trade issues and tight labor markets.

In addition, the Equipment Leasing and Finance Association reduced their growth estimate for 2019. We are watching these and other market factors closely and our approach to assessing risk and growth targets remain unchanged at this time.

Average loans and leases in the real estate division were down 2 percent from the prior quarter and 3 percent from the year ago. While originations were solid in the quarter, pre-payments continued to be a headwind in this space. Our portfolio is performing well as a result of the rigor in our underwriting process and strong client relationships.

Rail core average loans and leases are up 1 percent from last quarter and 2 percent from a year ago. Utilization remains strong and our diverse fleet is an advantage. Some industrial sectors are exhibiting slower growth, which has slowed loadings of certain cars, but we continue to actively manage the fleet and monitor the broader economic trends closely.

The consumer banking segment grew average core loans by 6 percent from last quarter, driven by consumer mortgages and small business lending. To further reduce risk in the legacy mortgage portfolio, we completed a sale earlier this month for about $200 million of non-performing legacy mortgage loans.

Customer deposits grew at the direct bank, albeit at a more measured pace, given we came off a very strong first quarter of growth. Since our last earnings call, we tightened the rate on our leading savings builder product twice and have seen strong retention of existing customers and continued growth of new customers. Going forward, we're focused on maintaining a strong customer value proposition while also adjusting to market dynamics.

Before I hand it to John, I also want to mention the addition of the new member of the management team, with Jim Gifas joining CIT earlier this month to lead the payments and treasury services initiatives across the enterprise.

Jim is a proven leader in this space and he will be driving the integration of these banking services in our product portfolio. This is an important area to advance our growth strategy and deliver a more holistic set of products and services. Jim will be working with Bob Rubino and team to unlock the potential in the business.

With that, let me turn it to John for a detailed account of financial results.

John Fawcett
Thank you, Ellen, and good morning, everyone. We had another solid quarter, with net income available to common shareholders of $128 million, or $1.33 per common share, as we continue to execute on our strategy and progress toward our 11 percent return on tangible common equity target for the fourth quarter of this year.

We grew average loans and leases in our core portfolio by 1 percent from the prior quarter and 8 percent from the year ago quarter, which was driven by continued strong origination activity across all of our businesses. We stayed disciplined in our underwriting. Credit metrics remained stable and we reduced non-accrual loans.

Our net efficiency ratio improved as operating expenses came down from elevated seasonal levels last quarter. And, we further optimized our balance sheet. We reduced our federal home loan bank debt, repurchased $158 million of common stock below tangible book value, which contributed to the 3.6 percent tangible book value per share growth this quarter.

Once again, there were no noteworthy items and I will now go into further detail on our financial results for the quarter. Turning to Slide 6 of the presentation, net finance revenue declined from the prior quarter, driven by higher deposit costs, which were partially offset by lower borrowing costs on secured debt.

Interest income was relatively constant. Higher interest on loans was essentially offset by approximately $6 million from the accelerated amortization of the premium on our mortgage back securities investments. The acceleration was driven by the reduction in long term interest rates, which resulted in higher actual and forecasted pre-payments.

Slide 7 is our net finance margin walk. Net finance margin was 3.13 percent, down 7 basis points from the prior quarter. The reduction was driven by higher deposit costs, resulting from the full quarter impact of last quarter's strong deposit growth, partially offset by lower borrowing costs. The margin was also negatively impacted by approximately 5 basis points, from the acceleration of the premium amortization on our mortgage back securities investment portfolio.

As I discussed last quarter, we ended the first quarter with a higher than normal percentage of cash and investments, which was driven by the strong performance in our savings builder deposit product. We redeployed excess cash by repaying about $2 billion of federal home loan bank debt since the end of February that had an average rate of around 2.7 percent.

We reduced our savings builder non-maturity deposit rate by 5 basis points on May 1st and then 10 basis points more on July 1st, which will further benefit the third quarter. And, we will continue to opportunistically look at options to further reduce rates as the Fed moves.

Loan yields improved modestly from an increase in day count, but the benefit was more than offset by lower yields on our mortgage backed securities book described above. The margin benefited from a higher level of interest recoveries and pre-payment benefits this quarter, which was mostly offset by the reduction in interest on the indemnification asset, which was related to a loss share agreement that expired on March 31st. Net operating lease yields in rail were relatively constant, as lower gross yields were offset by lower maintenance expense, reflecting some of our productivity initiatives.

