# CIT Group, Inc.

## Q3 2019 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 the CIT's Third Quarter 2019 Earnings Conference Call. My name is Keith, and I'll be your operator today. At this time, all participants will be in a listen-only mode. There will be a question-and-answer session later in the call. When that session begins, you may ask a question by pressing *, then 1 on your touchtone phone. If you would like to withdraw your question, please press *, then 2. If at any time during the call you require assistance, please press * and 0, and an operator will be happy to help 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**
Thank you, Keith. Good morning, and welcome to CIT's Third 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's 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. Thank you, and I'll now turn the call over to Ellen Alemany.

**Ellen Alemany**
Thanks, Barbara. Good morning, and thank you for joining the call. I'm pleased to report that we had another solid quarter performance and delivered continued progress on our strategic plan. We posted net income of $143 million or $1.50 per diluted common share for the third quarter. We had a few noteworthy items in the quarter as a result of our strategic initiatives that improved our net income by 20 million, and John will take you through those in more detail. Excluding those items, we posted income from continuing operations of 123 million or a $1.29 per diluted common share.

On slide two of the presentation, we highlight some key drivers of performance. Our core business continues to post steady growth with average loans and leases up 2% from last quarter and 8% from the prior year period. Our deposit costs remained relatively flat from the prior quarter, as we optimized pricing and continued to grow our non-maturity deposit accounts to about 65% of average total deposits, up from 55% last year.

We've remained disciplined on expenses and are on track to achieve our goal for the year, and credit performance remains strong, reflecting our strategic steps towards more collateral base lending. We ended the quarter with tangible book value of $55.60 per share, which is an 11% increase compared to last year. To further accelerate our strategic plan, in August we announced an agreement to acquire Mutual of Omaha Bank. This transaction will diversify our funding profile with scalable lower cost deposits through the addition of a market-leading homeowner's association banking business, and it will also expand our middle market commercial banking capabilities with additional products, technology, and a broader geographic footprint.

The transaction continues to move forward as planned. We submitted our application to the OCC on September 26th, which was a key milestone. We established an integration management office under the leadership of Mike Weitzman. Mike is a seasoned banking and integration professional who has joined CIT to lead this effort and drive a robust process around the deal. The full management team is engaged in the process to complete the transaction, deliver on a timely integration and achieve the synergies and growth opportunities that we have identified.

As we have said before, we believe this opportunity will create substantial long-term value for the franchise. In particular, we expect this deal to generate double-digit EPS accretion over time and improve our return on tangible common equities starting in 2020. The profitability enhancement next year will largely be driven by realizing cost savings and deploying excess capital related to the deal. This includes an immediate 20 basis-point improvement in our deposit funding through the addition of the homeowner's association business.

Over a two-year timeline, we believe we can continue to improve our returns, as we begin to leverage the growth synergies in the HOA space and middle market banking. Expected growth in the HOA channel should take some pressure off other deposit channels and allow us to further optimize our funding profile. In addition, a lower cost of deposits and integration of regional middle market banking teams should expand our addressable market and opportunity for fee income.

Other longer-term benefits of this deal are expected to include moving more rail assets into the bank, as the overall bank grows, which will lower funding costs for those assets. With lower cost of deposits, we can also improve our overall risk profile, which should contribute to our goal of achieving an investment grade credit rating at the holding company. Our operating leverage will expand through growth, which will further improve our efficiency ratio, and ultimately, we aim to free up additional capital, as our risk profile better aligns to peers in the industry.

To sum it up, we believe there are several elements of this transaction that will positively affect our business and unlock meaningful value over time. We're focused on a first quarter close pending regulatory approval and a smooth and timely integration. As a result of the multi-year transformation we have completed to date, I'm pleased to say that at the end of September, we were added to the KBW BKX index, which further recognizes CIT as a national bank. We're glad to be listed among other banks in our industry on the index.

Before I turn it to John, I just want to touch a few highlights in our business. We drove strong origination volume in the quarter, largely in the commercial finance, business capital, and consumer divisions. Markets remain competitive, however, and the rate environment has put some pressure on margins. We remain prudent in our risk appetite, and our growth comes from our expertise in key pockets of the market, where CIT has strength. The commercial finance business grew average loans and leases compared to last quarter and last year.

