

FIRST FINANCIAL BANCORP /OH/

Form 10-Q

August 08, 2018

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**FORM 10-Q**

**UNITED STATES**

**SECURITIES AND EXCHANGE COMMISSION**

**Washington D.C. 20549**

**x QUARTERLY REPORT UNDER SECTION 13 OR 15(d) OF THE SECURITIES EXCHANGE ACT OF 1934**

For the quarterly period ended June 30, 2018

**OR**

**o TRANSITION REPORT UNDER SECTION 13 OR 15(d) OF THE SECURITIES EXCHANGE ACT OF 1934**

For the transition period from \_\_\_\_\_ to \_\_\_\_\_

Commission file number 001-34762

**FIRST FINANCIAL BANCORP.**

(Exact name of registrant as specified in its charter)

Ohio	31-1042001
(State or other jurisdiction of incorporation or organization)	(I.R.S. Employer Identification No.)

255 East Fifth Street, Suite 700	45202
Cincinnati, Ohio	
(Address of principal executive offices)	(Zip Code)

Registrant's telephone number, including area code: (877) 322-9530

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 and posted on its corporate Web site, if any, every Interactive Data File required to be submitted and posted pursuant to Rule 405 of Regulation S-T (§ 232.405 of this chapter) during the

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preceding 12 months (or for such shorter period that the registrant was required to submit and post such files). Yes  No

Indicate by check mark whether the registrant is a large accelerated filer, an accelerated filer, a non-accelerated filer, smaller reporting company, or an emerging growth company. See the 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 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.

Class	Outstanding at 8/7/2018
Common stock, No par value	97,901,046

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**FIRST FINANCIAL BANCORP.**

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Table of Contents**Glossary of Abbreviations and Acronyms**

First Financial has identified the following list of abbreviations and acronyms that are used in the Notes to Consolidated Financial Statements and the Management's Discussion and Analysis of Financial Condition and Results of Operations.

ALLL	Allowance for loan and lease losses	FASB	Financial Accounting Standards Board
AOCI	Accumulated other comprehensive income	FDIC	Federal Deposit Insurance Corporation
ASC	Accounting standards codification	FHLB	Federal Home Loan Bank
ASU	Accounting standards update	First Financial	First Financial Bancorp.
ATM	Automated teller machine	Form 10-K	First Financial Bancorp. Annual Report on Form 10-K
Bank	First Financial Bank	FRB	Federal Reserve Bank
Basel III	Basel Committee regulatory capital reforms, Third Basel Accord	GAAP	U.S. Generally Accepted Accounting Principles
Bp/bps	Basis point(s)	Insignificant	Less than \$0.1 million
CDs	Certificates of deposit	IRLC	Interest Rate Lock Commitment
C&I	Commercial & Industrial	MSFG	MainSource Financial Group, Inc.
CRE	Commercial Real Estate	N/A	Not applicable
Company	First Financial Bancorp.	NII	Net interest income
ERM	Enterprise Risk Management	OREO	Other real estate owned
EVE	Economic value of equity	SEC	United States Securities and Exchange Commission
Fair Value Topic	FASB ASC Topic 825, Financial Instruments	TDR	Troubled debt restructuring

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**PART I - FINANCIAL INFORMATION**  
**ITEM I - FINANCIAL STATEMENTS**  
**FIRST FINANCIAL BANCORP. AND SUBSIDIARIES**  
**CONSOLIDATED BALANCE SHEETS**  
(Dollars in thousands)

	June 30, 2018 (Unaudited)	December 31, 2017
<b>Assets</b>		
Cash and due from banks	\$216,667	\$150,650
Interest-bearing deposits with other banks	37,915	33,974
Investment securities available-for-sale, at fair value (amortized cost \$2,677,257 at June 30, 2018 and \$1,348,227 at December 31, 2017)	2,654,909	1,349,408
Investment securities held-to-maturity (fair value \$435,785 at June 30, 2018 and \$653,101 at December 31, 2017)	443,957	654,008
Other investments	95,004	53,140
Loans held for sale	15,821	11,502
Loans and leases		
Commercial & industrial	2,440,596	1,912,743
Lease financing	96,198	89,347
Construction real estate	555,468	467,730
Commercial real estate	3,888,993	2,490,091
Residential real estate	918,904	471,391
Home equity	835,031	493,604
Installment	100,726	41,586
Credit card	48,665	46,691
<b>Total loans and leases</b>	8,884,581	6,013,183
Less: Allowance for loan and lease losses	54,076	54,021
<b>Net loans and leases</b>	8,830,505	5,959,162
Premises and equipment	223,950	125,036
Goodwill and other intangibles	934,656	209,379
Accrued interest and other assets	466,783	350,664
<b>Total assets</b>	\$13,920,167	\$8,896,923
<b>Liabilities</b>		
Deposits		
Interest-bearing demand	\$2,440,088	\$1,453,463
Savings	3,087,683	2,462,420
Time	2,104,044	1,317,105
<b>Total interest-bearing deposits</b>	7,631,815	5,232,988
Noninterest-bearing	2,471,932	1,662,058
<b>Total deposits</b>	10,103,747	6,895,046
Federal funds purchased and securities sold under agreements to repurchase	88,070	72,265
FHLB short-term borrowings	1,100,233	742,300
<b>Total short-term borrowings</b>	1,188,303	814,565
Long-term debt	469,423	119,654
<b>Total borrowed funds</b>	1,657,726	934,219
Accrued interest and other liabilities	145,757	136,994
<b>Total liabilities</b>	11,907,230	7,966,259
<b>Shareholders' equity</b>		

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Common stock - no par value		
Authorized - 160,000,000 shares; Issued - 104,281,794 shares in 2018 and 68,730,731 in 2017	1,632,572	573,109
Retained earnings	533,319	491,847
Accumulated other comprehensive loss	(43,008 )	(20,390 )
Treasury stock, at cost, 6,376,897 shares in 2018 and 6,661,644 shares in 2017	(109,946 )	(113,902 )
<b>Total shareholders' equity</b>	<b>2,012,937</b>	<b>930,664</b>
<b>Total liabilities and shareholders' equity</b>	<b>\$ 13,920,167</b>	<b>\$ 8,896,923</b>

See Notes to Consolidated Financial Statements.

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Table of Contents**FIRST FINANCIAL BANCORP. AND SUBSIDIARIES  
CONSOLIDATED STATEMENTS OF INCOME**

(Dollars in thousands, except per share data)

(Unaudited)

	Three months ended		Six months ended	
	June 30,	June 30,	June 30,	June 30,
	2018	2017	2018	2017
<b>Interest income</b>				
Loans and leases, including fees	\$ 122,290	\$ 67,748	\$ 197,210	\$ 134,616
Investment securities				
Taxable	20,844	12,598	34,514	24,206
Tax-exempt	4,068	1,457	5,725	2,810
Total interest on investment securities	24,912	14,055	40,239	27,016
Other earning assets	177	(1,014)	284	(2,015)
<b>Total interest income</b>	147,379	80,789	237,733	159,617
<b>Interest expense</b>				
Deposits	14,794	8,679	25,092	15,604
Short-term borrowings	4,132	2,051	6,795	3,483
Long-term borrowings	4,474	1,539	6,055	3,078
<b>Total interest expense</b>	23,400	12,269	37,942	22,165
<b>Net interest income</b>	123,979	68,520	199,791	137,452
Provision for loan and lease losses	3,735	467	6,038	834
<b>Net interest income after provision for loan and lease losses</b>	120,244	68,053	193,753	136,618
<b>Noninterest income</b>				
Service charges on deposit accounts	9,568	4,772	14,607	9,416
Trust and wealth management fees	3,697	3,405	7,651	7,152
Bankcard income	5,343	3,501	8,737	6,636
Client derivative fees	1,463	1,489	3,220	2,592
Net gain from sales of loans	2,316	1,327	2,904	2,543
Net gain (loss) on sales of investment securities	(30)	838	(30)	1,354
Other	5,899	2,122	8,105	5,125
<b>Total noninterest income</b>	28,256	17,454	45,194	34,818
<b>Noninterest expenses</b>				
Salaries and employee benefits	55,531	31,544	86,633	63,294
Net occupancy	6,631	4,302	11,128	8,817
Furniture and equipment	5,298	2,136	7,338	4,313
Data processing	14,304	3,501	17,976	6,799
Marketing	2,644	982	3,445	1,492
Communication	1,118	468	1,577	915
Professional services	5,659	1,469	7,857	3,227
State intangible tax	1,078	721	1,843	1,442
FDIC assessments	1,323	1,018	2,217	1,950
Loss (gain) - other real estate owned	(283)	162	(206)	186
Other	9,452	5,253	15,235	10,166
<b>Total noninterest expenses</b>	102,755	51,556	155,043	102,601
Income before income taxes	45,745	33,951	83,904	68,835
Income tax expense	9,327	11,215	16,980	21,685
<b>Net income</b>	\$ 36,418	\$ 22,736	\$ 66,924	\$ 47,150

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Net earnings per common share - basic	\$0.37	\$ 0.37	\$0.84	\$0.77
Net earnings per common share - diluted	\$0.37	\$ 0.37	\$0.83	\$0.76
Cash dividends declared per share	\$0.19	\$ 0.17	\$0.38	\$0.34
Average common shares outstanding - basic	97,347,533	61,543,478	79,599,709	61,471,347
Average common shares outstanding - diluted	98,432,072	62,234,022	80,629,495	62,187,473

See Notes to Consolidated Financial Statements.

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Table of Contents**FIRST FINANCIAL BANCORP. AND SUBSIDIARIES  
CONSOLIDATED STATEMENTS OF COMPREHENSIVE INCOME****(Dollars in thousands)  
(Unaudited)**

	Three months ended June 30,		Six months ended June 30,	
	2018	2017	2018	2017
Net income	\$36,418	\$22,736	\$66,924	\$47,150
Other comprehensive income (loss), net of tax:				
Unrealized gain (loss) on investment securities arising during the period	(8,978 )	4,076	(18,808 )	5,563
Change in retirement obligation	494	213	817	402
Unrealized gain (loss) on derivatives	159	128	315	256
Other comprehensive income (loss)	(8,325 )	4,417	(17,676 )	6,221
<b>Comprehensive income</b>	<b>\$28,093</b>	<b>\$27,153</b>	<b>\$49,248</b>	<b>\$53,371</b>

See Notes to Consolidated Financial Statements.

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**FIRST FINANCIAL BANCORP. AND SUBSIDIARIES**  
**CONSOLIDATED STATEMENTS OF CHANGES IN SHAREHOLDERS' EQUITY**  
**(Dollars in thousands except per share data)**  
**(Unaudited)**

	Common Stock	Common Stock	Retained	Accumulated other comprehensive	Treasury stock		Total
	Shares	Amount	Earnings	income (loss)	Shares	Amount	
Balance at January 1, 2017	68,730,731	\$ 570,382	\$ 437,188	\$ (28,443 )	(6,751,179 )	\$(113,903 )	\$ 865,224
Net income			47,150				47,150
Other comprehensive income (loss)				6,221			6,221
Cash dividends declared:							
Common stock at \$0.34 per share			(21,088 )				(21,088 )
Warrant exercises		(25 )			1,484	25	0
Exercise of stock options, net of shares purchased		(462 )			39,062	660	198
Restricted stock awards, net of forfeitures		(3,559 )			120,973	1,005	(2,554 )
Share-based compensation expense		2,966					2,966
Balance at June 30, 2017	68,730,731	\$ 569,302	\$ 463,250	\$ (22,222 )	(6,589,660 )	\$(112,213 )	\$ 898,117
Balance at January 1, 2018	68,730,731	\$ 573,109	\$ 491,847	\$ (20,390 )	(6,661,644 )	\$(113,902 )	\$ 930,664
Net income			66,924				66,924
Reclassification of certain tax effects from AOCI to retained earnings			4,942	(4,942 )			0
Other comprehensive income (loss)				(17,676 )			(17,676 )
Cash dividends declared:							
Common stock at \$0.38 per share			(30,394 )				(30,394 )
Common stock issued in connection with business combinations	35,551,063	1,045,876					1,045,876
Stock options and warrants acquired and converted in connection with business combinations		16,037					16,037
Warrant exercises		(922 )			53,907	922	0
Exercise of stock options, net of shares purchased		(275 )			31,554	542	267
Restricted stock awards, net of forfeitures		(4,699 )			199,286	2,492	(2,207 )
Share-based compensation expense		3,446					3,446
<b>Balance at June 30, 2018</b>	<b>104,281,794</b>	<b>\$ 1,632,572</b>	<b>\$ 533,319</b>	<b>\$ (43,008 )</b>	<b>(6,376,897 )</b>	<b>\$(109,946 )</b>	<b>\$ 2,012,937</b>

See Notes to Consolidated Financial Statements.

Table of Contents**FIRST FINANCIAL BANCORP. AND SUBSIDIARIES  
CONSOLIDATED STATEMENTS OF CASH FLOWS****(Dollars in thousands)****(Unaudited)**

	Six months ended	
	June 30,	
	2018	2017
<b>Operating activities</b>		
Net income	\$66,924	\$47,150
Adjustments to reconcile net income to net cash provided by operating activities:		
Provision for loan and lease losses	6,038	834
Depreciation and amortization	10,208	6,354
Stock-based compensation expense	3,446	2,966
Pension expense (income)	182	(637 )
Net amortization (accretion) on investment securities	5,178	4,998
Net (gains) losses on sales of investment securities	30	(1,354 )
Originations of loans held for sale	(54,041 )	(75,543 )
Net gains from sales of loans held for sale	(2,904 )	(2,543 )
Proceeds from sales of loans held for sale	50,004	78,771
Deferred income taxes	(12,104 )	3,987
Decrease (increase) cash surrender value of life insurance	398	(116 )
Decrease (increase) in interest receivable	(565 )	(1,397 )
Decrease (increase) in indemnification asset	1,900	2,418
(Decrease) increase in interest payable	2,596	148
Decrease (increase) in other assets	26,646	(18,472 )
(Decrease) increase in other liabilities	10,724	(5,571 )
Net cash provided by (used in) operating activities	114,660	41,993
<b>Investing activities</b>		
Proceeds from sales of securities available-for-sale	216,197	125,606
Proceeds from calls, paydowns and maturities of securities available-for-sale	161,733	102,893
Purchases of securities available-for-sale	(444,686 )	(464,543 )
Proceeds from calls, paydowns and maturities of securities held-to-maturity	26,834	72,078
Purchases of securities held-to-maturity	(14,014 )	(14,441 )
Net decrease (increase) in interest-bearing deposits with other banks	(3,941 )	52,611
Net decrease (increase) in loans and leases	(83,617 )	(121,944 )
Proceeds from disposal of other real estate owned	2,840	2,292
Purchases of premises and equipment	(13,662 )	(4,247 )
Net cash (paid) acquired from business combinations	64,887	0
Net cash paid for branch divestitures	(41,197 )	0
Net cash provided by (used in) investing activities	(128,626 )	(249,695 )
<b>Financing activities</b>		
Net (decrease) increase in total deposits	(55,757 )	(56,879 )
Net (decrease) increase in short-term borrowings	178,143	280,421
Payments on long-term debt	(51,985 )	0
Proceeds from FHLB borrowings	50,000	0
Cash dividends paid on common stock	(40,685 )	(20,243 )
Proceeds from exercise of stock options	267	283

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Net cash provided by (used in) financing activities	79,983	203,582
Cash and due from banks		
<b>Change in cash and due from banks</b>	66,017	(4,120 )
Cash and due from banks at beginning of period	150,650	121,598
<b>Cash and due from banks at end of period</b>	\$216,667	\$117,478

**Supplemental schedule for investing activities**

Business combinations

Assets acquired, net of purchase consideration	\$3,328,802	\$0
Liabilities assumed	4,007,743	0
Goodwill	\$678,941	\$0

See Notes to Consolidated Financial Statements.

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**FIRST FINANCIAL BANCORP. AND SUBSIDIARIES**  
**NOTES TO CONSOLIDATED FINANCIAL STATEMENTS**  
**June 30, 2018**  
**(Unaudited)**

**NOTE 1: BASIS OF PRESENTATION**

The Consolidated Financial Statements of First Financial Bancorp., a financial holding company principally serving Ohio, Indiana, Kentucky and Illinois, include the accounts and operations of First Financial and its wholly-owned subsidiary, First Financial Bank. All significant intercompany transactions and accounts have been eliminated in consolidation. Certain reclassifications of prior periods' amounts have been made to conform to current year presentation. Such reclassifications had no effect on net earnings.

The preparation of financial statements in conformity with GAAP requires management to make estimates, assumptions and judgments that affect the amounts reported in the Consolidated Financial Statements and accompanying Notes. These estimates, assumptions and judgments are inherently subjective and may be susceptible to significant change. Actual realized amounts could differ materially from these estimates.

These interim financial statements have been prepared in accordance with the instructions to Form 10-Q and Article 10 of Regulation S-X, and serve to update the Form 10-K for the year ended December 31, 2017. These interim financial statements may not include all information and notes necessary to constitute a complete set of financial statements under GAAP applicable to annual periods and it is suggested that these interim statements be read in conjunction with the Form 10-K. Management believes these unaudited consolidated financial statements reflect all adjustments of a normal recurring nature which are necessary for a fair presentation of the results for the interim periods presented. The results of operations for the interim periods are not necessarily indicative of the results that may be expected for the full year or any other interim period. The Consolidated Balance Sheet as of December 31, 2017 has been derived from the audited financial statements in the Company's 2017 Form 10-K.

**NOTE 2: RECENTLY ADOPTED AND ISSUED ACCOUNTING STANDARDS**

In May 2014, the FASB issued an update (ASU 2014-09, Revenue from Contracts with Customers) which outlines a single comprehensive model for entities to use in accounting for revenue arising from contracts with customers and supersedes most current revenue recognition guidance, including industry-specific guidance. Under the revised standard, an entity recognizes revenue to depict the transfer of promised goods or services to customers in an amount that reflects the consideration to which the entity expects to be entitled in exchange for those goods or services. The ASU applies to all contracts with customers except those that are within the scope of other topics in the FASB Accounting Standards Codification. Certain of the ASU's provisions also apply to transfers of nonfinancial assets, including in-substance nonfinancial assets that are not an output of an entity's ordinary activities, such as sales of property, plant, and equipment; real estate; or intangible assets. The ASU also requires significantly expanded disclosures about revenue recognition. For further detail, see Note 13 – Revenue Recognition.

In January 2016, the FASB issued an update (ASU 2016-01, Financial Instruments-Overall: Recognition and Measurement of Financial Assets and Financial Liabilities) which requires entities to measure many equity investments at fair value and recognize changes in fair value in net income. This update does not apply to equity investments that result in consolidation, those accounted for under the equity method and certain others, and will eliminate use of the available for sale classification for equity securities while providing a new measurement alternative for equity investments that do not have readily determinable fair values and do not qualify for the net asset value practical expedient. This update also requires public business entities to use the exit price notion when measuring the fair value of financial instruments for disclosure purposes. The guidance in this ASU became effective

in the first quarter of 2018 and did not have a material impact on the Consolidated Financial Statements. In accordance with the guidance, the Company measured the fair value of its financial instruments as of June 30, 2018 using an exit price notion. For further detail, see Note 15 – Fair Value Disclosures.

In February 2016, the FASB issued an update (ASU 2016-02, Leases) which requires lessees to record most leases on their balance sheet and recognize leasing expenses in the income statement. Operating leases, except for short-term leases that are subject to an accounting policy election, will be recorded on the balance sheet for lessees by establishing a lease liability and corresponding right-of-use asset. The guidance in this ASU will become effective for interim and annual reporting periods beginning after December 15, 2018, with early adoption permitted. Given operating leases outstanding as of June 30, 2018, First Financial does not expect this ASU to have a material impact on the income statement, but does anticipate an increase in the Company's assets and liabilities. Decisions to repurchase, modify or renew leases prior to the implementation date will impact this level of materiality.

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In June 2016, the FASB issued an update (ASU 2016-13, Financial Instruments-Credit Losses: Measurement of Credit Losses on Financial Instruments) which significantly changes how entities are required to measure credit losses for most financial assets and certain other instruments that are not measured at fair value through net income. This update will replace the current incurred loss approach for estimating credit losses with an expected loss model for instruments measured at amortized cost, including loans and leases. Expected credit losses are required to be based on amortized cost and reflect losses expected over the remaining contractual life of the asset. Management is expected to consider any available information relevant to assessing the collectibility of contractual cash flows, such as information about past events, current conditions, voluntary prepayments and reasonable and supportable forecasts, when developing expected credit loss estimates.

In addition to the new framework for calculating the ALLL, this update requires allowances for available-for-sale debt securities rather than a reduction of the security's carrying amount under the current other-than-temporary impairment model. This update also simplifies the accounting model for purchased credit-impaired debt securities and loans and will require new and updated footnote disclosures.

The guidance in this ASU will become effective for interim and annual reporting periods beginning after December 15, 2019. Early adoption is permitted for all entities for interim and annual reporting periods beginning after December 15, 2018. First Financial has formed an internal management committee and engaged a third party vendor to assist with the transition to the guidance set forth in this update. The committee is currently evaluating the impact of this update on First Financial's Consolidated Financial Statements.