Turning to Slide 8, other non-interest income increased $9 million compared to the prior quarter. The increase was primarily in commercial finance and included a gain on the sale of a loan that was previously written off. Capital market fees were down this quarter, reflecting the weaker sponsor driven middle market M&A environment, but the decline was more than offset by higher customer derivative income in commercial finance.

Turning to Slide 9, operating expenses, excluding intangible asset amortization, decreased $8 million from the prior quarter. $5 million of the decrease related to compensation and benefit costs, which are down from seasonally elevated levels last quarter.

We significantly reduced our advertising and marketing costs this quarter related to deposits, as our deposit growth in the first quarter was ahead of our expectations and exceeded the amount needed to offset this quarter's CD maturities. Other expenses increased $6 million, resulting from a combination of several smaller items.

We estimate that approximately $8 million of operating expenses resulted from the adoption of the new lease accounting standard this quarter, including $6 million of property tax expense that was offset in other non-interest income. The prior quarter included $9 million and, for the full year of 2019, we continue to estimate that the new lease accounting standard will increase operating expenses by $40 to $50 million with a $25 to $30 million offsetting increase in other non-interest income.

The net efficiency ratio improved to 56 percent from 58 percent last quarter, resulting from the reduction in operating expenses and reflects the aforementioned lease accounting changes, which we estimate increased the rate by a little more than 100 basis points. We remain committed to further reducing operating costs while also investing in our businesses, and we are on track to achieve our target operating cost reductions of at least $50 million through 2020 when compared to the 2018 level.

Slide 10 shows our consolidated average balance sheet. Average earning assets were essentially unchanged from the prior quarter. During the quarter, we deployed excess cash to repay federal home loan bank debt and fund investment securities.

We grew average loans and leases by 1 percent, which includes the impact from the runoff of the legacy consumer mortgage portfolio. Average interesting bearing cash and investments remained higher than our typical run rate at about 21 percent of average earning assets, resulting from our strong deposit growth in the first quarter, but declined to 19 percent at quarter end. The average duration of our investment securities book remained at around two years, reflecting the higher level of liquidity and the flatness of the yield curve.

We slowed deposit growth this quarter. On a period end basis, deposits increased 1 percent, but on an average basis, deposits increased 6 percent, reflecting the full quarter impact from last quarter's strong growth.

Slide 11 provides more detail on average loans and leases by division. Strong origination volume across all of our businesses drove growth in our core portfolios. Commercial finance grew 2 percent from the prior quarter. Given the diversity of our commercial finance business, we continue to see good collateral based lending opportunities, which is contributing to about 60 percent of origination volume. Pre-payments have also remained low, which contributed to the growth.

In business capital, continued strong new business volume drove growth across our equipment financing portfolios, which was mostly offset by a reduction in the factoring business. We also experienced an improvement in yields this quarter, driven by pricing increases in the second half of last year in the technology driven businesses within equipment finance and small business solutions. That said, we are starting to see some pricing pressure in certain areas given the decline in swap rates and from competitors looking to aggressively add assets. In real estate finance, origination activity increased from last quarter, but a continued high pre-payment level resulted in a net reduction in average loans.

Our rail portfolio increased modestly this quarter as new deliveries mostly offset depreciation and our portfolio management activity. Utilization declined slightly to just below 97 percent as leases repriced down to 15 percent on average this quarter.

We continue to see strength in tank car lease rates, driven by the chemical and petroleum markets. However, many industrial sectors are exhibiting slower growth, which is translating into weak rail industry loadings, such as in non-metallic minerals or sand, coal, and grain. In this environment, we expect some pressure of fleet utilization and re-pricing within these freight markets.

As we have mentioned in the past, our market position, strong portfolio management expertise, customer service, and young fleet are key strengths as we continue to navigate the various market cycles. We continue to expect lease renewals on the total fleet to reprice down 15 to 20 percent in 2019, but will vary quarter to quarter based on the amount and type of cars renewing.

In commercial banking, we grew average loans by 2 percent despite the continued runoff of the legacy consumer mortgage portfolio. We have seen an increase in pre-payment levels, driven by the current interest rate environment, but it is also driving stronger origination activity in our retail and correspondent lending channels. Eighty-five percent of our new retail mortgage originations came through our digital channel and total new originations continue to have LTVs below 80 percent and FICO scores in the 750 area.

