

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

FORM 10-Q

(Mark One)

QUARTERLY REPORT PURSUANT TO SECTION 13 OR 15(d) OF THE SECURITIES EXCHANGE ACT OF 1934

For the quarterly period ended September 30, 2019

or

TRANSITION REPORT PURSUANT TO SECTION 13 OR 15(d) OF THE SECURITIES EXCHANGE ACT OF 1934

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

Commission File Number: 001-31567

CENTRAL PACIFIC FINANCIAL CORP.

(Exact name of registrant as specified in its charter)

Hawaii

(State or other jurisdiction of incorporation or organization)

99-0212597

(I.R.S. Employer Identification No.)

220 South King Street, Honolulu, Hawaii 96813

(Address of principal executive offices) (Zip Code)

(808) 544-0500

(Registrant's telephone number, including area code)

**Securities registered pursuant to Section 12(b) of the Act:**

Title of each class	Trading Symbol(s)	Name of each exchange on which registered
Common stock, No Par Value	CPF	New York Stock Exchange

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

Indicate by check mark whether the registrant has submitted electronically every Interactive Data File required to be submitted pursuant to Rule 405 of Regulation S-T (§232.405 of this chapter) during the preceding 12 months (or for such shorter period that the registrant was required to submit such files). Yes  No

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

Large Accelerated Filer	<input checked="" type="checkbox"/>	Accelerated filer	<input type="checkbox"/>
Non-accelerated filer	<input type="checkbox"/>	Smaller reporting company	<input type="checkbox"/>
Emerging growth company	<input type="checkbox"/>		

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 Securities Act.

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

The number of shares outstanding of registrant's common stock, no par value, on October 31, 2019 was 28,376,894 shares.

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## PART I. FINANCIAL INFORMATION

### Forward-Looking Statements and Factors that Could Affect Future Results

This document may contain forward-looking statements concerning: projections of revenues, expenses, income or loss, earnings or loss per share, capital expenditures, the payment or nonpayment of dividends, capital position, net interest margin or other financial items; statements of plans, objectives and expectations of Central Pacific Financial Corp. or its management or Board of Directors, including those relating to business plans, use of capital resources, products or services and regulatory developments and regulatory actions; statements of future economic performance including anticipated performance results from our RISE2020 initiative; or any statements of the assumptions underlying or relating to any of the foregoing. Forward-looking statements can be identified by the fact that they do not relate strictly to historical or current facts, and may include the words "believes," "plans," "anticipates," "expects," "intends," "forecasts," "hopes," "targeting," "continue," "remain," "will," "should," "estimates," "may" or words of similar meaning.

While we believe that our forward-looking statements and the assumptions underlying them are reasonably based, such statements and assumptions are by their nature subject to risks and uncertainties, and thus could later prove to be inaccurate or incorrect. Accordingly, actual results could differ materially from those statements or projections for a variety of reasons, including, but not limited to: adverse changes in the financial performance and/or condition of our borrowers and, as a result, increased loan delinquency rates, deterioration in asset quality, and losses in our loan portfolio; our ability to successfully implement our RISE2020 initiative; current and projected levels of RISE2020-related expense, which include estimates of expense related to dedicated staff and management time and third-party expense; the impact of local, national, and international economies and events (including natural disasters such as wildfires, volcanic eruptions, hurricanes, tsunamis, storms and earthquakes) on the Company's business and operations and on tourism, the military, and other major industries operating within the Hawaii market and any other markets in which the Company does business; deterioration or malaise in domestic economic conditions, including any destabilization in the financial industry and deterioration of the real estate market, as well as the impact of declining levels of consumer and business confidence in the state of the economy in general and in financial institutions in particular; changes in estimates of future reserve requirements based upon the periodic review thereof under relevant regulatory and accounting requirements; the impact of the Dodd-Frank Wall Street Reform and Consumer Protection Act, changes in capital standards, other regulatory reform, including but not limited to regulations promulgated by the Consumer Financial Protection Bureau, government-sponsored enterprise reform, and any related rules and regulations on our business operations and competitiveness; the costs and effects of legal and regulatory developments, including the resolution of legal proceedings or regulatory or other governmental inquiries and proceedings and the resolution thereof, the results of regulatory examinations or reviews and the effect of, and our ability to comply with, any regulatory orders or actions we are or may become subject to; ability to successfully implement our initiatives to lower our efficiency ratio; the effects of and changes in trade, monetary and fiscal policies and laws, including the interest rate policies of the Board of Governors of the Federal Reserve System; inflation, interest rate, securities market and monetary fluctuations, including the anticipated replacement of the London Interbank Offered Rate Index and the impact on our loans and debt which are tied to that index; negative trends in our market capitalization and adverse changes in the price of the Company's common stock; political instability; acts of war or terrorism; changes in consumer spending, borrowings and savings habits; failure to maintain effective internal control over financial reporting or disclosure controls and procedures; the ability to address any material weakness in our internal controls over financial reporting or disclosure controls and procedures; technological changes and developments; changes in the competitive environment among financial holding companies and other financial service providers; the effect of changes in accounting policies and practices, as may be adopted by the regulatory agencies, as well as the Public Company Accounting Oversight Board, the Financial Accounting Standards Board and other accounting standard setters and the cost and resources required to implement such changes; our ability to attract and retain key personnel; changes in our organization, compensation and benefit plans; and our success at managing the risks involved in the foregoing items.

For further information with respect to factors that could cause actual results to materially differ from the expectations or projections stated in the forward-looking statements, please see the Company's publicly available Securities and Exchange Commission filings, including the Company's Form 10-K for the last fiscal year and, in particular, the discussion of "Risk Factors" set forth therein. We undertake no obligation to update any forward-looking statements to reflect events or circumstances after the date on which such statement is made, or to reflect the occurrence of unanticipated events except as required by law.

**CENTRAL PACIFIC FINANCIAL CORP. AND SUBSIDIARIES**  
**CONSOLIDATED BALANCE SHEETS (Unaudited)**

(dollars in thousands)	September 30, 2019	December 31, 2018
<b>Assets</b>		
Cash and due from banks	\$ 87,395	\$ 80,569
Interest-bearing deposits in other banks	7,803	21,617
Investment securities:		
Available-for-sale debt securities, at fair value	1,186,875	1,205,478
Held-to-maturity debt securities, at amortized cost; fair value of: none at September 30, 2019 and \$144,272 at December 31, 2018	—	148,508
Equity securities, at fair value	1,058	826
Total investment securities	1,187,933	1,354,812
Loans held for sale	7,016	6,647
Loans and leases	4,367,862	4,078,366
Allowance for loan and lease losses	(48,167)	(47,916)
Net loans and leases	4,319,695	4,030,450
Premises and equipment, net	44,095	45,285
Accrued interest receivable	16,220	17,000
Investment in unconsolidated subsidiaries	17,001	14,008
Other real estate owned	466	414
Mortgage servicing rights	15,058	15,596
Bank-owned life insurance	158,939	157,440
Federal Home Loan Bank stock	17,183	16,645
Right-of-use lease asset	52,588	—
Other assets	45,324	46,543
<b>Total assets</b>	<b>\$ 5,976,716</b>	<b>\$ 5,807,026</b>
<b>Liabilities</b>		
Deposits:		
Noninterest-bearing demand	\$ 1,399,200	\$ 1,436,967
Interest-bearing demand	998,037	954,011
Savings and money market	1,593,738	1,448,257
Time	1,046,684	1,107,255
Total deposits	5,037,659	4,946,490
Short-term borrowings	205,000	197,000
Long-term debt	101,547	122,166
Lease liability	52,807	—
Other liabilities	54,476	49,645
<b>Total liabilities</b>	<b>5,451,489</b>	<b>5,315,301</b>
<b>Shareholders' Equity</b>		
Preferred stock, no par value, authorized 1,000,000 shares; issued and outstanding: none at September 30, 2019 and December 31, 2018	—	—
Common stock, no par value, authorized 185,000,000 shares; issued and outstanding: 28,441,341 at September 30, 2019 and 28,967,715 at December 31, 2018	452,278	470,660
Additional paid-in capital	90,604	88,876
Accumulated deficit	(26,782)	(51,718)
Accumulated other comprehensive income (loss)	9,127	(16,093)
Total shareholders' equity	525,227	491,725
<b>Total liabilities and shareholders' equity</b>	<b>\$ 5,976,716</b>	<b>\$ 5,807,026</b>

*See accompanying notes to consolidated financial statements.*



**CENTRAL PACIFIC FINANCIAL CORP. AND SUBSIDIARIES**  
**CONSOLIDATED STATEMENTS OF INCOME (Unaudited)**

	Three Months Ended September 30,		Nine Months Ended September 30,	
	2019	2018	2019	2018
(dollars in thousands, except per share data)				
<b>Interest income:</b>				
Interest and fees on loans and leases	\$ 45,861	\$ 40,531	\$ 135,169	\$ 116,620
<b>Interest and dividends on investment securities:</b>				
Taxable interest	7,178	8,490	22,968	26,050
Tax-exempt interest	708	920	2,388	2,786
Dividends	14	26	46	44
Interest on deposits in other banks	33	109	147	310
Dividends on Federal Home Loan Bank stock	186	60	508	145
<b>Total interest income</b>	<b>53,980</b>	<b>50,136</b>	<b>161,226</b>	<b>145,955</b>
<b>Interest expense:</b>				
<b>Interest on deposits:</b>				
Demand	207	181	598	554
Savings and money market	1,549	593	3,847	1,421
Time	4,432	4,744	14,391	12,203
Interest on short-term borrowings	1,130	146	3,146	237
Interest on long-term debt	1,013	1,147	3,104	3,221
<b>Total interest expense</b>	<b>8,331</b>	<b>6,811</b>	<b>25,086</b>	<b>17,636</b>
Net interest income	45,649	43,325	136,140	128,319
Provision (credit) for loan and lease losses	1,532	(59)	4,219	262
Net interest income after provision (credit) for loan and lease losses	44,117	43,384	131,921	128,057
<b>Other operating income:</b>				
Mortgage banking income	1,764	1,923	4,789	5,545
Service charges on deposit accounts	2,125	2,189	6,247	6,169
Other service charges and fees	3,724	3,286	10,479	9,697
Income from fiduciary activities	1,126	1,159	3,220	3,132
Equity in earnings of unconsolidated subsidiaries	86	71	165	151
Fees on foreign exchange	170	220	539	708
Investment securities gains	36	—	36	—
Income from bank-owned life insurance	645	1,055	2,511	1,874
Loan placement fees	230	115	486	532
Net gain on sales of foreclosed assets	17	—	17	—
Other	343	802	3,544	1,596
<b>Total other operating income</b>	<b>10,266</b>	<b>10,820</b>	<b>32,033</b>	<b>29,404</b>
<b>Other operating expense:</b>				
Salaries and employee benefits	20,631	19,011	61,083	56,299
Net occupancy	3,697	3,488	10,680	10,114
Equipment	1,067	1,048	3,211	3,160
Amortization of core deposit premium	—	669	—	2,006
Communication expense	1,008	903	2,645	2,547
Legal and professional services	1,933	1,528	5,231	5,118
Computer software expense	2,713	2,672	7,870	7,244
Advertising expense	711	612	2,134	1,841
Foreclosed asset expense	15	212	223	537
Other	3,159	3,882	12,312	12,174
<b>Total other operating expense</b>	<b>34,934</b>	<b>34,025</b>	<b>105,389</b>	<b>101,040</b>
Income before income taxes	19,449	20,179	58,565	56,421
Income tax expense	4,895	4,986	14,440	12,727
<b>Net income</b>	<b>\$ 14,554</b>	<b>\$ 15,193</b>	<b>\$ 44,125</b>	<b>\$ 43,694</b>
Per common share data:				

Basic earnings per common share	\$	0.51	\$	0.52	\$	1.54	\$	1.48
Diluted earnings per common share	\$	0.51	\$	0.52	\$	1.53	\$	1.47
Cash dividends declared	\$	0.23	\$	0.21	\$	0.67	\$	0.61
Weighted average common shares outstanding used in computation:								
Basic shares		28,424,898		29,297,465		28,575,369		29,536,536
Diluted shares		28,602,338		29,479,812		28,762,057		29,743,238

*See accompanying notes to consolidated financial statements.*

**CENTRAL PACIFIC FINANCIAL CORP. AND SUBSIDIARIES**  
**CONSOLIDATED STATEMENTS OF COMPREHENSIVE INCOME (Unaudited)**

(dollars in thousands)	Three Months Ended September 30,		Nine Months Ended September 30,	
	2019	2018	2019	2018
Net income	\$ 14,554	\$ 15,193	\$ 44,125	\$ 43,694
Other comprehensive income (loss), net of tax:				
Net change in unrealized gain (loss) on investment securities	4,386	(6,072)	27,547	(24,712)
Defined benefit plans	283	217	773	623
Total other comprehensive income (loss), net of tax	4,669	(5,855)	28,320	(24,089)
Comprehensive income	\$ 19,223	\$ 9,338	\$ 72,445	\$ 19,605

*See accompanying notes to consolidated financial statements.*

**CENTRAL PACIFIC FINANCIAL CORP. AND SUBSIDIARIES**  
**CONSOLIDATED STATEMENTS OF CHANGES IN EQUITY (Unaudited)**

	Common Shares Outstanding	Preferred Stock	Common Stock	Additional Paid- In Capital	Accum. Deficit	Accum. Other Comp. Income (Loss)	Non- Controlling Interest	Total
(dollars in thousands, except per share data)								
<b>Balance at December 31, 2018</b>	28,967,715	\$ —	\$ 470,660	\$ 88,876	\$ (51,718)	\$ (16,093)	\$ —	\$ 491,725
Impact of the adoption of new accounting standards (1)	—	—	—	—	—	(3,100)	—	(3,100)
<b>Adjusted balance at January 1, 2019</b>	28,967,715	—	470,660	88,876	(51,718)	(19,193)	—	488,625
Net income	—	—	—	—	16,037	—	—	16,037
Other comprehensive income	—	—	—	—	—	11,238	—	11,238
Cash dividends declared (\$0.21 per share)	—	—	—	—	(6,052)	—	—	(6,052)
Common stock repurchased and retired and other related costs	(277,000)	—	(7,708)	—	—	—	—	(7,708)
Share-based compensation expense	32,326	—	—	498	—	—	—	498
<b>Balance at March 31, 2019</b>	28,723,041	\$ —	\$ 462,952	\$ 89,374	\$ (41,733)	\$ (7,955)	\$ —	\$ 502,638
Net income	—	—	—	—	13,534	—	—	13,534
Other comprehensive income	—	—	—	—	—	12,413	—	12,413
Cash dividends declared (\$0.23 per share)	—	—	—	—	(6,581)	—	—	(6,581)
Common stock purchased by directors' deferred compensation plan (14,600 shares, net)	—	—	(416)	—	—	—	—	(416)
Common stock repurchased and retired and other related costs	(213,700)	—	(6,243)	—	—	—	—	(6,243)
Share-based compensation expense	58,436	—	—	350	—	—	—	350
<b>Balance at June 30, 2019</b>	28,567,777	\$ —	\$ 456,293	\$ 89,724	\$ (34,780)	\$ 4,458	\$ —	\$ 515,695
Net income	—	—	—	—	14,554	—	—	14,554
Other comprehensive income	—	—	—	—	—	4,669	—	4,669
Cash dividends declared (\$0.23 per share)	—	—	—	—	(6,556)	—	—	(6,556)
Common stock repurchased and retired and other related costs	(140,600)	—	(4,015)	—	—	—	—	(4,015)
Share-based compensation	14,164	—	—	880	—	—	—	880
<b>Balance at September 30, 2019</b>	28,441,341	\$ —	\$ 452,278	\$ 90,604	\$ (26,782)	\$ 9,127	\$ —	\$ 525,227