In August 2016, the FASB issued an update (ASU 2016-15 Statement of Cash Flows: Classification of Certain Cash Receipts and Cash Payments) which may change how an entity classifies certain cash receipts and cash payments on its statement of cash flows to reduce diversity in practice. The update also provides guidance on when an entity should separate cash flows and classify them into more than one class and when an entity should classify the aggregate of those cash flows into a single class based on the predominance principle. The guidance in this ASU became effective in the first quarter of 2018 and did not have a material impact on the Consolidated Financial Statements.

In January 2017, the FASB issued an update (ASU 2017-04, Intangibles - Goodwill and Other (Topic 350), Simplifying the Test for Goodwill Impairment) which simplifies the subsequent measurement of goodwill by eliminating Step 2 from goodwill impairment testing. This update requires an entity to perform its annual, or interim, goodwill impairment test by comparing the fair value of a reporting unit with its carrying amount, and recognize an impairment charge for the amount by which the carrying amount exceeds the reporting unit's fair value, with any loss recognized not to exceed the total amount of goodwill allocated to that reporting unit. Additionally, the update requires consideration of the income tax effects from any tax deductible goodwill on the carrying amount of the reporting unit when measuring the goodwill impairment loss, if applicable, and eliminates the requirements for any reporting unit with a zero or negative carrying amount to perform a qualitative assessment. First Financial early adopted the provisions set forth in this update in 2017. Adoption of this update did not have a material impact on First Financial's Consolidated Financial Statements.

In March 2017, the FASB issued an update (ASU 2017-07, Compensation - Retirement Benefits (Topic 715), Improving the Presentation of the Net Periodic Pension Cost and Net Periodic Postretirement Benefit Cost) which requires disaggregation of the service cost component from the other components of net benefit cost. This update also provides explicit guidance on how to present the service cost component and the other components of net benefit cost in the income statement and allows only the service cost component of net benefit cost to be eligible for capitalization. The guidance in this ASU became effective in the first quarter of 2018 and did not have a material impact on the Consolidated Financial Statements.

In March 2017, the FASB issued an update (ASU 2017-08, Receivables - Nonrefundable Fees and Other Costs (Subtopic 310-20), Premium Amortization on Purchased Callable Debt Securities) which amends the amortization period for certain purchased callable debt securities held at a premium and shortens the amortization period for the premium to the earliest call date rather than as an adjustment of yield over the contractual life of the instrument. This update more closely aligns the amortization period of premiums and discounts to expectations incorporated in market pricing on the underlying securities, as in most cases, market participants price securities to the call date that produces the worst yield when the coupon is above current market rates (that is, the security is trading at a premium) and price securities to maturity when the coupon is below market rates (that is, the security is trading at a discount) in anticipation that the borrower will act in its economic best interest in an attempt to more closely align interest income recorded on bonds held at a premium or a discount with the economics of the underlying instrument. The guidance in this ASU will become effective for reporting periods, beginning after December 15, 2018, with early adoption permitted. First Financial is currently evaluating the impact of this update on its Consolidated Financial Statements.



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In May 2017, the FASB issued an update (ASU 2017-09, Compensation - Stock Compensation (Topic 718), Scope of Modification Accounting), which provides clarity and reduces the diversity in practice, cost and complexity when accounting for a change to the terms or conditions of a share-based payment award. The amendments in this update provide guidance about which changes to the terms or conditions of a share-based payment award require an entity to apply modification accounting in Topic 718 clarifying that an entity will not apply modification accounting to a share-based payment award if the award's fair value (or calculated value or intrinsic value), vesting conditions and classification as an equity or liability instrument are the same immediately before and after the change. The guidance in this ASU became effective in the first quarter of 2018 and did not have a material impact on the Consolidated Financial Statements.

In August 2017, the FASB issued an update (ASU 2017-12, Derivatives and Hedging: Targeted Improvements to Accounting for Hedging Activities) to better align financial reporting for hedging activities with the economic objectives of those activities. This update aligns certain aspects of hedge documentation, effectiveness assessments, accounting and disclosures, and expands permissible hedge strategies as of the date of adoption. The guidance in this ASU will become effective for reporting periods beginning after December 15, 2018, with early adoption permitted, and will require a modified retrospective transition method with recognition of the cumulative effect of the change on the opening balance of each affected component of equity. Amended disclosures will be required prospectively. First Financial is currently evaluating the impact of this update on its Consolidated Financial Statements.

In February 2018, the FASB issued an update (ASU 2018-02, Income statement-Reporting Comprehensive Income: Reclassification of Certain Tax Effects from Accumulated Other Comprehensive Income), which allows a reclassification from accumulated other comprehensive income to retained earnings for stranded tax effects resulting from the Tax Cuts and Jobs Act. Consequently, the amendments eliminated the stranded tax effects resulting from the Tax Cuts and Jobs Act and will improve the usefulness of information reported to financial statement users. The amendments only relate to the reclassification of the income tax effects of the Tax Cuts and Jobs Act, and the underlying guidance that requires that the effect of a change in tax laws or rates be included in income from continuing operations is not effected. The amendments in this update also require certain disclosures about stranded tax effects. The guidance in this ASU will become effective for reporting periods beginning after December 15, 2018, with early adoption permitted, and is applied either in the period of adoption or retrospectively to each period in which the effect of the change in the U.S. federal corporate income tax rate in the Tax Cuts and Jobs Act is recognized. First Financial early adopted the provisions set forth in this update in the first quarter of 2018, and as a result, reclassified \$4.9 million from accumulated other comprehensive income to retained earnings. There were no other income tax effects related to the Act that were reclassified as a result of the adoption of the accounting standard.

**NOTE 3: INVESTMENTS**

For the three and six months ended June 30, 2018, proceeds on the sale of \$216.2 million of available-for-sale securities, and resulted in insignificant gross gains and losses. For the three months ended June 30, 2017, proceeds on the sale of \$103.4 million of available-for-sale securities resulted in gains of \$1.0 million and losses of \$0.1 million. For the six months ended June 30, 2017, proceeds on the sale of \$125.6 million of available-for-sale securities resulted in gains of \$1.5 million and losses of \$0.1 million.

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The following is a summary of held-to-maturity and available-for-sale investment securities as of June 30, 2018:

<i>(Dollars in thousands)</i>	Held-to-maturity				Available-for-sale			
	Amortized cost	Unrecognized gain	Unrecognized loss	Fair value	Amortized cost	Unrealized gain	Unrealized loss	Fair value
U.S. Treasuries	\$0	\$ 0	\$ 0	\$0	\$98	\$ 0	\$(3 )	\$95
Securities of U.S. government agencies and corporations	0	0	0	0	34,896	84	(452 )	34,528
Mortgage-backed securities - residential	31,857	0	(1,515 )	30,342	644,358	1,314	(10,152 )	635,520
Mortgage-backed securities - commercial	152,906	13	(5,503 )	147,416	290,930	106	(5,059 )	285,977
Collateralized mortgage obligations	13,982	0	(675 )	13,307	873,923	965	(10,313 )	864,575
Obligations of state and other political subdivisions	245,212	936	(1,428 )	244,720	250,993	2,214	(1,910 )	251,297
Asset-backed securities	0	0	0	0	492,702	879	(1,354 )	492,227
Other securities	0	0	0	0	89,357	1,938	(605 )	90,690
<b>Total</b>	<b>\$443,957</b>	<b>\$ 949</b>	<b>\$ (9,121 )</b>	<b>\$435,785</b>	<b>\$2,677,257</b>	<b>\$ 7,500</b>	<b>\$(29,848 )</b>	<b>\$2,654,909</b>

The following is a summary of held-to-maturity and available-for-sale investment securities as of December 31, 2017:

<i>(Dollars in thousands)</i>	Held-to-maturity				Available-for-sale			
	Amortized cost	Unrecognized gain	Unrecognized loss	Fair value	Amortized cost	Unrealized gain	Unrealized loss	Fair value
U.S. Treasuries	\$0	\$ 0	\$ 0	\$0	\$98	\$ 0	\$(1 )	\$97
Securities of U.S. government agencies and corporations	11,168	0	(76 )	11,092	15,695	220	0	15,915
Mortgage-backed securities - residential	162,093	2,042	(1,535 )	162,600	290,793	849	(2,599 )	289,043
Mortgage-backed securities - commercial	255,027	1,372	(3,000 )	253,399	150,356	164	(1,417 )	149,103
Collateralized mortgage obligations	143,545	354	(1,602 )	142,297	306,095	1,158	(1,861 )	305,392
Obligations of state and other political subdivisions	82,175	1,804	(266 )	83,713	124,269	2,162	(676 )	125,755
Asset-backed securities	0	0	0	0	377,655	1,628	(306 )	378,977
Other securities	0	0	0	0	83,266	2,147	(287 )	85,126
<b>Total</b>	<b>\$654,008</b>	<b>\$ 5,572</b>	<b>\$ (6,479 )</b>	<b>\$653,101</b>	<b>\$1,348,227</b>	<b>\$ 8,328</b>	<b>\$(7,147 )</b>	<b>\$1,349,408</b>

The following table provides a summary of investment securities by contractual maturity as of June 30, 2018, except for residential and commercial mortgage-backed securities, collateralized mortgage obligations and asset-backed securities, which are shown as single totals due to the unpredictability of the timing in principal repayments.

<i>(Dollars in thousands)</i>	Held-to-maturity		Available-for-sale	
	Amortized cost	Fair value	Amortized cost	Fair value
<b>By Contractual Maturity:</b>				
Due in one year or less	\$0	\$0	\$4,125	\$4,123
Due after one year through five years	275	279	70,801	70,802
Due after five years through ten years	15,799	15,778	140,577	142,222
Due after ten years	229,138	228,663	159,841	159,463
Mortgage-backed securities - residential	31,857	30,342	644,358	635,520
Mortgage-backed securities - commercial	152,906	147,416	290,930	285,977
Collateralized mortgage obligations	13,982	13,307	873,923	864,575
Asset-backed securities	0	0	492,702	492,227
<b>Total</b>	<b>\$443,957</b>	<b>\$435,785</b>	<b>\$2,677,257</b>	<b>\$2,654,909</b>



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Unrealized gains and losses on debt securities are generally due to fluctuations in current market yields relative to the yields of the debt securities at their amortized cost. All securities with unrealized losses are reviewed quarterly to determine if any impairment is considered other than temporary, requiring a write-down to fair value. First Financial considers the percentage loss on a security, duration of the loss, average life or duration of the security, credit rating of the security and payment performance, as well as the Company's intent and ability to hold the security to maturity, when determining whether any impairment is other than temporary. At this time First Financial does not intend to sell, and it is not more likely than not that the Company will be required to sell, debt securities temporarily impaired prior to maturity or recovery of the recorded value. First Financial had no other than temporary impairment related to its investment securities portfolio as of June 30, 2018 or December 31, 2017.

As of June 30, 2018, the Company's investment securities portfolio consisted of 1,385 securities, of which 656 were in an unrealized loss position. As of December 31, 2017, the Company's investment securities portfolio consisted of 775 securities, of which 237 were in an unrealized loss position.

The following tables provide the fair value and gross unrealized losses on investment securities in an unrealized loss position, aggregated by investment category and the length of time the individual securities have been in a continuous loss position:

	June 30, 2018					
	Less than 12 months		12 months or more		Total	
	Fair value	Unrealized loss	Fair value	Unrealized loss	Fair value	Unrealized loss
<i>(Dollars in thousands)</i>						
U.S. Treasuries	\$95	\$(3 )	\$0	\$0	\$95	\$(3 )
Securities of U.S. Government agencies and corporations	19,890	(311 )	5,379	(141 )	25,269	(452 )
Mortgage-backed securities - residential	488,725	(5,650 )	129,218	(6,017 )	617,943	(11,667 )
Mortgage-backed securities - commercial	278,366	(5,414 )	88,624	(5,148 )	366,990	(10,562 )
Collateralized mortgage obligations	628,667	(6,910 )	99,142	(4,078 )	727,809	(10,988 )
Obligations of state and other political subdivisions	186,269	(2,195 )	27,441	(1,143 )	213,710	(3,338 )
Asset-backed securities	219,064	(1,215 )	13,591	(139 )	232,655	(1,354 )
Other securities	17,299	(226 )	7,571	(379 )	24,870	(605 )
<b>Total</b>	<b>\$1,838,375</b>	<b>\$(21,924 )</b>	<b>\$370,966</b>	<b>\$(17,045 )</b>	<b>\$2,209,341</b>	<b>\$(38,969 )</b>

	December 31, 2017					
	Less than 12 months		12 months or more		Total	
	Fair value	Unrealized loss	Fair value	Unrealized loss	Fair value	Unrealized loss
<i>(Dollars in thousands)</i>						
U.S. Treasuries	\$97	\$(1 )	\$0	\$0	\$97	\$(1 )
Securities of U.S. Government agencies and corporations	11,092	(76 )	0	0	11,092	(76 )
Mortgage-backed securities - residential	175,183	(1,109 )	108,782	(3,025 )	283,965	(4,134 )
Mortgage-backed securities - commercial	132,818	(1,713 )	72,139	(2,704 )	204,957	(4,417 )
Collateralized mortgage obligations	164,909	(1,138 )	101,436	(2,325 )	266,345	(3,463 )
Obligations of state and other political subdivisions	38,450	(507 )	21,639	(435 )	60,089	(942 )
Asset-backed securities	44,941	(200 )	24,396	(106 )	69,337	(306 )
Other securities	2,605	(1 )	7,124	(286 )	9,729	(287 )
<b>Total</b>	<b>\$570,095</b>	<b>\$(4,745 )</b>	<b>\$335,516</b>	<b>\$(8,881 )</b>	<b>\$905,611</b>	<b>\$(13,626 )</b>



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For further detail on the fair value of investment securities, see Note 15 – Fair Value Disclosures.

**NOTE 4: LOANS AND LEASES**

First Financial offers clients a variety of commercial and consumer loan and lease products with distinct interest rates and payment terms. Commercial loan categories include C&I, CRE, construction real estate and lease financing. Consumer loan categories include residential real estate, home equity, installment and credit card.

Lending activities are primarily concentrated in states where the Bank operates banking centers (Ohio, Indiana, Kentucky and Illinois). First Financial also offers two nationwide lending platforms, one that provides equipment and leasehold improvement financing for franchisees in the quick service and casual dining restaurant sector and another that provides loans primarily to insurance agents and brokers that are secured by commissions and cash collateral.

**Credit Quality.** To facilitate the monitoring of credit quality for commercial loans, and for purposes of determining an appropriate ALLL, First Financial utilizes the following categories of credit grades:

*Pass* - Higher quality loans that do not fit any of the other categories described below.

*Special Mention* - First Financial assigns a special mention rating to loans and leases with potential weaknesses that deserve management's close attention. If left uncorrected, these potential weaknesses may result in deterioration of the repayment prospects for the loan or lease or in First Financial's credit position at some future date.

*Substandard* - First Financial assigns a substandard rating to loans or leases that are inadequately protected by the current sound financial worth and paying capacity of the borrower or of the collateral pledged, if any. Substandard loans and leases have well-defined weaknesses that jeopardize repayment of the debt. Substandard loans and leases are characterized by the distinct possibility that the Company will sustain some loss if the deficiencies are not addressed.

*Doubtful* - First Financial assigns a doubtful rating to loans and leases with all the attributes of a substandard rating with the added characteristic that the weaknesses make collection or liquidation in full highly questionable and improbable, on the basis of currently existing facts, conditions and values. The possibility of loss is extremely high, but because of certain important and reasonably specific pending factors that may work to the advantage and strengthening of the credit quality of the loan or lease, its classification as an estimated loss is deferred until its more exact status may be determined. Pending factors include proposed merger, acquisition or liquidation procedures, capital injection, perfecting liens on additional collateral and refinancing plans.

The credit grades previously described are derived from standard regulatory rating definitions and are assigned upon initial approval of credit to borrowers and updated periodically thereafter.

First Financial considers repayment performance to be the best indicator of credit quality for consumer loans. Consumer loans that have principal and interest payments that are past due by 90 days or more are generally classified as nonperforming. Additionally, consumer loans that have been modified in a TDR are classified as nonperforming. Purchased impaired loans are not classified as nonperforming assets as the loans are considered to be performing under FASB ASC Topic 310-30.

Commercial and consumer credit exposure by risk attribute was as follows:

	As of June 30, 2018		
	Commercial	Real Estate	Lease
(Dollars in thousands)	Construction	Commercial	financing Total

	&					
	industrial					
Pass	\$2,367,649	\$543,479	\$3,794,902	\$94,763	\$6,800,793	
Special Mention	24,261	11,947	29,399	0	65,607	
Substandard	48,686	42	64,692	1,435	114,855	
Doubtful	0	0	0	0	0	
<b>Total</b>	<b>\$2,440,596</b>	<b>\$555,468</b>	<b>\$3,888,993</b>	<b>\$96,198</b>	<b>\$6,981,255</b>	

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<i>(Dollars in thousands)</i>	Residential real estate	Home equity	Installment	Credit card	Total
Performing	\$ 905,649	\$ 828,558	\$ 100,422	\$ 48,665	\$ 1,883,294
Nonperforming	13,255	6,473	304	0	20,032
<b>Total</b>	<b>\$ 918,904</b>	<b>\$ 835,031</b>	<b>\$ 100,726</b>	<b>\$ 48,665</b>	<b>\$ 1,903,326</b>

As of December 31, 2017					
<i>(Dollars in thousands)</i>	Commercial & industrial	Real Estate Construction	Commercial	Lease financing	Total
Pass	\$ 1,882,464	\$ 467,687	\$ 2,446,999	\$ 88,078	\$ 4,885,228
Special Mention	6,226	0	4,436	0	10,662
Substandard	24,053	43	38,656	1,269	64,021
Doubtful	0	0	0	0	0
<b>Total</b>	<b>\$ 1,912,743</b>	<b>\$ 467,730</b>	<b>\$ 2,490,091</b>	<b>\$ 89,347</b>	<b>\$ 4,959,911</b>

<i>(Dollars in thousands)</i>	Residential real estate	Home equity	Installment	Credit card	Total
Performing	\$ 463,459	\$ 489,148	\$ 41,331	\$ 46,691	\$ 1,040,629
Nonperforming	7,932	4,456	255	0	12,643
<b>Total</b>	<b>\$ 471,391</b>	<b>\$ 493,604</b>	<b>\$ 41,586</b>	<b>\$ 46,691</b>	<b>\$ 1,053,272</b>

**Delinquency.** Loans are considered past due or delinquent when the contractual principal or interest due in accordance with the terms of the loan agreement or any portion thereof remains unpaid after the date of the scheduled payment.



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Loan delinquency, including loans classified as nonaccrual, was as follows:

As of June 30, 2018

<i>(Dollars in thousands)</i>	30 – 59 days past due	60 – 89 days past due	> 90 days past due	Total past due	Current	Subtotal	Purchased impaired	Total	> 90 days past due and still accruing
<b>Loans</b>									
Commercial & industrial	\$ 1,885	\$ 389	\$ 2,814	\$ 5,088	\$ 2,429,204	\$ 2,434,292	\$ 6,304	\$ 2,440,596	\$ 0
Lease financing	0	0	0	0	96,198	96,198	0	96,198	0
Construction real estate	447	0	0	447	554,754	555,201	267	555,468	0
Commercial real estate	3,291	1,829	15,999	21,119	3,803,534	3,824,653	64,340	3,888,993	16
Residential real estate	1,962	601	2,945	5,508	872,404	877,912	40,992	918,904	0
Home equity	3,834	750	3,443	8,027	822,359	830,386	4,645	835,031	0
Installment	165	22	263	450	99,669	100,119	607	100,726	0
Credit card	427	216	311	954	47,711	48,665	0	48,665	311
<b>Total</b>	<b>\$ 12,011</b>	<b>\$ 3,807</b>	<b>\$ 25,775</b>	<b>\$ 41,593</b>	<b>\$ 8,725,833</b>	<b>\$ 8,767,426</b>	<b>\$ 117,155</b>	<b>\$ 8,884,581</b>	<b>\$ 327</b>

As of December 31, 2017

<i>(Dollars in thousands)</i>	30 – 59 days past due	60 – 89 days past due	> 90 days past due	Total past due	Current	Subtotal	Purchased impaired	Total	> 90 days past due and still accruing
<b>Loans</b>									
Commercial & industrial	\$ 755	\$ 1,657	\$ 5,078	\$ 7,490	\$ 1,901,821	\$ 1,909,311	\$ 3,432	\$ 1,912,743	\$ 0
Lease financing	485	0	0	485	88,862	89,347	0	89,347	0
Construction real estate	234	0	0	234	467,216	467,450	280	467,730	0
Commercial real estate	1,716	201	8,777	10,694	2,419,969	2,430,663	59,428	2,490,091	0
Residential real estate	526	811	1,992	3,329	430,500	433,829	37,562	471,391	0
Home equity	2,716	394	1,753	4,863	485,127	489,990	3,614	493,604	0
Installment	179	29	205	413	40,529	40,942	644	41,586	0
Credit card	285	87	62	434	46,257	46,691	0	46,691	62
<b>Total</b>	<b>\$ 6,896</b>	<b>\$ 3,179</b>	<b>\$ 17,867</b>	<b>\$ 27,942</b>	<b>\$ 5,880,281</b>	<b>\$ 5,908,223</b>	<b>\$ 104,960</b>	<b>\$ 6,013,183</b>	<b>\$ 62</b>

**Nonaccrual.** Loans are classified as nonaccrual when, in the opinion of management, collection of principal or interest is doubtful or when principal or interest payments are 90 days or more past due. Generally, loans are classified as nonaccrual due to the continued failure to adhere to contractual payment terms by the borrower, coupled with other pertinent factors. When a loan is classified as nonaccrual, the accrual of interest income is discontinued and previously accrued but unpaid interest is reversed. Any payments received while a loan is on nonaccrual status are applied as a reduction to the carrying value of the loan. A loan classified as nonaccrual may return to accrual status if collection of future principal and interest payments is no longer doubtful.