As Ellen indicated, as part of our continued effort to further improve our risk profile, last week, we sold approximately $200 million in book value of non-performing loans within the LCM

portfolio. We received proceeds in excess of carrying value. However, given most of the loans were PCI loans, where interest income is recognized on a level yield basis, based on the cash flows of the pools they reside in, the excess proceeds, or what would typically be characterized as a gain, will be recognized over the remaining life of the pool.

Slide 12 highlights our average funding mix, which reflects the trends I mentioned earlier. We continue to look for ways to optimize our funding mix, including shrinking our bank holding company and increasing our mix of assets funded with deposits.

Slide 13 illustrates the deposit mix by type and channel. Average deposits increased $2 billion from the prior quarter to $35.3 billion, reflecting strong growth in our online savings account deposits throughout last quarter and continued, albeit at a slower growth, in the second quarter. The cost of deposits increased as the cumulative beta since the first hike of the current tightening cycle in December of 2015 increased to 36 percent from 31 percent last quarter, consistent with our expectations.

We are focusing on optimizing deposit costs by increasing the proportion of non-maturity deposits, which we think will perform better, especially as rates decline. We have also reduced our savings rate builder rate by 15 basis points since the beginning of May and have not seen any meaningful levels of attrition as a result of these moves. Notwithstanding any rate reductions from the Fed, we are likely to continue to test the elasticity of our deposit rates, balancing our need to fund growth and our continuing effort to optimize our funding costs.

Turning to capital on Slide 14, during the quarter, we repurchased approximately $158 million in common shares, consisting of 3.2 million shares, at an average price of $49.64, below tangible book value, ending the quarter with just under 95 million shares outstanding.

Our CET1 ratio at the end of the quarter declined to 11.6 percent, reflecting the expiration of a loss share agreement with the FDIC, which increased RWAs by approximately $800 million. If you recall last quarter, we had a net increase in the Common Equity Tier 1 ratio related to the change in the regulatory definition of HVCRE loans, partially offset by the adoption of the new lease accounting standard.

In aggregate, the net impact of our capital ratios from both of these changes was minimal. We have reduced the Common Equity Tier 1 ratio from 12 percent at the beginning of the year to 11.6 percent and continue to target 11 percent by the end of this year.

Slide 15 highlights our credit trends. The credit provision this quarter was $29 million, modestly below our guidance range, and net charge offs were $31 million or 40 basis points within our guidance range. Net charge offs declined from $34 million in the prior quarter and continue to be primarily driven by commercial finance, most of which were previously reserved for, and small business solutions within business capital.

Non-accrual loans declined this quarter by $26 million or 9 percent and approximately 60 percent of the remaining non-accrual loans are current. About half the reduction was due to charge offs that had been previously reserved and we received slightly above book value on the other exited non-accruals.

Our credit metrics and the broad credit environment remained stable and new business originations continue to come in at better risk ratings than the overall risk rating of the performing portfolio. Our reserves remain stable and strong at 1.56 percent of total loans and up

slightly to 1.89 percent for commercial banking and continue to reflect more than four times the last 12 months net charge offs.

Slide 16 highlights our key performance metrics, reflecting the trends we just discussed. Our effective tax rate was 20 percent and benefited from net discrete items of $9 million, which was driven by audit settlements with several state and local tax authorities in the ordinary course of business.

Excluding those discrete items, the effective tax rate would have been 25 percent, in line with our guidance. Our return on tangible common equity from continuing operations was 10.3 percent. If you normalize for the semi-annual preferred dividend that is paid in the second and fourth quarters, our return on tangible common equity would have been 10.7 percent, up from 9.3 percent in the prior quarter, reflecting lower operating expenses and a lower effective tax rate.

We remain committed to continuing to improve our returns and are focused on achieving an ROTCE of 11 percent in the fourth quarter of 2019 and targeting at least 12 percent by the fourth quarter of 2020. When we set our initial outlook back in January, we assumed no rate increases or decreases and assumed GDP growth of 2 and a half to 3 percent.

As Ellen mentioned, we are starting to see customer sentiments shift a little in some of our commercial businesses, primarily resulting from the uncertainty related to trade and tariff discussions. In addition, the rate environment obviously continues to evolve and is now reflecting multiple rate cuts in 2019 and 2020.