Our market position in the aviation, renewable power, healthcare, and C&I areas enable us to win strong deals in these verticals, as we leverage our industry and collateral back to expertise. For example, we won a $425 million deal in the healthcare finance business in the quarter, where we served as lead arranger and administrative agent for a long-term client. This relationship and our proven track record enabled us to lead the deal and build a significant treasury management relationship and a stream of capital market fees over multiple years. This is an example of the deep relationships we cultivate in this business.

The business capital division posted another quarter of solid growth with the technology and industrial industries driving volume. Core factoring volume was up in the third quarter, largely due to seasonality in that business. Originations in the commercial real estate business were solid. However, pre-payments continue to be elevated. As a result, assets were down in the quarter but in line with our expectations for this area of the business.

Average loans and leases in the rail division were flat in the quarter, but our ongoing investments in a modern, diverse rail fleet allowed us to maintain a strong utilization rate of 95%. Industrial production has slowed, and railroads continue to rationalize their operations. But we believe the quality of our fleet, our market expertise, and service level are key advantages in the market.

We continue to post strong growth in our core mortgage and small business lending operations. Total average loans and leases were down slightly in the consumer banking segment, reflecting the sale of non-performing loans in the runoff portfolio, as we continue to improve our risk profile. As I mentioned earlier, we have made progress in shifting our deposit accounts towards more non-maturity deposits and strategically reducing our CD volume.

We have also optimized our pricing on the savings builder account to reflect changes in the rate environment, and retention in this product remains stable. We had very good, strong deposit growth in the first half, and we have taken a more measured approach to growth in the third quarter. Overall, we have been building on our momentum, and it was a solid quarter. With that, let me turn it to John.

**John Fawcett**
Thank you, Ellen, and good morning, everyone. We had another solid quarter with net income available to common shareholders, excluding noteworthy items, of $123 million or $1.29 per common share, and we continue to make steady progress on our strategic priorities. We grew average loans and leases in our core portfolio by 2% in the prior quarter and 8% from the year-ago quarter. Credit metrics remain stable, and we remain disciplined in our underwriting.

We reduced operating expenses slightly, despite higher costs related to the Mutual of Omaha Bank acquisition. We launched our bank note program and issued our first unsecured note, which had an investment grade rating from S&P of six non-call five-year term and pricing just inside 3%. And we grew tangible book value per share by over 2% to $55.60.

On page five, we had a few noteworthy items this quarter related to strategic priorities that resulted in a net after-tax benefit-to-earnings and increased the tangible book value to $20 million. First, we recognized a $53 million tax benefit related to our reassertion that earnings from our operations in Canada would be reinvested indefinitely, which resulted in the reversal of an accrued tax charge. If you recall, in 2016, we took a charge for a similar amount when we decided to sell our commercial and equipment finance businesses in Canada. With the restructuring completed, we have analyzed our remaining operations in Canada and have concluded that we expect to reinvest our earnings there indefinitely.

Second, during the quarter, we entered into an agreement to sell our Livingston office building and move our New Jersey operations, which is mostly corporate functional staff, to Morristown, New Jersey, where we entered into a 15-year lease. We took a $22 million after-tax charge, reflecting the impairment of the Livingston building. The new location will be more efficient for our needs, as the cost to keep Livingston building operational would’ve exceeded the increase in the operating cost for the move. In addition, we were awarded a $22 million New Jersey state tax credit to be used over a 10-year period starting in 2021.

And the third, for this quarter, we also took an $11 million after-tax restructuring charge related to initiatives to improve operating efficiency and expect these benefits to be realized over the next 18 to 24 months.

I will now go into further detail on our financial results for the quarter, which exclude the noteworthy items. Turning to slide six of the presentation, net finance revenue declined from the prior quarter, driven by lower interest income from lower market rates on our floating rate loans as well as lower purchased accounting accretion. Net operating lease revenues benefitted from lower maintenance costs this quarter, while interest expense was relatively flat.

Slide seven is our net finance margin walk. Net finance margin was 3.06%, down 7 basis points from the prior quarter and below our target rate. As I mentioned last quarter, we expected the margin to decline to the bottom of the target range with potential for further pressure, depending upon the rate environment. Yields on our loans were down across all businesses as well as our cash and investments, reflecting lower market rates.

Net operating lease yields in rail were higher this quarter, as lower growth yields from repricing rates were offset by lower maintenance expense, reflecting some of our productivity initiatives and a $3 million lease warranty recovery. As we anticipated, deposit costs were flat, reflecting the reduction in our non-maturity deposit rates, offset by the pricing of CDs. I will discuss deposit trends a little bit later.