Purchased impaired loans are classified as performing, even though they may be contractually past due, as any nonpayment of contractual principal or interest is considered in the periodic re-estimation of expected cash flows and is included in the resulting recognition of current period provision for loan and lease losses or prospective yield adjustments.

**Troubled Debt Restructurings.** A loan modification is considered a TDR when the borrower is experiencing financial difficulty and concessions are made by the Company that would not otherwise be considered for a borrower with similar credit characteristics. The most common types of modifications include interest rate reductions, maturity extensions and modifications to principal amortization, including interest-only structures. Modified terms are

dependent upon the financial position and needs of the individual borrower. If the modification agreement is violated, the loan is managed by the Company's credit administration group for resolution, which may result in foreclosure in the case of real estate.

TDRs are generally classified as nonaccrual for a minimum period of six months and may qualify for return to accrual status once they have demonstrated performance with the restructured terms of the loan agreement.

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First Financial had 205 TDRs totaling \$27.8 million at June 30, 2018, including \$21.8 million on accrual status and \$5.9 million classified as nonaccrual. First Financial had an insignificant amount of commitments outstanding to lend additional funds to borrowers whose loan terms have been modified through TDRs, and the ALLL included reserves of \$1.1 million related to TDRs at June 30, 2018. For each of the three and six month periods ended June 30, 2018 and 2017, the Company charged off \$0.1 million for the portion of TDRs determined to be uncollectible. Additionally, as of June 30, 2018, \$13.1 million of accruing TDRs have been performing in accordance with the restructured terms for more than one year.

First Financial had 214 TDRs totaling \$23.9 million at December 31, 2017, including \$17.5 million of loans on accrual status and \$6.4 million classified as nonaccrual. First Financial had an insignificant amount of commitments outstanding to lend additional funds to borrowers whose loan terms had been modified through TDRs. At December 31, 2017, the ALLL included reserves of \$1.3 million related to TDRs, and \$17.2 million of the accruing TDRs had been performing in accordance with the restructured terms for more than one year.

The following tables provide information on loan modifications classified as TDRs during the three and six months ended June 30, 2018 and 2017:

	Three months ended			June 30, 2017		
	June 30, 2018	Period	June 30, 2017	Period	Period	
<i>(Dollars in thousands)</i>	Number of Pre-modification loans	end of loan balance	Number of Pre-modification loans	end of loan balance	end of loan balance	
Commercial & industrial	8	\$ 6,221	\$ 6,183	4	\$ 2,177	\$ 2,183
Construction real estate	0	0	0	0	0	0
Commercial real estate	4	2,047	2,016	6	1,506	1,449
Residential real estate	1	201	201	0	0	0
Home equity	0	0	0	0	0	0
Installment	0	0	0	0	0	0
<b>Total</b>	<b>13</b>	<b>\$ 8,469</b>	<b>\$ 8,400</b>	<b>10</b>	<b>\$ 3,683</b>	<b>\$ 3,632</b>

	Six months ended			June 30, 2017		
	June 30, 2018	Period	June 30, 2017	Period	Period	
<i>(Dollars in thousands)</i>	Number of Pre-modification loans	end of loan balance	Number of Pre-modification loans	end of loan balance	end of loan balance	
Commercial & industrial	12	\$ 7,149	\$ 7,096	6	\$ 5,679	\$ 5,624
Construction real estate	0	0	0	0	0	0
Commercial real estate	6	2,119	2,088	6	1,506	1,449
Residential real estate	3	294	294	0	0	0
Home equity	0	0	0	0	0	0
Installment	0	0	0	0	0	0
<b>Total</b>	<b>21</b>	<b>\$ 9,562</b>	<b>\$ 9,478</b>	<b>12</b>	<b>\$ 7,185</b>	<b>\$ 7,073</b>

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The following table provides information on how TDRs were modified during the three and six months ended June 30, 2018 and 2017:

	Three months ended June 30,		Six months ended June 30,	
	2018	2017	2018	2017
<i>(Dollars in thousands)</i>				
Extended maturities	\$2,000	\$2,587	\$2,888	\$3,261
Adjusted interest rates	0	0	52	2,767
Combination of rate and maturity changes	0	180	0	180
Forbearance	6,199	827	6,199	827
Other <sup>(1)</sup>	201	38	339	38
<b>Total</b>	<b>\$8,400</b>	<b>\$3,632</b>	<b>\$9,478</b>	<b>\$7,073</b>

<sup>(1)</sup> Includes covenant modifications and other concessions, or combination of concessions, that do not consist of interest rate adjustments, forbearance and maturity extensions

First Financial considers repayment performance as an indication of the effectiveness of the Company's loan modifications. Borrowers that are 90 days or more past due on any principal or interest payments, or who prematurely terminate a restructured loan agreement without paying the contractual principal balance (for example, in a deed-in-lieu arrangement), are considered to be in payment default of the terms of the TDR agreement.

There was one TDR, insignificant in amount, for which there was a payment default during the period that occurred within twelve months of the loan modification for the three and six months ended June 30, 2018. There were no TDRs for which there was a payment default during the period that occurred within twelve months of the loan modification for the three or six month periods ended June 30, 2017.

**Impaired Loans.** Loans classified as nonaccrual and loans modified as TDRs are considered impaired. The following table provides information on impaired loans, excluding purchased impaired loans:

	June 30, December 31,	
<i>(Dollars in thousands)</i>	2018	2017
<b>Impaired loans</b>		
Nonaccrual loans <sup>(1)</sup>		
Commercial & industrial	\$3,448	\$ 5,229
Lease financing	0	82
Construction real estate	24	29
Commercial real estate	21,593	10,616
Residential real estate	9,278	4,140
Home equity	5,820	3,743
Installment	299	243
Nonaccrual loans	40,462	24,082
Accruing troubled debt restructurings	21,839	17,545
<b>Total impaired loans</b>	<b>\$62,301</b>	<b>\$ 41,627</b>

<sup>(1)</sup> Nonaccrual loans include nonaccrual TDRs of \$5.9 million and \$6.4 million as of June 30, 2018 and December 31, 2017, respectively.

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	Three months ended June 30,		Six months ended June 30,	
	2018	2017	2018	2017
<i>(Dollars in thousands)</i>				
<b>Interest income effect on impaired loans</b>				
Gross amount of interest that would have been recorded under original terms	\$ 1,132	\$ 1,158	\$ 1,934	\$ 1,974
Interest included in income				
Nonaccrual loans	146	163	226	305
Troubled debt restructurings	189	169	313	395
Total interest included in income	335	332	539	700
<b>Net impact on interest income</b>	<b>\$797</b>	<b>\$826</b>	<b>\$1,395</b>	<b>\$1,274</b>

First Financial individually reviews all impaired commercial loan relationships, as well as consumer loan TDRs, greater than \$250,000, to determine if a specific allowance is necessary based on the borrower's overall financial condition, payment record, support from guarantors and the realizable value of any collateral. Specific allowances are based on discounted cash flows using the loan's initial effective interest rate or the fair value of the collateral for certain collateral dependent loans.

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First Financial's investment in impaired loans was as follows:

	As of June 30, 2018			As of December 31, 2017		
<i>(Dollars in thousands)</i>	Current balance	Contractual principal balance	Related allowance	Current balance	Contractual principal balance	Related allowance
<b>Loans with no related allowance recorded</b>						
Commercial & industrial	\$10,856	\$ 14,647	\$ 0	\$7,162	\$ 8,460	\$ 0
Lease financing	0	0	0	82	82	0
Construction real estate	24	57	0	29	60	0
Commercial real estate	30,655	36,421	0	18,423	20,837	0
Residential real estate	12,216	14,383	0	6,876	8,145	0
Home equity	6,372	7,311	0	4,356	5,399	0
Installment	304	603	0	255	422	0
Total	60,427	73,422	0	37,183	43,405	0
<b>Loans with an allowance recorded</b>						
Commercial & industrial	379	379	179	169	169	169
Lease financing	0	0	0	0	0	0
Construction real estate	0	0	0	0	0	0
Commercial real estate	356	356	25	3,119	3,120	448
Residential real estate	1,039	1,039	160	1,056	1,063	160
Home equity	100	100	2	100	100	2
Installment	0	0	0	0	0	0
Total	1,874	1,874	366	4,444	4,452	779
<b>Total</b>						
Commercial & industrial	11,235	15,026	179	7,331	8,629	169
Lease financing	0	0	0	82	82	0
Construction real estate	24	57	0	29	60	0
Commercial real estate	31,011	36,777	25	21,542	23,957	448
Residential real estate	13,255	15,422	160	7,932	9,208	160
Home equity	6,472	7,411	2	4,456	5,499	2
Installment	304	603	0	255	422	0
<b>Total</b>	<b>\$62,301</b>	<b>\$ 75,296</b>	<b>\$ 366</b>	<b>\$41,627</b>	<b>\$ 47,857</b>	<b>\$ 779</b>

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First Financial's average impaired loans by class and interest income recognized by class was as follows:

	Three months ended			
	June 30, 2018		June 30, 2017	
	Average Interest	Recorded Income	Average Interest	Recorded Income
(Dollars in thousands)	Investment Recognized	Investment Recognized	Investment Recognized	Investment Recognized
<b>Loans with no related allowance recorded</b>				
Commercial & industrial	\$9,714	\$ 73	\$17,198	\$ 87
Lease financing	0	0	98	1
Construction real estate	25	1	1,075	0
Commercial real estate	27,516	140	25,465	144
Residential real estate	9,173	76	7,605	46
Home equity	5,222	27	3,926	27
Installment	305	1	357	1
<b>Total</b>	<b>51,955</b>	<b>318</b>	<b>55,724</b>	<b>306</b>
<b>Loans with an allowance recorded</b>				
Commercial & industrial	309	6	2,301	11
Lease financing	0	0	0	0
Construction real estate	0	0	0	0
Commercial real estate	358	3	658	8
Residential real estate	1,042	7	1,126	6
Home equity	101	1	101	1
Installment	0	0	0	0
<b>Total</b>	<b>1,810</b>	<b>17</b>	<b>4,186</b>	<b>26</b>
<b>Total</b>				
Commercial & industrial	10,023	79	19,499	98
Lease financing	0	0	98	1
Construction real estate	25	1	1,075	0
Commercial real estate	27,874	143	26,123	152
Residential real estate	10,215	83	8,731	52
Home equity	5,323	28	4,027	28
Installment	305	1	357	1
<b>Total</b>	<b>\$53,765</b>	<b>\$ 335</b>	<b>\$59,910</b>	<b>\$ 332</b>

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	Six months ended			
	June 30, 2018		June 30, 2017	
	Average Interest	Average Interest	Recorded Income	Recorded Income
(Dollars in thousands)	Investment Recognized	Investment Recognized	Investment Recognized	Investment Recognized
<b>Loans with no related allowance recorded</b>				
Commercial & industrial	\$8,863	\$ 99	\$15,607	\$ 196
Lease financing	27	0	149	2
Construction real estate	26	2	538	0
Commercial real estate	24,485	239	19,939	304
Residential real estate	8,407	123	8,032	92
Home equity	4,933	47	4,111	51
Installment	288	1	413	3
Total	47,029	511	48,789	648
<b>Loans with an allowance recorded</b>				
Commercial & industrial	262	6	1,094	24
Lease financing	0	0	0	0
Construction real estate	0	0	0	0
Commercial real estate	1,278	6	4,374	13
Residential real estate	1,047	14	1,185	13
Home equity	100	2	101	2
Installment	0	0	0	0
Total	2,687	28	6,754	52
<b>Total</b>				
Commercial & industrial	9,125	105	16,701	220
Lease financing	27	0	149	2
Construction real estate	26	2	538	0
Commercial real estate	25,763	245	24,313	317
Residential real estate	9,454	137	9,217	105
Home equity	5,033	49	4,212	53
Installment	288	1	413	3
<b>Total</b>	<b>\$49,716</b>	<b>\$ 539</b>	<b>\$55,543</b>	<b>\$ 700</b>

**Acquired loans.** Acquired loans are recorded at their estimated fair value at the time of acquisition. Estimated fair values for acquired loans are based on a discounted cash flow methodology that considers various factors including the type of loan and related collateral, classification status, interest rate, term of loan, whether or not the loan was amortizing and a discount rate reflecting the Company's assessment of risk inherent in the cash flow estimates. Acquired loans are grouped together according to similar characteristics and treated in the aggregate when applying various valuation techniques.

First Financial evaluates acquired loans for impairment in accordance with the provisions of FASB ASC Topic 310-30, Loans and Debt Securities Acquired with Deteriorated Credit Quality. Acquired loans with evidence of credit deterioration since origination are accounted for under FASB ASC Topic 310-30 and are referred to as purchased impaired loans. Interest income, through accretion of the difference between the carrying value of the loans and the expected cash flows (accretable difference) is recognized on all purchased impaired loans. First Financial had purchased impaired loans totaling \$117.2 million at June 30, 2018, which included \$24.1 million acquired in the



merger with MSFG. Accretable yield, or income expected to be collected, and nonaccretable yield on the purchase impaired loans acquired in the MSFG merger was \$1.2 million and \$2.7 million, respectively, on the date of acquisition. First Financial had \$105.0 million of purchased impaired loans at December 31, 2017.

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Acquired loans outside of the scope of FASB ASC Topic 310-30 are accounted for under FASB ASC Topic 310-20, Receivables-Nonrefundable Fees and Costs. In its merger with MSFG, First Financial acquired loans with a fair value of \$2.7 billion and gross contractual amounts receivable of \$2.9 billion on the date of acquisition that were accounted for in accordance with FASB ASC Topic 310-20.

**OREO.** OREO consists of properties acquired by the Company primarily through the loan foreclosure or repossession process, or other resolution activity that results in partial or total satisfaction of problem loans.

Changes in OREO were as follows:

	Three months ended June 30,		Six months ended June 30,	
<i>(Dollars in thousands)</i>	2018	2017	2018	2017
Balance at beginning of period	\$1,065	\$5,300	\$2,781	\$6,284
Additions				
Commercial & industrial	1,020	50	1,190	172
Residential real estate	525	1,913	984	2,078
Total additions	1,545	1,963	2,174	2,250
Disposals				
Commercial & industrial	(326 )	(682 )	(2,430 )	(1,607 )
Residential real estate	(292 )	(448 )	(410 )	(685 )
Total disposals	(618 )	(1,130 )	(2,840 )	(2,292 )
Valuation adjustment				
Commercial & industrial	0	(116 )	(97 )	(162 )
Residential real estate	(139 )	(56 )	(165 )	(119 )
Total valuation adjustment	(139 )	(172 )	(262 )	(281 )
<b>Balance at end of period</b>	<b>\$1,853</b>	<b>\$5,961</b>	<b>\$1,853</b>	<b>\$5,961</b>

**NOTE 5: ALLOWANCE FOR LOAN AND LEASE LOSSES**

**Loans and leases.** Management maintains the ALLL at a level that it considers sufficient to absorb probable incurred loan and lease losses inherent in the portfolio. Management determines the adequacy of the ALLL based on historical loss experience as well as other significant factors such as composition of the portfolio, economic conditions, geographic footprint, the results of periodic internal and external evaluations of delinquent, nonaccrual and classified loans and any other adverse situations that may affect a specific borrower's ability to repay, including the timing of future payments.

The ALLL is increased by provision expense and decreased by charge-offs, net of recoveries of amounts previously charged-off. First Financial's policy is to charge-off all or a portion of a loan when, in management's opinion, it is unlikely to collect the principal amount owed in full either through payments from the borrower or from the liquidation of collateral.

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Changes in the ALLL by loan category were as follows:

	Three months ended June 30, 2018									
			Real Estate							
<i>(Dollars in thousands)</i>	Commercial and industrial	Lease financing	Construction	Commercial	Residential	Home Equity	Installment	Credit card	Total	
<b>Allowance for loan and lease losses:</b>										
Balance at beginning of period	\$ 18,038	\$ 626	\$ 4,267	\$ 20,321	\$ 4,727	\$ 4,828	\$ 290	\$ 1,283	\$ 54,380	
Provision for loan and lease losses	3,328	170	(282 )	(619 )	(28 )	171	136	859	3,735	
Gross charge-offs	(4,356 )	0	0	(78 )	(101 )	(385 )	(218 )	(684 )	(5,822 )	
Recoveries	518	1	0	887	70	187	82	38	1,783	
Total net charge-offs	(3,838 )	1	0	809	(31 )	(198 )	(136 )	(646 )	(4,039 )	
<b>Ending allowance for loan and lease losses</b>	<b>\$ 17,528</b>	<b>\$ 797</b>	<b>\$ 3,985</b>	<b>\$ 20,511</b>	<b>\$ 4,668</b>	<b>\$ 4,801</b>	<b>\$ 290</b>	<b>\$ 1,496</b>	<b>\$ 54,076</b>	
	Three months ended June 30, 2017									
			Real Estate							
<i>(Dollars in thousands)</i>	Commercial and industrial	Lease financing	Construction	Commercial	Residential	Home Equity	Installment	Credit card	Total	
<b>Allowance for loan and lease losses:</b>										
Balance at beginning of period	\$ 17,148	\$ 616	\$ 3,607	\$ 23,745	\$ 5,485	\$ 3,774	\$ 419	\$ 1,532	\$ 56,326	
Provision for loan and lease losses	3,537	(67 )	(280 )	(2,941 )	(305 )	526	19	(22 )	467	
Loans charged off	(3,065 )	0	0	(485 )	(223 )	(384 )	(126 )	(215 )	(4,498 )	
Recoveries	693	1	89	1,398	59	222	43	73	2,578	
Total net charge-offs	(2,372 )	1	89	913	(164 )	(162 )	(83 )	(142 )	(1,920 )	
<b>Ending allowance for loan and lease losses</b>	<b>\$ 18,313</b>	<b>\$ 550</b>	<b>\$ 3,416</b>	<b>\$ 21,717</b>	<b>\$ 5,016</b>	<b>\$ 4,138</b>	<b>\$ 355</b>	<b>\$ 1,368</b>	<b>\$ 54,873</b>	
	Six months ended June 30, 2018									
			Real Estate							
<i>(Dollars in thousands)</i>	Commercial & industrial	Lease financing	Construction	Commercial	Residential	Home equity	Installment	Credit card	Total	
<b>Allowance for loan and lease losses:</b>										
Balance at beginning of period	\$ 17,598	\$ 675	\$ 3,577	\$ 20,930	\$ 4,683	\$ 4,935	\$ 307	\$ 1,316	\$ 54,021	
Provision for loan and lease losses	4,217	121	408	196	86	(123 )	87	1,046	6,038	
Loans charged off	(5,241 )	0	0	(2,254 )	(197 )	(627 )	(234 )	(938 )	(9,491 )	
Recoveries	954	1	0	1,639	96	616	130	72	3,508	
Total net charge-offs	(4,287 )	1	0	(615 )	(101 )	(11 )	(104 )	(866 )	(5,983 )	
<b>Ending allowance for loan and lease losses</b>	<b>\$ 17,528</b>	<b>\$ 797</b>	<b>\$ 3,985</b>	<b>\$ 20,511</b>	<b>\$ 4,668</b>	<b>\$ 4,801</b>	<b>\$ 290</b>	<b>\$ 1,496</b>	<b>\$ 54,076</b>	
	As of June 30, 2018									
			Real Estate							
<i>(Dollars in thousands)</i>	Commercial & industrial	Lease financing	Construction	Commercial	Residential	Home equity	Installment	Credit card	Total	
<b>Ending allowance balance attributable to loans</b>										
Individually evaluated for impairment	\$ 179	\$ 0	\$ 0	\$ 25	\$ 160	\$ 2	\$ 0	\$ 0	\$ 366	
Collectively evaluated for impairment	17,349	797	3,985	20,486	4,508	4,799	290	1,496	53,710	
<b>Ending allowance for loan and lease losses</b>	<b>\$ 17,528</b>	<b>\$ 797</b>	<b>\$ 3,985</b>	<b>\$ 20,511</b>	<b>\$ 4,668</b>	<b>\$ 4,801</b>	<b>\$ 290</b>	<b>\$ 1,496</b>	<b>\$ 54,076</b>	
<b>Loans</b>										
Individually evaluated for impairment	\$ 11,235	\$ 0	\$ 24	\$ 31,011	\$ 13,255	\$ 6,472	\$ 304	\$ 0	\$ 62,301	
Collectively evaluated for impairment	2,429,361	96,198	555,444	3,857,982	905,649	828,559	100,422	48,665	8,822,280	
<b>Total loans</b>	<b>\$ 2,440,596</b>	<b>\$ 96,198</b>	<b>\$ 555,468</b>	<b>\$ 3,888,993</b>	<b>\$ 918,904</b>	<b>\$ 835,031</b>	<b>\$ 100,726</b>	<b>\$ 48,665</b>	<b>\$ 8,884,581</b>	