While a 25 basis point interest rate cut next week and another later this year would pressure our net finance revenue, we believe we would still be able to achieve our fourth quarter 2019 return on tangible common equity target of 11 percent. And, we remain focused on continuous improvement. The uncertain environment is making 2020 more challenging to predict, but achieving at least a 12 percent return on tangible common equity in the fourth quarter of 2020 remains our target. We will keep you posted on our progress as we navigate through the current environment and plan to update our 2020 guidance on our fourth quarter earnings call.

Page 17 highlights our outlook for the third quarter. We continue to expect low single digit quarterly growth in our core portfolio and slightly lower growth in the total portfolio, reflecting the sale of the non-performing legacy consumer mortgage assets and continued runoff of that portfolio.

We think our margin for 2019 will now be at the low end of our target range, reflecting a 25 basis point cut in the third quarter and another one in the fourth quarter. But, the third quarter, net finance margin is expected to continue to trend down to the bottom end of the target range and could be pressured further, depending on the environment for rates and deposits, as well as other factors.

We expect deposit rates to be relatively flat as continued migration of our CD depositors into higher rate products is offset by a reduction in our savings builder rate. We think rail yields will continue to reprice down, but will be mostly offset by lower maintenance costs. And, as I've mentioned--and as I have mentioned earlier, we had a higher level of interest recoveries and pre-payment benefits this quarter, which are difficult to predict and a potential headwind to next quarter. We expect operating expenses to be flat to slightly higher next quarter, related to marketing costs as deposit activities normalize.

The net efficiency ratio is expected to remain in the mid 50 percent area next quarter, reflecting the trends I just mentioned, and includes the impact of the lease accounting changes. Credit metrics and the effective tax rate, absent any discrete tax items, are expected to be consistent with our full year outlook.

And, with that, I will turn the call back over to Ellen.

Ellen Alemany
Thanks, John. As John mentioned, we remain committed to creating long term shareholder value and are focused on achieving our return of tangible common equity goal of 11 percent in the fourth quarter of this year, and at least 12 percent in the fourth quarter of next year.

We're pleased with the progress on the first half of the year and are focused on continuing to deliver on the plan and unlock the full potential in CIT. With that, we're happy to take your questions.

QUESTION AND ANSWER

Operator
Thank you. We will now begin the question and answer session. To ask a question, you may press Star, then 1 on your touchtone phone. If you are using a speakerphone, please pick up your handset before pressing the keys. To withdraw your question, please press Star, then 2.

Our first question comes from Moshe Orenbuch of Credit Suisse. Please go ahead.

Moshe Orenbuch
Great. Thanks for all of that detail. I'm just wondering if--John, if you could kind of talk a little bit about how you see the moving parts within the net interest margin over the balance of the year, because there's just a lot of moving parts there.

John Fawcett
Yeah, Moshe. Look, without question, I mean the biggest element to this is going to be our ability to actually manage deposits. I think we got ahead of it a little bit in the second quarter. In May, we cut 5 basis points and then on July 1st we cut another 10 basis points.

I think it remains to be seen how fast we can come down. I think obviously betas were lower going up than I think most expected. I think we're going to be as aggressive as we possibly can. But, that really becomes linchpin.

I think the other thing that's kind of out there is we're starting to see some softness, a little bit of softness, in parts of the rail portfolio, specifically in the freight, specifically in the sand. It's not a big problem for us, but it's an element out there that we are closely watching. So, I think those are the two wildcards.

On the asset side of the balance sheet, I think thus far, if you look at originations and origination rates across our entire book of business, I think we've been pretty effective. I think there have been changes in the mix of yields, but we started last year in the third quarter in terms of business capital, which is our fastest growing business, and we've been able to hold onto that.

I think it becomes an exercise in terms of understanding the difference between rate and price point. As rates come down, it'll be interesting to see how much competitive pressure we can continue to maintain in business capital. In commercial finance, I think we're more than holding our own. Pockets of strength are still in healthcare, real estate, energy, aviation. That seems to be holding on.

Real estate, again we're not competing on terms and conditions, and so it's unlikely you're going to see a lot of move there. And, then in the consumer space, it's pretty immune because I think for the most part, it's largely a law of small numbers. So, I think going back to what I started with, the big driver in the quarter is going to be our ability to manage rates coming down, especially in the online portfolio and our non-maturity deposits, which is hard to predict, especially since we just can't do it in a vacuum because it's a function of what's going on in the broader environment with the competition.