**CENTRAL PACIFIC FINANCIAL CORP. AND SUBSIDIARIES**  
**CONSOLIDATED STATEMENTS OF CHANGES IN EQUITY (Unaudited)**

	Common Shares Outstanding	Preferred Stock	Common Stock	Additional Paid- In Capital	Accum. Deficit	Accum. Other Comp. Income (Loss)	Non- Controlling Interest	Total
(dollars in thousands, except per share data)								
<b>Balance at December 31, 2017</b>	30,024,222	\$ —	\$ 503,988	\$ 86,098	\$ (89,036)	\$ (1,039)	\$ 24	\$ 500,035
Impact of the adoption of new accounting standards (2)	—	—	—	—	139	(139)	—	—
<b>Adjusted balance at January 1, 2018</b>	30,024,222	—	503,988	86,098	(88,897)	(1,178)	24	500,035
Impact of the adoption of new accounting standards (3)	—	—	—	—	1,836	(1,836)	—	—
Net income	—	—	—	—	14,277	—	—	14,277
Other comprehensive loss	—	—	—	—	—	(14,715)	—	(14,715)
Cash dividends declared (\$0.19 per share)	—	—	—	—	(5,670)	—	—	(5,670)
Common stock purchased by directors' deferred compensation plan (2,850 shares, net)	—	—	(83)	—	—	—	—	(83)
Common stock repurchased and retired and other related costs (344,362 shares)	(344,362)	—	(10,111)	—	—	—	—	(10,111)
Share-based compensation	27,262	—	—	399	—	—	—	399
Distribution from variable interest entity	—	—	—	—	—	—	(24)	(24)
<b>Balance at March 31, 2018</b>	29,707,122	\$ —	\$ 493,794	\$ 86,497	\$ (78,454)	\$ (17,729)	\$ —	\$ 484,108
Net income	—	—	—	—	14,224	—	—	14,224
Other comprehensive income	—	—	—	—	—	(3,519)	—	(3,519)
Cash dividends declared (\$0.21 per share)	—	—	—	—	(6,205)	—	—	(6,205)
Common stock purchased by directors' deferred compensation plan (14,100 shares, net)	—	—	(421)	—	—	—	—	(421)
Common stock repurchased and retired and other related costs (269,885 shares)	(269,885)	—	(7,971)	—	—	—	—	(7,971)
Share-based compensation	52,717	—	—	452	—	—	—	452
<b>Balance at June 30, 2018</b>	29,489,954	\$ —	\$ 485,402	\$ 86,949	\$ (70,435)	\$ (21,248)	\$ —	\$ 480,668
Net income	—	—	—	—	15,193	—	—	15,193
Other comprehensive income	—	—	—	—	—	(5,855)	—	(5,855)
Cash dividends declared (\$0.21 per share)	—	—	—	—	(6,164)	—	—	(6,164)
Common stock repurchased and retired and other related costs (235,043 shares)	(235,043)	—	(6,681)	—	—	—	—	(6,681)
Share-based compensation	15,487	—	—	990	—	—	—	990
<b>Balance at September 30, 2018</b>	29,270,398	\$ —	\$ 478,721	\$ 87,939	\$ (61,406)	\$ (27,103)	\$ —	\$ 478,151

- (1) Represents the impact of the adoption of Accounting Standards Update ("ASU") ASU 2017-12. See Note 2 to the consolidated financial statements for additional information.  
(2) Represents the impact of the adoption of ASU 2016-01.  
(3) Represents the impact of the adoption of ASU 2018-02.

*See accompanying notes to consolidated financial statements.*

**CENTRAL PACIFIC FINANCIAL CORP. AND SUBSIDIARIES**  
**CONSOLIDATED STATEMENTS OF CASH FLOWS (Unaudited)**

(dollars in thousands)	Nine Months Ended September 30,	
	2019	2018
<b>Cash flows from operating activities:</b>		
Net income	\$ 44,125	\$ 43,694
Adjustments to reconcile net income to net cash provided by operating activities:		
Provision for loan and lease losses	4,219	262
Depreciation and amortization of premises and equipment	4,628	4,700
Non-cash lease expense	220	—
Cash flows from operating leases	(4,663)	—
Loss on sale of other real estate, net of write-downs	138	431
Amortization of core deposit premium and mortgage servicing rights	1,727	3,419
Net amortization and accretion of premium/discounts on investment securities	6,808	8,465
Share-based compensation expense	1,728	1,841
Net (gain) on sales of investment securities	(36)	—
Net gain on sales of residential mortgage loans	(2,836)	(3,013)
Proceeds from sales of loans held for sale	152,684	183,967
Originations of loans held for sale	(150,217)	(169,078)
Equity in earnings of unconsolidated subsidiaries	(165)	(151)
Distributions from unconsolidated subsidiaries	175	614
Net increase in cash surrender value of bank-owned life insurance	(1,499)	(792)
Deferred income taxes	7,548	12,542
Net tax benefits from share-based compensation	209	185
Net change in other assets and liabilities	(12,309)	(8,266)
<b>Net cash provided by operating activities</b>	<b>52,484</b>	<b>78,820</b>
<b>Cash flows from investing activities:</b>		
Proceeds from maturities of and calls on investment securities available-for-sale	194,626	114,508
Proceeds from sales of investment securities available-for-sale	53,935	—
Purchases of investment securities available-for-sale	(54,975)	(85,334)
Proceeds from maturities of and calls on investment securities held-to-maturity	—	38,491
Proceeds from sale of MasterCard stock	2,555	—
Net loan proceeds (originations)	(214,834)	(190,022)
Purchases of loan portfolios	(78,820)	(20,867)
Proceeds from sale of foreclosed loans/other real estate owned	—	46
Net purchases of premises and equipment	(3,438)	(2,536)
Net return of capital from unconsolidated subsidiaries	622	—
Net (purchases of) proceeds from redemption of FHLB stock	(538)	(3,204)
<b>Net cash used in investing activities</b>	<b>(100,867)</b>	<b>(148,918)</b>
<b>Cash flows from financing activities:</b>		
Net increase in deposits	91,169	47,326
Repayments of long-term debt	(20,619)	—
Net increase (decrease) in short-term borrowings	8,000	73,000
Cash dividends paid on common stock	(19,189)	(18,039)
Repurchases of common stock and other related costs	(17,966)	(24,763)
<b>Net cash provided by financing activities</b>	<b>41,395</b>	<b>77,524</b>
Net (decrease) increase in cash and cash equivalents	(6,988)	7,426
Cash and cash equivalents at beginning of period	102,186	82,293
<b>Cash and cash equivalents at end of period</b>	<b>\$ 95,198</b>	<b>\$ 89,719</b>
<b>Supplemental disclosure of cash flow information:</b>		
Cash paid during the period for:		
Interest	\$ 24,735	\$ 15,969

Income taxes	17,601	23
<b>Supplemental disclosure of non-cash information:</b>		
Net change in common stock held by directors' deferred compensation plan	416	504
Net reclassification of loans to foreclosed loans/other real estate owned	190	40
Net transfer of investment securities held-to-maturity to available-for-sale	149,042	—
Right-of-use lease assets obtained in exchange for lease liabilities	55,887	—

*See accompanying notes to consolidated financial statements.*

**CENTRAL PACIFIC FINANCIAL CORP. AND SUBSIDIARIES**  
**NOTES TO CONSOLIDATED FINANCIAL STATEMENTS (Unaudited)**

**1. SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES**

**Basis of Presentation**

The accompanying unaudited consolidated financial statements of Central Pacific Financial Corp. and Subsidiaries (herein referred to as the "Company," "we," "us" or "our") have been prepared in accordance with U.S. generally accepted accounting principles ("GAAP") for interim financial information and with the instructions to Form 10-Q and Rule 10-01 of Regulation S-X. Accordingly, certain information and footnote disclosures normally included in financial statements prepared in accordance with GAAP have been condensed or omitted pursuant to such rules and regulations.

These interim condensed consolidated financial statements and notes should be read in conjunction with the Company's consolidated financial statements and notes thereto filed on Form 10-K for the fiscal year ended December 31, 2018. In the opinion of management, all adjustments necessary for a fair presentation have been made and include all normal recurring adjustments. Interim results of operations are not necessarily indicative of results to be expected for the year.

**Principles of Consolidation**

The consolidated financial statements include the accounts of the Company and its majority-owned subsidiaries. All significant intercompany accounts and transactions have been eliminated in consolidation.

We also have non-controlling equity investments in affiliates that are accounted for under the cost method and are included in investment in unconsolidated subsidiaries.

Our investments in unconsolidated subsidiaries accounted for under the equity, proportional amortization and cost methods were \$0.2 million, \$15.2 million and \$1.6 million, respectively, at September 30, 2019 and \$0.2 million, \$11.6 million and \$2.2 million, respectively, at December 31, 2018. Our policy for determining impairment of these investments includes an evaluation of whether a loss in value of an investment is other than temporary. Evidence of a loss in value includes absence of an ability to recover the carrying amount of the investment or the inability of the investee to sustain an earnings capacity which would justify the carrying amount of the investment. We perform impairment tests whenever indicators of impairment are present. If the value of an investment declines and it is considered other than temporary, the investment is written down to its respective fair value in the period in which this determination is made.

The Company sponsors the Central Pacific Bank Foundation, which is not consolidated in the Company's financial statements.

**Reclassifications**

Certain prior year amounts in the consolidated financial statements and the notes thereto have been reclassified to conform to the fiscal 2019 presentation. Such reclassifications had no effect on the Company's reported net income or shareholders' equity.

**2. RECENT ACCOUNTING PRONOUNCEMENTS**

**Accounting Standards Adopted in 2019**

In February 2016, the FASB issued ASU 2016-02, "*Leases (Topic 842)*." ASU 2016-02 increases transparency and comparability among organizations by recognizing lease assets and lease liabilities on the balance sheet and disclosing key information about leasing arrangements. The ASU establishes a right-of-use ("ROU") model that requires a lessee to recognize a ROU lease asset and lease liability on the balance sheet for all leases with a term of longer than 12 months. The FASB has also made available several practical expedients to assist entities with the adoption of ASU 2016-02. Among other things, these practical expedients require no reassessment of whether existing contracts are or contain leases as well as no reassessment of lease classification for current leases. In July 2018, the FASB released ASU 2018-11, "*Leases (Topic 842): Targeted Improvements*," which adds an additional practical expedient that allows entities to elect not to recast comparative periods presented when transitioning to Topic 842. The Company elected to adopt the practical expedient allowed under ASU 2018-11. During the year ended December 31, 2018, the Company engaged a software vendor to assist in the implementation of ASU 2016-02. The Company adopted ASU 2016-02 effective January 1, 2019 using the modified retrospective approach and recorded a ROU lease asset and corresponding lease liability on the Company's consolidated balance sheet of \$55.9 million for its operating leases where it is a lessee. There was no impact to the Company's financial statements for its leases where it is a

lessor. As of September 30, 2019, the ROU lease asset and lease liability was \$52.6 million and \$52.8 million, respectively. See Note 12 - Leases for required disclosures on this new standard.

In August 2017, the FASB issued ASU 2017-12, *"Derivatives and Hedging (Topic 815): Targeted Improvements to Accounting for Hedging Activities."* ASU 2017-12 was issued to better align an entity's risk management activities and financial reporting for hedging relationships through changes to both the designation and measurement guidance for qualifying hedging relationships and the presentation of hedge results. The FASB believes that such amendments will: 1) improve the transparency of information about an entity's risk management activities and 2) simplify the application of hedge accounting. The ASU allows an entity that qualifies for the last-of-layer method a one-time opportunity to reclassify securities from the held-to-maturity category to the available-for-sale category. The Company adopted ASU 2017-12 effective January 1, 2019 and transferred its entire held-to-maturity investment securities portfolio with a fair value of \$144.3 million at January 1, 2019 to the available-for-sale portfolio. On the date of adoption, the Company recorded a cumulative effect adjustment related to the unrealized loss on the investment securities transferred, which decreased available-for-sale investments by \$4.2 million, increased deferred tax assets by \$1.1 million, and decreased opening accumulated other comprehensive income (loss) ("AOCI") by \$3.1 million. The ASU did not have a material impact on our current derivative activities.

In August 2018, the FASB issued ASU 2018-15, *"Intangibles—Goodwill and Other— Internal-Use Software (Subtopic 350-40): Customer's Accounting for Implementation Costs Incurred in a Cloud Computing Arrangement That Is a Service Contract,"* which requires an entity in a cloud computing arrangement (i.e., hosting arrangement) that is a service contract to follow the internal-use software guidance in ASC 350-40 to determine which implementation costs to capitalize as assets or expense as incurred. Capitalized implementation costs should be presented in the same line item on the balance sheet as amounts prepaid for the hosted service, if any (generally as an "other asset"). The capitalized costs will be amortized over the term of the hosting arrangement, with the amortization expense being presented in the same income statement line item as the fees paid for the hosted service. ASU 2018-15 is effective for the Company's reporting period beginning January 1, 2020 and early adoption is permitted. The Company early adopted ASU 2018-15 during the second quarter of 2019. The adoption of the ASU did not have a material impact on our consolidated financial statements.

### **Impact of Other Recently Issued Accounting Pronouncements on Future Filings**

In June 2016, the FASB issued ASU 2016-13, *"Financial Instruments—Credit Losses (Topic 326): Measurement of Credit Losses on Financial Instruments,"* and subsequent amendments to the guidance, ASU 2019-04 in April 2019 and ASU 2019-05 in May 2019. The standard significantly changes how entities will measure credit losses for most financial assets and certain other instruments that aren't measured at fair value through net income. In issuing the standard, the FASB is responding to criticism that today's "incurred loss" guidance delays the recognition of credit losses on loans, leases, held-to-maturity debt securities, loan commitments, and financial guarantees, and instead provides for a current expected credit loss ("CECL") approach to determine the allowance for credit losses. CECL requires an organization to measure all expected credit losses for financial assets held at the reporting date based on historical experience, current conditions, and reasonable and supportable forecasts. In addition, this guidance modifies the accounting treatment for other-than-temporary impairment for available-for-sale debt securities. Organizations will continue to use judgment to determine which loss estimation methods are appropriate for their circumstances. This guidance requires entities to record a cumulative effect adjustment to the consolidated balance sheet as of the beginning of the first reporting period in which the guidance is effective. However, an organization may elect to phase in the regulatory capital impact over a three-year transition period if adoption of the new standard results in a reduction of retained earnings. This update is effective for fiscal years, and interim periods within those fiscal years, beginning after December 15, 2019, with earlier adoption permitted. As such, the Company will implement CECL for the reporting period beginning January 1, 2020. The new guidance will require significant operational changes, particularly in existing processes, data collection and analysis.

The Company has formed a steering committee that is responsible for oversight of the Company's implementation strategy for compliance with provisions of the new standard. The Company has also established a project management governance process to manage the implementation across affected disciplines. To date, the Company has established appropriate loan pools by segment and sub-segment, developed internal loss driver models, and has leveraged a third-party software solution to measure expected losses under CECL. As part of this process, the Company has also engaged an additional third party specializing in economic forecasting to enable it to incorporate reasonable and supportable forecasts in its process. Finally, the Company is developing and enhancing internal controls, having its CECL framework independently validated by a third-party expert, performing parallel runs, and addressing remaining gaps. While the Company is evaluating the full impact of adopting this new guidance, management expects that it will be significantly influenced by its own historical experience, the composition and quality of the Company's loans, the underlying assumptions embedded in its methodology, as well as economic condition expectations as of the date of adoption. The Company also anticipates significant changes to its reserve calculation processes

and procedures and continues to evaluate the potential impact on our consolidated financial statements through sensitivity analysis of underlying assumptions and economic scenarios.

In August 2018, the FASB issued ASU 2018-13, "*Fair Value Measurement (Topic 820): Disclosure Framework—Changes to the Disclosure Requirements for Fair Value Measurement.*" The ASU is part of the FASB's disclosure framework project to improve the effectiveness of disclosures in the notes to financial statements by facilitating clear communication of the information required by generally accepted accounting principles. The ASU modifies disclosure requirements on fair value measurements in Topic 820 and is effective for the Company's reporting period beginning January 1, 2020. Early adoption is permitted. Based on preliminary evaluation, the ASU will not have a material impact on disclosures in our consolidated financial statements.

In August 2018, the FASB issued ASU 2018-14, "*Compensation—Retirement Benefits—Defined Benefit Plans—General (Subtopic 715-20): Disclosure Framework—Changes to the Disclosure Requirements for Defined Benefit Plans.*" Like ASU 2018-13, this ASU is part of the FASB's disclosure framework project. This ASU modifies disclosure requirements for employers that sponsor defined benefit pension or other postretirement plans. The ASU is effective for the Company's reporting period beginning January 1, 2021. Early adoption is permitted. Based on preliminary evaluation, the ASU will not have a material impact on disclosures in our consolidated financial statements.