The margin was also negatively impacted by lower interest recoveries and pre-payment benefits, which were elevated in the second quarter. In addition, as Ellen mentioned, as we continue to improve our risk profile, we sold approximately $200 million of non-performing loans from our legacy consumer mortgage or LCM portfolio in July. We received proceeds in excess of the carrying value, which will be recognized over the remaining life of the pool.

However, given the higher risk profile, these loans were also higher yielding. On a pro forma basis, we estimate the sale reduces margin by approximately 1 basis point after considering the reinvestment into new mortgages with the stronger credit profile and the current market rates. We are continuing to look for opportunities for additional sales of LCM loans in the coming quarters.

Turning to slide eight, other non-interest income decreased by $5 million, compared to the prior quarter, which if you recall included a $5 million gain on the sale of the loan that was previously written off. Fee revenues, factoring commissions, gain on sale of lease equipment and income from our bank-owned life insurance program all increased modestly.

Turning to slide nine, operating expenses, excluding a tangible asset amortization, decreased slightly from the prior quarter but includes nearly $8 million in expenses related to the Mutual of Omaha Bank acquisition. The prior quarter included a little under $3 million in expense related to the acquisition, and the net difference is reflected in the increase in professional fees. Costs incurred were tied to diligence, legal and regulatory matters in a normal course, including the OCC application process, as well as external support related to ongoing integration.

Advertising and marketing costs related to deposits increased to a more normalized level this quarter, as we had significantly reduced the spending in prior quarter, as a result of our excess deposit growth earlier in the year. We estimate that approximately $8 to $9 million of operating expense this quarter resulted from the adoption of the new lease accounting standard, including $5 million of property tax expense that was offset in other non-interest income.

Year-to-date operating expenses include approximately $25 million related to the new lease accounting standard, and we now estimate that the new standard will increase operating expenses by $35 to $40 million in 2018 with a $22 to $25 million offsetting increase in other non-interest income. The net efficiency ratio increased to 57% from 56% last quarter, resulting from the reduction in revenues slightly offset by the reduction in expenses and reflects the aforementioned lease accounting changes, which we estimate increases the rate by more than 100 basis points.

While our operating expenses have been elevated for the acquisition costs, we have been running ahead of schedule in achieving our 2020 target operating cost reductions. As a result, we expect to meet our 2019 guidance, despite the higher costs related to Mutual of Omaha Bank acquisition.

Slide 10 shows our consolidated average balance sheet. Average earning assets were essentially unchanged from the prior quarter. During the quarter, we reduced investments and grew average loans and leases by 1%. The increase includes 2% growth in our core portfolio, partially offset by the sale of the non-performing LCM loans previously mentioned as well as the continued runoff of that portfolio.

Slide 11 provides more detail on average loans and leases by division. Strong origination volume across most of our business has drove quarterly growth in our core portfolios. Commercial finance grew 2% from the prior quarter, driven by aviation lending, healthcare, renewable power, and various sub-verticals within C&I. We continue to focus on collateral-based lending, which represented about 60% of commercial finances origination volume.

While risk-adjusted spreads have remained relatively stable, loans in this business are floating rate and the reduction of portfolio yields reflect the decline in liable rates this quarter. In business capital, continued strong new business volume in our equipment financing portfolios in higher seasonal factoring activity drove an increase in average loans and leases. Growth in our equipment finance and small business solution portfolios continues to outpace the industry. However, new business yields in certain areas are being pressured from the decline in swap rates and from competitors looking to aggressively add assets.

In real estate finance, we continue to see good origination activity, and while pre-payments remain high, they occurred later in the quarter, and as a result, average loans were flat. New business spreads have remained relatively stable. However, portfolio yields declined this quarter as a result of lower Libor levels. Our rail portfolio increased modestly this quarter, as new deliveries mostly offset depreciation at our portfolio management activity.

Despite growing excess capacity in the North American fleet industry and slowing growth in many industrial sectors, our rail team continues to successfully manage fleet utilization, which declined to just above 95%. Leases repriced down 9% on average this quarter. We continue to see strength in tank and car lease rates, particularly in certain chemical petroleum markets. This has led to improved pricing and demand for those cars, and as a result, the repricing gap is closing faster than originally expected.