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Six months ended June 30, 2017

(Dollars in thousands)	Real Estate								Total
	Commercial & industrial	Lease financing	Construction	Commercial	Residential	Home equity	Installment	Credit card	
<b>Allowance for loan and lease losses:</b>									
Balance at beginning of period	\$ 19,225	\$ 716	\$ 3,282	\$ 26,540	\$ 3,208	\$ 3,043	\$ 388	\$ 1,559	\$ 57,961
Provision for loan and lease losses	2,941	(167 )	45	(5,507 )	2,024	1,331	28	139	834
Loans charged off	(4,808 )	0	0	(970 )	(284 )	(564 )	(175 )	(447 )	(7,248 )
Recoveries	955	1	89	1,654	68	328	114	117	3,326
Total net charge-offs	(3,853 )	1	89	684	(216 )	(236 )	(61 )	(330 )	(3,922 )
<b>Ending allowance for loan and lease losses</b>	<b>\$ 18,313</b>	<b>\$ 550</b>	<b>\$ 3,416</b>	<b>\$ 21,717</b>	<b>\$ 5,016</b>	<b>\$ 4,138</b>	<b>\$ 355</b>	<b>\$ 1,368</b>	<b>\$ 54,873</b>

As of December 31, 2017

(Dollars in thousands)	Real Estate								Total
	Commercial & industrial	Lease financing	Construction	Commercial	Residential	Home equity	Installment	Credit card	
<b>Ending allowance balance attributable to loans</b>									
Individually evaluated for impairment	\$ 169	\$ 0	\$ 0	\$ 448	\$ 160	\$ 2	\$ 0	\$ 0	\$ 779
Collectively evaluated for impairment	17,429	675	3,577	20,482	4,523	4,933	307	1,316	53,242
<b>Ending allowance for loan and lease losses</b>	<b>\$ 17,598</b>	<b>\$ 675</b>	<b>\$ 3,577</b>	<b>\$ 20,930</b>	<b>\$ 4,683</b>	<b>\$ 4,935</b>	<b>\$ 307</b>	<b>\$ 1,316</b>	<b>\$ 54,021</b>

**Loans**

Individually evaluated for impairment	\$ 7,331	\$ 82	\$ 29	\$ 21,542	\$ 7,932	\$ 4,456	\$ 255	\$ 0	\$ 41,627
Collectively evaluated for impairment	1,905,412	89,265	467,701	2,468,549	463,459	489,148	41,331	46,691	5,971,556
<b>Total loans</b>	<b>\$ 1,912,743</b>	<b>\$ 89,347</b>	<b>\$ 467,730</b>	<b>\$ 2,490,091</b>	<b>\$ 471,391</b>	<b>\$ 493,604</b>	<b>\$ 41,586</b>	<b>\$ 46,691</b>	<b>\$ 6,013,183</b>

**NOTE 6: GOODWILL AND OTHER INTANGIBLE ASSETS**

**Goodwill.** Assets and liabilities acquired in a business combination are recorded at their estimated fair values as of the acquisition date. The excess cost of the acquisition over the fair value of net assets acquired is recorded as goodwill. During the second quarter of 2018, First Financial recorded additions to goodwill resulting from the merger with MSFG. No additions to goodwill were recorded during 2017. For further detail on the merger with MSFG, see Note 16 - Business Combinations.

Changes in the carrying amount of goodwill for the six months ended June 30, 2018 and the year ended December 31, 2017 were as follows:

(Dollars in thousands)	June 30, 2018	December 31, 2017
Balance at beginning of year	\$ 204,084	\$ 204,084
Goodwill resulting from business combinations	678,941	0
<b>Balance at end of period</b>	<b>\$ 883,025</b>	<b>\$ 204,084</b>

Goodwill is evaluated for impairment on an annual basis as of October 1 of each year, or whenever events or changes in circumstances indicate that the fair value of a reporting unit may be below its carrying value. First Financial performed its most recent annual impairment test as of October 1, 2017 and no impairment was indicated. As of June 30, 2018, no events or changes in circumstances indicated that the fair value of a reporting unit was below its carrying value.

**Other intangible assets.** As of June 30, 2018 and December 31, 2017, First Financial had \$51.6 million and \$5.3 million, respectively, of other intangible assets included in Goodwill and other intangibles in the Consolidated Balance Sheets, which primarily consist of core deposit intangibles. Core deposit intangibles represent the estimated fair value of acquired customer deposit relationships on the date of acquisition and are amortized on an accelerated basis over their estimated useful lives. Core deposit intangibles were \$42.5 million and \$3.3 million as of June 30, 2018 and December 31, 2017, respectively. First Financial's core deposit intangibles have an estimated weighted average remaining life of 9.3 years. Amortization expense recognized on intangible assets for the three months ended June 30, 2018 and 2017 was \$2.4 million and \$0.3 million, respectively. Amortization expense recognized on intangible assets for the six months ended June 30, 2018 and 2017 was \$2.6 million and \$0.7 million, respectively.

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Short-term borrowings on the Consolidated Balance Sheets include repurchase agreements utilized for corporate sweep accounts with cash management account agreements in place, overnight advances from the FHLB and a short-term line of credit. All repurchase agreements are subject to terms and conditions of repurchase/security agreements between the Bank and the client. To secure its liability to the client, the Bank is authorized to sell or repurchase U.S. Treasury, government agency and mortgage-backed securities.

First Financial had \$1.1 billion in short-term borrowings with the FHLB at June 30, 2018 and \$742.3 million as of December 31, 2017. These short-term borrowings are used to manage normal liquidity needs and support the Company's asset and liability management strategies.

First Financial has a \$15.0 million short-term credit facility with an unaffiliated bank that matured in July 2018, but is in the process of being extended. This facility can have a variable or fixed interest rate and provides First Financial additional liquidity, if needed, for various corporate activities including the repurchase of First Financial common stock and the payment of dividends to shareholders. As of June 30, 2018 and December 31, 2017, there was no outstanding balance. The credit agreement requires First Financial to comply with certain covenants including those related to asset quality and capital levels, and First Financial was in compliance with all covenants associated with this facility as of June 30, 2018 and December 31, 2017.

In conjunction with its merger with MSFG, First Financial acquired certain variable rate short-term borrowings with an unaffiliated bank. As of June 30, 2018, the balance outstanding was \$8.3 million and the interest rate was 4.19%. This term debt is paid quarterly and matures in 2019.

First Financial had \$469.4 million and \$119.7 million of long-term debt as of June 30, 2018 and December 31, 2017, respectively, which included subordinated notes, FHLB long term advances and an interest free loan with a municipality.

The following is a summary of First Financial's long-term debt:

	June 30, 2018		December 31, 2017	
<i>(Dollars in thousands)</i>	Amount	Average rate	Amount	Average rate
Subordinated notes	\$177,887	5.13 %	\$120,000	5.13 %
Unamortized discount and debt issuance costs	(8,819 )	N/A	(1,362 )	N/A
FHLB borrowings	299,580	1.90 %	241	1.09 %
Capital loan with municipality	775	0.00 %	775	0.00 %
<b>Total long-term debt</b>	<b>\$469,423</b>	<b>3.16 %</b>	<b>\$119,654</b>	<b>5.14 %</b>

In 2015, First Financial issued \$120.0 million of subordinated notes, which have a fixed interest rate of 5.125% payable semiannually and mature on August 25, 2025. These notes are not redeemable by the Company, or callable by the holders of the notes prior to maturity. The subordinated notes are treated as Tier 2 capital for regulatory capital purposes. In addition, First Financial acquired, \$49.5 million of variable rate subordinated notes in the MSFG merger that was issued to previously formed trusts in exchange for the trust proceeds. Interest on the acquired subordinated notes is payable quarterly, in arrears, and the Company has the option to defer interest payments for a period not to exceed 20 consecutive quarters. The acquired subordinated notes mature 30 years from issuance and may be called at par at any point following the 5 years anniversary of issuance. First Financial also acquired \$8.4 million of 6.95% fixed rate private placement subordinated debt in conjunction with the MSFG merger that matures in 2025.

In addition to subordinated notes, long-term debt included \$299.6 million and \$0.2 million of fixed rate FHLB long-term advances as of June 30, 2018 and December 31, 2017, respectively. As of June 30, 2018, these long-term advances had a weighted average interest rate of 1.90%. These instruments are primarily utilized to reduce overnight liquidity risk and to mitigate interest rate sensitivity on the Consolidated Balance Sheets.

**NOTE 8: ACCUMULATED OTHER COMPREHENSIVE INCOME (LOSS)**

Shareholders' equity is affected by transactions and valuations of asset and liability positions that require adjustments to accumulated other comprehensive income (loss). The related tax effects allocated to other comprehensive income



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e and reclassifications out of accumulated other comprehensive income (loss) are as follows:

Three months ended June 30, 2018										
<i>(Dollars in thousands)</i>	Total other comprehensive income (loss)					Total accumulated other comprehensive income (loss)				
	Prior to Reclass	Reclass from	Pre-tax	Tax effect	Net of tax	Beginning Balance	Net Activity	Ending Balance		
Unrealized gain (loss) on investment securities	\$ (11,456 )	\$ (30 )	\$ (11,426 )	\$ 2,448	\$ (8,978 )	\$ (10,051 )	\$ (8,978 )	\$ (19,029 )		
Unrealized gain (loss) on derivatives	203	0	203	(44 )	159	(545 )	159	(386 )		
Retirement obligation	0	(452 )	452	42	494	(24,087 )	494	(23,593 )		
<b>Total</b>	\$ (11,253 )	\$ (482 )	\$ (10,771 )	\$ 2,446	\$ (8,325 )	\$ (34,683 )	\$ (8,325 )	\$ (43,008 )		
Three months ended June 30, 2017										
<i>(Dollars in thousands)</i>	Total other comprehensive income (loss)					Total accumulated other comprehensive income (loss)				
	Prior to Reclass	Reclass from	Pre-tax	Tax effect	Net of tax	Beginning Balance	Net Activity	Ending Balance		
Unrealized gain (loss) on investment securities	\$ 7,170	\$ 838	\$ 6,332	\$ (2,256 )	\$ 4,076	\$ (3,062 )	\$ 4,076	\$ 1,014		
Unrealized gain (loss) on derivatives	202	0	202	(74 )	128	(963 )	128	(835 )		
Retirement obligation	0	(335 )	335	(122 )	213	(22,614 )	213	(22,401 )		
<b>Total</b>	\$ 7,372	\$ 503	\$ 6,869	\$ (2,452 )	\$ 4,417	\$ (26,639 )	\$ 4,417	\$ (22,222 )		
Six months ended June 30, 2018										
<i>(Dollars in thousands)</i>	Total other comprehensive income					Total accumulated other comprehensive income (loss)				
	Prior to Reclass	Reclass from	Pre-tax	Tax effect	Net of tax	Beginning Balance	Net Activity	Reclass of Stranded Tax Effects	Ending Balance	
Unrealized gain (loss) on investment securities	\$ (23,992 )	\$ (30 )	\$ (23,962 )	\$ 5,154	\$ (18,808 )	\$ (182 )	\$ (18,808 )	\$ (39 )	\$ (19,029 )	
Unrealized gain (loss) on derivatives	405	0	405	(90 )	315	(577 )	315	(124 )	(386 )	
Retirement obligation	0	(871 )	871	(54 )	817	(19,631 )	817	(4,779 )	(23,593 )	
<b>Total</b>	\$ (23,587 )	\$ (901 )	\$ (22,686 )	\$ 5,010	\$ (17,676 )	\$ (20,390 )	\$ (17,676 )	\$ (4,942 )	\$ (43,008 )	

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	Six months ended June 30, 2017					Total accumulated other comprehensive income (loss)		
	Prior to Reclass	Reclass from	Pre-tax	Tax effect	Net of tax	Beginning Balance	Net Activity	Ending Balance
<i>(Dollars in thousands)</i>								
Unrealized gain (loss) on investment securities	\$ 10,002	\$ 1,354	\$ 8,648	\$(3,085)	\$ 5,563	\$(4,549)	\$ 5,563	\$ 1,014
Unrealized gain (loss) on derivatives	405	0	405	(149)	256	(1,091)	256	(835)
Retirement obligation	0	(670)	670	(268)	402	(22,803)	402	(22,401)
<b>Total</b>	<b>\$ 10,407</b>	<b>\$ 684</b>	<b>\$ 9,723</b>	<b>\$(3,502)</b>	<b>\$ 6,221</b>	<b>\$(28,443)</b>	<b>\$ 6,221</b>	<b>\$(22,222)</b>

The following table presents the activity reclassified from accumulated other comprehensive income into income during the three and six month periods ended June 30, 2018 and 2017, respectively:

	Amount reclassified from accumulated other comprehensive income <sup>(1)</sup>				Affected Line Item in the Consolidated Statements of Income
	Three months ended June 30, 2018	Six months ended June 30, 2017	Three months ended June 30, 2018	Six months ended June 30, 2017	
<i>(Dollars in thousands)</i>					
Realized gain (loss) on securities available-for-sale	\$(30)	\$838	\$(30)	\$1,354	Net gain (loss) on sales of investments securities
Defined benefit pension plan					
Amortization of prior service cost <sup>(2)</sup>	103	104	206	207	Other noninterest expense (2018) Salaries and employee benefits (2017)
Recognized net actuarial loss <sup>(2)</sup>	(555)	(439)	(1,077)	(877)	Other noninterest expense (2018) Salaries and employee benefits (2017)
Defined benefit pension plan total	(452)	(335)	(871)	(670)	
<b>Total reclassifications for the period, before tax</b>	<b>\$(482)</b>	<b>\$503</b>	<b>\$(901)</b>	<b>\$684</b>	

<sup>(1)</sup> Negative amounts are reductions to net income.

<sup>(2)</sup> Included in the computation of net periodic pension cost (see Note 12 - Employee Benefit Plans for additional details).

**NOTE 9: DERIVATIVES**

First Financial uses certain derivative instruments, including interest rate caps, floors and swaps, to meet the needs of its clients while managing the interest rate risk associated with certain transactions. First Financial does not use derivatives for speculative purposes.

First Financial primarily utilizes interest rate swaps as a means to offer borrowers credit-based products that meet their needs. First Financial may also utilize interest rate swaps to manage the interest rate risk profile of the Company.

Interest rate payments are exchanged with counterparties based on the notional amount established in the interest rate agreement. As only interest rate payments are exchanged, the cash requirements and credit risk associated with interest rate swaps are significantly less than the notional amount and the Company's credit risk exposure is limited to the market value of the instruments. First Financial manages market value credit risk through counterparty credit policies, which require the Company to maintain a total derivative notional position of less than 35% of assets, total credit exposure of less than 3% of capital and no single counterparty credit risk exposure greater than \$20.0 million. The Company is currently below all single counterparty and portfolio limits.

At June 30, 2018, the Company had a total counterparty notional amount outstanding of \$1.2 billion, spread among

fourteen counterparties, with an outstanding asset from these contracts of \$21.8 million. At December 31, 2017, the Company had a total counterparty notional amount outstanding of \$837.5 million, spread among thirteen counterparties, with an outstanding liability from these contracts of \$1.3 million.

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First Financial monitors its derivative credit exposure to borrowers by monitoring the creditworthiness of the related loan customers through the normal credit review processes the Company performs on all borrowers. Additionally, the Company monitors derivative credit risk exposure related to problem loans through the Company's ALLL committee. First Financial considers the market value of a derivative instrument to be part of the carrying value of the related loan for these purposes as the borrower is contractually obligated to pay First Financial this amount in the event the derivative contract is terminated.

**Client Derivatives.** First Financial utilizes interest rate swaps as a means to offer commercial borrowers fixed rate funding while providing the Company with floating rate assets. The following table details the classification and amounts recognized in the Consolidated Balance Sheets for client derivatives:

(Dollars in thousands)	Balance sheet classification	June 30, 2018			December 31, 2017		
		Notional amount	Estimated fair value		Notional amount	Estimated fair value	
			Gain	Loss		Gain	Loss
Client derivatives - instruments associated with loans							
Matched interest rate swaps with borrower	Accrued interest and other assets	\$ 1,179,156	\$ 3,261	\$(24,306)	\$ 837,040	\$ 7,153	\$(5,529)
Matched interest rate swaps with counterparty	Accrued interest and other liabilities	1,179,156	24,306	(3,259)	837,040	5,529	(7,158)
<b>Total</b>		<b>\$ 2,358,312</b>	<b>\$ 27,567</b>	<b>\$(27,565)</b>	<b>\$ 1,674,080</b>	<b>\$ 12,682</b>	<b>\$(12,687)</b>

In connection with its use of derivative instruments, First Financial and its counterparties may be required to post cash collateral to offset the market position of the derivative instruments. First Financial maintains the right to offset these derivative positions with the collateral posted against them by or with the relevant counterparties. First Financial classifies the derivative cash collateral outstanding with its counterparties as an adjustment to the fair value of the derivative contracts within Accrued interest and other assets or Accrued interest and other liabilities in the Consolidated Balance Sheets.

The following table discloses the gross and net amounts of client derivative liabilities recognized in the Consolidated Balance Sheets:

(Dollars in thousands)	June 30, 2018			December 31, 2017		
	Gross amounts of recognized liabilities	Gross amounts offset in the Consolidated Balance Sheets	Net amounts of liabilities presented in the Consolidated Balance Sheets	Gross amounts of recognized liabilities	Gross amounts offset in the Consolidated Balance Sheets	Net amounts of liabilities presented in the Consolidated Balance Sheets
Client derivatives						
Matched interest rate swaps with counterparty	\$ 27,567	\$(7,152)	\$ 20,415	\$ 12,687	\$ 2,279	\$ 14,966

The following table details the derivative financial instruments, the average remaining maturities and the weighted-average interest rates being paid and received by First Financial at June 30, 2018:

(Dollars in thousands)	Notional amount	Average maturity (years)	Fair value	Weighted-average rate	
				Receive	Pay
Client derivatives					
Receive fixed, matched interest rate swaps with borrower	\$ 1,179,156	4.8	\$(21,045)	4.50 %	4.25 %
Pay fixed, matched interest rate swaps with counterparty	1,179,156	4.8	21,047	4.25 %	4.50 %
<b>Total client derivatives</b>	<b>\$ 2,358,312</b>	<b>4.8</b>	<b>\$ 2</b>	<b>4.37 %</b>	<b>4.37 %</b>

**Credit Derivatives.** In conjunction with participating interests in commercial loans, First Financial periodically enters into risk participation agreements with counterparties whereby First Financial assumes a portion of the credit exposure associated with an interest rate swap on the participated loan in exchange for a fee. Under these agreements, First Financial will make payments to the counterparty if the loan customer defaults on its obligation to perform under the interest rate swap contract with the counterparty. The total notional value of these agreements totaled \$146.3 million as of June 30, 2018 and \$95.9 million as of December 31, 2017. The fair value of these agreements is recorded in Accrued interest and other liabilities on the Consolidated Balance Sheets and was \$0.1 million at both June 30, 2018 and December 31, 2017.

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**Mortgage Derivatives.** First Financial enters into IRLCs and forward commitments for the future delivery of mortgage loans to third party investors, which are considered derivatives. When borrowers secure an IRLC with First Financial and the loan is intended to be sold, First Financial will enter into forward commitments for the future delivery of the loans to third party investors in order to hedge against the effect of changes in interest rates impacting IRLCs and loans held for sale. At June 30, 2018, the notional amount of the IRLCs was \$37.2 million and the notional amount of forward commitments was \$35.6 million. As of December 31, 2017, the notional amount of IRLCs was \$12.3 million and the notional amount of forward commitments was \$15.4 million. The fair value of these agreements was insignificant at both June 30, 2018 and \$0.1 million December 31, 2017 and was recorded in Accrued interest and other assets on the Consolidated Balance Sheets.

### **NOTE 10: COMMITMENTS AND CONTINGENCIES**

First Financial offers a variety of financial instruments including standby letters of credit and outstanding commitments to extend credit to assist clients in meeting their requirement for liquidity and credit enhancement. GAAP does not require these financial instruments to be recorded in the Consolidated Financial Statements.

First Financial utilizes the same credit policies in issuing commitments and conditional obligations as it does for credit instruments recorded on the Consolidated Balance Sheets. First Financial's exposure to credit loss in the event of nonperformance by the counterparty is represented by the contractual amounts of those instruments. First Financial utilizes the ALLL methodology to maintain a reserve that it considers sufficient to absorb probable incurred losses inherent in letters of credit and outstanding loan commitments and records the reserve within Accrued interest and other liabilities on the Consolidated Balance Sheets. First Financial had \$1.1 million and \$0.5 million of reserves for unfunded commitments as of June 30, 2018 and December 31, 2017, respectively.