### 3. INVESTMENT SECURITIES

A summary of our available-for-sale investment securities is as follows:

(dollars in thousands)	Amortized Cost	Gross Unrealized Gains	Gross Unrealized Losses	Fair Value
<b>September 30, 2019</b>				
Available-for-sale:				
Debt securities:				
States and political subdivisions	\$ 122,171	\$ 2,593	\$ (53)	\$ 124,711
Corporate securities	30,436	277	—	30,713
U.S. Treasury obligations and direct obligations of U.S Government agencies	43,213	17	(333)	42,897
Mortgage-backed securities:				
Residential - U.S. Government-sponsored entities	721,081	5,796	(3,233)	723,644
Commercial - U.S. Government agencies and sponsored entities	86,697	1,431	(386)	87,742
Residential - Non-government agencies	38,140	969	—	39,109
Commercial - Non-government agencies	134,724	3,335	—	138,059
Total available-for-sale securities	<u>\$ 1,176,462</u>	<u>\$ 14,418</u>	<u>\$ (4,005)</u>	<u>\$ 1,186,875</u>

(dollars in thousands)	Amortized Cost	Gross Unrealized Gains	Gross Unrealized Losses	Fair Value
<b>December 31, 2018</b>				
Held-to-maturity:				
Mortgage-backed securities:				
Residential - U.S. Government-sponsored entities	\$ 83,436	\$ 19	\$ (3,174)	\$ 80,281
Commercial - U.S. Government-sponsored entities	65,072	—	(1,081)	63,991
Total held-to-maturity securities	<u>\$ 148,508</u>	<u>\$ 19</u>	<u>\$ (4,255)</u>	<u>\$ 144,272</u>
Available-for-sale:				
Debt securities:				
States and political subdivisions	\$ 174,114	\$ 1,035	\$ (1,475)	\$ 173,674
Corporate securities	55,259	—	(410)	54,849
U.S. Treasury obligations and direct obligations of U.S Government agencies	33,257	—	(683)	32,574
Mortgage-backed securities:				
Residential - U.S. Government-sponsored entities	736,175	369	(19,492)	717,052
Commercial - U.S. Government agencies and sponsored entities	53,014	—	(1,531)	51,483
Residential - Non-government agencies	41,245	337	(464)	41,118
Commercial - Non-government agencies	134,867	1,013	(1,152)	134,728
Total available-for-sale securities	<u>\$ 1,227,931</u>	<u>\$ 2,754</u>	<u>\$ (25,207)</u>	<u>\$ 1,205,478</u>

The amortized cost and fair value of our equity investment securities is as follows:

(dollars in thousands)	Amortized Cost	Fair Value
<b>September 30, 2019</b>		
Equity securities	\$ 898	\$ 1,058
<b>December 31, 2018</b>		
Equity securities	826	826

As discussed in Note 2 - Recent Accounting Pronouncements, on January 1, 2019 in connection with the adoption of ASU 2017-12, the Company transferred all of its held-to-maturity investment securities with an amortized cost of \$148.5 million and fair value of \$144.3 million to its available-for-sale investment securities portfolio.

The amortized cost and estimated fair value of our available-for-sale investment securities at September 30, 2019 by contractual maturity are shown below. Actual maturities may differ from contractual maturities because issuers may have the right to call or prepay obligations with or without call or prepayment penalties. Securities not due at a single maturity date are shown separately.

(dollars in thousands)	September 30, 2019	
	Amortized Cost	Fair Value
<b>Available-for-sale:</b>		
Due in one year or less	\$ 32,455	\$ 32,658
Due after one year through five years	60,696	61,195
Due after five years through ten years	63,661	64,715
Due after ten years	39,008	39,753
<b>Mortgage-backed securities:</b>		
Residential - U.S. Government-sponsored entities	721,081	723,644
Commercial - U.S. Government agencies and sponsored entities	86,697	87,742
Residential - Non-government agencies	38,140	39,109
Commercial - Non-government agencies	134,724	138,059
Total available-for-sale securities	\$ 1,176,462	\$ 1,186,875

For the three and nine months ended September 30, 2019, proceeds from the sale of available-for-sale investment securities were \$53.9 million and resulted in a gross realized gain of \$36 thousand. We did not sell any available-for-sale securities during the three and nine months ended September 30, 2018.

Investment securities of \$662.2 million and \$980.2 million at September 30, 2019 and December 31, 2018, respectively, were pledged to secure public funds on deposit and other short-term borrowings.

Provided below is a summary of the 98 and 336 investment securities which were in an unrealized or unrecognized loss position at September 30, 2019 and December 31, 2018, respectively, aggregated by major security type and length of time in a continuous unrealized or unrecognized loss position.

(dollars in thousands)	Less Than 12 Months		12 Months or Longer		Total	
	Fair Value	Unrealized Losses	Fair Value	Unrealized Losses	Fair Value	Unrealized Losses
<b>September 30, 2019</b>						
<b>Debt securities:</b>						
States and political subdivisions	\$ 7,007	\$ (26)	\$ 1,253	\$ (27)	\$ 8,260	\$ (53)
Corporate securities	—	—	—	—	—	—
U.S. Treasury obligations and direct obligations of U.S. Government agencies	16,815	(122)	20,507	(211)	37,322	(333)
<b>Mortgage-backed securities:</b>						
Residential - U.S. Government-sponsored entities	103,254	(631)	247,482	(2,602)	350,736	(3,233)
Residential - Non-government agencies	—	—	—	—	—	—
Commercial - U.S. Government agencies and sponsored entities	36,068	(386)	—	—	36,068	(386)
Commercial - Non-government agencies	—	—	—	—	—	—
Total temporarily impaired securities	\$ 163,144	\$ (1,165)	\$ 269,242	\$ (2,840)	\$ 432,386	\$ (4,005)

(dollars in thousands)	Less Than 12 Months		12 Months or Longer		Total	
	Fair Value	Unrealized Losses	Fair Value	Unrealized Losses	Fair Value	Unrealized Losses
<b>December 31, 2018</b>						
Debt securities:						
States and political subdivisions	\$ 38,099	\$ (157)	\$ 49,505	\$ (1,318)	\$ 87,604	\$ (1,475)
Corporate securities	49,729	(250)	5,120	(160)	54,849	(410)
U.S. Treasury obligations and direct obligations of U.S Government agencies	30,029	(613)	2,545	(70)	32,574	(683)
Mortgage-backed securities:						
Residential - U.S. Government-sponsored entities	88,957	(1,229)	666,685	(21,437)	755,642	(22,666)
Residential - Non-government agencies	—	—	24,515	(464)	24,515	(464)
Commercial - U.S. Government-sponsored entities	13,973	(247)	101,500	(2,365)	115,473	(2,612)
Commercial - Non-government agencies	33,847	(233)	46,680	(919)	80,527	(1,152)
Total temporarily impaired securities	<u>\$ 254,634</u>	<u>\$ (2,729)</u>	<u>\$ 896,550</u>	<u>\$ (26,733)</u>	<u>\$ 1,151,184</u>	<u>\$ (29,462)</u>

#### Visa and MasterCard Class B Common Stock

As of September 30, 2019, the Company owns 34,631 shares of Class B common stock of Visa, Inc. ("Visa"). These shares were received in 2008 as part of Visa's initial public offering ("IPO"). These shares are transferable only under limited circumstances until they can be converted into shares of the publicly traded Class A common stock. This conversion will not occur until the resolution of certain litigation, which is indemnified by Visa members. Since its IPO, Visa has funded a litigation reserve to settle these litigation claims. At its discretion, Visa may continue to increase the litigation reserve based upon a change in the conversion ratio of each member bank's restricted Class B common stock to unrestricted Class A common stock. Due to the existing transfer restriction and the uncertainty of the outcome of the Visa litigation, the Company has determined that the Visa Class B common stock does not have a readily determinable fair value and chooses to carry the shares on the Company's consolidated balance sheets at zero cost basis.

During the first quarter of 2019, the Company converted the 11,170 shares of Class B common stock of MasterCard, Inc. ("MasterCard") it received during their initial public offering to an equal number of Class A common stock and sold the shares for \$2.6 million. The shares were carried on the Company's consolidated balance sheets at zero cost basis and the proceeds received were recorded as a gain in other operating income - other in the Company's consolidated statements of income. The Company no longer owns any shares of MasterCard Class B common stock.

#### 4. LOANS AND LEASES

Loans and leases, excluding loans held for sale, consisted of the following as of September 30, 2019 and December 31, 2018:

(dollars in thousands)	September 30, 2019	December 31, 2018
Commercial, financial and agricultural	\$ 576,343	\$ 581,177
Real estate:		
Construction	96,996	67,269
Residential mortgage	1,554,752	1,424,384
Home equity	475,211	468,966
Commercial mortgage	1,135,408	1,041,685
Consumer	526,429	492,268
Leases	31	124
Gross loans and leases	<u>4,365,170</u>	<u>4,075,873</u>
Net deferred costs	2,692	2,493
Total loans and leases, net of deferred costs	<u>\$ 4,367,862</u>	<u>\$ 4,078,366</u>

During the nine months ended September 30, 2019, we foreclosed on one loan totaling \$0.2 million.

During the nine months ended September 30, 2018, we foreclosed on one loan totaling \$40 thousand.

During the nine months ended September 30, 2019 and 2018, we did not transfer any loans to the held-for-sale category.

We did not sell any portfolio loans during the nine months ended September 30, 2019 and 2018.

Through the third quarter of 2019, we purchased consumer loans with outstanding balances at the time of purchases totaling \$80.0 million for \$78.8 million, or a net discount of \$1.2 million.

In 2018, we purchased consumer loans totaling \$58.6 million, which included a \$0.1 million premium over the \$58.5 million outstanding balance at the time of purchase.

### Impaired Loans

The following tables present by class, the balance in the allowance for loan and lease losses (the "Allowance") and the recorded investment in loans and leases based on the Company's impairment measurement method as of September 30, 2019 and December 31, 2018:

(dollars in thousands)	Comml, Fin & Ag	Real Estate			Comml Mortgage	Consumer	Leases	Total
		Constr	Resi Mortgage	Home Equity				
<b>September 30, 2019</b>								
Allowance:								
Individually evaluated for impairment	\$ —	\$ —	\$ —	\$ —	\$ —	\$ —	\$ —	\$ —
Collectively evaluated for impairment	7,781	1,693	13,546	4,287	12,209	8,651	—	48,167
Total ending balance	<u>\$ 7,781</u>	<u>\$ 1,693</u>	<u>\$ 13,546</u>	<u>\$ 4,287</u>	<u>\$ 12,209</u>	<u>\$ 8,651</u>	<u>\$ —</u>	<u>\$ 48,167</u>
Loans and leases:								
Individually evaluated for impairment	\$ 157	\$ —	\$ 7,516	\$ 95	\$ 1,985	\$ —	\$ —	\$ 9,753
Collectively evaluated for impairment	576,186	96,996	1,547,236	475,116	1,133,423	526,429	31	4,355,417
Subtotal	576,343	96,996	1,554,752	475,211	1,135,408	526,429	31	4,365,170
Net deferred costs (income)	269	(335)	3,983	354	(1,496)	(83)	—	2,692
Total loans and leases, net of deferred costs (income)	<u>\$ 576,612</u>	<u>\$ 96,661</u>	<u>\$ 1,558,735</u>	<u>\$ 475,565</u>	<u>\$ 1,133,912</u>	<u>\$ 526,346</u>	<u>\$ 31</u>	<u>\$ 4,367,862</u>

(dollars in thousands)	Comml, Fin & Ag	Real Estate			Comml Mortgage	Consumer	Leases	Total
		Constr	Resi Mortgage	Home Equity				
<b>December 31, 2018</b>								
Allowance:								
Individually evaluated for impairment	\$ —	\$ —	\$ —	\$ —	\$ —	\$ —	\$ —	\$ —
Collectively evaluated for impairment	8,027	1,202	14,349	3,788	13,358	7,192	—	47,916
Total ending balance	<u>\$ 8,027</u>	<u>\$ 1,202</u>	<u>\$ 14,349</u>	<u>\$ 3,788</u>	<u>\$ 13,358</u>	<u>\$ 7,192</u>	<u>\$ —</u>	<u>\$ 47,916</u>
Loans and leases:								
Individually evaluated for impairment	\$ 220	\$ 2,273	\$ 10,075	\$ 275	\$ 2,348	\$ —	\$ —	\$ 15,191
Collectively evaluated for impairment	580,957	64,996	1,414,309	468,691	1,039,337	492,268	124	4,060,682
Subtotal	581,177	67,269	1,424,384	468,966	1,041,685	492,268	124	4,075,873
Net deferred costs (income)	483	(342)	3,821	—	(1,407)	(62)	—	2,493
Total loans and leases, net of deferred costs (income)	<u>\$ 581,660</u>	<u>\$ 66,927</u>	<u>\$ 1,428,205</u>	<u>\$ 468,966</u>	<u>\$ 1,040,278</u>	<u>\$ 492,206</u>	<u>\$ 124</u>	<u>\$ 4,078,366</u>

There were no impaired loans with an allowance recorded as of September 30, 2019 and December 31, 2018. The following table presents by class, information related to impaired loans as of September 30, 2019 and December 31, 2018:

(dollars in thousands)	September 30, 2019			December 31, 2018		
	Unpaid Principal Balance	Recorded Investment	Allowance Allocated	Unpaid Principal Balance	Recorded Investment	Allowance Allocated
<b>Impaired loans:</b>						
Commercial, financial and agricultural	\$ 267	\$ 157	\$ —	\$ 330	\$ 220	\$ —
<b>Real estate:</b>						
Construction	—	—	—	3,076	2,273	—
Residential mortgage	8,239	7,516	—	11,019	10,075	—
Home equity	95	95	—	275	275	—
Commercial mortgage	1,985	1,985	—	2,348	2,348	—
<b>Total impaired loans</b>	<b>\$ 10,586</b>	<b>\$ 9,753</b>	<b>\$ —</b>	<b>\$ 17,048</b>	<b>\$ 15,191</b>	<b>\$ —</b>

The following table presents by class, the average recorded investment and interest income recognized on impaired loans for the three and nine months ended September 30, 2019 and 2018:

(dollars in thousands)	Three Months Ended				Nine Months Ended			
	September 30, 2019		September 30, 2018		September 30, 2019		September 30, 2018	
	Average Recorded Investment	Interest Income Recognized						
Commercial, financial and agricultural	\$ 164	\$ 2	\$ 399	\$ 12	\$ 188	\$ 7	\$ 498	\$ 17
<b>Real estate:</b>								
Construction	—	—	2,382	30	1,323	62	2,476	84
Residential mortgage	7,536	63	12,857	123	8,763	776	13,208	419
Home equity	190	—	447	—	332	13	516	—
Commercial mortgage	2,021	22	3,483	36	2,162	68	3,653	110
<b>Total</b>	<b>\$ 9,911</b>	<b>\$ 87</b>	<b>\$ 19,568</b>	<b>\$ 201</b>	<b>\$ 12,768</b>	<b>\$ 926</b>	<b>\$ 20,351</b>	<b>\$ 630</b>

For the three and nine months ended September 30, 2019 and 2018, the amount of interest income recognized on impaired loans within the period that the loans were impaired were primarily related to loans modified in a troubled debt restructuring ("TDR") that were on accrual status. For the three and nine months ended September 30, 2019 and 2018, the amount of interest income recognized using a cash-based method of accounting during the period that the loans were impaired was not material.

#### Foreclosure Proceedings

The Company had \$0.3 million and \$0.7 million of residential mortgage loans collateralized by residential real estate property that were in the process of foreclosure at September 30, 2019 and December 31, 2018, respectively.