As it relates to our freight cars with the persistent industry surplus, which increased to 22% and slowdown in manufacturing sector, freight car repricing levels remain modest with downward repricing in most markets. The sand market continues to show the most weakness. In addition, the late harvest season and continued uncertainty in trade policies are impacting the export demand for grain and other agricultural products.

As we have mentioned in the past, our market decision, strong portfolio management expertise, customer service, and the quality of our fleet are key strengths, as we continue to navigate in an uncertain environment. We continue to expect lease renewals on the total fleet to reprice down 10% to 15% through 2019 and into 2020, but we expect this to vary quarter to quarter, depending upon the number and type of cars renewing.

In consumer banking, average loans were down slightly, reflecting growth in the core business, offset by the sale of the non-performing loans and continued runoff of the legacy consumer mortgage portfolio. Retail mortgage origination activity remains strong, driven by refinancings with a little over 80% of our retail volume coming through our digital channel. Total new originations continue to have LTVs below 80% and FICO scores in the 775 area.

Slide 12 highlights our average funding mix. Total deposits declined slightly but remained at 85% of total funding. Average unsecured borrowings remained relatively flat from the prior quarter but increased at the end of the quarter, as we took advantage of strong market and CIT-specific fundamentals at the end of September and funded a significant portion of our needs for the Mutual of Omaha Bank acquisition. As I mentioned earlier, we launched our bank note program and issued $555 million six-year non-call-five unsecured notes at a rate just below 3%. It was rated investment grade by S&P, and the new offering was significantly over-subscribed.

Slide 13 illustrates the deposit mix by type and channel. Overall deposit rates remained relatively flat, reflecting a reduction in rates in our non-maturity deposits offset by an increase from repricing CDs. We continue to shift to a higher portion of non-maturity deposits, which we believe will perform better, especially as rates continue to decline. In line with that strategy, average deposit balances were down slightly, reflecting a reduction in time deposits, partially offset by an increase in our savings and money market accounts.

In the direct bank in addition to the 5 basis-point reduction in rate on May 1st, we reduced our savings rate builder by another 20 basis points over the course of the quarter, while growing the average savings deposit balance by 4%. We continue to reduce the savings builder rate by another 10 basis points on October 1st 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 optimize our deposit rates, balancing our need to fund growth in our continuing effort to optimize our overall funding costs.

Turning to capital on Slide 14, the common equity tier 1 ratio remained at 11.6%, reflecting quarterly earnings, RWA growth, and a decrease in disallows deferred tax assets. Capital ratio remained elevated relative to our targets, as we stopped repurchasing shares due to the pending Mutual of Omaha Bank acquisition. As a result, we now expect our common equity tier 1 ratio to remain in the mid-to-high 11% range by the end of the year.

Upon closing of the acquisition, our common equity tier 1 ratio is expected to decrease to approximately 10%, the lower end of our target range. After the close, our intention is to remain out of the market for our common shares in order to increase our common equity tier 1 ratio to 10.5% within the ensuing 12 months, which is in the middle of our target range.

Slide 15 highlights our credit trends. The credit provision this quarter was $27 million, and net charge offs declined to $26 million and 34 basis points, both slightly below our guidance range. Net charge offs continue to be primarily driven by commercial finance as well business solutions within business capital.

Non-accrual loans increased by $27 million, driven by an increase in commercial finance and business capital, partially offset by a reduction from the LCM loan sale.  A little over 60% of non-accrual loans occurring and total non-accrual loans remain below 1% of total loans. Our credit metrics in the broad credit environment remain stable.

New business originations reflect our continued efforts to enhance our risk profile, and as a result, continue to come in at a better risk ratings than the overall risk rating of the performing portfolio. Our reserves remain stable and strong at 1.55% of total loans and 1.87% for commercial banking and continue to reflect more than four times the last 12 months net charge offs.

As I mentioned in September at the Barclays conference, we will adopt CECL at the beginning of next year, upon which the allowance for credit losses must cover credit losses over the entire remaining expected life of the loans and commitments and will consider future changes in macroeconomic conditions.

We have formed cross-functional implementation working groups in preparation for the adoption of CECL, and we continue to develop and test our loss forecasting models and methodologies. Our expectation today is that the impact on tangible book value will be relatively modest at $50 million to $100 million. This excludes any impact from the Mutual of Omaha Bank acquisition, which we are still working through.