**Loan commitments.** Loan commitments are agreements to extend credit to a client, absent any violation of conditions established in the commitment agreement. Commitments generally have fixed expiration dates or other termination clauses and may require payment of a fee. Since many of the commitments are expected to expire without being drawn upon, the total commitment amounts do not necessarily represent future cash requirements. The amount of collateral obtained, if deemed necessary by First Financial upon extension of credit, is based on management's credit evaluation of the client. The collateral held varies, but may include securities, real estate, inventory, plant or equipment. First Financial had commitments outstanding to extend credit totaling \$2.9 billion and \$2.1 billion at June 30, 2018 and December 31, 2017, respectively. As of June 30, 2018, loan commitments with a fixed interest rate totaled \$215.8 million while commitments with variable interest rates totaled \$2.6 billion. At December 31, 2017, loan commitments with a fixed interest rate totaled \$44.3 million while commitments with variable interest rates totaled \$2.0 billion. First Financial's fixed rate loan commitments have interest rates ranging from 0.00% to 21.00% and maturities ranging from less than 1 year to 30 years.

**Letters of credit.** Letters of credit are conditional commitments issued by First Financial to guarantee the performance of a client to a third party. First Financial's portfolio of letters of credit consists primarily of performance assurances made on behalf of clients who have a contractual commitment to produce or deliver goods or services. The risk to First Financial arises from its obligation to make payment in the event of the client's contractual default to produce the contracted good or service to a third party. First Financial issued letters of credit aggregating \$35.6 million and \$25.3 million at June 30, 2018 and December 31, 2017, respectively. Management conducts regular reviews of these instruments on an individual client basis.

**Investments in affordable housing tax credits.** First Financial has made investments in certain qualified affordable housing tax credits. These credits are an indirect federal subsidy that provide tax incentives to encourage investment in the development, acquisition and rehabilitation of affordable rental housing, and allow investors to claim tax credits and other tax benefits (such as deductions from taxable income for operating losses) on their federal income tax

returns. The principal risk associated with qualified affordable housing investments is the potential for noncompliance with the tax code requirements, such as failure to rent property to qualified tenants, resulting in the unavailability or recapture of the tax credits and other tax benefits. Investments in affordable housing projects are accounted for under the proportional amortization method and are included in Accrued interest and other assets in the Consolidated Balance Sheets.

First Financial's affordable housing commitments totaled \$34.3 million and \$35.9 million as of June 30, 2018 and December 31, 2017, respectively. The Company recognized tax credits of \$1.2 million and \$0.8 million and \$2.3 million and \$1.6 million for the three months and six months ended June 30, 2018 and 2017, respectively. The Company recognized amortization expense which was included in income tax expense of \$1.6 million and \$1.2 million for the three months ended June 30, 2018 and 2017, respectively and \$2.8 million and \$2.2 million for the six months ended June 30, 2018 and 2017, respectively. First Financial had no affordable housing contingent commitments as of June 30, 2018 or December 31, 2017.

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**Investments in historic tax credits.** First Financial has noncontrolling financial investments in private investment funds and partnerships which are not consolidated. These investments may generate a return through the realization of federal and state income tax credits, as well as other tax benefits, such as tax deductions from net operating losses of the investments over a period of time. Investments in historic tax credits are accounted for under the equity method of accounting and are carried in Accrued interest and other assets on the Consolidated Balance Sheets. The Company's recorded investment in these entities was approximately \$2.9 million at June 30, 2018 and \$3.0 million at December 31, 2017. The maximum exposure to loss related to these investments was \$2.9 million at June 30, 2018 and \$3.0 million at December 31, 2017, representing the Company's investment balance and its unfunded commitments to invest additional amounts. Investments in historic tax credits resulted in \$0.1 million of tax credits for each of the three months ended June 30, 2018 and 2017, and \$0.2 million and \$0.3 million of tax credits for the six months ended June 30, 2018 and 2017, respectively.

**Contingencies/Litigation.** From time to time, First Financial and its subsidiaries may be engaged in various matters of litigation, other assertions of improper or fraudulent loan practices or lending violations and other matters. Additionally, as part of the ordinary course of business, First Financial and its subsidiaries are parties to litigation involving claims to the ownership of funds in particular accounts, the collection of delinquent accounts, challenges to security interests in collateral and foreclosure interests that are incidental to our regular business activities. While the ultimate liability with respect to these other litigation matters and claims cannot be determined at this time, First Financial believes that damages, if any, and other amounts relating to pending matters are not probable or cannot be reasonably estimated as of June 30, 2018. Reserves are established for these various matters of litigation, when appropriate, under FASB ASC Topic 450, Contingencies, based in part upon the advice of legal counsel. First Financial had no reserves related to litigation matters as of June 30, 2018 or December 31, 2017.

**NOTE 11: INCOME TAXES**

For the second quarter 2018, income tax expense was \$9.3 million, resulting in an effective tax rate of 20.4% compared with income tax expense of \$11.2 million and an effective tax rate of 33.0% for the comparable period in 2017. For the first six months of 2018, income tax expense was \$17.0 million, resulting in an effective tax rate of 20.2% compared with income tax expense of \$21.7 million and an effective tax rate of 31.5% for the comparable period in 2017. On December 22, 2017, the Tax Cuts and Jobs Act was signed into law. As a result, First Financial valued its deferred tax assets and liabilities as well as its investments in affordable housing projects utilizing a 21% federal rate during the first half of 2018 compared to a 35% rate in the first half of 2017.

ASU 2016-09, Compensation-Stock Compensation Improvements to Employee Share-Based Payment Accounting, requires the recognition of the income tax effects of share-based awards through the income statement as a component of income tax expense. First Financial recorded a \$0.1 million tax benefit as a result of share awards vesting and exercised during the second quarter of 2018 and \$0.5 million and \$1.2 million for the first six months of 2018 and 2017, respectively. Tax benefits resulting from the vesting and exercise of share awards in the second quarter of 2017 were insignificant.

At both June 30, 2018 and December 31, 2017, First Financial had \$2.9 million of unrecognized tax benefits, as determined in FASB ASC Topic 740-10, Income Taxes that, if recognized, would favorably affect the effective income tax rate in future periods. The unrecognized tax benefits relate to state income tax exposures from taking tax positions where the Company believes it is likely that, upon examination, a state may take a position contrary to the position taken by First Financial. The Company believes that resolution regarding our uncertain tax positions is reasonably possible within the next twelve months and could result in full, partial or no recognition of the benefit. First Financial recognizes interest accrued related to unrecognized tax benefits and penalties as income tax expense. At June 30, 2018 and December 31, 2017, the Company had no interest or penalties recorded.



First Financial and its subsidiaries are subject to U.S. federal income tax as well as state and local income tax in several jurisdictions. Tax years prior to 2014 have been closed and are no longer subject to U.S. federal income tax examinations. Tax years 2014 through 2017 remain open to examination by the federal taxing authority.

First Financial is no longer subject to state and local income tax examinations for years prior to 2011. Tax years 2011 through 2017 remain open to state and local examination in various jurisdictions.

Table of Contents**NOTE 12: EMPLOYEE BENEFIT PLANS**

First Financial sponsors a non-contributory defined benefit pension plan covering substantially all employees and uses a December 31 measurement date for the plan. Plan assets were primarily invested in fixed income and publicly traded equity mutual funds. The pension plan does not directly own any shares of First Financial common stock or any other First Financial security or product.

First Financial made no cash contributions to fund the pension plan during the six months ended June 30, 2018, or the year ended December 31, 2017, and does not expect to make cash contributions to the plan through the remainder of 2018. As a result of the plan's actuarial projections, which included consideration of the impact of the merger with MSFG, First Financial recorded expense of \$0.3 million for the three months ended June 30, 2018 and \$0.2 million for the six months ended June 30, 2018. Conversely, First Financial recorded income of \$0.3 million for the three months ended June 30, 2017 and \$0.6 million for the six months ended June 30, 2017.

The following table sets forth information concerning amounts recognized in First Financial's Consolidated Statements of Income related to the Company's pension plan:

	Three months ended June 30,		Six months ended June 30,	
	2018	2017	2018	2017
<i>(Dollars in thousands)</i>				
Service cost	\$1,735	\$1,239	\$3,030	\$2,477
Interest cost	601	589	1,191	1,178
Expected return on assets	(2,450 )	(2,481 )	(4,910 )	(4,962 )
Amortization of prior service cost	(103 )	(104 )	(206 )	(207 )
Net actuarial loss	555	439	1,077	877
<b>Net periodic benefit cost (income)</b>	<b>\$338</b>	<b>\$(318 )</b>	<b>\$182</b>	<b>\$(637 )</b>

**NOTE 13: REVENUE RECOGNITION**

On January 1, 2018, the Company adopted ASU No. 2014-09, Revenue from Contracts with Customers using the modified retrospective method applied to all contracts not completed as of January 1, 2018. Results for reporting periods beginning after January 1, 2018 are presented under the guidance set forth in this update while prior period amounts continue to be reported in accordance with legacy GAAP. Adoption of this update did not result in a change to the accounting for any of the in-scope revenue streams. As such, no cumulative effect adjustment to retained earnings was recorded.

The majority of the Company's revenues come from interest income and other sources, including loans, leases, securities and derivatives, that are outside the scope of this guidance. The Company's services that fall within the scope of this ASU are presented within Noninterest income and are recognized as revenue as the Company satisfies its obligation to the customer. Services within the scope of this guidance include service charges on deposits, wealth management fees, bankcard income, investment brokerage fees and the sale of OREO.

**Service charges on deposit accounts.** The Company earns fees from its deposit customers for transaction-based, account maintenance and overdraft services. Transaction-based fees, which include services such as ATM use fees, stop payment charges, statement rendering and ACH fees, are recognized at the time the transaction is executed as that is the point in time the Company fulfills the customer's request. Account maintenance fees, which relate primarily to monthly maintenance, are earned over the course of a month, representing the period over which the Company satisfies the performance obligation. Similarly, overdraft fees are recognized at the point in time that the overdraft

occurs as this corresponds with the Company's performance obligation. Service charges on deposit accounts are withdrawn from the customer's account balance.

**Trust and wealth management fees.** Trust and wealth management fees are primarily asset-based, but can also include flat fees based upon a specific service rendered, such as tax preparation services. The Company's performance obligation is generally satisfied over time and the resulting fees are recognized monthly, based upon the month-end market value of the assets under management and the applicable fees. The Company does not earn performance-based incentives. Optional services such as real estate sales and tax return preparation services are also available to existing trust and wealth management customers. The Company's performance obligation for these transactional-based services is generally satisfied, and related revenue recognized, as incurred.

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**Bankcard income.** The Company earns interchange fees from cardholder transactions conducted through the Visa payment network. Interchange fees from cardholder transactions represent a percentage of the underlying transaction value and are recognized concurrent with the transaction processing services provided to the cardholder. Interchange income is presented on the Consolidated Statements of Income net of expenses. Gross interchange income for the second quarter of 2018 was \$8.1 million, which was partially offset by \$2.8 million of expenses within Noninterest income. Gross interchange income for the first six months of 2018 was \$13.5 million, which was partially offset by \$4.8 million of expenses.

**Gain/loss on sale of OREO.** The Company records a gain or loss from the sale of OREO when control of the property transfers to the buyer, which generally occurs at the time of the executed deed. When the Company finances the sale of OREO to the buyer, the Company assesses whether the buyer is committed to perform their obligations under the contract and whether collectibility of the transaction price is probable. Once these criteria are met, the OREO asset is derecognized and the gain or loss on sale is recorded upon the transfer of control of the property to the buyer.

**Other.** Other noninterest income consists of other recurring revenue streams such as transaction fees, safe deposit rental income, insurance commissions, merchant referral income and brokerage revenue. Transaction fees primarily include check printing sales commissions, collection fees and wire transfer fees which arise from in-branch transactions. Safe deposit rental income arises from services charged to the customer on an annual basis and recognized upon receipt of payment. Insurance commissions are agent commissions earned by the Company and earned upon the effective date of the bound coverage. Merchant referral income is associated with a program whereby the Company receives a share of processing revenue that is generated from clients that were referred by First Financial to the service provider. Revenue is recognized at the point in time when the transaction occurs. Brokerage revenue represents fees from investment brokerage services provided to customers by a third party provider. The Company receives commissions from the third-party service provider on a monthly basis based upon customer activity for the month. The fees are recognized monthly and a receivable is recorded until commissions are paid the following month. Because the Company (i) acts as an agent in arranging the relationship between the customer and the third-party service provider and (ii) does not control the services rendered to the customers, investment brokerage fees are presented net of related costs.

**NOTE 14: EARNINGS PER COMMON SHARE**

The following table sets forth the computation of basic and diluted earnings per share:

	Three months ended June 30,		Six months ended June 30,	
	2018	2017	2018	2017
<i>(Dollars in thousands, except per share data)</i>				
<b>Numerator</b>				
Net income available to common shareholders	\$36,418	\$ 22,736	\$66,924	\$ 47,150
<b>Denominator</b>				
Basic earnings per common share - weighted average shares	97,347,536	91,543,478	79,599,709	91,471,347
Effect of dilutive securities				
Employee stock awards	545,374	625,031	504,914	649,706
Warrants	539,165	65,513	524,872	66,420
Diluted earnings per common share - adjusted weighted average shares	98,432,075	92,234,022	80,629,495	92,187,473
Earnings per share available to common shareholders				
Basic	\$0.37	\$ 0.37	\$0.84	\$ 0.77

Diluted	\$0.37	\$ 0.37	\$0.83	\$ 0.76
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First Financial has two categories of warrants outstanding to purchase the Company's common stock as of June 30, 2018. The first type of warrant represents the right to purchase one share of common stock, no par value per share, and has an exercise price of \$12.11 per share. First Financial had warrants outstanding to purchase 22,698 and 112,233 shares of First Financial's common stock as of June 30, 2018 and 2017, respectively and these warrants expire in December of 2018. The second category of warrant was acquired in the MSFG merger and the Company had one such warrant outstanding as of June 30, 2018.

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This warrant represents the right to purchase 793,520 shares of First Financial's common stock at an exercise price of \$10.72 per share and expires in January 2019.

Stock options and warrants with exercise prices greater than the average market price of the common shares were not included in the computation of net income per diluted share, as they would have been antidilutive. Using the end of period price of the Company's common shares, there were no antidilutive options at June 30, 2018 and June 30, 2017.

**NOTE 15: FAIR VALUE DISCLOSURES**

The fair value framework as disclosed in the Fair Value Topic includes a hierarchy which focuses on prioritizing the inputs used in valuation techniques. The fair value hierarchy gives the highest priority to quoted prices in active markets for identical assets or liabilities (Level 1), a lower priority to observable inputs other than quoted prices in active markets for identical assets and liabilities (Level 2) and the lowest priority to unobservable inputs (Level 3). When determining the fair value measurements for assets and liabilities, First Financial looks to active markets to price identical assets or liabilities whenever possible and classifies such items in Level 1. When identical assets and liabilities are not traded in active markets, First Financial looks to observable market data for similar assets and liabilities and classifies such items as Level 2. Certain assets and liabilities are not actively traded in observable markets and First Financial must use alternative techniques, based on unobservable inputs, to determine the fair value and classifies such items as Level 3. The level within the fair value hierarchy is based on the lowest level of input that is significant in the fair value measurement.

The estimated fair values of First Financial's financial instruments not measured at fair value on a recurring or nonrecurring basis in the consolidated financial statements were as follows:

	Carrying value	Estimated fair value			
		Total	Level 1	Level 2	Level 3
<i>(Dollars in thousands)</i>					
<b>June 30, 2018</b>					
<b>Financial assets</b>					
Cash and short-term investments	\$ 254,582	\$254,582	\$254,582	\$ 0	\$ 0
Investment securities held-to-maturity	443,957	435,785	0	435,785	0
Other investments	95,004	N/A	N/A	N/A	N/A
Loans held for sale	15,821	15,821	0	15,821	0
Loans and leases	8,830,505	8,847,519	0	0	8,847,519
Accrued interest receivable	40,152	40,152	0	13,939	26,213
<b>Financial liabilities</b>					
Deposits	10,103,747	10,073,140		10,073,140	0
Short-term borrowings	1,188,303	1,188,303	1,188,303	0	0
Long-term debt	469,423	462,478	0	462,478	0
Accrued interest payable	9,550	9,550	1,577	7,973	0

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	Carrying value	Estimated fair value			
		Total	Level 1	Level 2	Level 3
<i>(Dollars in thousands)</i>					
<b>December 31, 2017</b>					
<b>Financial assets</b>					
Cash and short-term investments	\$ 184,624	\$ 184,624	\$ 184,624	\$ 0	\$ 0
Investment securities held-to-maturity	654,008	653,101	0	653,101	0
Other investments	53,140	N/A	N/A	N/A	N/A
Loans held for sale	11,502	11,502	0	11,502	0
Loans and leases	5,959,162	6,006,656	0	0	6,006,656
Accrued interest receivable	24,496	24,496	0	8,265	16,231
<b>Financial liabilities</b>					
Deposits	6,895,046	6,884,615	0	6,884,615	0
Short-term borrowings	814,565	814,565	814,565	0	0
Long-term debt	119,654	117,908	0	117,908	0
Accrued interest payable	5,104	5,104	204	4,900	0

N/A = Not applicable

The methods utilized to estimate the fair value of financial instruments at December 31, 2017 did not necessarily represent an exit price. In accordance with our adoption of ASU 2016-01 in 2018, the methods utilized to measure the fair value of financial instruments at June 30, 2018 represent an approximation of exit price, however, an actual exit price may differ.

The following methods, assumptions and valuation techniques were used by First Financial to measure different financial assets and liabilities at fair value on a recurring or nonrecurring basis.

**Investment securities.** Investment securities classified as trading and available-for-sale are recorded at fair value on a recurring basis. Fair value measurement is based upon quoted market prices, when available (Level 1). If quoted market prices are not available, fair values are measured utilizing independent valuation techniques of identical or similar investment securities. First Financial compiles prices from various sources who may apply such techniques as matrix pricing to determine the value of identical or similar investment securities (Level 2). Matrix pricing is a mathematical technique widely used in the banking industry to value investment securities without relying exclusively on quoted prices for the specific investment securities but rather relying on the investment securities' relationship to other benchmark quoted investment securities. Any investment securities not valued based upon the methods previously described are considered Level 3.

First Financial utilizes values provided by third-party pricing vendors to price the investment securities portfolio in accordance with the fair value hierarchy of the Fair Value Topic and reviews the pricing methodologies utilized by the pricing vendors to ensure that the fair value determination is consistent with the applicable accounting guidance. First Financial's pricing process includes a series of quality assurance activities where prices are compared to recent market conditions, historical prices and other independent pricing services. Further, the Company periodically validates the fair value of a sample of securities in the portfolio by comparing the fair values to prices from other independent sources for the same or similar securities. First Financial analyzes unusual or significant variances, conducts additional research with the pricing vendor, and if necessary, takes appropriate action based on its findings. The results of the quality assurance process are incorporated into the selection of pricing providers by the portfolio manager.

**Impaired loans.** The fair value of impaired loans are specifically reviewed for purposes of determining the appropriate amount of impairment to be allocated to the ALLL. Fair value is generally measured based on the value of the collateral securing the loans. Collateral may be in the form of real estate or business assets including equipment, inventory and accounts receivable. The value of real estate collateral is determined utilizing an income or market valuation approach based on an appraisal conducted by an independent, licensed third-party appraiser (Level 3). The value of business equipment is based on an outside appraisal, if deemed significant, or the net book value on the applicable borrower financial statements. Likewise, values for inventory and accounts receivable collateral are based on borrower financial statement balances or aging reports on a discounted basis as appropriate (Level 3). Impaired loans are measured at fair value on a nonrecurring basis. Any fair value adjustments are recorded in the period incurred as provision for loan and lease losses on the Consolidated Statements of Income.



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**OREO.** Assets acquired through loan foreclosure are recorded at fair value less costs to sell, with any difference between the fair value of the property and the carrying value of the loan recorded as a charge-off. If the fair value is higher than the carrying amount of the loan, the excess is recognized first as a recovery and then as noninterest income. Subsequent declines in value are reported as adjustments to the carrying amount and are recorded in noninterest expense. The carrying value of OREO is not re-measured to fair value on a recurring basis, but is subject to fair value adjustments when the carrying value differs from the fair value, less estimated selling costs. Fair value is based on recent real estate appraisals and is updated at least annually. The Company classifies OREO in level 3 of the fair value hierarchy.

**Derivatives.** The fair values of derivative instruments are based primarily on a net present value calculation of the cash flows related to the interest rate swaps at the reporting date, using primarily observable market inputs such as interest rate yield curves which represents the cost to terminate the swap if First Financial should choose to do so. Additionally, First Financial utilizes an internally-developed model to value the credit risk component of derivative assets and liabilities, which is recorded as an adjustment to the fair value of the derivative asset or liability on the reporting date. Derivative instruments are classified as Level 2 in the fair value hierarchy.