## Aging Analysis of Accruing and Non-Accruing Loans and Leases

For all loan types, the Company determines delinquency status by considering the number of days full payments required by the contractual terms of the loan are past due. The following tables present by class, the aging of the recorded investment in past due loans and leases as of September 30, 2019 and December 31, 2018:

(dollars in thousands)	Accruing Loans 30 - 59 Days Past Due	Accruing Loans 60 - 89 Days Past Due	Accruing Loans Greater Than 90 Days Past Due	Nonaccrual Loans	Total Past Due and Nonaccrual	Loans and Leases Not Past Due	Total
<b>September 30, 2019</b>							
Commercial, financial and agricultural	\$ 5,845	\$ 87	\$ —	\$ —	\$ 5,932	\$ 570,680	\$ 576,612
Real estate:							
Construction	—	—	—	—	—	96,661	96,661
Residential mortgage	—	2,327	—	799	3,126	1,555,609	1,558,735
Home equity	320	250	—	95	665	474,900	475,565
Commercial mortgage	—	—	—	—	—	1,133,912	1,133,912
Consumer	2,974	1,296	235	—	4,505	521,841	526,346
Leases	—	—	—	—	—	31	31
Total	\$ 9,139	\$ 3,960	\$ 235	\$ 894	\$ 14,228	\$ 4,353,634	\$ 4,367,862

(dollars in thousands)	Accruing Loans 30 - 59 Days Past Due	Accruing Loans 60 - 89 Days Past Due	Accruing Loans Greater Than 90 Days Past Due	Nonaccrual Loans	Total Past Due and Nonaccrual	Loans and Leases Not Past Due	Total
<b>December 31, 2018</b>							
Commercial, financial and agricultural	\$ 1,348	\$ 162	\$ —	\$ —	\$ 1,510	\$ 580,150	\$ 581,660
Real estate:							
Construction	—	—	—	—	—	66,927	66,927
Residential mortgage	3,966	157	—	2,048	6,171	1,422,034	1,428,205
Home equity	433	104	298	275	1,110	467,856	468,966
Commercial mortgage	—	—	—	—	—	1,040,278	1,040,278
Consumer	2,340	872	238	—	3,450	488,756	492,206
Leases	—	—	—	—	—	124	124
Total	\$ 8,087	\$ 1,295	\$ 536	\$ 2,323	\$ 12,241	\$ 4,066,125	\$ 4,078,366

## Modifications

Troubled debt restructurings ("TDRs") included in nonperforming assets at September 30, 2019 consisted of one Hawaii residential mortgage loan with a principal balance of \$0.3 million.

Concessions made to the original contractual terms of these loans consisted primarily of the deferral of interest and/or principal payments due to deterioration in the borrowers' financial condition. The principal balances on these TDRs had matured and/or were in default at the time of restructure, and we have no commitments to lend additional funds to any of these borrowers. There were \$8.9 million of TDRs still accruing interest at September 30, 2019, none of which were more than 90 days delinquent. At December 31, 2018, there were \$12.9 million of TDRs still accruing interest, none of which were more than 90 days delinquent.

Some loans modified in a TDR may already be on nonaccrual status and partial charge-offs may have already been taken against the outstanding loan balance. Thus, these loans have already been identified as impaired and have already been evaluated under the Company's allowance for loan and lease losses (the "Allowance") methodology. Loans that were not on nonaccrual status when modified in a TDR may have the financial effect of increasing the specific allowance associated with the loan. The loans modified in a TDR did not have a material effect on our provision for loan and lease losses (the "Provision") and the Allowance during the three and nine months ended September 30, 2019.

No loans were modified in a TDR during the three and nine months ended September 30, 2019 and 2018.

No loans were modified as a TDR within the previous twelve months that subsequently defaulted during the three and nine months ended September 30, 2019 and 2018.

We had no commitments on TDRs during the three and nine months ended September 30, 2019 and 2018.

### Credit Quality Indicators

The Company categorizes loans and leases into risk categories based on relevant information about the ability of borrowers to service their debt such as: current financial information, historical payment experience, credit documentation, public information, and current economic trends, among other factors. The Company analyzes loans and leases individually by classifying the loans and leases by credit risk. This analysis includes non-homogeneous loans and leases, such as commercial and commercial real estate loans. This analysis is performed on a quarterly basis. The Company uses the following definitions for risk ratings:

**Special Mention.** Loans and leases classified as special mention, while still adequately protected by the borrower's capital adequacy and payment capability, exhibit distinct weakening trends and/or elevated levels of exposure to external conditions. If left unchecked or uncorrected, these potential weaknesses may result in deteriorated prospects of repayment. These exposures require management's close attention so as to avoid becoming undue or unwarranted credit exposures.

**Substandard.** Loans and leases classified as substandard are inadequately protected by the borrower's current financial condition and payment capability or of the collateral pledged, if any. Loans and leases so classified have a well-defined weakness or weaknesses that jeopardize the orderly repayment of debt. They are characterized by the distinct possibility that the bank will sustain some loss if the deficiencies are not corrected.

**Doubtful.** Loans and leases classified as doubtful have all the weaknesses inherent in those classified as substandard, with the added characteristic that the weaknesses make collection or orderly repayment in full, on the basis of current existing facts, conditions and values, highly questionable and improbable. Possibility of loss is extremely high, but because of certain important and reasonably specific factors that may work to the advantage and strengthening of the exposure, its classification as an estimated loss is deferred until its more exact status may be determined.

**Loss.** Loans and leases classified as loss are considered to be non-collectible and of such little value that their continuance as bankable assets is not warranted. This does not mean the loan has absolutely no recovery value, but rather it is neither practical nor desirable to defer writing off the loan, even though partial recovery may be obtained in the future. Losses are taken in the period in which they surface as uncollectible.

Loans and leases not meeting the criteria above are considered to be pass-rated. The following table presents by class and credit indicator, the recorded investment in the Company's loans and leases as of September 30, 2019 and December 31, 2018:

(dollars in thousands)	Pass	Special Mention	Substandard	Loss	Subtotal	Net Deferred Costs (Income)	Total
<b>September 30, 2019</b>							
Commercial, financial and agricultural	\$ 561,372	\$ 3,318	\$ 11,653	\$ —	\$ 576,343	\$ 269	\$ 576,612
Real estate:							
Construction	96,996	—	—	—	96,996	(335)	96,661
Residential mortgage	1,553,869	—	883	—	1,554,752	3,983	1,558,735
Home equity	475,116	—	95	—	475,211	354	475,565
Commercial mortgage	1,096,341	25,757	13,310	—	1,135,408	(1,496)	1,133,912
Consumer	526,193	—	149	87	526,429	(83)	526,346
Leases	31	—	—	—	31	—	31
Total	<u>\$ 4,309,918</u>	<u>\$ 29,075</u>	<u>\$ 26,090</u>	<u>\$ 87</u>	<u>\$ 4,365,170</u>	<u>\$ 2,692</u>	<u>\$ 4,367,862</u>

(dollars in thousands)	<u>Pass</u>	<u>Special Mention</u>	<u>Substandard</u>	<u>Loss</u>	<u>Subtotal</u>	<u>Net Deferred Costs (Income)</u>	<u>Total</u>
<b>December 31, 2018</b>							
Commercial, financial and agricultural	\$ 552,706	\$ 7,961	\$ 20,510	\$ —	\$ 581,177	\$ 483	\$ 581,660
Real estate:							
Construction	67,269	—	—	—	67,269	(342)	66,927
Residential mortgage	1,422,240	—	2,144	—	1,424,384	3,821	1,428,205
Home equity	468,394	—	572	—	468,966	—	468,966
Commercial mortgage	1,029,581	10,412	1,692	—	1,041,685	(1,407)	1,040,278
Consumer	492,030	—	80	158	492,268	(62)	492,206
Leases	124	—	—	—	124	—	124
Total	<u>\$ 4,032,344</u>	<u>\$ 18,373</u>	<u>\$ 24,998</u>	<u>\$ 158</u>	<u>\$ 4,075,873</u>	<u>\$ 2,493</u>	<u>\$ 4,078,366</u>

## 5. ALLOWANCE FOR LOAN AND LEASE LOSSES

The following table presents by class, the activity in the Allowance for the periods indicated:

(dollars in thousands)	Commercial, Financial & Agricultural	Real Estate					Consumer	Leases	Total
		Construction	Residential Mortgage	Home Equity	Commercial Mortgage				
<b>Three Months Ended September 30, 2019</b>									
Beginning balance	\$ 8,109	\$ 1,313	\$ 13,367	\$ 4,313	\$ 11,668	\$ 9,497	\$ —	\$ 48,267	
Provision (credit) for loan and lease losses	107	374	75	(45)	541	480	—	1,532	
	8,216	1,687	13,442	4,268	12,209	9,977	—	49,799	
Charge-offs	797	—	—	5	—	1,832	—	2,634	
Recoveries	362	6	104	24	—	506	—	1,002	
Net charge-offs (recoveries)	435	(6)	(104)	(19)	—	1,326	—	1,632	
Ending balance	\$ 7,781	\$ 1,693	\$ 13,546	\$ 4,287	\$ 12,209	\$ 8,651	\$ —	\$ 48,167	
<b>Three Months Ended September 30, 2018</b>									
Beginning balance	\$ 7,525	\$ 1,811	\$ 14,252	\$ 3,168	\$ 15,094	\$ 6,331	\$ —	\$ 48,181	
Provision (credit) for loan and lease losses	495	(526)	(168)	544	(1,632)	1,228	—	(59)	
	8,020	1,285	14,084	3,712	13,462	7,559	—	48,122	
Charge-offs	731	—	—	—	—	1,762	—	2,493	
Recoveries	578	6	51	6	8	548	—	1,197	
Net charge-offs (recoveries)	153	(6)	(51)	(6)	(8)	1,214	—	1,296	
Ending balance	\$ 7,867	\$ 1,291	\$ 14,135	\$ 3,718	\$ 13,470	\$ 6,345	\$ —	\$ 46,826	

(dollars in thousands)	Commercial, Financial & Agricultural	Real Estate					Consumer	Leases	Total
		Construction	Residential Mortgage	Home Equity	Commercial Mortgage				
<b>Nine Months Ended September 30, 2019</b>									
Beginning balance	\$ 8,027	\$ 1,202	\$ 14,349	\$ 3,788	\$ 13,358	\$ 7,192	\$ —	\$ 47,916	
Provision (credit) for loan and lease losses	943	(113)	(1,301)	462	(1,174)	5,402	—	4,219	
	8,970	1,089	13,048	4,250	12,184	12,594	—	52,135	
Charge-offs	2,099	—	—	5	—	5,542	—	7,646	
Recoveries	910	604	498	42	25	1,599	—	3,678	
Net charge-offs (recoveries)	1,189	(604)	(498)	(37)	(25)	3,943	—	3,968	
Ending balance	\$ 7,781	\$ 1,693	\$ 13,546	\$ 4,287	\$ 12,209	\$ 8,651	\$ —	\$ 48,167	
<b>Nine Months Ended September 30, 2018</b>									
Beginning balance	\$ 7,594	\$ 1,835	\$ 14,328	\$ 3,317	\$ 16,801	\$ 6,126	\$ —	\$ 50,001	
Provision (credit) for loan and lease losses	1,227	(1,749)	(291)	383	(3,383)	4,075	—	262	
	8,821	86	14,037	3,700	13,418	10,201	—	50,263	
Charge-offs	1,971	—	—	—	—	5,424	—	7,395	
Recoveries	1,017	1,205	98	18	52	1,568	—	3,958	
Net charge-offs (recoveries)	954	(1,205)	(98)	(18)	(52)	3,856	—	3,437	
Ending balance	\$ 7,867	\$ 1,291	\$ 14,135	\$ 3,718	\$ 13,470	\$ 6,345	\$ —	\$ 46,826	

In accordance with GAAP, loans held for sale and other real estate assets are not included in our assessment of the Allowance.

Our Provision was a debit of \$1.5 million and a debit of \$4.2 million in the three and nine months ended September 30, 2019, respectively, compared to a credit of \$0.1 million and a debit of \$0.3 million in the three and nine months ended September 30, 2018, respectively.

## 6. INVESTMENTS IN UNCONSOLIDATED SUBSIDIARIES

The components of the Company's investments in unconsolidated subsidiaries were as follows:

(dollars in thousands)	September 30, 2019	December 31, 2018
Investments in low income housing tax credit partnerships	\$ 15,228	\$ 11,603
Investments in common securities of statutory trusts	1,547	2,169
Investments in affiliates	172	182
Other	54	54
<b>Total</b>	<b>\$ 17,001</b>	<b>\$ 14,008</b>

The Company invests in low-income housing tax credit ("LIHTC") partnerships. As of September 30, 2019 and December 31, 2018, the Company had \$11.7 million and \$8.3 million, respectively, in unfunded commitments related to the LIHTC partnerships. The expected payments for the unfunded commitments as of September 30, 2019 for the remainder of fiscal year 2019, the next five succeeding fiscal years and all years thereafter are as follows (dollars in thousands):

Year Ending December 31,	
2019 (remainder)	\$ 3,669
2020	3,466
2021	1,494
2022	3,010
2023	10
2024	26
Thereafter	49
<b>Total unfunded commitments</b>	<b>\$ 11,724</b>

Prior to 2018, the Company's investments in LIHTC partnerships were accounted for using the cost method. In 2018, the Company voluntarily changed its accounting policy for LIHTC partnerships from the cost method to the proportional amortization method using the practical expedient available under ASC 323, *"Investments - Equity Method and Joint Ventures"*, which permits an investor to amortize the initial cost of the investment in proportion to only the tax credits allocated to the investor. The Company believes the proportional amortization method is preferable because it better reflects the economics of an investment that is made for the primary purpose of receiving tax credits and other tax benefits. In addition to a change in the timing of the recognition of amortization expense on LIHTC investments, amortization expense on LIHTC investments is now reflected in the income tax expense line, which provides users a better understanding of the nature of the returns of such investments, instead of in other operating expenses on the consolidated statements of income.

The following table presents amortization and tax credits recognized associated with our investments in LIHTC partnerships for the three and nine months ended September 30, 2019 and September 30, 2018:

(dollars in thousands)	Three Months Ended September 30, 2019	Three Months Ended September 30, 2018	Nine Months Ended September 30, 2019	Nine Months Ended September 30, 2018
Proportional amortization method:				
Amortization expense recognized in income tax expense	\$ 259	\$ 114	\$ 776	\$ 341
Tax credits recognized in income tax expense	307	152	922	457

## 7. CORE DEPOSIT PREMIUM AND MORTGAGE SERVICING RIGHTS

The following table presents changes in core deposit premium and mortgage servicing rights for the periods presented:

(dollars in thousands)	<b>Core Deposit Premium</b>	<b>Mortgage Servicing Rights</b>	<b>Total</b>
Balance, January 1, 2018	\$ 2,006	\$ 15,843	\$ 17,849
Additions	—	1,204	1,204
Amortization	(2,006)	(1,413)	(3,419)
Balance, September 30, 2018	<u>\$ —</u>	<u>\$ 15,634</u>	<u>\$ 15,634</u>
Balance, January 1, 2019	\$ —	\$ 15,596	\$ 15,596
Additions	—	1,189	1,189
Amortization	—	(1,727)	(1,727)
Balance, September 30, 2019	<u>\$ —</u>	<u>\$ 15,058</u>	<u>\$ 15,058</u>

Income generated as the result of new mortgage servicing rights is reported as gains on sales of loans and totaled \$0.4 million and \$1.2 million for the three and nine months ended September 30, 2019, respectively, compared to \$0.4 million and \$1.2 million for the three and nine months ended September 30, 2018, respectively.

Amortization of mortgage servicing rights totaled \$0.7 million and \$1.7 million for the three and nine months ended September 30, 2019, respectively, compared to \$0.5 million and \$1.4 million for the three and nine months ended September 30, 2018, respectively.

The following table presents the fair market value and key assumptions used in determining the fair market value of our mortgage servicing rights:

(dollars in thousands)	<b>Nine Months Ended September 30, 2019</b>	<b>Nine Months Ended September 30, 2018</b>
Fair market value, beginning of period	\$ 17,696	\$ 17,161
Fair market value, end of period	15,965	18,315
Weighted average discount rate	9.5%	9.5%
Forecasted constant prepayment rate assumption <sup>(1)</sup>	14.6	14.0

<sup>(1)</sup> Represents annualized loan prepayment rate assumption.

The gross carrying value and accumulated amortization related to our core deposit premium and mortgage servicing rights are presented below:

(dollars in thousands)	<b>September 30, 2019</b>			<b>December 31, 2018</b>		
	<b>Gross Carrying Value</b>	<b>Accumulated Amortization</b>	<b>Net Carrying Value</b>	<b>Gross Carrying Value</b>	<b>Accumulated Amortization</b>	<b>Net Carrying Value</b>
Core deposit premium	\$ 44,642	\$ (44,642)	\$ —	\$ 44,642	\$ (44,642)	\$ —
Mortgage servicing rights	67,202	(52,144)	15,058	66,013	(50,417)	15,596
Total	<u>\$ 111,844</u>	<u>\$ (96,786)</u>	<u>\$ 15,058</u>	<u>\$ 110,655</u>	<u>\$ (95,059)</u>	<u>\$ 15,596</u>

Based on the mortgage servicing rights held as of September 30, 2019, estimated amortization expense for the remainder of fiscal year 2019, the next five succeeding fiscal years and all years thereafter are as follows (dollars in thousands):

<b>Year Ending December 31,</b>			
2019 (remainder)		\$	669
2020			2,373
2021			1,918
2022			1,585
2023			1,319
2024			1,118
Thereafter			6,076
Total		\$	<u>15,058</u>

We perform an impairment assessment of our mortgage servicing rights whenever events or changes in circumstance indicate that the carrying value of the asset may not be recoverable.