From a regulatory capital perspective, we maintain the option of phasing in the capital impact over a three-year period. We expect an increase in our allowance for loan loss reserves, however, to be around $200 million to $300 million, as the increase is expected to be largely driven by our Purchase Credit Impaired or PCI loans in the legacy consumer mortgage portfolio. I would emphasize that tangible book value would not be impacted by the increase in reserves from PCI loans, as the reserve will essentially replace the existing non-accrual discount with a corresponding increase in the loan balance.

Our current estimated range assumes moderate economic growth, continued low levels of unemployment, and a stable credit environment. It also will be driven by economic conditions in the composition of our loan portfolios at the adoption date and, therefore, is subject to change. We have included a slide in the appendix that illustrates our current thoughts.

Slide 16 highlights our key performance metrics, reflecting the trends we just discussed. Our effective tax rate was 24%, excluding the noteworthy items, which is slightly below our guidance. Our return on tangible common equity from continuing operations was 9.8%. If you normalize for the semi-annual preferred dividend that is paid in the second and fourth quarters, our ROTCE would have been 9.5%.

Page 17 highlights our outlook for the fourth quarter. For the fourth quarter, we continue to expect low-to-single-digit quarterly growth in our core portfolio and slightly lower growth in our total portfolio. Given the challenging rate environment, we expect our margin for the fourth quarter continue to decline to between 2.9% and 3%, resulting in our full-year margin being around the bottom of our target range. This takes into account the impact of the September rate cut and a continued rate decline in the fourth quarter, which will continue to pressure yields on loans and investment securities.

Net rail yields are expected to decline from re-pricing of renewed leases. Also, we had a $3 million warranty settlement in the third quarter that is not expected to reoccur. We expect declines in deposit rates to only partially offset the asset yield declines. As I mentioned earlier, we expect to meet our full-year 2019 operating expense guidance, despite the additional costs related to the Mutual of Omaha Bank acquisition, which implies the fourth quarter operating expenses should be flat to slightly down when compared to the third quarter.

The net efficiency ratio is expected to be around the mid-50s next quarter, reflecting a higher level of capital markets fees and gains on sale of assets to offset the loan and finance revenue. Credit performance remains strong, and as a result, for the fourth quarter, our expectation is for the credit provision to be $25 million to $35 million, a $5 million reduction from our previous outlook. The effective tax rate, absent any discrete items, is expected to be consistent with our full-year outlook.

We expect our common equity tier 1 ratio will remain high in the mid-to-high 11% range. Given the impact of the rate environment and the higher capital level, our return on tangible common equity for the fourth quarter normalized for the preferred dividend is now expected to be 9.5% to 10%. We remain focused on continuous improvement in closing the Mutual of Omaha Bank transaction, and we will update our 2020 guidance on our fourth quarter earnings call.

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

**Ellen Alemany**
Thanks, John. Moving forward, we are focused on advancing our strategic priorities, growing our core businesses, optimizing our deposit costs, managing our expenses, and maintaining credit discipline. In addition, we are focused on completing the Mutual of Omaha Bank transaction pending regulatory approval. We believe this field will drive significant value for CIT and unlock potential for our customers, communities, and shareholders.

With that, we are happy to take your questions.

**Question-and-Answer Session**

**Operator**
Yes, thank you. We will now begin the question-and-answer session. To ask a question, you may press *, then 1 on your touchtone phone. If you are using a speakerphone, please pick up our handset before pressing the keys. To withdraw your question, please press *, then 2. At this time, we will pause momentarily to assemble the roster. The first question comes from Scott Valentin with Compass Point.

**Scott Valentin**
Good morning, everyone. Thanks for taking my question. Just trying to look out into 2020 on the cadence of the margin. Obviously not looking for exact guidance, but a lot of it obviously depends on what the fed does. If we assume the fed cuts rates again in the fourth quarter, then kind of holds off with the margin, then drops again in 1Q 2020, and then with Mutual Omaha Bank closing at the end of 1Q, potentially margin could improve in 2Q given the lower cost deposits. Is that a fair cadence?

**John Fawcett**
Yes. I think it's a fair cadence, Scott. The reality is you're going to have a series of rate cuts that happen this year that are going to continue to flow through into 2020. So, you will have July, September, and we are modeling October, and who knows what happens in December.

With your point spot on in part of the value of Mutual of Omaha Bank transaction is obviously the lower cost deposits that are then scalable, and so, that provides us an instantaneous benefit of 20 basis points in terms of deposit funding, and more important than that, I think from our perspective, is the fact that it's actually scalable.