The financial assets and liabilities measured at fair value on a recurring basis in the consolidated financial statements were as follows:

<i>(Dollars in thousands)</i>	Fair value measurements using			Assets/liabilities at fair value
	Level 1	Level 2	Level 3	
<b>June 30, 2018</b>				
<b>Assets</b>				
Derivatives	\$ 0	\$ 28,113	\$ 0	\$ 28,113
Investment securities available-for-sale	7,737	2,647,172	0	2,654,909
<b>Total</b>	<b>\$ 7,737</b>	<b>\$ 2,675,285</b>	<b>\$ 0</b>	<b>\$ 2,683,022</b>

<b>Liabilities</b>				
Derivatives	\$ 0	\$ 27,624	\$ 0	\$ 27,624

<i>(Dollars in thousands)</i>	Fair value measurements using			Assets/liabilities at fair value
	Level 1	Level 2	Level 3	
<b>December 31, 2017</b>				
<b>Assets</b>				
Derivatives	\$ 0	\$ 12,757	\$ 0	\$ 12,757
Investment securities available-for-sale	2,969	1,346,439	0	1,349,408
<b>Total</b>	<b>\$ 2,969</b>	<b>\$ 1,359,196</b>	<b>\$ 0</b>	<b>\$ 1,362,165</b>

<b>Liabilities</b>				
Derivatives	\$ 0	\$ 12,755	\$ 0	\$ 12,755

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Certain financial assets and liabilities are measured at fair value on a nonrecurring basis. Adjustments to the fair market value of these assets usually result from the application of fair value accounting or write-downs of individual assets. The following table summarizes financial assets and liabilities measured at fair value on a nonrecurring basis.

Fair value measurements using  
(Dollars in thousands) Level 1 Level 2 Level 3

**June 30, 2018****Assets**

Impaired loans	\$ 0	\$ 0	\$ 531
OREO	0	0	284

Fair value measurements using  
(Dollars in thousands) Level 1 Level 2 Level 3

**December 31, 2017****Assets**

Impaired loans	\$ 0	\$ 0	\$ 2,671
OREO	0	0	1,086

**NOTE 16: BUSINESS COMBINATIONS**

On April 1, 2018, the Company completed its acquisition of MainSource Financial Group, Inc. and its banking subsidiary, MainSource Bank. Therefore, results of MSFG have been included in the results of operations beginning on April 1, 2018. Under the terms of the merger agreement, shareholders of MSFG received 1.3875 common shares of First Financial common stock for each share of MSFG common stock, with cash paid in lieu of fractional shares. Including outstanding options and warrants to purchase MSFG common stock, the total purchase consideration was \$1.1 billion and resulted in goodwill of \$678.9 million. The goodwill arising from the acquisition largely reflected synergies and cost savings resulting from combining the operations of the companies. First Financial incurred \$25.9 million of merger related expenses related to the acquisition of MSFG during the six months ended June 30, 2018.

The acquisition is expected to provide additional revenue growth and diversification. The goodwill is not deductible for income tax purposes as the transaction was accounted for as a tax-free exchange. For further detail, see Note 6 – Goodwill and Other Intangible Assets.

The MainSource transaction was accounted for using the acquisition method of accounting and accordingly, assets acquired, liabilities assumed and consideration exchanged were recorded at estimated fair value on the acquisition date, in accordance with FASB ASC Topic 805, Business Combinations. The fair value measurements of assets acquired and liabilities assumed are subject to refinement for up to one year after the closing date of the acquisition as additional information relative to closing date fair values become available. The Company continues to finalize the fair values of loans, intangible assets and liabilities. As a result, the fair value adjustments are preliminary and may change as information becomes available. Fair value adjustments will be finalized no later than April 2019.

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The following table provides the purchase price calculation as of the acquisition date, identifiable assets purchased and liabilities assumed at their estimated fair value. As a condition of the merger, acquired assets and liabilities held for sale were divested subsequent to the closing of the merger. There was no gain or loss recorded in the Consolidated Statement of Income in conjunction with the divestiture.

(Dollars in thousands) MainSource

**Purchase consideration**

Cash consideration	\$ 43
Stock consideration	1,045,876
Warrant consideration	14,460
Options consideration	1,577
Total purchase consideration	1,061,956

**Assets acquired**

Cash	71,681
Investment securities available-for-sale	901,008
Investment securities held-to-maturity	171,423
Other investments	28,763
Loans	2,791,954
Premises and equipment	99,098
Other real estate owned	1,361
Intangible assets	41,750
Other assets	155,945
Assets held for sale	127,775
Total assets acquired	4,390,758

**Liabilities assumed**

Deposits	3,264,038
Subordinated notes	49,027
FHLB advances	291,887
Other borrowings	205,620
Other liabilities	21,449
Liabilities held for sale	175,722
Total liabilities assumed	4,007,743

Net identifiable assets	383,015
<b>Goodwill</b>	<b>\$ 678,941</b>

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The following table presents supplemental pro forma information as if the acquisition had occurred at the beginning of 2017. The pro forma information includes adjustments for interest income on acquired loans, amortization of intangible assets arising from the transaction, depreciation expense on property acquired, interest expense on deposits acquired, merger-related expenses incurred and the related income tax effects. The pro forma financial information is not necessarily indicative of the results of operations that would have occurred had the transactions been effected on the assumed date. The disclosures regarding the results of operations for MSFG subsequent to its acquisition date are omitted as this information is not practical to obtain. The Company converted MSFG's core system in the second quarter of 2018, which is the same quarter as its acquisition date.

	Six months ended	
	June 30,	
<i>(Dollars in thousands, except per share data)</i>	2018	2017
<b>Pro Forma Condensed Combined Income</b>		
<b>Statement Information</b>		
Net interest income	\$242,130	\$219,984
Net income	\$106,556	\$58,755
Basic earnings per share	\$1.09	\$0.61
Diluted earnings per share	\$1.08	\$0.60

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**ITEM 2 - MANAGEMENT'S DISCUSSION AND ANALYSIS OF FINANCIAL  
CONDITION AND RESULTS OF OPERATIONS (MD&A)  
FIRST FINANCIAL BANCORP. AND SUBSIDIARIES  
(Unaudited)**

All reclassifications of prior period amounts, if applicable, have been made to conform to the current period's presentation and had no effect on the Company's previously reported net income or financial condition. Additionally, due to impact from the merger with MSFG in the second quarter of 2018, certain prior period comparisons may not be discussed in these statements as historical points of comparison are not presented on a combined pro forma basis unless otherwise noted.

**SUMMARY**

First Financial is a \$13.9 billion financial holding company headquartered in Cincinnati, Ohio, that operates primarily in Ohio, Indiana, Kentucky and Illinois through its subsidiaries. These subsidiaries include the Bank, which is an Ohio-chartered commercial bank, operating 158 banking centers and 194 ATMs at June 30, 2018. First Financial provides banking and financial services products to business and retail clients through its six lines of business: Commercial, Retail Banking, Mortgage Banking, Wealth Management, Investment Commercial Real Estate and Commercial Finance. Commercial Finance provides equipment and leasehold improvement financing for franchisees in the quick service and casual dining restaurant sector and commission-based financing, primarily to insurance agents and brokers, throughout the United States. Wealth management had \$2.7 billion in assets under management as of June 30, 2018 and provides wealth planning, portfolio management, trust and estate, brokerage and retirement plan services.

**MARKET STRATEGY AND BUSINESS COMBINATIONS**

First Financial's goal is to develop a competitive advantage by utilizing a local market focus to provide a superior level of service and build long-term relationships with clients to help them reach greater levels of financial success. First Financial serves a combination of metropolitan and non-metropolitan markets in Ohio, Indiana, Kentucky and Illinois through its full-service banking centers, and provides financing to franchise owners and clients within the financial services industry throughout the United States. First Financial's market selection process includes a number of factors, but markets are primarily chosen for their potential for growth and long-term profitability. First Financial intends to concentrate plans for future growth and capital investment within its current metropolitan markets, and will continue to evaluate additional growth opportunities in metropolitan markets located within, or in close proximity to, the Company's current geographic footprint. Additionally, First Financial may assess strategic acquisitions that provide product line extensions or additional industry verticals that compliment our existing business. First Financial's investment in non-metropolitan markets is an important part of the Bank's core funding base and has historically provided stable, low-cost funding sources.

On April 1, 2018, the Company completed its acquisition of MainSource Financial Group, Inc. and its banking subsidiary, MainSource Bank. The merger positions the combined company to better serve the complementary geographies of Ohio, Indiana, Kentucky and Illinois by creating a higher performing bank with greater scale and capabilities. Under the terms of the merger agreement, shareholders of MainSource received 1.3875 common shares of First Financial common stock for each share of MainSource common stock. Including outstanding options and warrants on MainSource common stock, total purchase consideration was \$1.1 billion. In the merger, First Financial acquired total assets of \$4.4 billion, loans of \$2.9 billion and deposits of \$3.4 billion, resulting in goodwill of \$678.9 million.

The MainSource transaction was accounted for using the acquisition method of accounting and accordingly, assets acquired, liabilities assumed and consideration exchanged were recorded at estimated fair value on the acquisition date, in accordance with FASB ASC Topic 805, Business Combinations. The fair value measurements of assets acquired and liabilities assumed are subject to refinement for up to one year after the closing date of the acquisition as additional information relative to closing date fair values become available. As a result, the fair value adjustments are preliminary and may change as information becomes available, but no later than the second quarter of 2019.

See Note 16 – Business Combinations in the Notes to Consolidated Financial Statements, for further discussion of the merger with MSFG.

## **OVERVIEW OF OPERATIONS**

Second quarter 2018 net income was \$36.4 million and earnings per diluted common share were \$0.37. This compares with second quarter 2017 net income of \$22.7 million and earnings per diluted common share of \$0.37. For the six months ended

June 30, 2018, net income was \$66.9 million, and earnings per diluted common share were \$0.83. This compares with net

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income of \$47.2 million and earnings per diluted common share of \$0.76 for the first six months of 2017.

Return on average assets for the second quarter 2018 was 1.05% compared to 1.06% for the same period in 2017 and return on average shareholders' equity for the second quarter 2018 was 7.30% compared to 10.25% for the second quarter 2017. Return on average assets for the six months ended June 30, 2018 was 1.18% compared to 1.12% for the same period in 2017, and return on average shareholders' equity was 9.19% and 10.80% for the first six months of 2018 and 2017, respectively.

A discussion of First Financial's results of operations for the three and six months ended June 30, 2018 follows.

**NET INTEREST INCOME**

Net interest income, First Financial's principal source of income, is the excess of interest received from earning assets, including loan-related fees, less interest paid on interest-bearing liabilities. The amount of net interest income is determined by the volume and mix of earning assets, the rates earned on these earning assets and the volume, mix and rates paid for the deposits and borrowed money that support the earning assets.

For analytical purposes, net interest income is also presented in the table that follows, adjusted to a tax equivalent basis assuming a 21% marginal tax rate for 2018 and a 35% marginal tax rate for 2017. Net interest income is presented on a tax equivalent basis to consistently reflect income from tax-exempt assets, such as municipal loans and investments, in order to facilitate a comparison between taxable and tax-exempt amounts. Management believes that it is a standard practice in the banking industry to present net interest margin and net interest income on a fully tax equivalent basis as these measures provide useful information to make peer comparisons.

	Three months ended		Six months ended	
	June 30,		June 30,	
<i>(Dollars in thousands)</i>	2018	2017	2018	2017
Net interest income	\$123,979	\$68,520	\$199,791	\$137,452
Tax equivalent adjustment	1,420	1,294	2,138	2,519
<b>Net interest income - tax equivalent</b>	<b>\$125,399</b>	<b>\$69,814</b>	<b>\$201,929</b>	<b>\$139,971</b>
Average earning assets	\$12,120,000	\$7,855,564	\$10,115,063	\$7,776,082
Net interest margin <sup>(1)</sup>	4.10	% 3.50	% 3.98	% 3.56
Net interest margin (fully tax equivalent) <sup>(1)</sup>	4.15	% 3.56	% 4.03	% 3.63

<sup>(1)</sup> Calculated using annualized net interest income divided by average earning assets.

Net interest income for the second quarter 2018 was \$124.0 million, and increased \$55.5 million, or 80.9%, from second quarter 2017 net interest income of \$68.5 million. The increase in net interest income for the second quarter 2018 as compared to the same period in 2017 was primarily driven by a \$66.6 million, or 82.4%, increase in interest income, which was partially offset by an \$11.1 million, or 90.7%, increase in interest expense. Net interest income on a fully tax equivalent basis for the second quarter 2018 was \$125.4 million compared to \$69.8 million for the second quarter 2017. Net interest income on a fully tax equivalent basis for the six months ended June 30, 2018 was \$201.9 million compared to \$140.0 million for the same period of the prior year.

Net interest margin on a fully tax equivalent basis increased 59 bps to 4.15% for the second quarter 2018 compared to 3.56% for the comparable quarter in 2017. The increase in net interest margin was driven by higher earning asset yields, which more than offset higher funding costs and a lower tax equivalent adjustment. Higher earning asset yields resulted from higher interest rates and the impact from purchase accounting accretion while rising rates and shifts in funding mix drove higher costs during the period. Net interest margin on a fully tax equivalent basis for the six

months ended June 30, 2018 was 4.03%, an increase of 40 bps over the same period in 2017.

Higher interest income primarily resulted from a merger related increase in average earning assets from \$7.9 billion in the second quarter 2017 to \$12.1 billion in the second quarter 2018, as well as an increase in the yield on earning assets over those same periods from 4.13% to 4.88%, respectively. The increase in average earning assets included an increase in average loan balances of \$3.1 billion, or 54.0%, and a \$1.1 billion, or 55.1% increase in average investment security balances in the second quarter 2018 compared to the second quarter 2017. The yield on earning assets was impacted by higher interest earned on



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loans and investment securities, reflecting recent increases in interest rates, the impact from purchase accounting and slower investment prepayment speeds.

Interest expense increased as a result of higher interest-bearing liability balances, as well as higher rates paid on deposits and borrowed funds during the period. Higher interest-bearing liabilities were driven by a \$2.9 billion, or 57.5%, increase in average interest-bearing deposits from the second quarter 2017 as a result of the merger coupled with strong deposit generation efforts in recent quarters, in addition to higher long-term debt balances resulting from the merger and the implementation of funding strategies aligned with the Company's post-merger balance sheet. Rising interest rates and a deposit mix shift in recent periods contributed to a 6 bps increase in deposit costs from 69 bps for the second quarter 2017 to 75 bps for the second quarter 2018, while rising rates drove the costs of borrowed funds higher during 2018.

**CONSOLIDATED AVERAGE BALANCE SHEETS AND NET INTEREST INCOME ANALYSIS**

	Quarterly Averages				Year-to-Date Averages			
	June 30, 2018		June 30, 2017		June 30, 2018		June 30, 2017	
	Balance	Yield	Balance	Yield	Balance	Yield	Balance	Yield
<i>(Dollars in thousands)</i>								
<b>Earning assets</b>								
Investments								
Investment securities	\$3,157,339	3.16 %	\$2,035,334	2.77 %	\$2,603,139	3.12 %	\$1,971,372	2.76 %
Interest-bearing deposits with other banks	29,261	2.43 %	20,293	1.11 %	28,173	2.03 %	30,582	0.90 %
Gross loans <sup>(1)</sup>	8,933,400	5.49 %	5,799,937	4.61 %	7,483,751	5.31 %	5,774,128	4.63 %
<b>Total earning assets</b>	<b>12,120,000</b>	<b>4.88 %</b>	<b>7,855,564</b>	<b>4.13 %</b>	<b>10,115,063</b>	<b>4.74 %</b>	<b>7,776,082</b>	<b>4.14 %</b>
<b>Nonearning assets</b>								
Allowance for loan and lease losses	(55,318 )		(57,379 )		(55,168 )		(57,917 )	
Cash and due from banks	224,824		116,123		170,760		115,922	
Accrued interest and other assets	1,666,854		668,653		1,176,774		662,409	
<b>Total assets</b>	<b>\$13,956,360</b>		<b>\$8,582,961</b>		<b>\$11,407,429</b>		<b>\$8,496,496</b>	
<b>Interest-bearing liabilities</b>								
Deposits								
Interest-bearing demand	\$2,573,150	0.36 %	\$1,483,186	0.27 %	\$1,997,574	0.37 %	\$1,483,803	0.23 %
Savings	3,196,059	0.54 %	2,408,950	0.69 %	2,825,437	0.58 %	2,317,338	0.59 %
Time	2,192,196	1.50 %	1,164,087	1.23 %	1,831,323	1.47 %	1,198,667	1.20 %
Total interest-bearing deposits	7,961,405	0.75 %	5,056,223	0.69 %	6,654,334	0.76 %	4,999,808	0.63 %
Borrowed funds								
Short-term borrowings	916,617	1.81 %	875,481	0.94 %	829,048	1.65 %	862,175	0.81 %
Long-term debt	491,407	3.65 %	119,651	5.16 %	309,883	3.94 %	119,628	5.19 %
Total borrowed funds	1,408,024	2.45 %	995,132	1.45 %	1,138,931	2.28 %	981,803	1.35 %
<b>Total interest-bearing liabilities</b>	<b>9,369,429</b>	<b>1.00 %</b>	<b>6,051,355</b>	<b>0.81 %</b>	<b>7,793,265</b>	<b>0.98 %</b>	<b>5,981,611</b>	<b>0.75 %</b>
<b>Noninterest-bearing liabilities</b>								
Noninterest-bearing demand deposits	2,421,230		1,513,995		1,998,251		1,506,587	
Other liabilities	165,608		128,007		148,172		127,838	
Shareholders' equity	2,000,093		889,604		1,467,741		880,460	
<b>Total liabilities and shareholders' equity</b>	<b>\$13,956,360</b>		<b>\$8,582,961</b>		<b>\$11,407,429</b>		<b>\$8,496,496</b>	
<b>Net interest income</b>	<b>\$123,979</b>		<b>\$68,520</b>		<b>\$199,791</b>		<b>\$137,452</b>	

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<b>Net interest spread</b>	3.88 %	3.32 %	3.76 %	3.39 %
Contribution of noninterest-bearing sources of funds	0.22 %	0.18 %	0.22 %	0.17 %
<b>Net interest margin <sup>(2)</sup></b>	4.10 %	3.50 %	3.98 %	3.56 %
Tax equivalent adjustment	0.05 %	0.06 %	0.05 %	0.07 %
<b>Net interest margin (fully tax equivalent) <sup>(2)</sup></b>	4.15 %	3.56 %	4.03 %	3.63 %

(1) Loans held for sale, nonaccrual loans, covered loans and indemnification asset are included in gross loans.

(2) The net interest margin exceeds the interest spread as noninterest-bearing funding sources, demand deposits, other liabilities and shareholders' equity also support earning assets.

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The impact on net interest income from changes in interest rates as well as the volume of interest-earning assets and interest-bearing liabilities is illustrated in the table below:

	Changes for the three months ended June 30, 2018			Changes for the six months ended June 30, 2018		
	Comparable quarter income variance			Comparable quarter income variance		
<i>(Dollars in thousands)</i>	Rate	Volume	Total	Rate	Volume	Total
<b>Earning assets</b>						
Investment securities	\$ 2,004	\$ 8,853	\$ 10,857	\$ 3,457	\$ 9,766	\$ 13,223
Interest-bearing deposits with other banks	67	54	121	171	(24)	147
Gross loans <sup>(1)</sup>	12,718	42,894	55,612	19,694	45,052	64,746
<b>Total earning assets</b>	14,789	51,801	66,590	23,322	54,794	78,116
<b>Interest-bearing liabilities</b>						
Total interest-bearing deposits	717	5,398	6,115	3,249	6,239	9,488
Borrowed funds						
Short-term borrowings	1,896	185	2,081	3,584	(272)	3,312
Long-term debt	(450)	3,385	2,935	(741)	3,718	2,977
Total borrowed funds	1,446	3,570	5,016	2,843	3,446	6,289
<b>Total interest-bearing liabilities</b>	2,163	8,968	11,131	6,092	9,685	15,777
<b>Net interest income</b>	\$ 12,626	\$ 42,833	\$ 55,459	\$ 17,230	\$ 45,109	\$ 62,339

<sup>(1)</sup> Loans held for sale, nonaccrual loans and indemnification asset are included in gross loans.

**NONINTEREST INCOME**

Second quarter 2018 noninterest income was \$28.3 million, increasing \$10.8 million, or 61.9%, from \$17.5 million in the second quarter of 2017. This increase resulted from merger-driven increases in service charges on deposit accounts, trust and wealth management fees, bankcard income and net gains from sales of loans. Other noninterest income was \$5.9 million for the quarter, which was a \$3.8 million increase compared to \$2.1 million in the second quarter of 2017. In addition to merger-related growth, other noninterest income was positively impacted in the second quarter of 2018 by a non-resident tax refund and benefits received on BOLI policies. Second quarter 2018 noninterest income was in line with management's expectations for the Company's performance subsequent to the merger, although changes in mix are expected as certain income streams are subject to seasonal variance.

Noninterest income for the six months ended June 30, 2018 was \$45.2 million, increasing \$10.4 million, or 29.8%, from \$34.8 million in the first two quarters of 2017. Similar to the three month period changes previously described, higher noninterest income was primarily the result of the scale created from the merger as service charges on deposit accounts, bankcard income, gain on sale of loans, derivative fees and other noninterest income increased during the period. These increases were partially offset by a decline in gains on the sale of investment securities.

**NONINTEREST EXPENSE**

Second quarter 2018 noninterest expense was \$102.8 million compared to \$51.6 million for the second quarter 2017. The increase from the comparable quarter in 2017 included increases across all noninterest expense categories as the Company incurred \$23.9 million of merger-related expenses, in addition to general increases in expense levels due to the scale created by the merger. As of June 30, 2018, the majority of merger-related activity is complete, and management remains focused on efficiency while also making strategic investments to support the continued success of the Company.