## 8. DERIVATIVES

We utilize various designated and undesignated derivative financial instruments to reduce our exposure to movements in interest rates including interest rate lock commitments and forward sale commitments. We measure all derivatives at fair value on our consolidated balance sheet. In each reporting period, we record the derivative instruments in other assets or other liabilities depending on whether the derivatives are in an asset or liability position. For derivative instruments that are designated as cash flow hedging instruments, we record the effective portion of the changes in the fair value of the derivative in AOCI, net of tax, until earnings are affected by the variability of cash flows of the hedged transaction. We immediately recognize the portion of the gain or loss in the fair value of the derivative that represents hedge ineffectiveness in current period earnings. For derivative instruments that are not designated as hedging instruments, changes in the fair value of the derivative are included in current period earnings. At September 30, 2019 and December 31, 2018, we were not party to any derivatives designated as part of a fair value or cash flow hedge.

### Interest Rate Lock and Forward Sale Commitments

We enter into interest rate lock commitments on certain mortgage loans that are intended to be sold. To manage interest rate risk on interest rate lock commitments, we also enter into forward loan sale commitments. The interest rate locks and forward loan sale commitments are accounted for as undesignated derivatives and are recorded at their respective fair values in other assets or other liabilities, with changes in fair value recorded in current period earnings. These instruments serve to reduce our exposure to movements in interest rates. At September 30, 2019, we were a party to interest rate lock and forward sale commitments on \$1.6 million and \$8.4 million of mortgage loans, respectively.

The following table presents the location of all assets and liabilities associated with our derivative instruments within the consolidated balance sheets:

Derivatives Financial Instruments Not Designated as Hedging Instruments	Balance Sheet Location	Asset Derivatives		Liability Derivatives	
		Fair Value at		Fair Value at	
		September 30, 2019	December 31, 2018	September 30, 2019	December 31, 2018
(dollars in thousands)					
Interest rate lock and forward sale commitments	Other assets / other liabilities	\$ 49	\$ 11	\$ 3	\$ 95

The following table presents the impact of derivative instruments and their location within the consolidated statements of income:

Derivatives Financial Instruments Not Designated as Hedging Instruments (dollars in thousands)	Location of Gain (Loss) Recognized in Earnings on Derivatives	Amount of Gain (Loss) Recognized in Earnings on Derivatives
<b>Three Months Ended September 30, 2019</b>		
Interest rate lock and forward sale commitments	Mortgage banking income	\$ 110
Loans held for sale	Other income	(1)
<b>Three Months Ended September 30, 2018</b>		
Interest rate lock and forward sale commitments	Mortgage banking income	91
Loans held for sale	Other income	(6)
<b>Nine Months Ended September 30, 2019</b>		
Interest rate lock and forward sale commitments	Mortgage banking income	131
Loans held for sale	Other income	(1)
<b>Nine Months Ended September 30, 2018</b>		
Interest rate lock and forward sale commitments	Mortgage banking income	76
Loans held for sale	Other income	(6)

## 9. SHORT-TERM BORROWINGS AND LONG-TERM DEBT

### Federal Home Loan Bank Advances and Other Borrowings

The bank is a member of the Federal Home Loan Bank of Des Moines (the "FHLB") and maintained a \$1.80 billion line of credit as of September 30, 2019, compared to \$1.43 billion at December 31, 2018. At September 30, 2019, \$1.43 billion was undrawn under this arrangement, compared to \$1.18 billion at December 31, 2018. Short-term borrowings under this arrangement totaled \$205.0 million at September 30, 2019, compared to \$197.0 million at December 31, 2018. Letters of credit under this arrangement that are used to collateralize certain government deposits totaled \$118.9 million at September 30, 2019, compared to \$4.6 million at December 31, 2018. Long-term borrowings under this arrangement totaled \$50.0 million at September 30, 2019 and December 31, 2018. FHLB advances and standby letters of credit available at September 30, 2019 were secured by certain real estate loans with a carrying value of \$2.42 billion in accordance with the collateral provisions of the Advances, Security and Deposit Agreement with the FHLB.

At September 30, 2019 and December 31, 2018, our bank had additional unused borrowings available at the Federal Reserve discount window of \$65.6 million and \$73.9 million, respectively. As of September 30, 2019 and December 31, 2018, certain commercial and commercial real estate loans with a carrying value totaling \$118.9 million and \$123.3 million, respectively, were pledged as collateral on our line of credit with the Federal Reserve discount window. The Federal Reserve does not have the right to sell or repledge these loans.

### Subordinated Debentures

In October 2003, we created two wholly-owned statutory trusts, CPB Capital Trust II ("Trust II") and CPB Statutory Trust III ("Trust III"). Trust II issued \$20.0 million in floating rate trust preferred securities bearing an interest rate of three-month LIBOR plus 2.85% and maturing on October 7, 2033. The principal assets of Trust II were \$20.6 million of the Company's junior subordinated debentures with an identical interest rate and maturity as the Trust II trust preferred securities. Trust II issued \$0.6 million of common securities to the Company.

On January 7, 2019, the Company completed the redemption of \$20.0 million in floating rate trust preferred securities of Trust II. The redemption price was 100% of the aggregate liquidation amount of the securities plus accumulated but unpaid distributions up to but not including the redemption date. The Company also redeemed \$0.6 million of common securities issued by Trust II and held by the Company, as a result of the concurrent redemption of 100% of the principal assets of Trust II, or \$20.6 million of the Company's junior subordinated debentures with an identical interest rate and maturity as the Trust II

trust preferred securities. The redemption was pursuant to the optional prepayment provisions of the indenture. On January 22, 2019, Trust II was canceled with the state of Delaware.

Trust III issued \$20.0 million in floating rate trust preferred securities bearing an interest rate of three-month LIBOR plus 2.85% and maturing on December 17, 2033. The principal assets of Trust III were \$20.6 million of the Company's junior subordinated debentures with an identical interest rate and maturity as the Trust III trust preferred securities. Trust III issued \$0.6 million of common securities to the Company.

On December 17, 2018, the Company completed the redemption of \$20.0 million in floating rate trust preferred securities of Trust III. The redemption price was 100% of the aggregate liquidation amount of the securities plus accumulated but unpaid distributions up to but not including the redemption date. The Company also redeemed \$0.6 million of common securities issued by Trust III and held by the Company, as a result of the concurrent redemption of 100% of the principal assets of Trust III, or \$20.6 million of the Company's junior subordinated debentures with an identical interest rate and maturity as the Trust III trust preferred securities. The redemption was pursuant to the optional prepayment provisions of the indenture. On January 9, 2019, Trust III was canceled with the state of Connecticut.

In September 2004, we created a wholly-owned statutory trust, CPB Capital Trust IV ("Trust IV"). Trust IV issued \$30.0 million in floating rate trust preferred securities bearing an interest rate of three-month LIBOR plus 2.45% and maturing on December 15, 2034. The principal assets of Trust IV are \$30.9 million of the Company's junior subordinated debentures with an identical interest rate and maturity as the Trust IV trust preferred securities. Trust IV issued \$0.9 million of common securities to the Company.

In December 2004, we created a wholly-owned statutory trust, CPB Statutory Trust V ("Trust V"). Trust V issued \$20.0 million in floating rate trust preferred securities bearing an interest rate of three-month LIBOR plus 1.87% and maturing on December 15, 2034. The principal assets of Trust V are \$20.6 million of the Company's junior subordinated debentures with an identical interest rate and maturity as the Trust V trust preferred securities. Trust V issued \$0.6 million of common securities to the Company.

At September 30, 2019 and December 31, 2018, the Company had the following junior subordinated debentures outstanding, which is recorded in long-term debt on the Company's consolidated balance sheets:

(dollars in thousands)

Name of Trust	September 30, 2019	
	Amount of Subordinated Debentures	Interest Rate
Trust IV	\$ 30,928	Three month LIBOR + 2.45%
Trust V	20,619	Three month LIBOR + 1.87%
Total	<u>\$ 51,547</u>	

Name of Trust	December 31, 2018	
	Amount of Subordinated Debentures	Interest Rate
Trust II	\$ 20,619	Three month LIBOR + 2.85%
Trust IV	30,928	Three month LIBOR + 2.45%
Trust V	20,619	Three month LIBOR + 1.87%
Total	<u>\$ 72,166</u>	

The floating trust preferred securities, the junior subordinated debentures that are the assets of Trusts IV and V and the common securities issued by Trusts IV and V are redeemable in whole or in part on any interest payment date on or after December 15, 2009 for Trust IV and V, or at any time in whole but not in part within 90 days following the occurrence of certain events. Our obligations with respect to the issuance of the trust preferred securities constitute a full and unconditional guarantee by the Company of each trust's obligations with respect to its trust preferred securities. Subject to certain exceptions and limitations, we may elect from time to time to defer interest payments on the subordinated debentures, which would result in a deferral of

distribution payments on the related trust preferred securities, for up to 20 consecutive quarterly periods without default or penalty.

The subordinated debentures may be included in Tier 1 capital, with certain limitations applicable, under current regulatory guidelines and interpretations.

## 10. REVENUE FROM CONTRACTS WITH CUSTOMERS

The following presents the Company's other operating income, segregated by revenue streams that are in-scope and out-of-scope of ASC 606, "Revenue from Contracts with Customers" for the three and nine months ended September 30, 2019 and 2018.

(dollars in thousands)	Three Months Ended September 30,		Nine Months Ended September 30,	
	2019	2018	2019	2018
Other operating income:				
In-scope of ASC 606				
Service charges on deposit accounts	\$ 2,125	\$ 2,189	\$ 6,247	\$ 6,169
Other service charges and fees	3,260	2,778	9,021	8,169
Income on fiduciary activities	1,126	1,159	3,220	3,132
Fees on foreign exchange	21	26	75	86
Loan placement fees	230	115	486	532
Net gain on sales of foreclosed assets	17	—	17	—
In-scope other operating income	6,779	6,267	19,066	18,088
Out-of-scope other operating income	3,487	4,553	12,967	11,316
Total other operating income	\$ 10,266	\$ 10,820	\$ 32,033	\$ 29,404

## 11. SHARE-BASED COMPENSATION

### Restricted Stock Units

The table below presents the activity of restricted stock units for the nine months ended September 30, 2019:

	Shares	Weighted Average Grant Date Fair Value
Non-vested restricted stock units, beginning of period	362,725	\$ 26.98
Changes during the period:		
Granted	181,431	28.89
Vested	(155,474)	24.40
Forfeited	(15,205)	29.24
Non-vested restricted stock units, end of period	373,477	28.89

## 12. LEASES

We lease certain land and buildings for our bank branches and ATMs. In some instances, a lease may contain renewal options to extend the term of the lease. All renewal options are likely to be exercised and therefore have been recognized as part of our right-of-use assets and lease liabilities in accordance with ASC 842, "Leases". Certain leases also contain variable payments that are primarily determined based on common area maintenance costs and Hawaii state tax rates. All leases are operating leases and we do not include any short term leases in the calculation of the right-of-use assets and lease liabilities. The most significant assumption related to the Company's application of ASC 842 was the discount rate assumption. As most of the Company's lease agreements do not provide for an implicit interest rate, the Company uses the collateralized interest rate that the Company would have to pay to borrow over a similar term to estimate the Company's lease liability.

Total lease cost, cash flow information, weighted-average remaining lease term and weighted-average discount rate is summarized below for the period indicated:

(dollars in thousands)	Three Months Ended September 30,		Nine Months Ended September 30,	
	2019		2019	
<b>Lease cost:</b>				
Operating lease cost	\$	1,627	\$	4,883
Variable lease cost		699		1,950
Less: sublease income		(11)		(33)
<b>Total lease cost</b>	<b>\$</b>	<b>2,315</b>		<b>6,800</b>
<b>Other information:</b>				
Operating cash flows from operating leases	\$	(1,558)	\$	(4,663)
Weighted-average remaining lease term - operating leases		13.80 years		13.80 years
Weighted-average discount rate - operating leases		3.92%		3.92%

The following is a schedule of annual undiscounted cash flows for our operating leases and a reconciliation of those cash flows to the operating lease liabilities for the remainder of fiscal year 2019, the next five succeeding fiscal years and all years thereafter (dollars in thousands):

Year Ending December 31,	Undiscounted Cash Flows	Lease Liability Expense	Lease Liability Reduction
2019 (remainder)	\$ 1,550	\$ 512	\$ 1,038
2020	6,018	1,939	4,079
2021	5,708	1,787	3,921
2022	5,271	1,645	3,626
2023	4,973	1,512	3,461
2024	4,814	1,383	3,431
Thereafter	40,920	7,669	33,251
<b>Total</b>	<b>\$ 69,254</b>	<b>\$ 16,447</b>	<b>\$ 52,807</b>

In addition, the Company, as lessor, leases certain properties that it owns. All of these leases are operating leases. The following represents lease income related to these leases that was recognized for the period indicated:

(dollars in thousands)	Three Months Ended September 30,		Nine Months Ended September 30,	
	2019		2019	
Total rental income recognized	\$	522		1,576

Based on the Company's leases as lessor as of September 30, 2019, estimated lease payments for the remainder of fiscal year 2019, the next five succeeding fiscal years and all years thereafter are as follows (dollars in thousands):

**Year Ending December 31,**

2019 (remainder)	\$	503
2020		1,837
2021		1,868
2022		1,308
2023		449
2024		97
Thereafter		262
Total	\$	<u>6,324</u>

**13. ACCUMULATED OTHER COMPREHENSIVE INCOME (LOSS)**

The following tables present the components of other comprehensive income for the three and nine months ended September 30, 2019 and 2018, by component:

(dollars in thousands)

	<u>Before Tax</u>	<u>Tax Effect</u>	<u>Net of Tax</u>
<b>Three Months Ended September 30, 2019</b>			
Net unrealized gains on investment securities:			
Net unrealized gains arising during the period	\$ 6,027	\$ 1,615	\$ 4,412
Less: Reclassification adjustments from AOCI realized in net income	(36)	(10)	(26)
Net unrealized gains on investment securities	<u>5,991</u>	<u>1,605</u>	<u>4,386</u>
Defined benefit plans:			
Amortization of net actuarial loss	310	31	279
Amortization of net transition obligation	5	3	2
Amortization of prior service cost	4	2	2
Defined benefit plans, net	<u>319</u>	<u>36</u>	<u>283</u>
Other comprehensive income	<u>\$ 6,310</u>	<u>\$ 1,641</u>	<u>\$ 4,669</u>

(dollars in thousands)

	<u>Before Tax</u>	<u>Tax Effect</u>	<u>Net of Tax</u>
<b>Three Months Ended September 30, 2018</b>			
Net unrealized losses on investment securities:			
Net unrealized losses arising during the period	\$ (8,297)	\$ (2,225)	\$ (6,072)
Less: Reclassification adjustments from AOCI realized in net income	—	—	—
Net unrealized losses on investment securities	<u>(8,297)</u>	<u>(2,225)</u>	<u>(6,072)</u>
Defined benefit plans:			
Amortization of net actuarial loss	289	78	211
Amortization of net transition obligation	5	2	3
Amortization of prior service cost	4	1	3
Defined benefit plans, net	<u>298</u>	<u>81</u>	<u>217</u>
Other comprehensive loss	<u>\$ (7,999)</u>	<u>\$ (2,144)</u>	<u>\$ (5,855)</u>

(dollars in thousands)	Before Tax	Tax Effect	Net of Tax
<b>Nine Months Ended September 30, 2019</b>			
Net unrealized gains on investment securities:			
Net unrealized gains arising during the period	\$ 37,671	\$ 10,098	\$ 27,573
Less: Reclassification adjustments from AOCI realized in net income	(36)	(10)	(26)
Net unrealized gains on investment securities	<u>37,635</u>	<u>10,088</u>	<u>27,547</u>
Defined benefit plans:			
Amortization of net actuarial loss	837	84	753
Amortization of net transition obligation	14	4	10
Amortization of prior service cost	13	3	10
Defined benefit plans, net	<u>864</u>	<u>91</u>	<u>773</u>
Other comprehensive income	<u>\$ 38,499</u>	<u>\$ 10,179</u>	<u>\$ 28,320</u>