So, yes, I think for the rest of this year, you expect July, September, and October to work through, impact rest of 2020 with the benefit of Mutual of Omaha Bank coming in hopefully early in the first quarter. Then, I think the other lever that we have to play is on the deposits, and so if you look at what we have done already, so we have had two rate cuts. We've pulled down the online rate on our savings builder product by 35 basis points.

We expect that we would move again very early in November to kind of keep pace with the fed actions, and so, that becomes the wildcard. Again, as you look at the change of what we can actually do in the deposit space, you have two levers. You have rate, which is in large part driven by competition in the marketplace, and you have advertising and marketing, which we've also tried to be very circumspect around. So, you don't want to cut too quickly, and I think so far, we've hit a pretty good note, because we haven't seen any meaningful levels of attrition in the savings builder product.

**Scott Valentin**
Thanks, those are helpful. Just one follow-up question. The average core loan growth was a little better than I expected. It was 2.3% linked quarter. I know you mentioned factoring seasonality. Is that a primary driver, or are you seeing broad-based better outlook, maybe in terms of core loan growth?

**Ellen Alemany**
Scott, this is Ellen. We had a really solid quarter, and we're actually going into the fourth quarter with a very, very strong pipeline. That's despite customers being cautious with capital spending, fears of an economic slowdown, etc., but I would say that in business capital, that's probably the strongest growth in the business. In commercial finance, the key verticals that have been performing include aviation lending, healthcare, real estate, and renewable project finance.

In real estate, we're not expecting any significant growth, and as John mentioned, we had a lot of pre-payments, but we had some really good capital markets fees from syndicating more deals in real estate. So overall, it wasn't just the seasonality in factoring business, and pipeline is very strong.

**Scott Valentin**
Okay. Thanks very much.

**Operator**
Thank you, and the next question comes from Eric Wasserstrom with UBS.

**Eric Wasserstrom**
Thanks very much. Just two points of clarification, please. The first, just on the NPL trend, you mentioned the NPLs that you sold, but then, it looks like the NPL ratio also increased in the absolute level, also sequential increased. Can you just walk us through what is occurring there?

**John Fawcett**
Yes. So, the NPLs have been, for at least the time that I've been here, $300 million plus or minus 25 or so. I think there's probably a little bit of confusion around the impact of the LCM

portfolio. So, the LCM portfolio, which is about $205 million, those were for the most part not included in non-accrual loans at all.

So, it's not like we came down and went back up. Most of the LCM portfolio was purchased credit impaired and never included in non-accrual. So, what you are seeing is non-accrual is kind of trending right around 1% of total loans. So, nothing has really changed in the last probably eight to ten quarters that I've been here.

**Ellen Alemany**
And I just want to reiterate that we don't see any specific indicators that suggests any type of a credit downturn, and I think we've been talking about this a lot this year, how we have really transformed the whole credit profile of this Company. But just right now, criticized loans at the end of the third quarter totaled $3 billion, which is just like 9% of commercial loans and leases. This is kind of the lowest level that I've ever seen this at the Company here.

It's down about a $1 billion from a year ago, and also, we have at the Company less exposure to consumer debt. We're underweight on residential mortgage. We're not in the credit card business. Cash flow loans now are only about 10% of our total exposure. So, I feel we are in really good shape here on the credit line.

**Eric Wasserstrom**
Yes. Thank you for that. And so, just to follow-up on the NIM. I think as I just sort of extrapolate what the short-term trend is, let's say heading a bit lower, factor in potentially the impact of Mutual of Omaha, and then look out into next year, it seems that the consensus expectation is for a 30 or 40 basis-point rise from the current level, and maybe some of that is reflecting the expectation of the benefit from the lower funding costs from the acquisition.
But not pushing for guidance, but just directionally, how do we think about the roll forward of the NIM into over the next few periods?

**John Fawcett**
I think it's the same analysis I went through with Scott. The reality is that we are in the midst of our planning process right now, and it's a little bit of a juggling act because we are trying to do is dimension exactly when we think the Mutual of Omaha Bank transaction is going to close. And we think it will be in the first quarter, hopefully sooner rather than later, but that'll have a huge bearing on the NIM guidance.

And so, as I said, we're in the midst of our planning process right now, and so, I really can't say much more than that. I do expect that we will come through in the fourth quarter with more comprehensive guidance and hopefully even have some perspective from the SEC in terms of when we might expect the trade to close.