Moshe Orenbuch
Got it. Just a follow up, I mean as you're thinking about getting from what was 10.7 percent adjusted for the dividend in the quarter, but it sounds like nominally between the tax rate and what your guidance for the margin is, that maybe the numerator that is coming down--like, how do you think about actually getting from that 10.7 but maybe on an adjusted basis, something less than that, back up to 11, but over the next two quarters?

John Fawcett
Yeah, so look, I think we remain committed. I think in Ellen's call script and my call script, we remain committed to the 11 percent. We've certainly got some levers that we can kind of pull. It goes back to deposit rates and betas and the question is, how fast can we pull the rates back down?

As I said before, I think we were very early on, in terms of the moves we did in May and the 1st of July. I think there are elements within the way we fund the place in terms of a mix between deposits and federal home loan bank borrowings. We have an enormous amount of capacity there.

In op-ex, there remains some opportunities to take more costs out faster and there are also opportunities to kind of delay spend. If you look over to non-interest income, we've been very aggressive in terms of growing the BOLI. We added some more BOLI in the third quarter and we're kind of up to our limit on that.

Ellen kind of touched briefly on a new JV that we just launched which was important. Our legacy consumer mortgage portfolio sale and rail sales continue. And, then I think we continue to strategically look at moving HoldCo Assets into the bank, which to the extent that we can do that, that's generally worth about 200 basis points in funding the differential between senior unsecured debt and deposits. So, we have two levers.

Ellen Alemany
Yeah, I mean, I just want to add that if there's a 25 basis point cut next week and there's another one later this year, it would put pressure on our net finance revenue, but we still think that we could hit the fourth quarter target of 11 percent. And, we do have some drivers here.

We do have some remaining capital return left. We do expect non-spread income to trend higher this year. We think there's a little more room, as John said, on the operating expense

line. And, we are going to continue to look at putting more assets in the bank and optimizing our funding structure.

Moshe Orenbuch
Got you. Thank you.

John Fawcett
Thanks, Moshe.

Operator
Our next question comes from Chris Kotowski of Oppenheimer. Please go ahead.

Chris Kotowski
Yeah, kind of expanding on Moshe's question, it seemed like on the ins and outs on the margin, you mentioned three things to keep in mind. I guess one is the amortization of the premium on the mortgage backs and presumably, that goes away if you just don't have long rates coming down further. And then secondly--first off, question one is do you agree with that, that that goes away, just as long as--as soon as long term rates stabilize?

And then question number two would be, you mentioned the PCI loan sales and I think you said there was $200 million. But, you're not taking that as an upfront gain? You're taking that as an ongoing benefit to the margin?

And, then thirdly, does your guidance envision further rate cuts in 2020 or is the guidance as we see it just based on two rate cuts and then we're done?

John Fawcett
So, on the PCI gain, the accounting dictates the extent that this is a sale out of the purchase credit impaired portfolio, that the gain, which is kind of in the $20 to $25 million range, gets spread out over the remaining portfolio. So, if you think about it in the context that what's left in the LCM portfolio is essentially probably a 10 year life, it'll be spread out over the 10 years.

In terms of the 2020 cuts, I think look, it's incredibly fluid. When I think back to the way we did the plan, we started doing the plan--we had four hikes. Then by the time we got to November/December, we got down to zero and that's the way we modeled the plan, no hikes, no cuts.

And, now we're looking, I guess, at potentially two cuts the remainder of this year, maybe three. And, I think a lot of it depends on when and how much. It sounds like some of the rhetoric around the 50 basis points coming in July has died down. I think everybody's kind of baked in a quarter point in July, another quarter point sometime in the fourth quarter. Whether it's in the beginning or the end, who knows. And, then two more in 2020 is the way we're modeling.

But, I think the way we think about it is we've got to be incredibly nimble and flexible because the one constant in this environment seems to be change. And, it seems like the world remains incredibly fluid, even for no other reason.

And, then I think was there another question?--

Chris Kotowski
--Yeah, about the amortization of the mortgage backed premiums.