Noninterest expense for the six months ending June 30, 2018 was \$155.0 million, compared to \$102.6 million for the first six months of 2017 with similar increases across all noninterest expense categories. As with the three month period previously discussed, the Company incurred higher expenses due to the changes in size and scale of the Company post-merger, in addition to incurring one-time merger related expenses of \$25.9 million during the period.

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**INCOME TAXES**

Income tax expense was \$9.3 million for the second quarter of 2018, resulting in an effective tax rate of 20.4% compared to \$11.2 million and 33.0% for the comparable period in 2017. Income tax expense was \$17.0 million for the first six months of 2018, resulting in an effective tax rate of 20.2% compared to \$21.7 million and 31.5% for the same period in 2017. The lower effective tax rate during 2018 related primarily to the Tax Cuts and Jobs Act which lowered the Company's statutory federal tax rate from 35% to 21% effective January 1, 2018.

While the Company's effective tax rate may fluctuate from quarter to quarter due to tax jurisdiction changes, the level of tax-enhanced assets and tax credit investments, the full year effective tax rate for 2018 is expected to be approximately 19.5%.

**LOANS**

Loans, excluding loans held for sale, totaled \$8.9 billion as of June 30, 2018, and increased \$2.9 billion, or 47.8%, compared to December 31, 2017. The increase in loan balances from December 31, 2017 was largely attributable to the acquisition of \$2.8 billion of loans in conjunction with the MSFG merger, net of branch divestitures.

Second quarter 2018 average loans, excluding loans held for sale, increased \$3.1 billion, or 54.3%, from the second quarter 2017. Increases in average loan balances were attributable to the merger, strong organic loan growth in recent periods and funding of prior period commitments. Organic loan growth in recent periods reflects the Company's sales efforts, expanded presence in key metropolitan markets and investment in a diversified product suite, however absent the impact from the merger, loan balances were relatively flat in the second quarter of 2018 due lower loan origination and higher prepayment activity.

Loans accounted for under FASB ASC Topic 310-30, Loans and Debt Securities Acquired with Deteriorated Credit Quality, are referred to as purchased impaired loans. The majority of the purchased impaired loans were previously covered under loss sharing agreements. First Financial had purchased impaired loans totaling \$117.2 million at June 30, 2018, which included \$24.1 million acquired in the merger with MSFG. First Financial had \$105.0 million of purchased impaired loans at December 31, 2017. These balances exclude contractual interest not yet accrued.

**ASSET QUALITY**

Nonperforming assets consist of nonaccrual loans, accruing TDRs (collectively, nonperforming loans) and OREO. Loans are classified as nonaccrual when, in the opinion of management, collection of principal or interest is doubtful or when principal or interest payments are 90 days or more past due. Generally, loans are classified as nonaccrual due to a borrower's continued failure to adhere to contractual payment terms, coupled with other pertinent factors. When a loan is classified as nonaccrual, the accrual of interest income is discontinued and previously accrued but unpaid interest is reversed.

Nonperforming assets were \$64.2 million, or 46 bps as a percent of total assets, at June 30, 2018 compared to \$44.4 million and 50 bps as of December 31, 2017. The increase included a \$16.4 million increase in nonaccrual balances and a \$4.3 million increase in accruing TDRs, which were partially offset by a \$0.9 million decline in OREO balances during the period. Higher nonperforming loans at June 30, 2018 were primarily driven by the merger in addition to two commercial relationships downgraded to nonaccrual status during the period.

Loans are classified as TDRs when borrowers are experiencing financial difficulties and concessions are made by the Company that would not otherwise be considered for a borrower with similar credit characteristics. TDRs are generally classified as nonaccrual for a minimum period of six months and may qualify for return to accrual status

once they have demonstrated performance with the restructured terms of the loan agreement. TDRs that are acquired are no longer classified as such. Generally, if the acquired loan is performing under the current restructured terms, and there is no indication the borrower will not be able to continue paying, it would be classified as a purchased performing loan, and accounted for under ASC 310-20. If the restructured loan is below a current market rate for a loan with similar credit risks, the loan is generally classified as a purchased impaired loan and accounted for under ASC 310-30. TDRs totaled \$27.8 million at June 30, 2018, which is a \$3.8 million increase from \$23.9 million at December 31, 2017.

Classified assets, which are defined by the Company as nonperforming assets plus performing loans internally rated substandard or worse, increased to \$139.3 million as of June 30, 2018 compared to \$87.3 million at December 31, 2017 primarily related to the acquisition of MSFG. Classified assets as a percentage of total assets was 1.0% at June 30, 2018, which was relatively unchanged from 98 bps as of December 31, 2017.

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The following table details nonperforming, underperforming and classified assets, in addition to related credit quality ratios as of June 30, 2018 and the four previous quarters.

	Quarter ended				
	2018 June 30,	Mar. 31,	2017 Dec. 31,	Sept. 30,	June 30,
<i>(Dollars in thousands)</i>					
<b>Nonperforming loans, nonperforming assets, and underperforming assets</b>					
Nonaccrual loans <sup>(1)</sup>					
Commercial and industrial	\$3,448	\$6,275	\$5,229	\$9,026	\$15,099
Lease financing	0	0	82	87	94
Construction real estate	24	26	29	824	1,075
Commercial real estate	21,593	16,878	10,616	12,244	12,617
Residential real estate	9,278	3,324	4,140	4,333	4,442
Home equity	5,820	3,484	3,743	3,364	2,937
Installment	299	296	243	240	307
Nonaccrual loans	40,462	30,283	24,082	30,118	36,571
Accruing troubled debt restructurings	21,839	14,943	17,545	19,692	20,135
Total nonperforming loans	62,301	45,226	41,627	49,810	56,706
Other real estate owned	1,853	1,065	2,781	3,116	5,961
Total nonperforming assets	64,154	46,291	44,408	52,926	62,667
Accruing loans past due 90 days or more	311	529	61	84	124
Total underperforming assets	\$64,465	\$46,820	\$44,469	\$53,010	\$62,791
Total classified assets	\$139,300	\$87,577	\$87,293	\$94,320	\$98,391

**Credit quality ratios**

Allowance for loan and lease losses to						
Nonaccrual loans	133.65	% 179.57	% 224.32	% 181.07	% 150.05	%
Nonperforming loans	86.80	% 120.24	% 129.77	% 109.48	% 96.77	%
Total ending loans	0.61	% 0.89	% 0.90	% 0.91	% 0.93	%
Nonperforming loans to total loans	0.70	% 0.74	% 0.69	% 0.83	% 0.97	%
Nonperforming assets to						
Ending loans, plus OREO	0.72	% 0.76	% 0.74	% 0.89	% 1.07	%
Total assets	0.46	% 0.52	% 0.50	% 0.60	% 0.72	%
Nonperforming assets, excluding accruing TDRs to						
Ending loans, plus OREO	0.48	% 0.51	% 0.45	% 0.56	% 0.72	%
Total assets	0.30	% 0.35	% 0.30	% 0.38	% 0.49	%
Classified assets to total assets	1.00	% 0.98	% 0.98	% 1.08	% 1.13	%

<sup>(1)</sup> Nonaccrual loans include nonaccrual TDRs of \$5.9 million, \$6.0 million, \$6.4 million, \$9.1 million, and \$9.4 million as of June 30, 2018, March 31, 2018, December 31, 2017, September 30, 2017, and June 30, 2017, respectively.

years as of June 30, 2018 and 2.9 years as of

December 31, 2017.

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The Company invests in certain securities whose realization is dependent on future principal and interest repayments and thus carry credit risk. First Financial performs a detailed pre-purchase collateral and structural analysis on these securities and strategically invests in asset classes in which First Financial has expertise and experience, as well as a senior position in the capital structure. First Financial continuously monitors credit risk and geographic concentration risk in its evaluation of market opportunities that enhance the overall performance of the portfolio.

First Financial recorded a \$19.0 million unrealized after-tax loss on the investment portfolio as a component of equity in accumulated other comprehensive income at June 30, 2018. The total unrealized loss on the investment portfolio increased \$18.8 million from \$0.2 million at December 31, 2017.

First Financial will continue to monitor loan and deposit demand, as well as balance sheet composition, capital sensitivity and the interest rate environment as it manages investment strategies in future periods.

## **DEPOSITS AND FUNDING**

Total deposits as of June 30, 2018 were \$10.1 billion compared to \$6.9 billion at December 31, 2017. This \$3.2 billion, or 46.5%, increase was driven by \$3.3 billion of deposits acquired in conjunction with the Company's merger with MSFG, net of branch divestitures. As a result, noninterest-bearing demand deposits increased \$809.9 million, or 48.7%, interest-bearing demand deposits increased \$986.6 million, or 67.9%, savings deposits increased \$625.3 million, or 25.4% and time deposits rose \$786.9 million, or 59.7% compared to December 31, 2017. In addition to acquired balances, higher brokered CD balances contributed to the increase in time deposits. Brokered CDs are periodically used by First Financial as a lower cost alternative to short and long-term borrowings.

Average deposits for the second quarter 2018 increased \$3.8 billion, or 58.0%, to \$10.4 billion from \$6.6 billion at June 30, 2017. The combination of the merger and strong organic deposit generation efforts in recent periods, including significant growth in money market deposits in light of rising interest rates, led to the increase in average balances. Average deposits for the six months ended June 30, 2018 were \$8.7 billion compared to \$6.5 billion for the same period period in 2017, an increase of \$2.1 billion, or 33.0%.

Borrowed funds increased to \$1.7 billion at June 30, 2018 from \$934.2 million at December 31, 2017, due to the MSFG merger and the Company's overall funding needs. First Financial utilizes short-term borrowings and longer-term advances from the FHLB as wholesale funding sources. First Financial had \$1.1 billion in short-term borrowings with the FHLB at June 30, 2018 and \$742.3 million as of December 31, 2017. In addition to FHLB borrowings, short term borrowings included fed funds purchased and repurchase agreements of \$88.1 million and \$72.3 million at June 30, 2018 and December 31, 2017, respectively.

Total long-term debt was \$469.4 million and \$119.7 million at June 30, 2018 and December 31, 2017, respectively, and included subordinated notes, FHLB long term advances and an interest free loan with a municipality. As of June 30, 2018 and December 31, 2017, outstanding subordinated debt totaled \$169.1 million and \$118.6 million, respectively, which included prepaid debt issuance costs of \$8.8 million and \$1.4 million. Long-term debt also included FHLB long-term advances, which increased to \$299.6 million at June 30, 2018 from \$0.2 million as of December 31, 2017, as the Company implemented post-merger funding strategies to manage liquidity and interest rate risk. First Financial's total remaining borrowing capacity from the FHLB was \$287.1 million at June 30, 2018.

See Note 7 – Borrowings in the Notes to Consolidated Financial Statements, for further discussion of First Financial's borrowed funds.

## **LIQUIDITY**

Liquidity management is the process by which First Financial manages the continuing flow of funds necessary to meet its financial commitments on a timely basis and at a reasonable cost. These funding commitments include withdrawals by depositors, credit commitments to borrowers, shareholder dividends, share repurchases, operating expenses and capital expenditures. Liquidity is derived primarily from deposit growth, principal and interest payments on loans and investment securities, maturing loans and investment securities, access to wholesale funding sources and collateralized borrowings.

First Financial's most stable source of liability-funded liquidity for both long and short-term needs is deposit growth and retention of the core deposit base. In addition to core deposit funding, First Financial also utilizes a variety of other short and long-term funding sources, which include subordinated notes, longer-term advances from the FHLB and its short-term line of credit.

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Both First Financial and the Bank received investment grade credit ratings from Kroll Bond Rating Agency, Inc, an independent rating agency. These credit ratings impact the cost and availability of financing to First Financial, and a downgrade to these credit ratings could affect First Financial's or the Bank's ability to access the credit markets, and potentially increase borrowing costs, negatively impacting financial condition and liquidity. Key factors in maintaining high credit ratings include consistent and diverse earnings, strong credit quality and capital ratios, varied funding sources and disciplined liquidity monitoring procedures. The ratings of First Financial and the Bank at June 30, 2018 were as follows:

	First Financial Bancorp	First Financial Bank
Senior Unsecured Debt	BBB+	A-
Subordinated Debt	BBB	BBB+
Short-Term Debt	K2	K2
Deposit	N/A	A-
Short-Term Deposit	N/A	K2

For ease of borrowing execution, First Financial utilizes a blanket collateral agreement with the FHLB. First Financial pledged \$5.7 billion of certain eligible residential, commercial and farm real estate loans, home equity lines of credit and government, agency and CMBS securities as collateral for borrowings from the FHLB as of June 30, 2018.

First Financial maintains a short-term credit facility with an unaffiliated bank for \$15.0 million that matured in July 2018, but is in the process of being extended. This facility can have a variable or fixed interest rate and provides First Financial additional liquidity, if needed, for various corporate activities, including the repurchase of First Financial shares and the payment of dividends to shareholders. As of June 30, 2018 and December 31, 2017, there was no outstanding balance. The credit agreement requires First Financial to comply with certain covenants including those related to asset quality and capital levels, and First Financial was in compliance with all covenants associated with this line of credit as of June 30, 2018 and December 31, 2017.

In conjunction with its merger with MSFG, First Financial acquired certain variable rate short-term borrowings with an unaffiliated bank. As of June 30, 2018, the balance outstanding was \$8.3 million and the interest rate was 4.19%. This term debt is paid quarterly and matures in 2019.

First Financial's principal source of asset-funded liquidity is marketable investment securities, particularly those of shorter maturities. The market value of investment securities classified as available-for-sale totaled \$2.7 billion and \$1.3 billion at June 30, 2018 and December 31, 2017, respectively. Securities classified as held-to-maturity that are maturing within a short period of time are an additional source of liquidity and totaled \$1.3 million and \$21.8 million at June 30, 2018 and December 31, 2017, respectively. Other sources of liquidity include cash and due from banks, interest-bearing deposits with other banks and loans maturing within one year.

At June 30, 2018, in addition to liquidity on hand of \$254.6 million, First Financial had unused and available overnight wholesale funding of \$3.0 billion, or 21.7% of total assets, to fund loan and deposit activities, in addition to other general corporate requirements.

Certain restrictions exist regarding the ability of First Financial's subsidiary, First Financial Bank, to transfer funds to First Financial in the form of cash dividends, loans, other assets or advances. The approval of the Bank's primary federal regulator is required to pay dividends in excess of regulatory limitations. Dividends paid to First Financial from the Bank totaled \$33.6 million for the first six months of 2018. As of June 30, 2018, the Bank had retained earnings of \$597.2 million, of which \$141.1 million was available for distribution to First Financial without prior regulatory approval. Additionally, First Financial had \$72.0 million in cash at the parent company as of June 30, 2018, which approximates the Company's regular annual shareholder dividend and operating expenses.

Share repurchases, if any, also impact First Financial's liquidity. For further information regarding share repurchases, see the Capital section that follows.

Capital expenditures, such as banking center expansions and technology investments, were \$13.7 million and \$4.2 million for the first six months of 2018 and 2017, respectively. Management believes that sufficient liquidity exists to fund its future capital expenditure commitments.

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Management is not aware of any other events or regulatory requirements that, if implemented, are likely to have a material effect on First Financial's liquidity.

**CAPITAL**

**Risk-Based Capital.** The Board of Governors of the Federal Reserve System approved a rule implementing changes intended to strengthen the regulatory capital framework for all banking organizations (Basel III), subject to a phase-in period for certain provisions. Basel III established and defined quantitative measures to ensure capital adequacy which require First Financial to maintain minimum amounts and ratios of Common Equity tier 1 capital, total and tier 1 capital to risk-weighted assets and tier 1 capital to average assets (leverage ratio).

The rule includes a minimum ratio of common equity tier 1 capital to risk-weighted assets of 4.5% and a capital conservation buffer of 2.5% of risk-weighted assets that began on January 1, 2016 at 0.625% and will be phased in over a four year period, increasing by the same amount on each subsequent January 1, until fully phased-in on January 1, 2019. Further, the minimum ratio of Tier 1 capital to risk-weighted assets increased from 4.0% to 6.0% and all banks are now subject to a 4.0% minimum leverage ratio. The required total risk-based capital ratio is unchanged. Failure to maintain the required common equity Tier 1 capital conservation buffer will result in potential restrictions on a bank's ability to pay dividends, repurchase stock and/or pay discretionary compensation to its employees. The capital requirements also provide strict eligibility criteria for regulatory capital instruments and change the method for calculating risk-weighted assets in an effort to better identify riskier assets, such as highly volatile commercial real estate and nonaccrual loans.

Management believes, as of June 30, 2018, that First Financial met all capital adequacy requirements to which it was subject. To be categorized as well-capitalized, First Financial must maintain minimum Total risk-based capital, Tier 1 risk-based capital and Tier 1 leverage ratios as set forth in the table that follows. The Company's most recent regulatory notifications categorized First Financial as "well-capitalized" under the regulatory framework for prompt corrective action. There have been no conditions or events since those notifications that management believes have changed the Company's categorization. Total regulatory capital exceeded the minimum requirement by \$356.9 million on a consolidated basis at June 30, 2018.

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The following tables present the actual and required capital amounts and ratios as of June 30, 2018 and December 31, 2017 under the Basel III Capital Rules. The minimum required capital amounts presented include the minimum required capital levels based on the phase-in provisions of the Basel III Capital Rules as of the period presented, as well as the minimum required capital levels as of January 1, 2019 when the Basel III Capital Rules have been fully phased-in. Capital levels required to be considered "well capitalized" are based upon prompt corrective action regulations, as amended to reflect the changes under the Basel III Capital Rules.

	Actual		Minimum capital required - Basel III current period		Required to be considered well capitalized - current period		Minimum capital required - Basel III fully phased-in	
	Capital amount	Ratio	Capital amount	Ratio	Capital amount	Ratio	Capital amount	Ratio
<i>(Dollars in thousands)</i>								
<b>June 30, 2018</b>								
Common equity tier 1 capital to risk-weighted assets								
Consolidated	\$1,142,718	11.15 %	\$653,511	6.38 %	N/A	N/A	\$717,580	7.00 %
First Financial Bank	1,233,460	12.04 %	652,992	6.38 %	\$665,796	6.50 %	717,011	7.00 %
Tier 1 capital to risk-weighted assets								
Consolidated	1,184,471	11.55 %	807,278	7.88 %	N/A	N/A	871,347	8.50 %
First Financial Bank	1,233,564	12.04 %	806,638	7.88 %	819,441	8.00 %	870,657	8.50 %
Total capital to risk-weighted assets								
Consolidated	1,369,231	13.36 %	1,012,301	9.88 %	N/A	N/A	1,076,370	10.50 %
First Financial Bank	1,296,250	12.65 %	1,011,498	9.88 %	1,024,302	10.00 %	1,075,517	10.50 %
Leverage ratio								
Consolidated	1,184,471	9.06 %	522,726	4.00 %	N/A	N/A	522,726	4.00 %
First Financial Bank	1,233,564	9.44 %	522,870	4.00 %	653,588	5.00 %	522,870	4.00 %

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<i>(Dollars in thousands)</i>	Actual		Minimum capital required - Basel III		Required to be considered well capitalized		Minimum capital required - Basel III fully phased-in	
	Capital amount	Ratio	Capital amount	Ratio	Capital amount	Ratio	Capital amount	Ratio
<b>December 31, 2017</b>								
Common equity tier 1 capital to risk-weighted assets								
Consolidated	\$755,735	10.63 %	\$408,746	5.75 %	N/A	N/A	\$497,604	7.00 %
First Financial Bank	794,251	11.21 %	407,220	5.75 %	\$460,336	6.50 %	495,746	7.00 %
Tier 1 capital to risk-weighted assets								
Consolidated	755,839	10.63 %	515,376	7.25 %	N/A	N/A	604,233	8.50 %
First Financial Bank	794,355	11.22 %	513,452	7.25 %	566,567	8.00 %	601,978	8.50 %
Total capital to risk-weighted assets								
Consolidated	929,148	13.07 %	657,548	9.25 %	N/A	N/A	746,406	10.50 %
First Financial Bank	856,363	12.09 %	655,093	9.25 %	708,209	10.00 %	743,619	10.50 %
Leverage ratio								
Consolidated	755,839	8.84 %	342,198	4.00 %	N/A	N/A	342,198	4.00 %
First Financial Bank	794,355	9.29 %	342,113	4.00 %	427,642	5.00 %	342,113	4.00 %

First Financial generally seeks to balance the return of earnings to shareholders through shareholder dividends and share repurchases with capital retention, in order to maintain adequate levels of capital and support the Company's growth plans.

**Shareholder Dividends.** First Financial paid a dividend of \$0.19 per common share on June 15, 2018 to shareholders of record as of June 1, 2018. Additionally, First Financial's board of directors authorized a dividend of \$0.20 per common share, payable on September 17, 2018 to shareholders of record as of September 3, 2018.

**Share Repurchases.** In October 2012, First Financial's board of directors approved a share repurchase plan under which the Company has the ability to repurchase up to 5,000,000 shares. First Financial did not repurchase any shares under this plan during the three and six month periods ending June 30, 2018 and 2017. At June 30, 2018, 3,509,133 common shares remained available for repurchase under the 2012 share repurchase plan.