**Eric Wasserstrom**
Excellent. Thanks very much.

**Operator**
Thank you, and the next question comes from Chris Kotowski with Oppenheimer & Company.

**Chris Kotowski**
Yes, good morning. As I was reading this kind of in a hurry this morning, I noticed you said in the text somewhere that RWAs went up because you increased the rail order book, and I guess that particularly makes sense since the share buyback is being suspended and you have

excess capital right now. But how long does it take? A, how material is it in terms of the uptick in the risk-weighted assets, and how long does it take before those, the order becomes an earning assets, and how much is involved?

**John Fawcett**
Yes, we have a fairly rigorous program around portfolio management. So, I think, Chris, as you know, we've been taking cars out of the HoldCo, which is subject to fresh start accounting and realizing gains, and we've probably been doing $15 to $20 million a quarter. When we buy new cars, which is on a fairly regular basis, they come when they come. I think we took a delivery of 600 cars in the quarter, but I want to say about 400 of those cars were in the tank space. And so, it's not really a special event.

The extra thing I would say about RWAs is that we are going to be very circumspect in terms of managing RWAs across the fourth quarter just because it's going to work into the calculation of the amount of shares that we are actually going to deliver to Mutual of Omaha. So, I think we are going to be very mindful in terms of the way we think about risk-weighted assets in terms of the assets we put on, the kind of returns they're generating, the importance they are, they might have to the customer, and where we have an optionality probably for a little bit less so that we can kind of provide a little bit less common equity to Mutual of Omaha, which is, we can deliver up to $150 million in shares to the Mutual of Omaha parent.

**Chris Kotowski**
Okay. That's it from me. Thank you.

**Operator**
Thank you, and once again, if you would like to ask a question, please press * and then 1 on your touchtone phone. The next question comes from Vincent Caintic with Stephens.

**Vincent Caintic**
Thanks, good morning. I appreciate the fourth quarter guidance and the details there. Just kind of when you think about 2020, I know it's early and you're still planning, but kind of broadly speaking, when you think about the fourth quarter, is that a good jumping point for 2020? Are there particular items there that we should note? And then kind of focusing on the NIM again, remember the last time we had low interest rates, you had floors, and I was just kind of wondering, if there are any other mitigating factors to asset yields that we should be thinking about for asset yields declining for 2020?

**Ellen Alemany**
I think we're in great shape going into 2020. One is, we've further strengthened the management team. One is, we have one really experienced individual, who has done a lot of integration work running the Mutual of Omaha integration for us, and then on the commercial banking side, Bob's brought in Dave Harnisch to run the commercial finance group, very seasoned, and Phil Robbins to run the asset management capital markets and Jim Gifas to run treasury management.

So, what you're going to see on the commercial banking side is more a traditional thinking model as we integrate Mutual of Omaha, which is leading transactions, more asset management strategies. We have (an asset management vehicle) and Northbridge both up and running. Those are JV structures that allow us to originate deals that wouldn't be our like credit appetite, but we moved them into these joint ventures. And then, Jim Gifas running treasury management, so that we can generate more merchant card, commercial card, treasury management revenue from our customers.

So, all that is kind of in place, up and running now, and I think the Mutual of Omaha deal is going to be game changing for us because a 20 basis points drop in deposits is going to allow us to play in space from a probability default to not just below where we play today, which will put us in regular more commercial banking land, in terms of the competitive landscape.

So, I feel really positive. We got our application in for Mutual of Omaha in 30 days. We're in the common period now, which ends on Saturday, and as John said, we're hoping that this deal gets approved in the first quarter. Obviously the earlier we can get approval on this, the better for us, but we are in good shape.

**John Fawcett**
And Vincent, just to hit your questions of Q4 being a good jump off point, I would say it is definitely not. We're going to continue to aggressively manage our deposit cost down, as we have thus far, and as Ellen said, the Mutual of Omaha Bank transaction is a game changer for us. It just gives us an enormous amount of optionality. So on a go forward basis, we feel very good about the trade, and I think the more time we spend looking at it, the better we feel.

**Vincent Caintic**
Okay, great, and I guess on the asset yield side, just following up on that the asset yield side, are you close to your floors, or are there other mitigating factors on how we typically think about LIBOR declining and that just directly translating, or is there other factors to that?