John Fawcett
Yeah, so on the mortgage backs, we think it'll smooth out over time. It'll modestly be lower. It depends on the accounting, and I don't want to get into the weeds. I think we're on a retrospective basis of accounting, which contemplates not only existing moves in tens, but forward rates--forward moves in tens. And, so we're following the curve versus a contractual basis. And, that's why you might be seeing a difference in terms of the impact between us and other banks. I suspect there's a universe that follows retrospect, but I think there's a universe that follows contractual. But for us, it should be relatively smooth on a go forward basis.

Chris Kotowski
Okay. And, then just, I guess secondarily, I mean, you--you're flagging kind of a slowdown of activity on the rail front. Do you see that reflected in behavior or action or payment rates on the general commercial portfolio?

John Fawcett
No and look, I think it's early days. I think there's a lot of things that are going on in rail. I mean, as I said in my script, year to date rail loadings are down 2 percent, driven by coal. We do have some coal cars, non-metallic minerals, which is sand, and then agricultural and forest products.

I think in the sand space, there's a geological debate going on in terms of the virtue of northern white sand and locally sourced brown sand in terms of fracking. And, I think drillers have kind of transitioned to it's cheaper to deliver brown sand and it remains to be seen what the geology is in terms of how that affects the effectiveness--efficiency and effectiveness of--and productivity of the drilling site. So, that's one pressure point.

I think the other one is around PSR, which is kind of again, at the margin but historically, it impacts railroad service levels, forcing shippers to just conform to more rigid schedules. And, so that's a little bit of a pain point.

And, then you've got the overhang of tariffs, and so the extent that you've got customers with import and export activity, I think they're generally more hesitant to invest in operations given trade uncertainties. And, so that's led a little bit to making it more difficult to gauge freight repricing.

What I would say is if you looked in the first two quarters of the year, we've actually had pretty modest levels of repricing. So, in the first quarter, there was about between 3000 and 3500 cars. Same thing for the second quarter, which you would expect in the normal course, given you've got 115,000 cars and an average life of four and a half years. You'd expect about 26,000 cars to reprice every year, call it 6,000 cars a quarter.

So, we're a little bit under that. What we've seen thus far is the tanks continue to reprice well ahead of our plan, albeit still below prior. And, freights are continuing to reprice modestly below plan. But, it's early days and we'll see how this all pans out.

And, maybe as the quarters go, we'll get more visibility in terms of what the impact of PSR is and where tariffs go and the impact that that's having on imports and exports.

Chris Kotowski
Okay, great. Thank you. That's it for me.

John Fawcett
Thanks, Chris.

Operator
Our next question comes from Arren Cyganovich of Citi. Please go ahead.

Arren Cyganovich
Thanks. As we think about the deposits and the deposit costs, it obviously rose in the second quarter as that was a bit of a catchup. But, if we--even excluding a rate cut that's expected for this quarter, if you kept everything equal, would you say your deposit costs have now kind of peaked?

John Fawcett
I would say yeah. I think typically, in a rising rate environment, we model that it takes six months for the entire portfolio to reprice. I think as rates have started to come down and we've pulled back on our offer rates on our savings builder account, I would say yes on the non-maturity deposits in the online bank, they've clearly peaked, at least in my mind.

Arren Cyganovich
Okay. And, then I guess the expectation that there would be some pressure to the net finance margin for the next two cuts as you laid out. Is that more of a timing aspect? I mean, I know we have to see what the rest of the market does in terms of online deposit kind of resetting. But, assuming it's a rationale move, would you expect that there's just a lag between the repricing of your loans or what would you expect that it's just not going to catch up as much as the loans reprice?

John Fawcett
Well, look, I think we've tried to get ahead on the deposit pricing. So, we've done 15 basis points before the Fed has moved at all and I think we're poised for more cuts. So, conceptually, you could say that this cut, if we did another 10 basis points on August 1st, would have 100 percent beta if they do a quarter point.

If they do more, I think we'll respond accordingly. But, again, it depends. We're not the highest rate in the market right now. We're at 230. There are still banks at 250, 245, 240, 235, and some of them are big banks. And, so we have to be mindful of what the competition is doing. But, I think we watch this very carefully.

The other thing that's really important is to the extent that we've actually transitioned, the customers segment in this portfolio, the thesis was they were smaller balances and stickier balances. And, so as we've cut these rates, we've actually gone through two statement cycles and essentially seen no attrition.