**ATM Offering.** In March 2017, First Financial initiated an "at-the-market" equity offering program to provide flexibility with respect to capital planning and to support future growth. First Financial was not active through the ATM program during the period.

**Shareholders' Equity.** Total shareholders' equity at June 30, 2018 was \$2.0 billion compared to \$930.7 million at June 30, 2017. This increase was the result of the merger with MSFG in the second quarter of 2018.

For further detail, see the Consolidated Statements of Changes in Shareholders' Equity.

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**RISK MANAGEMENT**

First Financial manages risk through a structured ERM approach that routinely assesses the overall level of risk, identifies specific risks and evaluates specific actions to mitigate those risks. First Financial continues to enhance its risk management capabilities and has embedded risk awareness into the culture of the Company. First Financial has identified ten types of risk that it monitors in its ERM framework. These risks include credit, market, operational, compliance, strategic, reputation, information technology, cyber, legal and environmental/external.

For a full discussion of these risks, see the Enterprise Risk Management section in Management's Discussion and Analysis in First Financial's 2017 Annual Report. The sections that follow provide additional discussion related to credit risk and market risk.

**CREDIT RISK**

Credit risk represents the risk of loss due to failure of a customer or counterparty to meet its financial obligations in accordance with contractual terms. First Financial manages credit risk through its underwriting process, periodically reviewing and approving its credit exposures using credit policies and guidelines approved by the board of directors.

**ALLL.** The ALLL is a reserve accumulated on the Consolidated Balance Sheets through the recognition of the provision for loan and lease losses. First Financial records a provision for loan and lease losses in the Consolidated Statements of Income to maintain the ALLL at a level considered sufficient to absorb probable incurred loan and lease losses inherent in the portfolio.

The ALLL was \$54.1 million as of June 30, 2018 and \$54.0 million as of December 31, 2017, and as a percentage of period-end loans, the ALLL was 0.61% as of June 30, 2018 compared to 0.90% as of December 31, 2017. The ALLL is consistent with the Company's stable credit outlook and classified asset balances, while the decline in the ALLL as a percentage of period end loans is consistent with GAAP for acquired loans as these loans are recorded at estimated fair value at the acquisition date with no carryover of the related ALLL. At June 30, 2018, the fair value of acquired MSFG loans included a \$33.1 million credit adjustment.

The ALLL as a percentage of nonaccrual loans was 133.65% at June 30, 2018 and 224.32% at December 31, 2017. The ALLL as a percentage of nonperforming loans, including accruing TDRs, declined to 86.80% as of June 30, 2018 from 129.77% as of December 31, 2017 due to a \$20.7 million, or 49.7%, increase in nonperforming loans. The increase in nonperforming loans was primarily attributed to the merger, coupled with two commercial relationships downgraded to nonaccrual status during the period, which offset the Company's resolution efforts and positive credit risk rating migration.

Second quarter 2018 net charge-offs were \$4.0 million, or 0.18% of average loans and leases on an annualized basis, compared to net charge-offs of \$0.3 million, or 0.02% of average loans and leases on an annualized basis for the comparable quarter in 2017. The increase in net charge-offs was primarily related to a single agriculture relationship charged down during the period. For the six months ended June 30, 2018, net charge-offs were \$6.0 million, or 0.16% of annualized average loans, compared to \$3.9 million, or 0.14% of annualized average loans for the same period of 2017.

Provision expense is a product of the Company's ALLL model, as well as net charge-off activity during the period. Second quarter 2018 provision expense of \$3.7 million approximated second quarter charge-offs. This compared to a provision of \$0.5 million during the second quarter in 2017. For the six months ended June 30, 2018  
2017.



See Note 5 – Allowance for Loan and Lease Losses in the Notes to Consolidated Financial Statements, for further discussion of First Financial's ALLL.

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The table that follows includes the activity in the ALLL for the quarterly periods presented.

<i>(Dollars in thousands)</i>	Three months ended				Six months ended		
	2018 June 30,	Mar. 31,	2017 Dec. 31,	Sept. 30,	June 30,	2018 June 30,	2017
<b>Allowance for loan and lease loss activity</b>							
Balance at beginning of period	\$54,380	\$54,021	\$54,534	\$54,873	\$56,326	\$54,021	\$57,961
Provision for loan losses	3,735	2,303	(205 )	2,953	467	6,038	834
Gross charge-offs							
Commercial and industrial	4,356	885	1,264	4,122	3,065	5,241	4,808
Lease financing	0	0	0	0	0	0	0
Construction real estate	0	0	1	0	0	0	0
Commercial real estate	78	2,176	10	58	485	2,254	970
Residential real estate	101	96	128	23	223	197	284
Home equity	385	242	278	71	384	627	564
Installment	218	16	26	24	126	234	175
Credit card	684	254	209	201	215	938	447
Total gross charge-offs	5,822	3,669	1,916	4,499	4,498	9,491	7,248
Recoveries							
Commercial and industrial	518	436	370	325	693	954	955
Lease financing	1	0	0	0	1	1	1
Construction real estate	0	0	0	0	89	0	89
Commercial real estate	887	752	480	585	1,398	1,639	1,654
Residential real estate	70	26	77	70	59	96	68
Home equity	187	429	589	110	222	616	328
Installment	82	48	46	74	43	130	114
Credit card	38	34	46	43	73	72	117
Total recoveries	1,783	1,725	1,608	1,207	2,578	3,508	3,326
Total net charge-offs	4,039	1,944	308	3,292	1,920	5,983	3,922
<b>Ending allowance for loan and lease losses</b>	<b>\$54,076</b>	<b>\$54,380</b>	<b>\$54,021</b>	<b>\$54,534</b>	<b>\$54,873</b>	<b>\$54,076</b>	<b>\$54,873</b>

**Net charge-offs to average loans and leases (annualized)**

Commercial and industrial	0.46	% 0.10	% 0.19	% 0.82	% 0.53	% 0.33	% 0.44	%
Lease financing	0.00	% 0.00	% 0.00	% 0.00	% 0.00	% 0.00	% 0.00	%
Construction real estate	0.00	% 0.00	% 0.00	% 0.00	% (0.08)	)% 0.00	% (0.04)	)%
Commercial real estate	(0.11)	)% 0.23	% (0.07)	)% (0.08)	)% (0.15)	)% 0.04	% (0.06)	)%
Residential real estate	0.01	% 0.06	% 0.04	% (0.04)	)% 0.13	% 0.03	% 0.09	%
Home equity	0.10	% (0.16)	)% (0.25)	)% (0.03)	)% 0.14	% 0.00	% 0.10	%
Installment	0.37	% (0.32)	)% (0.19)	)% (0.43)	)% 0.65	% 0.22	% 0.24	%
Credit card	5.38	% 1.90	% 1.39	% 1.39	% 1.28	% 3.67	% 1.50	%
<b>Total net charge-offs</b>	<b>0.18</b>	<b>% 0.13</b>	<b>% 0.02</b>	<b>% 0.22</b>	<b>% 0.13</b>	<b>% 0.16</b>	<b>% 0.14</b>	<b>%</b>

Table of Contents**MARKET RISK**

Market risk is the risk of loss arising from adverse changes in the fair value of financial instruments due to changes in interest rates, foreign exchange rates and equity prices. The primary source of market risk for First Financial is interest rate risk. Interest rate risk is the risk to earnings and the value of the Company's equity arising from changes in market interest rates. Interest rate risk arises in the normal course of business to the extent that there is a divergence between the amount of interest-earning assets and the amount of interest-bearing liabilities that are prepaid, withdrawn, re-priced or mature in specified periods. First Financial seeks to achieve consistent growth in net interest income and equity while managing volatility from shifts in market interest rates.

First Financial monitors the Company's interest rate risk position using income simulation models and EVE sensitivity analyses that capture both short-term and long-term interest rate risk exposure. Income simulation involves forecasting NII under a variety of interest rate scenarios. EVE is calculated by discounting the cash flows for all balance sheet instruments under different interest-rate scenarios and First Financial uses EVE sensitivity analysis to understand the impact of changes in interest rates on long-term cash flows, income and capital. For both NII and EVE modeling, First Financial leverages instantaneous parallel shocks to evaluate interest rate risk exposure across rising and falling rate scenarios. Additional scenarios evaluated include implied market forward rate forecasts and various non-parallel yield curve twists.

First Financial's interest rate risk models are based on the contractual and assumed cash flows and repricing characteristics for the Company's assets, liabilities and off-balance sheet exposure. A number of assumptions are also incorporated into the interest rate risk models, including prepayment behaviors and repricing spreads for assets in addition to attrition and repricing rates for liabilities. Assumptions are primarily derived from behavior studies of the Company's historical client base and are continually refined. Modeling the sensitivity of NII and EVE to changes in market interest rates is highly dependent on the assumptions incorporated into the modeling process.

Non-maturity deposit modeling is particularly dependent on the assumption for repricing sensitivity known as a beta. Beta is the amount by which First Financial's interest bearing non-maturity deposit rates will increase when short-term interest rates rise. The Company utilized a weighted average deposit beta of 59% in its interest rate risk modeling as of June 30, 2018. First Financial also includes an assumption for the migration of non-maturity deposit balances into CDs for all upward rate scenarios beginning with the +100 bps scenario, thereby increasing deposit costs and reducing asset sensitivity.

Presented below is the estimated impact on First Financial's NII and EVE position as of June 30, 2018, assuming immediate, parallel shifts in interest rates:

	% Change from base case			
	for			
	immediate parallel changes			
	in rates			
	-100 bps	+100 bps	+200 bps	
NII-Year 1 (5.30)%	1.12 %	1.81 %		
NII-Year 2 (6.67)%	1.75 %	2.94 %		
EVE (3.78)%	0.06 %	0.62 %		

"*Risk-neutral*" refers to the absence of a strong bias toward either asset or liability sensitivity. "*Asset sensitivity*" is when a company's interest-earning assets reprice more quickly or in greater quantities than interest-bearing liabilities. Conversely, "*liability sensitivity*" is when a company's interest-bearing liabilities reprice more quickly or in greater quantities than interest-earning assets. In a rising interest rate environment, asset sensitivity results in higher net interest income while liability sensitivity results in lower net interest income. In a declining interest rate environment,

asset sensitivity results in lower net interest income while liability sensitivity results in higher net interest income.

First Financial was within policy limits set for the disclosed interest rate scenarios as of June 30, 2018. The projected results for NII and EVE continued to reflect modest asset sensitivity during the second quarter of 2018. Second quarter results migrated closer to neutral following the MSFG merger as the combined company has a lower mix of floating rate assets and implemented longer term funding strategies. First Financial continues to manage its balance sheet with a bias toward asset sensitivity while simultaneously balancing the potential earnings impact of this strategy.

First Financial continually evaluates the sensitivity of its interest rate risk position to modeling assumptions. The following table reflects First Financial's estimated NII sensitivity profile as of June 30, 2018 assuming a 25% increase and a 25% reduction to the beta assumption on managed rate deposits:

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	Beta sensitivity (% change from base)			
	+100 BP		+200 BP	
	Beta	Beta	Beta	Beta
	25%	25%	25%	25%
	lower	higher	lower	higher
NII-Year 1	2.83%	(0.60)%	4.95%	(1.33)%
NII-Year 2	3.46%	0.04%	6.06%	(0.19)%

See the Net Interest Income section of Management's Discussion and Analysis for further discussion.

**CRITICAL ACCOUNTING POLICIES**

First Financial's Consolidated Financial Statements are prepared based on the application of the Company's accounting policies. These policies require the reliance on estimates and assumptions. Changes in underlying factors, assumptions or estimates could have a material impact on First Financial's future financial condition and results of operations. In management's opinion, certain accounting policies have a more significant impact than others on First Financial's financial reporting. For First Financial, these areas currently include accounting for the ALLL, goodwill, pension and income taxes. These accounting policies are discussed in detail in the Critical Accounting Policies section of Management's Discussion and Analysis in First Financial's 2017 Annual Report. There were no material changes to these accounting policies during the six months ended June 30, 2018.

**ACCOUNTING AND REGULATORY MATTERS**

Note 2 - Recently Adopted and Issued Accounting Standards in the Notes to Consolidated Financial Statements, discusses new accounting standards adopted by First Financial during 2018 and the expected impact of accounting standards recently issued but not yet required to be adopted. To the extent the adoption of new accounting standards materially affects financial condition, results of operations or liquidity, the impacts are discussed in the applicable section(s) of Management's Discussion and Analysis and the Notes to the Consolidated Financial Statements.

**FORWARD-LOOKING STATEMENT**

Certain statements contained in this report which are not statements of historical fact constitute forward-looking statements within the meaning of the Private Securities Litigation Reform Act of 1995. Words such as "believes," "anticipates," "likely," "expected," "estimated," "intends" and other similar expressions are intended to identify forward-looking statements but are not the exclusive means of identifying such statements. Examples of forward looking statements include, but are not limited to, statements we make about (i) our future operating or financial performance, including revenues, income or loss and earnings or loss per share, (ii) future common stock dividends, (iii) our capital structure, including future capital levels, (iv) our plans, objectives and strategies, and (v) the assumptions that underlie our forward-looking statements.

As with any forecast or projection, forward-looking statements are subject to inherent uncertainties, risks and changes in circumstances that may cause actual results to differ materially from those set forth in the forward-looking statements. Forward-looking statements are not historical facts but instead express only management's beliefs regarding future results or events, many of which, by their nature, are inherently uncertain and outside of management's control. It is possible that actual results and outcomes may differ, possibly materially, from the anticipated results or outcomes indicated in these forward-looking statements. Important factors that could cause actual results to differ materially from those in our forward-looking statements include the following, without limitation: (i) economic, market, liquidity, credit, interest rate, operational and technological risks associated with the

Company's business; (ii) the effect of and changes in policies and laws or regulatory agencies, including the Dodd-Frank Wall Street Reform and Consumer Protection Act and other legislation and regulation relating to the banking industry; (iii) management's ability to effectively execute its business plans; (iv) mergers and acquisitions, including costs or difficulties related to the integration of acquired companies; (v) the possibility that any of the anticipated benefits of the Company's recent merger with MainSource Financial Group, Inc. will not be realized or will not be realized within the expected time period; (vi) the effect of changes in accounting policies and practices; (vii) changes in consumer spending, borrowing and saving and changes in unemployment; (viii) changes in customers' performance and creditworthiness; and (ix) the costs and effects of litigation and of unexpected or adverse outcomes in such litigation. Additional factors that may cause our actual results to differ materially from those described in our forward-looking statements can be found in the Form 10-K for the year ended December 31, 2017, as well as its other filings with the SEC, which are available on the SEC website at [www.sec.gov](http://www.sec.gov).

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All forward-looking statements included in this filing are made as of the date hereof and are based on information available at the time of the filing. Except as required by law, the Company does not assume any obligation to update any forward-looking statement.

**ITEM 3. QUANTITATIVE AND QUALITATIVE DISCLOSURES ABOUT MARKET RISK**

The information contained in “Item 2-Management’s Discussion and Analysis of Financial Condition and Results of Operations—Market Risk” of this report is incorporated herein by reference in response to this item.

**ITEM 4. CONTROLS AND PROCEDURES**

**Disclosure Controls and Procedures**

Management is responsible for establishing and maintaining effective disclosure controls and procedures, as defined under

Rule 13a-15 of the Securities Exchange Act of 1934, that are designed to cause the material information required to be disclosed by First Financial in the reports it files or submits under the Securities Exchange Act of 1934 to be recorded, processed, summarized, and reported to the extent applicable within the time periods required by the Securities and Exchange Commission’s rules and forms. In designing and evaluating the disclosure controls and procedures, management recognized that a control system, no matter how well designed and operated, can provide only reasonable, not absolute, assurance that the objectives of the control system are met. Because of the inherent limitations in all control systems, no evaluation of controls can provide absolute assurance that all control issues and instances of fraud, if any, within a company have been detected.

As of the end of the period covered by this report, First Financial performed an evaluation under the supervision and with the participation of management, including the Chief Executive Officer and Chief Financial Officer, of the effectiveness of the design and operation of its disclosure controls and procedures pursuant to Rule 13a-15 of the Securities Exchange Act of 1934. Based upon that evaluation, the Chief Executive Officer and Chief Financial Officer concluded that the disclosure controls and procedures were effective at the reasonable assurance level.

**Changes in Internal Control over Financial Reporting**

No changes were made to the Company's internal control over financial reporting (as defined in Rule 13a-15 under the Securities Exchange Act of 1934) during the last fiscal quarter that materially affected, or are reasonably likely to materially affect, the Corporation’s internal control over financial reporting.

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**PART II-OTHER INFORMATION**

Item 1. Legal Proceedings.

There have been no material changes to the disclosure in response to "Part I - Item 3. Legal Proceedings" in the Company's Annual Report on Form 10-K for the year ended December 31, 2017.

Item 1A. Risk Factors.

There are a number of factors that may adversely affect the Company's business, financial results, or stock price. See "Risk Factors" as disclosed in response to "Item 1A. to Part I - Risk Factors" of Form 10-K for the year ended December 31, 2017.



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## Item 2. Unregistered Sales of Equity Securities and Use of Proceeds

(c) The following table shows the total number of shares repurchased in the second quarter of 2018.

**Issuer Purchases of Equity Securities**

Period	(a) Total Number Of Shares Purchased <sup>(1)</sup>	(b) Average Price Paid Per Share	(c) Total Number of Shares Purchased as Part of Publicly Announced Plans <sup>(2)</sup>	(d) Maximum Number of Shares that may yet be purchased Under the Plans
<b>April 1 to April 30, 2018</b>				
Share repurchase program	0	\$ 0.00	0	3,509,133
Stock Plans	0	0.00	N/A	N/A
<b>May 1 to May 31, 2018</b>				
Share repurchase program	0	\$ 0.00	0	3,509,133
Stock Plans	3,800	31.65	N/A	N/A
<b>June 1 to June 30, 2018</b>				
Share repurchase program	0	\$ 0.00	0	3,509,133
Stock Plans	15,954	32.50	N/A	N/A
<b>Total</b>				
Share repurchase program	0	\$ 0.00	0	
Stock Plans	19,754	\$ 32.34	N/A	

The number of shares purchased in column (a) and the average price paid per share in column (b) include the purchase of shares other than through publicly announced plans. The shares purchased other than through publicly announced plans were purchased pursuant to First Financial's 1999 Stock Incentive Plan for Officers and Employees, Amended and Restated 2009 Non-Employee Director Stock Plan, 2012 Stock Plan, and Amended and Restated 2012 Stock Plan (collectively referred to hereafter as the Stock Plans). The table shows the number of shares purchased pursuant to the Stock Plans and the average price paid per share. Under the Stock Plans, shares were purchased from plan participants at the then current market value in satisfaction of stock option exercise prices.

First Financial has one previously announced stock repurchase plan under which it is authorized to purchase shares of its common stock. The plan has no expiration date. The table that follows provides additional information regarding this plan.

Announcement Date	Total Shares Approved for Repurchase	Total Shares Repurchased Under the Plan	Expiration Date
10/25/2012	5,000,000	1,490,867	None

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Item 6. Exhibits

(a) Exhibits:

Exhibit  
Number

31.1 Certification by Chief Executive Officer Pursuant to Section 302 of the Sarbanes-Oxley Act of 2002 filed herewith.

31.2 Certification by Chief Financial Officer Pursuant to Section 302 of the Sarbanes-Oxley Act of 2002 filed herewith.

32.1 Certification of Periodic Financial Report by Chief Executive Officer Pursuant to Section 906 of the Sarbanes-Oxley Act of 2002 furnished herewith.

32.2 Certification of Periodic Financial Report by Chief Financial Officer Pursuant to Section 906 of the Sarbanes-Oxley Act of 2002 furnished herewith.

101.1 Financial statements from the Quarterly Report on Form 10-Q of the Company for the quarter ended June 30, 2018, formatted in XBRL (eXtensible Business Reporting Language) pursuant to Rule 405 of Regulation S-T: (i) Consolidated Balance Sheets, (ii) Consolidated Statements of Income, (iii) Consolidated Statements of Comprehensive Income, (iv) Consolidated Statements of Changes in Shareholders' Equity, (v) Consolidated Statements of Cash Flows and (vi) Notes to Consolidated Financial Statements, as blocks of text and in detail.\*

First Financial will furnish, without charge, to a security holder upon request a copy of the documents and will furnish any other Exhibit upon payment of reproduction costs. Unless as otherwise noted, documents incorporated by reference involve File No. 001-34762.

\* As provided in Rule 406T of Regulation S-T, this information shall not be deemed "filed" for purposes of Section 11 and 12 of the Securities Act of 1933 and Section 18 of the Securities Exchange Act of 1934 or otherwise subject to liability under those sections.

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**SIGNATURES**

Pursuant to the requirements of the Securities Exchange Act of 1934, the registrant has duly caused this report to be signed on its behalf by the undersigned hereunto duly authorized.

FIRST  
FINANCIAL  
BANCORP.  
(Registrant)

/s/ James M. Anderson James M. Anderson Executive Vice President and Chief Financial Officer	/s/ Scott T. Crawley Scott T. Crawley First Vice President and Controller  (Principal Accounting Officer)
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Date 8/8/2018 Date 8/8/2018