**John Fawcett**
It's a contract-by-contract thing. So, I think a lot of the relationships have floors. A lot of them don't. So, it depends. As low as LIBOR goes, so goes the net interest margin. I think the other thing too is, you wonder at some point, our spread is going to start to widen out a little bit to offset some of that, but it's just incredibly hard to forecast. 50% of our loans right now are floating.

So, if you look at all of commercial finance, that's essentially all tied to one- and three-month LIBOR. If you looked at commercial real estate, that's 100% floating that's tied to largely one- to three-month LIBOR, which were down 31 and 27 basis points in the third quarter. And then essentially, half of our consumer mortgage book is floating rate. So, it's a big part of the book.

**Vincent Caintic**
Okay, got you. And then switching gears on the just kind of broadly, as you are talking to your customers, is there any sort of things you are hearing? I know when we read these reports, people are concerned about a recession and maybe a slowdown. Just kind of wanting to get a sense of what you are hearing from your customers, since you're probably good read into the U.S. economy. And then, any sort of watch list industries you are looking at. I know energy has been a concern for some banks, just your thoughts there. Thanks.

**Ellen Alemany**
So, I would say just in general what we are observing is that customers are cautious with capital spending, I think that there are kind of indicators in the market of a potential macro slowdown. There's obviously the geopolitical risk out there. We are hearing anecdotally that tariffs are affecting some of our customers.

We had actually some of our leasing customers, the used equipment market is really, really strong right now because new orders on some equipment, like material handling equipment, is taking six to 12 months. Some consumer electronics are taking much longer order book because of the impact on tariffs. So, we are seeing some of that.

In the factoring business, I think what we've heard from customers is that tariffs aren't affecting the Christmas season, but it may impact potentially the spring season. I think in terms of energy, obviously we finance oil and gas exploration and production companies through our rail car leasing business, but as energy production in the U.S. has moved to really greener and cleaner, so as our lending business, and we've been doing a lot of project finance in the renewable energy space.

E&P midstream and services energy loan exposure is like less than $1 billion dollars. I think it's $945 million or less than 3% of our total loans. And so, I think that we have reduced our exposure substantially in the energy space. So, I think on the credit side, and really if you think about everything we've done over the last several years, we've de-risked the Company from certain businesses like financial freedom, NACCO, which would be international rail, the commercial air portfolio.

We are now a heightened standard bank. We have stress testing in our portfolio, etc. We've kept all those processes in place, even though we are no longer a CCAR bank. We've built out second line of defense. We have a credit review in place. These were all things CIT didn't have several years ago that are in place now. So, I think we feel we're better prepared to withstand challenges of a downturn in the market than we ever have in the Company's history.

**Vincent Caintic**
Great, all very helpful. Thanks so much.

**Operator**
Thank you, and the next question comes from Arren Cyganovich with Citi.

**Arren Cyganovich**
Thanks. One of the things about the Mutual of Omaha acquisition that seem to come up, and I'm coming at the sort of view that I view this as a positive deal. But some of the pushback I got from speaking with investors after this was, how many of these do we expect in the future and should be concerned about this management team diluting shareholders further by future gears of deals with kind of longer earn back period. So, what's your view post this acquisition or your appetite for additional deals in the future?

**Ellen Alemany**
We feel that Mutual of Omaha was a really unique opportunity for CIT, and that it enhanced our deposit funding, and it really helped us build out a middle market banking franchise. Although on a short-term basis it was dilutive, we think it's going to have a positive impact of like 80 basis points of ROTCE in the first 12 months and hundred thereafter.

But any feedback that we have ever had on CIT is you need more long-term source of lower beta deposits and, secondly, more earnings, and this deal solves for both those issues. So, we thought it was a really good opportunity for us, and we think that the benefits of this deal is going to have really long-term implications for the Company in terms of kind of fixing those two challenges that we had.

And I would say that this management team has time and time again said that we’re always open to opportunities that are going to help accelerate or create more value for the shareholders. But right now, this team is really focused on executing this deal as quickly as possible and really showing the market that even though we made a long-term decision here for the Company. We took a little short-term pain to do it, but this team is going to execute this deal and show the market that we have really created a lot of value here.

**Arren Cyganovich**
Thank you.

**Operator**
Thank you, and at this time, I would like to return the floor to management for any closing comments.

**Barbara Callahan**
Great. Thank you, everyone, for joining 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. Thanks again for your time and have a great day.

**Operator**
Thank you. That concludes today's call.  Thank you for participating.