(dollars in thousands)	Before Tax	Tax Effect	Net of Tax
<b>Nine Months Ended September 30, 2018</b>			
Net unrealized losses on investment securities:			
Net unrealized losses arising during the period	\$ (33,809)	\$ (9,097)	\$ (24,712)
Less: Reclassification adjustments from AOCI realized in net income	—	—	—
Net unrealized losses on investment securities	<u>(33,809)</u>	<u>(9,097)</u>	<u>(24,712)</u>
Defined benefit plans:			
Amortization of net actuarial loss	865	262	603
Amortization of net transition obligation	14	4	10
Amortization of prior service cost	13	3	10
Defined benefit plans, net	<u>892</u>	<u>269</u>	<u>623</u>
Other comprehensive loss	<u>\$ (32,917)</u>	<u>\$ (8,828)</u>	<u>\$ (24,089)</u>

The following tables present the changes in each component of AOCI, net of tax, for the three and nine months ended September 30, 2019 and 2018:

(dollars in thousands)	Investment Securities	Defined Benefit Plans	AOCI
<b>Three Months Ended September 30, 2019</b>			
Balance at beginning of period	10,418	(5,960)	4,458
Other comprehensive income before reclassifications	4,412	—	4,412
Reclassification adjustments from AOCI	(26)	283	257
Total other comprehensive income	<u>4,386</u>	<u>283</u>	<u>4,669</u>
Balance at end of period	<u>\$ 14,804</u>	<u>\$ (5,677)</u>	<u>\$ 9,127</u>

(dollars in thousands)	<b>Investment Securities</b>	<b>Defined Benefit Plans</b>	<b>AOCI</b>
<b>Three Months Ended September 30, 2018</b>			
Balance at beginning of period	\$ (14,161)	\$ (7,087)	\$ (21,248)
Other comprehensive loss before reclassifications	(6,072)	—	(6,072)
Reclassification adjustments from AOCI	—	217	217
Total other comprehensive income (loss)	(6,072)	217	(5,855)
Balance at end of period	<u>\$ (20,233)</u>	<u>\$ (6,870)</u>	<u>\$ (27,103)</u>

(dollars in thousands)	<b>Investment Securities</b>	<b>Defined Benefit Plans</b>	<b>AOCI</b>
<b>Nine Months Ended September 30, 2019</b>			
Balance at beginning of period	\$ (9,643)	\$ (6,450)	\$ (16,093)
Impact of the adoption of new accounting standards	(3,100)	—	(3,100)
Adjusted balance at beginning of period	(12,743)	(6,450)	(19,193)
Other comprehensive income before reclassifications	27,573	—	27,573
Reclassification adjustments from AOCI	(26)	773	747
Total other comprehensive income	27,547	773	28,320
Balance at end of period	<u>\$ 14,804</u>	<u>\$ (5,677)</u>	<u>\$ 9,127</u>

(dollars in thousands)	<b>Investment Securities</b>	<b>Defined Benefit Plans</b>	<b>AOCI</b>
<b>Nine Months Ended September 30, 2018</b>			
Balance at beginning of period	\$ 5,073	\$ (6,112)	\$ (1,039)
Impact of the adoption of new accounting standards	(139)	—	(139)
Adjusted balance at beginning of period	4,934	(6,112)	(1,178)
Impact of the adoption of new accounting standards	(455)	(1,381)	(1,836)
Other comprehensive loss before reclassifications	(24,712)	—	(24,712)
Reclassification adjustments from AOCI	—	623	623
Total other comprehensive income (loss)	(24,712)	623	(24,089)
Balance at end of period	<u>\$ (20,233)</u>	<u>\$ (6,870)</u>	<u>\$ (27,103)</u>

The following table presents the amounts reclassified out of each component of AOCI for the three and nine months ended September 30, 2019 and 2018:

Details about AOCI Components (dollars in thousands)	Amount Reclassified from AOCI		Affected Line Item in the Statement Where Net Income is Presented
	Three months ended September 30,		
	2019	2018	
Sale of investment securities available-for-sale:			
Realized gains (losses) on securities available-for-sale	\$ 36	\$ —	Investment securities gains (losses)
Tax effect	(10)	—	Income tax benefit (expense)
Net of tax	<u>\$ 26</u>	<u>\$ —</u>	
Defined benefit retirement and supplemental executive retirement plan items:			
Amortization of net actuarial loss	\$ (310)	\$ (289)	Salaries and employee benefits
Amortization of net transition obligation	(5)	(5)	Salaries and employee benefits
Amortization of prior service cost	(4)	(4)	Salaries and employee benefits
Total before tax	<u>(319)</u>	<u>(298)</u>	
Tax effect	36	81	Income tax benefit (expense)
Net of tax	<u>\$ (283)</u>	<u>\$ (217)</u>	
Total reclassification adjustments from AOCI for the period, net of tax	<u>\$ (257)</u>	<u>\$ (217)</u>	
Details about AOCI Components (dollars in thousands)	Amount Reclassified from AOCI		Affected Line Item in the Statement Where Net Income is Presented
	Nine months ended September 30,		
	2019	2018	
Sale of investment securities available-for-sale:			
Realized gains (losses) on securities available-for-sale	\$ 36	\$ —	Investment securities gains (losses)
Tax effect	(10)	—	Income tax benefit (expense)
Net of tax	<u>\$ 26</u>	<u>\$ —</u>	
Defined benefit retirement and supplemental executive retirement plan items:			
Amortization of net actuarial loss	\$ (837)	\$ (865)	Salaries and employee benefits
Amortization of net transition obligation	(14)	(14)	Salaries and employee benefits
Amortization of prior service cost	(13)	(13)	Salaries and employee benefits
Total before tax	<u>(864)</u>	<u>(892)</u>	
Tax effect	91	269	Income tax benefit (expense)
Net of tax	<u>\$ (773)</u>	<u>\$ (623)</u>	
Total reclassification adjustments from AOCI for the period	<u>\$ (747)</u>	<u>\$ (623)</u>	Net of tax

## 14. EARNINGS PER SHARE

The following table presents the information used to compute basic and diluted earnings per common share for the periods indicated:

(dollars in thousands, except per share data)	Three Months Ended September 30,		Nine Months Ended September 30,	
	2019	2018	2019	2018
Net income	\$ 14,554	\$ 15,193	\$ 44,125	\$ 43,694
Weighted average common shares outstanding - basic	28,424,898	29,297,465	28,575,369	29,536,536
Dilutive effect of employee stock options and awards	177,440	182,347	186,688	206,702
Weighted average common shares outstanding - diluted	28,602,338	29,479,812	28,762,057	29,743,238
Basic earnings per common share	\$ 0.51	\$ 0.52	\$ 1.54	\$ 1.48
Diluted earnings per common share	\$ 0.51	\$ 0.52	\$ 1.53	\$ 1.47
Anti-dilutive employee stock options and awards outstanding	—	—	—	—

## 15. FAIR VALUE OF FINANCIAL ASSETS AND LIABILITIES

### Disclosures about Fair Value of Financial Instruments

Fair value estimates, methods and assumptions are set forth below for our financial instruments.

#### Short-Term Financial Instruments

The carrying values of short-term financial instruments are deemed to approximate fair values. Such instruments are considered readily convertible to cash and include cash and due from financial institutions, interest-bearing deposits in other financial institutions, accrued interest receivable, the majority of Federal Home Loan Bank advances and other short-term borrowings, and accrued interest payable.

#### Investment Securities

The fair value of investment securities is based on market price quotations received from third-party pricing services. The third-party pricing services utilize pricing models supported with timely market data information. Where quoted market prices are not available, fair values are based on quoted market prices of comparable securities.

#### Loans

Fair values of loans are estimated based on discounted cash flows of portfolios of loans with similar financial characteristics including the type of loan, interest terms and repayment history. Fair values are calculated by discounting scheduled cash flows through estimated maturities using estimated market discount rates. Estimated market discount rates are reflective of credit and interest rate risks inherent in the Company's various loan types and are derived from available market information, as well as specific borrower information. In accordance with ASU 2016-01, the fair value of loans are measured based on the notion of exit price.

#### Loans Held for Sale

The fair value of loans classified as held for sale are generally based upon quoted prices for similar assets in active markets, acceptance of firm offer letters with agreed upon purchase prices, discounted cash flow models that take into account market observable assumptions, or independent appraisals of the underlying collateral securing the loans. We report the fair values of Hawaii and U.S. Mainland construction and commercial real estate loans, if any, net of applicable selling costs on our consolidated balance sheets.

### Deposit Liabilities

The fair values of deposits with no stated maturity, such as noninterest-bearing demand deposits and interest-bearing demand and savings accounts, are equal to the amount payable on demand. The fair value of time deposits is estimated using discounted cash flow analyses. The discount rate is estimated using the rates currently offered for deposits of similar remaining maturities.

### Long-Term Debt

The fair value of our long-term debt is estimated by discounting scheduled cash flows over the contractual borrowing period at the estimated market rate for similar borrowing arrangements.

### Derivatives

The fair values of derivative financial instruments are based upon current market values, if available. If there are no relevant comparables, fair values are based on pricing models using current assumptions for interest rate swaps and options.

### Off-Balance Sheet Financial Instruments

The fair values of off-balance sheet financial instruments are estimated based on the fees currently charged to enter into similar agreements, taking into account the remaining terms of the agreements and the present creditworthiness of the counterparties, current settlement values or quoted market prices of comparable instruments.

### Limitations

Fair value estimates are made at a specific point in time based on relevant market information and information about the financial instrument. These estimates do not reflect any premium or discount that could result from offering for sale at one time our entire holdings of a particular financial instrument. Because no market exists for a significant portion of our financial instruments, fair value estimates are based on judgments regarding future expected loss experience, current economic conditions, risk characteristics of various financial instruments and other factors. These estimates are subjective in nature and involve uncertainties and matters of significant judgment and therefore cannot be determined with precision. Changes in assumptions could significantly affect the estimates.

Fair value estimates are based on existing on- and off-balance sheet financial instruments without attempting to estimate the value of future business and the value of assets and liabilities that are not considered financial instruments. For example, significant assets and liabilities that are not considered financial assets or liabilities include deferred tax assets, premises and equipment and intangible assets.

(dollars in thousands)	Carrying Amount	Estimated Fair Value	Fair Value Measurement Using		
			Quoted Prices in Active Markets for Identical Assets (Level 1)	Significant Other Observable Inputs (Level 2)	Significant Unobservable Inputs (Level 3)
<b>September 30, 2019</b>					
Financial assets:					
Cash and due from banks	\$ 87,395	\$ 87,395	\$ 87,395	\$ —	\$ —
Interest-bearing deposits in other banks	7,803	7,803	7,803	—	—
Investment securities	1,187,933	1,187,933	1,058	1,175,373	11,502
Loans held for sale	7,016	7,016	—	7,016	—
Net loans and leases	4,319,695	4,328,177	—	9,752	4,318,425
Accrued interest receivable	16,220	16,220	16,220	—	—
Financial liabilities:					
Deposits:					
Noninterest-bearing demand	1,399,200	1,399,200	1,399,200	—	—
Interest-bearing demand and savings and money market	2,591,775	2,591,775	2,591,775	—	—
Time	1,046,684	1,043,147	—	—	1,043,147
Short-term borrowings	205,000	205,000	—	205,000	—
Long-term debt	101,547	97,324	—	97,324	—
Accrued interest payable (included in other liabilities)	5,402	5,402	5,402	—	—

(dollars in thousands)	Notional Amount	Carrying Amount	Estimated Fair Value	Fair Value Measurement Using		
				Quoted Prices in Active Markets for Identical Assets (Level 1)	Significant Other Observable Inputs (Level 2)	Significant Unobservable Inputs (Level 3)
<b>September 30, 2019</b>						
Derivatives:						
Interest rate lock commitments	\$ 1,569	\$ 49	\$ 49	\$ —	\$ 49	\$ —
Forward sale commitments	8,412	(3)	(3)	—	(3)	—
Off-balance sheet financial instruments:						
Commitments to extend credit	1,106,657	1,295	1,295	—	1,295	—
Standby letters of credit and financial guarantees written	11,275	169	169	—	169	—

(dollars in thousands)	Carrying Amount	Estimated Fair Value	Fair Value Measurement Using		
			Quoted Prices in Active Markets for Identical Assets (Level 1)	Significant Other Observable Inputs (Level 2)	Significant Unobservable Inputs (Level 3)
<b>December 31, 2018</b>					
Financial assets:					
Cash and due from banks	\$ 80,569	\$ 80,569	\$ 80,569	\$ —	\$ —
Interest-bearing deposits in other banks	21,617	21,617	21,617	—	—
Investment securities	1,354,812	1,350,576	826	1,338,581	11,169
Loans held for sale	6,647	6,647	—	6,647	—
Net loans and leases	4,030,450	3,938,380	—	—	3,938,380
Accrued interest receivable	17,000	17,000	17,000	—	—
Financial liabilities:					
Deposits:					
Noninterest-bearing demand	1,436,967	1,436,967	1,436,967	—	—
Interest-bearing demand and savings and money market	2,402,268	2,402,268	2,402,268	—	—
Time	1,107,255	1,099,560	—	—	1,099,560
Short-term borrowings	197,000	197,000	—	197,000	—
Long-term debt	122,166	118,057	—	118,057	—
Accrued interest payable (included in other liabilities)	5,051	5,051	5,051	—	—

(dollars in thousands)	Notional Amount	Carrying Amount	Estimated Fair Value	Fair Value Measurement Using		
				Quoted Prices in Active Markets for Identical Assets (Level 1)	Significant Other Observable Inputs (Level 2)	Significant Unobservable Inputs (Level 3)
<b>December 31, 2018</b>						
Derivatives:						
Interest rate lock commitments	\$ 2,158	\$ 11	\$ 11	\$ —	\$ 11	\$ —
Forward sale commitments	8,530	(95)	(95)	—	(95)	—
Off-balance sheet financial instruments:						
Commitments to extend credit	1,030,322	1,205	1,205	—	1,205	—
Standby letters of credit and financial guarantees written	13,377	201	201	—	201	—

## Fair Value Measurements

We group our financial assets and liabilities at fair value into three levels based on the markets in which the financial assets and liabilities are traded and the reliability of the assumptions used to determine fair value as follows:

- Level 1 — Valuation is based upon quoted prices (unadjusted) for identical assets or liabilities traded in active markets. A quoted price in an active market provides the most reliable evidence of fair value and shall be used to measure fair value whenever available.
- Level 2 — Valuation is based upon quoted prices for similar instruments in active markets, quoted prices for identical or similar instruments in markets that are not active, and model-based valuation techniques for which all significant assumptions are observable in the market.
- Level 3 — Valuation is generated from model-based techniques that use significant assumptions not observable in the market. These unobservable assumptions reflect our own estimates of assumptions that market participants would use in pricing the asset or liability. Valuation techniques include use of discounted cash flow models and similar techniques that requires the use of significant judgment or estimation.

We base our fair values on the price that we would expect to receive if an asset were sold, or the price that we would expect to pay to transfer a liability in an orderly transaction between market participants at the measurement date. We also maximize the use of observable inputs and minimize the use of unobservable inputs when developing fair value measurements.

We use fair value measurements to record adjustments to certain financial assets and liabilities and to determine fair value disclosures. Available-for-sale and equity securities and derivatives are recorded at fair value on a recurring basis. From time to time, we may be required to record other financial assets at fair value on a nonrecurring basis such as loans held for sale, impaired loans, mortgage servicing rights, and other real estate owned. These nonrecurring fair value adjustments typically involve application of the lower of cost or fair value accounting or write-downs of individual assets.

The Company's policy is to recognize transfers into or out of a level as of the end of the reporting period. There were no transfers of financial assets and liabilities between Level 1 and Level 2 of the fair value hierarchy during the three and nine months ended September 30, 2019. Also, there were no transfers of financial assets and liabilities into or out of Level 3 of the fair value hierarchy during the three and nine months ended September 30, 2019.