On the left hand side of the balance sheet, again, the markets remain incredibly competitive and I think specifically in business capital, we're very mindful of the mix between price and volume. And, the volume in the business has been absolutely terrific. But, we're not tone deaf to the effect that at some point, there will be a tipping point that we're going to have to respond to from a pricing perspective. And, so we watch that closely.

But, it's literally day to day in terms of what we're seeing others do in the market. It's just a tough place to be. It's a very fluid environment.

Arren Cyganovich
Okay. And, then on the new asset management JV, maybe if you could just talk a little bit about what's the potential size of that? Would you be adding additional partners over time? And, then is this based on purely on volume or is there any kind of ongoing recurring fee income associated with that?

Ellen Alemany
Yeah. So, we just announced our new structure, [asset management vehicle], and basically it allows us to offer expanded cash flow revolving and term loan options through a managed financing vehicle by an A rated insurance company. So, this is our cash flow vehicle and then we also have the Northbridge JV ABL in place.

And, right now in Northbridge, we've probably done about $300 million in volume. But, it's basically allowing us to serve our customers better and increase our capacity to provide customers' financing that we would not be able to do on our own books. This is more the type of business that's being done in the BDCs and also at a long-term recovering revenue stream.

I mean, it's really early stages to project how much we're going to do, but it's just another outlet for us to book more business.

Arren Cyganovich
And, just on the topic, is it volume based or is it where you'll have some kind of actual recurring fees from that?

Ellen Alemany
It's really both.

Arren Cyganovich
Okay. All right, thank you.

Operator
Once again, if you have a question, please press Star, then 1. Our next question comes from Scott Valentine of Compass Point Research. Please go ahead.

Scott Valentin
Yeah, good morning. Thanks, everyone, for taking my question. I think Ellen, John, one of you referred to additional capital management going forward as one of the ways to hit the ROTCE targets. And, you have $112 million left on the current authorization. Does that imply there's room for additional authorization before year end?

Ellen Alemany
No. I mean, our authorization was through the end of September.

John Fawcett
Yeah, so Scott, I mean what we've done is, is now that we're no longer a CCAR bank, what we've done is we've aligned our--essentially requesting the Fed with our strategic planning cycle, which runs October 1st to September 30th. So, on September 30th, we will have exhausted the $450 million that was approved by our board and by the Fed.

We would expect that over the course of the coming weeks, that we would have an incremental request that would go to the Fed that would cover the fourth quarter of ’19 and the first three quarters of ’20. And, that would be necessary, arithmetically, for us to actually manage down to the 11 percent Common Equity Tier 1 ratio, which we’ve been messaging for the better part of the year.

Scott Valentin
Thanks, that’s very helpful. And, just to follow up on credit quality, it improved in quarter. I know you said there’s some--the economy is slowing down. Are you seeing any sectors maybe that stand out in terms of any watch list issues or are you seeing increased delinquencies in any one sector?

Ellen Alemany
No, I think overall, we feel pretty good about the quarterly provision and the guidance that we’ve put out of it running between $30 and $40 million [per quarter]. We’ve been going through a major transition at the company over the last several years. We’ve exited businesses with higher credit, asset and regulatory risk, including Financial Freedom, Commercial Air, NACCO.

Our strategy has been lending against assets that are higher quality and collateral based, and we’ve been meaningfully reducing our cash flow loans. Our cash flow loans now are only 10 percent of our loan and lease commitments.

We also are a heightened standard bank, so we have built second line defense, and op risk, credit review and compliance. We’re no longer a SIFI bank, but we kept all of the robust liquidity and capital stress testing in place. And, even with our cash flow loans, that 10 percent of our exposure, they’re all--we have first lien positions. The average senior leverage levels are less than four times. The average total leverage levels are less than five times. We have a lot of industry--we’re lending by industry verticals, so we have a lot of industry expertise.

So, we--last quarter, we saw a tiny bit more [net charge-offs] in small restaurants and a little in the smaller owner operator transportation in business capital. But, other than that, knock on wood, credits remain really solid for us.

Scott Valentine
Okay, thanks for that color. Thanks very much.

Operator
There are no other questions at this time. I would like to turn the conference back over to management for any closing remarks.

CONCLUSION

Barbara Callahan
Thank you, Nicole, and thank you, everyone, for joining us this morning. If you have any follow up questions, please feel free to contact the Investor Relations team. You can find our contact information, along with other information, on CIT.com. Thank you again for your time and have a great day.

Operator
That concludes today’s call. Thank you for participating.