The following tables present the fair value of assets and liabilities measured on a recurring basis as of September 30, 2019 and December 31, 2018:

(dollars in thousands)	Fair Value	Fair Value at Reporting Date Using		
		Quoted Prices in Active Markets for Identical Assets (Level 1)	Significant Other Observable Inputs (Level 2)	Significant Unobservable Inputs (Level 3)
<b>September 30, 2019</b>				
Available-for-sale securities:				
Debt securities:				
States and political subdivisions	\$ 124,711	\$ —	\$ 113,209	\$ 11,502
Corporate securities	30,713	—	30,713	—
U.S. Treasury obligations and direct obligations of U.S Government agencies	42,897	—	42,897	—
Mortgage-backed securities:				
Residential - U.S. Government sponsored entities	723,644	—	723,644	—
Commercial - U.S. Government agencies and sponsored entities	87,742	—	87,742	—
Residential - Non-government agencies	39,109	—	39,109	—
Commercial - Non-government agencies	138,059	—	138,059	—
Total available-for-sale securities	1,186,875	—	1,175,373	11,502
Equity securities	1,058	1,058	—	—
Derivatives: Interest rate lock and forward sale commitments	46	—	46	—
Total	\$ 1,187,979	\$ 1,058	\$ 1,175,419	\$ 11,502

	Fair Value at Reporting Date Using			
	Fair Value	Quoted Prices in Active Markets for Identical Assets (Level 1)	Significant Other Observable Inputs (Level 2)	Significant Unobservable Inputs (Level 3)
(dollars in thousands)				
<b>December 31, 2018</b>				
Available-for-sale securities:				
Debt securities:				
States and political subdivisions	\$ 173,674	\$ —	\$ 162,505	\$ 11,169
Corporate securities	54,849	—	54,849	—
U.S. Treasury obligations and direct obligations of U.S Government agencies	32,574	—	32,574	—
Mortgage-backed securities:				
Residential - U.S. Government sponsored entities	717,052	—	717,052	—
Commercial - U.S. Government agencies and sponsored entities	41,118	—	41,118	—
Residential - Non-government agencies	51,483	—	51,483	—
Commercial - Non-government agencies	134,728	—	134,728	—
Total available-for-sale securities	1,205,478	—	1,194,309	11,169
Equity securities	826	826	—	—
Derivatives: Interest rate lock and forward sale commitments	(84)	—	(84)	—
Total	\$ 1,206,220	\$ 826	\$ 1,194,225	\$ 11,169

For the nine months ended September 30, 2019 and 2018, the changes in Level 3 assets and liabilities measured at fair value on a recurring basis are summarized as follows:

	Available-For-Sale Debt Securities: States and Political Subdivisions
(dollars in thousands)	
<b>Balance at December 31, 2018</b>	\$ 11,169
Principal payments received	(285)
Unrealized net gain included in other comprehensive income	618
<b>Balance at September 30, 2019</b>	\$ 11,502
<b>Balance at December 31, 2017</b>	\$ 11,794
Principal payments received	(280)
Unrealized net loss included in other comprehensive income	(370)
<b>Balance at September 30, 2018</b>	\$ 11,144

Within the states and political subdivisions available-for-sale debt securities category, the Company holds four mortgage revenue bonds issued by the City & County of Honolulu with an aggregate fair value of \$11.5 million and \$11.1 million at September 30, 2019 and September 30, 2018, respectively. The Company estimates the fair value of its mortgage revenue bonds by using a discounted cash flow model to calculate the present value of estimated future principal and interest payments.

The significant unobservable input used in the fair value measurement of the Company's mortgage revenue bonds is the weighted average discount rate. As of September 30, 2019, the weighted average discount rate utilized was 3.94% compared to 5.28% at September 30, 2018 and 5.06% at December 31, 2018, which was derived by incorporating a credit spread over the FHLB Fixed-Rate Advance curve. Significant increases (decreases) in the weighted average discount rate could result in a significantly lower (higher) fair value measurement.

The following table presents the fair value of assets measured on a nonrecurring basis and the level of valuation assumptions used to determine the respective fair values as of September 30, 2019 and December 31, 2018:

(dollars in thousands)	Fair Value	Fair Value Measurements Using		
		Quoted Prices in Active Markets for Identical Assets (Level 1)	Significant Other Observable Inputs (Level 2)	Significant Unobservable Inputs (Level 3)
<b>September 30, 2019</b>				
Other real estate <sup>(1)</sup>	\$ 466	\$ —	\$ 466	\$ —
<b>December 31, 2018</b>				
Other real estate <sup>(1)</sup>	\$ 414	\$ —	\$ 414	\$ —

<sup>(1)</sup> Represents other real estate that is carried at fair value less costs to sell. Fair value is generally based upon independent market prices or appraised values of the collateral.

## 16. SEGMENT INFORMATION

We have the following three reportable segments: Banking Operations, Treasury and All Others. These segments are consistent with our internal functional reporting lines and are managed separately because each unit has different target markets, technological requirements, and specialized skills.

The Banking Operations segment includes construction and real estate development lending, commercial lending, residential mortgage lending, indirect auto lending, trust services, retail brokerage services and our retail branch offices, which provide a full range of deposit and loan products, as well as various other banking services. The Treasury segment is responsible for managing the Company's investment securities portfolio and wholesale funding activities. The All Others segment consists of all activities not captured by the Banking Operations or Treasury segments described above and includes activities such as electronic banking, data processing and management of bank owned properties.

The accounting policies of the segments are consistent with the Company's accounting policies that are described in Note 1 - Summary of Significant Accounting Policies to the consolidated financial statements in the Annual Report on Form 10-K for the year ended December 31, 2018 filed with the SEC. The majority of the Company's net income is derived from net interest income. Accordingly, management focuses primarily on net interest income, rather than gross interest income and expense amounts, in evaluating segment profitability.

Intersegment net interest income (expense) was allocated to each segment based upon a funds transfer pricing process that assigns costs of funds to assets and earnings credits to liabilities based on market interest rates that reflect interest rate sensitivity and maturity characteristics. All administrative and overhead expenses are allocated to the segments at cost. Cash, investment securities, loans and leases and their related balances are allocated to the segment responsible for acquisition and maintenance of those assets. Segment assets also include all premises and equipment used directly in segment operations.

Segment profits and assets are provided in the following tables for the periods indicated.

(dollars in thousands)	<b>Banking Operations</b>	<b>Treasury</b>	<b>All Others</b>	<b>Total</b>
<b>Three Months Ended September 30, 2019</b>				
Net interest income	\$ 42,790	\$ 2,859	\$ —	\$ 45,649
Inter-segment net interest income (expense)	4,788	(2,825)	(1,963)	—
Credit (provision) for loan and lease losses	(1,532)	—	—	(1,532)
Other operating income:				
Mortgage banking income	1,360	—	404	1,764
Service charges on deposit accounts	2,125	—	—	2,125
Other service charges and fees	1,470	—	2,254	3,724
Income from fiduciary activities	1,126	—	—	1,126
Equity in earnings of unconsolidated subsidiaries	86	—	—	86
Fees on foreign exchange	20	150	—	170
Investments securities gains (losses)	—	36	—	36
Income from bank-owned life insurance	—	645	—	645
Loan placement fees	230	—	—	230
Net gain (loss) sale of foreclosed assets	—	—	17	17
Other	154	4	185	343
Other operating income	6,571	835	2,860	10,266
Other operating expense	(16,482)	(352)	(18,100)	(34,934)
Administrative and overhead expense allocation	(17,495)	(204)	17,699	—
Income before taxes	18,640	313	496	19,449
Income tax (expense) benefit	(4,702)	(89)	(104)	(4,895)
Net income (loss)	\$ 13,938	\$ 224	\$ 392	\$ 14,554

(dollars in thousands)	<b>Banking Operations</b>	<b>Treasury</b>	<b>All Others</b>	<b>Total</b>
<b>Three Months Ended September 30, 2018</b>				
Net interest income	\$ 38,872	\$ 4,453	\$ —	\$ 43,325
Inter-segment net interest income (expense)	7,524	(4,327)	(3,197)	—
Credit (provision) for loan and lease losses	59	—	—	59
Other operating income:				
Mortgage banking income	1,173	—	750	1,923
Service charges on deposit accounts	2,189	—	—	2,189
Other service charges and fees	1,318	8	1,960	3,286
Income from fiduciary activities	1,159	—	—	1,159
Equity in earnings of unconsolidated subsidiaries	71	—	—	71
Fees on foreign exchange	22	198	—	220
Income from bank-owned life insurance	—	1,055	—	1,055
Loan placement fees	115	—	—	115
Other	448	58	296	802
Other operating income	6,495	1,319	3,006	10,820
Other operating expense	(16,265)	(335)	(17,425)	(34,025)
Administrative and overhead expense allocation	(15,481)	(206)	15,687	—
Income before taxes	21,204	904	(1,929)	20,179
Income tax (expense) benefit	(5,128)	(215)	357	(4,986)
Net income (loss)	\$ 16,076	\$ 689	\$ (1,572)	\$ 15,193

(dollars in thousands)	Banking Operations	Treasury	All Others	Total
<b>Nine Months Ended September 30, 2019</b>				
Net interest income	\$ 127,059	\$ 9,081	\$ —	\$ 136,140
Inter-segment net interest income (expense)	18,080	(8,119)	(9,961)	—
Credit (provision) for loan and lease losses	(4,219)	—	—	(4,219)
Other operating income:				
Mortgage banking income	2,967	—	1,822	4,789
Service charges on deposit accounts	6,247	—	—	6,247
Other service charges and fees	4,130	—	6,349	10,479
Income from fiduciary activities	3,220	—	—	3,220
Equity in earnings of unconsolidated subsidiaries	165	—	—	165
Fees on foreign exchange	67	472	—	539
Investments securities gains (losses)	—	36	—	36
Income from bank-owned life insurance	—	2,511	—	2,511
Loan placement fees	486	—	—	486
Net gain (loss) sale of foreclosed assets	—	—	17	17
Other	453	2,558	533	3,544
Other operating income	17,735	5,577	8,721	32,033
Other operating expense	(48,289)	(1,097)	(56,003)	(105,389)
Administrative and overhead expense allocation	(49,953)	(624)	50,577	—
Income before taxes	60,413	4,818	(6,666)	58,565
Income tax (expense) benefit	(14,896)	(1,188)	1,644	(14,440)
Net income (loss)	\$ 45,517	\$ 3,630	\$ (5,022)	\$ 44,125

(dollars in thousands)	Banking Operations	Treasury	All Others	Total
<b>Nine Months Ended September 30, 2018</b>				
Net interest income	\$ 112,295	\$ 16,024	\$ —	\$ 128,319
Inter-segment net interest income (expense)	21,360	(14,717)	(6,643)	—
Credit (provision) for loan and lease losses	(262)	—	—	(262)
Other operating income:				
Mortgage banking income	3,089	—	2,456	5,545
Service charges on deposit accounts	6,169	—	—	6,169
Other service charges and fees	3,748	22	5,927	9,697
Income from fiduciary activities	3,132	—	—	3,132
Equity in earnings of unconsolidated subsidiaries	151	—	—	151
Fees on foreign exchange	75	633	—	708
Income from bank-owned life insurance	—	1,874	—	1,874
Loan placement fees	532	—	—	532
Other	803	60	733	1,596
Other operating income	17,699	2,589	9,116	29,404
Other operating expense	(47,967)	(1,078)	(51,995)	(101,040)
Administrative and overhead expense allocation	(45,594)	(652)	46,246	—
Income before taxes	57,531	2,166	(3,276)	56,421
Income tax (expense) benefit	(12,707)	(478)	458	(12,727)
Net income	\$ 44,824	\$ 1,688	\$ (2,818)	\$ 43,694

(dollars in thousands)	<b>Banking Operations</b>	<b>Treasury</b>	<b>All Others</b>	<b>Total</b>
<b>September 30, 2019</b>				
Investment securities	\$ —	\$ 1,187,933	\$ —	\$ 1,187,933
Loans and leases (including loans held for sale)	4,374,878	—	—	4,374,878
Other assets	25,867	250,474	137,564	413,905
<b>Total assets</b>	<b>\$ 4,400,745</b>	<b>\$ 1,438,407</b>	<b>\$ 137,564</b>	<b>\$ 5,976,716</b>

(dollars in thousands)	<b>Banking Operations</b>	<b>Treasury</b>	<b>All Others</b>	<b>Total</b>
<b>December 31, 2018</b>				
Investment securities	\$ —	\$ 1,354,812	\$ —	\$ 1,354,812
Loans and leases (including loans held for sale)	4,085,013	—	—	4,085,013
Other assets	36,905	256,652	73,644	367,201
<b>Total assets</b>	<b>\$ 4,121,918</b>	<b>\$ 1,611,464</b>	<b>\$ 73,644</b>	<b>\$ 5,807,026</b>

## 17. LEGAL PROCEEDINGS

We are involved in legal actions arising in the ordinary course of business. Management, after consultation with our legal counsel, believes the ultimate disposition of those matters will not have a material adverse effect on our consolidated financial statements.

## Item 2. Management's Discussion and Analysis of Financial Condition and Results of Operations

### Overview

Central Pacific Financial Corp. ("CPF") is a Hawaii corporation and a bank holding company. Our principal business is to serve as a holding company for our bank subsidiary, Central Pacific Bank. We refer to Central Pacific Bank herein as "our bank" or "the bank," and when we say "the Company," "we," "us" or "our," we mean the holding company on a consolidated basis with the bank and our other consolidated subsidiaries.

Central Pacific Bank is a full-service community bank with 35 branches and 78 ATMs located throughout the state of Hawaii. The bank offers a broad range of products and services including accepting time, savings, money market, and demand deposits and originating loans, including commercial loans, construction loans, commercial real estate loans, residential mortgage loans, and consumer loans.

### Basis of Presentation

Management's discussion and analysis of financial condition and results of operations should be read in conjunction with the accompanying consolidated financial statements under "Part I, Item 1. Financial Statements (Unaudited)." The following discussion should also be read in conjunction with the Company's Annual Report on Form 10-K for the year ended December 31, 2018 filed with the U.S. Securities and Exchange Commission (the "SEC") on February 28, 2019.

### Critical Accounting Policies and Use of Estimates

The preparation of financial statements in accordance with accounting principles generally accepted in the United States of America ("GAAP") requires that management make certain judgments and use certain estimates and assumptions that affect amounts reported and disclosures made. Accounting estimates are deemed critical when a different estimate could have reasonably been used or where changes in the estimate are reasonably likely to occur from period to period and would materially impact our consolidated financial statements as of or for the periods presented. Management has discussed the development and selection of the critical accounting estimates noted below with the Audit Committee of the Board of Directors, and the Audit Committee has reviewed the accompanying disclosures.

#### Allowance for Loan and Lease Losses

The allowance for loan and lease losses (the "Allowance") is management's estimate of incurred credit losses inherent in our loan and lease portfolio at the balance sheet date. We maintain our Allowance at an amount we expect to be sufficient to absorb probable losses incurred in our loan and lease portfolio.

The Company's approach to developing the Allowance has three basic elements. These elements include specific reserves for individually impaired loans, a general allowance for loans other than those analyzed as individually impaired, and qualitative adjustments based on environmental and other factors which may be internal or external to the Company.

#### *Specific Reserve*

Individually impaired loans in all loan categories are evaluated using one of three valuation methods as prescribed under Accounting Standards Codification ("ASC") 310-10, "*Fair Value of Collateral, Observable Market Price, or Cash Flow*". A loan is generally evaluated for impairment on an individual basis if it meets one or more of the following characteristics: risk-rated as substandard, doubtful or loss, loans on nonaccrual status, troubled debt restructures, or any loan deemed prudent by management to so analyze. If the valuation of the impaired loan is less than the recorded investment in the loan, the deficiency will be charged off against the Allowance or, alternatively, a specific reserve will be established and included in the overall Allowance balance. The Company did not record a specific reserve as of September 30, 2019 and December 31, 2018.

#### *General Allowance*

In determining the general allowance component of the Allowance, the Company utilizes a comprehensive approach to segment the loan portfolio into homogeneous groups. The Company's methodology segments the portfolio generally by FDIC Call Report codes. In the second quarter of 2017, an additional segment was added for auto dealer purchased loans. In the third quarter of 2018, another segment was broken out for multifamily commercial real estate loans. This results in eleven segments, and is consistent with general industry practice. For the purpose of determining general allowance loss factors, loss experience is derived from a migration analysis, with the exception of national syndicated loans and auto dealer purchased loans where an

average historical loss rate is applied due to limited historical loss experience. The key inputs to run a migration analysis are the length and frequency of the migration period, the dates for the migration periods to start and the number of migration periods used for the analysis. For each migration period, the analysis will determine the outstanding balance in each segment and/or sub-segment at the start of each period. These loans will then be followed for the length of the migration period to identify the amount of associated charge-offs and recoveries. A loss rate for each migration period is calculated using the formula 'net charge-offs over the period divided by beginning loan balance'. The Allowance methodology applies a look back period to January 1, 2010. The Company extends its look back period with each additional quarter passing. As of September 30, 2019, the look back period was nine years and nine months.

#### *Qualitative Adjustments*

Our Allowance methodology uses qualitative adjustments to address changes in conditions, trends, and circumstances such as economic conditions and industry changes that could have a significant impact on the risk profile of the loan portfolio, and provide for losses in the loan portfolio that may not be reflected and/or captured in the historical loss data. In order to ensure that the qualitative adjustments are in compliance with current regulatory standards and U.S. GAAP, the Company is primarily basing adjustments on the nine standard factors outlined in the 2006 Interagency Policy Statement on the Allowance for Loan and Lease Losses. These factors include: lending policies, economic conditions, loan profile, lending staff, problem loan trends, loan review, collateral, credit concentrations and other internal and external factors.

In recognizing that current and relevant environmental (economic, market or other) conditions that can affect repayment may not yet be fully reflected in historical loss experience, qualitative adjustments are applied to factor in current loan portfolio and market intelligence. These adjustments, which are added to the historical loss rate, consider the nature of the Company's primary markets and are reasonable, consistently determined and appropriately documented. Management reviews the results of the qualitative adjustment quarterly to ensure it is consistent with the trends in the overall economy, and from time to time may make adjustments, if necessary, to ensure directional consistency.

#### **Financial Summary**

Net income for the three months ended September 30, 2019 was \$14.6 million, or \$0.51 per diluted share, compared to \$15.2 million, or \$0.52 per diluted share for the three months ended September 30, 2018. Net income for the nine months ended September 30, 2019 was \$44.1 million, or \$1.53 per diluted share, compared to \$43.7 million, or \$1.47 per diluted share for the nine months ended September 30, 2018.

The following table presents annualized returns on average assets and average shareholders' equity, and basic and diluted earnings per share for the periods indicated. Returns on average assets and average shareholders' equity are annualized based on a 30/360 day convention.

	<b>Three Months Ended September 30,</b>		<b>Nine Months Ended September 30,</b>	
	<b>2019</b>	<b>2018</b>	<b>2019</b>	<b>2018</b>
Return on average assets	0.99%	1.06%	1.00%	1.03%
Return on average shareholders' equity	11.11	12.54	11.58	11.99
Basic earnings per common share	\$ 0.51	\$ 0.52	\$ 1.54	\$ 1.48
Diluted earnings per common share	0.51	0.52	1.53	1.47

#### **Material Trends**

The majority of our operations are concentrated in the state of Hawaii. As a result, our performance is significantly influenced by the real estate markets, economic environment and environmental conditions in Hawaii. Macroeconomic conditions also influence our performance. A favorable business environment is generally characterized by expanding gross state product, low unemployment and rising personal income; while an unfavorable business environment is characterized by the reverse.

Hawaii's economy depends significantly on conditions in the U.S. economy and key international economies, especially Japan. The growth of Hawaii's economy has slowed, yet the Hawaii Department of Business, Economic Development and Tourism ("DBEDT") sees a positive forecast with continued growth through the remainder of 2019 and in 2020. Tourism continues to be Hawaii's center of strength and its most significant economic driver. While visitor arrivals to Hawaii grew during the eight months ended August 30, 2019, visitor spending was down from the same prior year period. According to the Hawaii Tourism

Authority ("HTA"), 7.1 million visitors visited the state in the eight months ended August 30, 2019. This was an increase of 5.2% from the number of visitor arrivals in the eight months ended August 31, 2018. The HTA also reported total spending by visitors decreased to \$12.1 billion in the eight months ended August 30, 2019, or a decrease of \$61.5 million, or 0.5%, from the eight months ended August 31, 2018. According to DBEDT, total visitor arrivals are expected to increase 3.5%, while visitor spending is expected to decrease 0.2% in 2019. Total visitor arrivals and visitor spending are both expected to increase 2.0% and 2.3% in 2020, respectively.

DBEDT reported Hawaii's economy, as measured by the growth of real personal income and real gross state product, continued positive growth in 2018. DBEDT projects real personal income and real gross state product to grow at a rate of 1.2% and 1.1%, respectively, for 2019 and 1.1% and 1.2%, respectively, for 2020.

Hawaii's labor market continues to be among the best in the nation. The Department of Labor and Industrial Relations reported that Hawaii's seasonally adjusted annual unemployment rate was 2.7% in September 2019, compared to 2.6% in September 2018. Hawaii's unemployment rate in September 2019 remained below the national seasonally adjusted unemployment rate of 3.5%. DBEDT projects Hawaii's seasonally adjusted annual unemployment rate to be 3.0% in 2019 and 3.2% in 2020.

Real estate lending is a primary focus for us, including residential mortgage and commercial mortgage loans. As a result, we are dependent on the strength of Hawaii's real estate market. Home sales in Hawaii remained strong in 2018. The Oahu real estate market closed out 2018 with its eighth straight year of appreciation, however the sales volume for the year dropped. During the nine months ended September 30, 2019, Oahu sales volume and median sales prices have slowed. According to the Honolulu Board of Realtors, Oahu unit sales volume increased slightly by 0.8% for single-family homes but declined by 6.7% for condominiums for the nine months ended September 30, 2019, compared to the same time period last year. For the nine months ended September 30, 2019, the median sales price for single-family homes on Oahu was \$785,000, representing a decrease of 0.5% from \$789,000 in the same prior year period. The median sales price for condominiums on Oahu for the nine months ended September 30, 2019 was \$425,000, representing a decrease of 1.0% from \$429,500 in the same prior year period.

As we have seen in the past, our operating results are significantly impacted by the economy in Hawaii and the composition of our loan portfolio. Loan demand, deposit growth, provision for loan and lease losses ("Provision"), asset quality, noninterest income and noninterest expense are all affected by changes in economic conditions. If the residential and commercial real estate markets we have exposure to deteriorate, our results of operations would be negatively impacted.

In late 2008, the Federal Reserve lowered the target Federal Funds range to 0%-0.25%. In an attempt to help the overall economy, the Federal Reserve kept interest rates low through its targeted Federal Funds rate until the recession was safely over. In recent years, the Federal Reserve has begun raising the target Federal Funds range.

During 2018, the Federal Reserve increased the Federal Funds range four times, each by 25 basis points to 2.25%-2.50% as of December 31, 2018. The Federal Reserve left the Federal Funds range unchanged during the first half of 2019 but cut the Federal Funds range by 25 basis points at the July 2019 meeting and again by 25 basis points at the September 2019 meeting to 1.75%-2.00%. The Federal Reserve pledged future moves will be done patiently and with an eye toward how global economic and financial developments unfold.

Further decreases in the Federal Funds rate would likely result in lower overall interest rates and may support the continued expansion of the U.S. economy. Changes in monetary policy, including changes in interest rates, could influence, among other things, (i) the amount of interest we receive on loans and securities, (ii) the amount of interest we pay on deposits and borrowings, (iii) our ability to originate loans and obtain deposits and (iv) the fair value of our assets and liabilities.

## **RISE2020**

Commencing in the second quarter of 2019, the Company launched RISE2020, a new multifaceted initiative intended to enhance customer experience, drive stronger long-term growth and profitability, improve shareholder returns and lower our efficiency ratio. RISE2020 includes initiatives in the following key areas of opportunity: Digital Banking, Revenue Enhancements, Branch Transformation and Operational Excellence. RISE2020 is intended to provide Central Pacific Bank with best-in class products and services in several strategic areas. During the third quarter of 2019, the outsourcing of the Company's residential mortgage loan servicing was completed. The Company is on track to complete the launch of its new website under the cpb.bank domain name, the employee pilot phase of our upgraded online and mobile banking platforms and the implementation of its end-to-end commercial loan origination system in the fourth quarter of 2019. The Company believes its efforts to meet its 2020 milestones in its branch modernization and digital banking initiatives are progressing on schedule.

The Company plans to invest approximately \$40 million in RISE2020 during the remainder of 2019 and throughout 2020. Some of these investments will be capitalized, while others are recurring annually. The Company expects annual RISE2020-related expense to approximate \$7 million by the start of 2021. During the third quarter of 2019, the Company incurred approximately \$1.2 million in RISE2020-related expenses. While operating expenses are expected to increase, the Company is forecasting enhanced revenue growth. As a result, we expect our efficiency ratio to be in the 63-65% range in 2019 and 2020. Longer-term, the Company is targeting a 15% return on average shareholders' equity and a 57% efficiency ratio by the end of 2022.

## Results of Operations

### Net Interest Income

Net interest income, when annualized and expressed as a percentage of average interest earning assets, is referred to as "net interest margin." Interest income, which includes loan fees and resultant yield information, is expressed on a taxable equivalent basis using a federal statutory tax rate of 21% for the three and nine months ended September 30, 2019 and 2018. A comparison of net interest income on a taxable-equivalent basis ("net interest income") for the three and nine months ended September 30, 2019 and 2018 is set forth below.

	Three Months Ended September 30,								
	2019			2018			Variance		
(dollars in thousands)	Average Balance	Average Yield/Rate	Interest Income/Expense	Average Balance	Average Yield/Rate	Interest Income/Expense	Average Balance	Average Yield/Rate	Interest Income/Expense
<b>Assets</b>									
Interest earning assets:									
Interest-bearing deposits in other banks	\$ 6,295	2.05%	33	\$ 22,057	1.97%	109	\$ (15,762)	0.08 %	(76)
Investment securities, excluding valuation allowance:									
Taxable (1)	1,093,352	2.63	7,192	1,284,411	2.65	8,516	(191,059)	(0.02)	(1,324)
Tax-exempt (1)	117,784	3.04	896	163,172	2.86	1,165	(45,388)	0.18	(269)
Total investment securities	1,211,136	2.67	8,088	1,447,583	2.67	9,681	(236,447)	—	(1,593)
Loans and leases, including loans held for sale (2)	4,293,455	4.25	45,861	3,941,511	4.09	40,531	351,944	0.16	5,330
Federal Home Loan Bank stock	16,646	4.46	186	7,773	3.11	60	8,873	1.35	126
Total interest earning assets	5,527,532	3.90	54,168	5,418,924	3.70	50,381	108,608	0.20	3,787
Noninterest-earning assets	379,675			290,901			88,774		
Total assets	\$ 5,907,207			\$ 5,709,825			\$ 197,382		
<b>Liabilities and Equity</b>									
Interest-bearing liabilities:									
Interest-bearing demand deposits	\$ 1,002,875	0.08%	207	\$ 933,405	0.08%	181	\$ 69,470	— %	26
Savings and money market deposits	1,582,795	0.39	1,549	1,524,121	0.15	593	58,674	0.24	956
Time deposits under \$100,000	167,331	0.69	293	177,108	0.53	236	(9,777)	0.16	57
Time deposits \$100,000 and over	874,192	1.88	4,139	1,049,446	1.70	4,508	(175,254)	0.18	(369)
Total interest-bearing deposits	3,627,193	0.68	6,188	3,684,080	0.59	5,518	(56,887)	0.09	670
Short-term borrowings	191,564	2.34	1,130	25,163	2.30	146	166,401	0.04	984
Long-term debt	101,547	3.96	1,013	92,785	4.90	1,147	8,762	(0.94)	(134)
Total interest-bearing liabilities	3,920,304	0.84	8,331	3,802,028	0.71	6,811	118,276	0.13	1,520
Noninterest-bearing deposits	1,360,221			1,378,981			(18,760)		
Other liabilities	102,599			44,079			58,520		
Total liabilities	5,383,124			5,225,088			158,036		
Shareholders' equity	524,083			484,737			39,346		
Non-controlling interest	—			—			—		
Total equity	524,083			484,737			39,346		
Total liabilities and equity	\$ 5,907,207			\$ 5,709,825			\$ 197,382		
Net interest income			\$ 45,837			\$ 43,570			\$ 2,267
Interest rate spread		3.06%			2.99%			0.07 %	
Net interest margin		3.30%			3.20%			0.10 %	

(1) At amortized cost.

(2) Includes nonaccrual loans.

(dollars in thousands)	Nine Months Ended September 30,								
	2019			2018			Variance		
	Average Balance	Average Yield/Rate	Interest Income/Expense	Average Balance	Average Yield/Rate	Interest Income/Expense	Average Balance	Average Yield/Rate	Interest Income/Expense
<b>Assets</b>									
Interest earning assets:									
Interest-bearing deposits in other banks	\$ 8,540	2.30%	147	\$ 23,713	1.75%	310	\$ (15,173)	0.55 %	(163)
Investment securities, excluding valuation allowance:									
Taxable investment securities (1)	1,147,217	2.67	23,014	1,325,180	2.63	26,094	(177,963)	0.04	(3,080)
Tax-exempt investment securities (1)	137,750	2.93	3,023	164,174	2.86	3,527	(26,424)	0.07	(504)
Total investment securities	1,284,967	2.70	26,037	1,489,354	2.65	29,621	(204,387)	0.05	(3,584)
Loans and leases, including loans held for sale (2)	4,183,703	4.32	135,169	3,856,420	4.04	116,620	327,283	0.28	18,549
Federal Home Loan Bank stock	15,650	4.33	508	7,261	2.67	145	8,389	1.66	363
Total interest earning assets	5,492,860	3.94	161,861	5,376,748	3.64	146,696	116,112	0.30	15,165
Noninterest-earning assets	365,364			294,090			71,274		
Total assets	\$ 5,858,224			\$ 5,670,838			\$ 187,386		
<b>Liabilities and Equity</b>									
Interest-bearing liabilities:									
Interest-bearing demand deposits	\$ 972,316	0.08%	598	\$ 940,154	0.08%	554	\$ 32,162	— %	44
Savings and money market deposits	1,544,759	0.33	3,847	1,506,565	0.13	1,421	38,194	0.20	2,426
Time deposits under \$100,000	172,204	0.69	884	178,363	0.48	645	(6,159)	0.21	239
Time deposits \$100,000 and over	921,003	1.96	13,507	1,042,353	1.48	11,558	(121,350)	0.48	1,949
Total interest-bearing deposits	3,610,282	0.70	18,836	3,667,435	0.52	14,178	(57,153)	0.18	4,658
Short-term borrowings	168,350	2.50	3,146	14,683	2.16	237	153,667	0.34	2,909
Long-term debt	101,547	4.09	3,104	92,785	4.64	3,221	8,762	(0.55)	(117)
Total interest-bearing liabilities	3,880,179	0.86	25,086	3,774,903	0.62	17,636	105,276	0.24	7,450
Noninterest-bearing deposits	1,370,972			1,367,574			3,398		
Other liabilities	99,143			42,414			56,729		
Total liabilities	5,350,294			5,184,891			165,403		
Shareholders' equity	507,930			485,942			21,988		
Non-controlling interest	—			5			(5)		
Total equity	507,930			485,947			21,983		
Total liabilities and equity	\$ 5,858,224			\$ 5,670,838			\$ 187,386		
Net interest income			\$ 136,775			\$ 129,060			\$ 7,715
Interest rate spread		3.08%			3.02%			0.06 %	
Net interest margin		3.32%			3.20%			0.12 %	

(1) At amortized cost.

(2) Includes nonaccrual loans.

Net interest income (expressed on a taxable-equivalent basis) was \$45.8 million for the three months ended September 30, 2019, representing an increase of 5.2% from \$43.6 million in the three months ended September 30, 2018. Net interest income (expressed on a taxable-equivalent basis) was \$136.8 million for the nine months ended September 30, 2019, representing an increase of 6.0% from \$129.1 million in the nine months ended September 30, 2018. The increase in the three and nine months ended September 30, 2019 was primarily attributable to a significant increase in average loans and leases balances funded by

runoff of the investment securities portfolio and short-term borrowings, combined with higher yields earned on the loans and leases portfolio. In addition, average government time deposits (included in time deposits \$100,000 and over) declined significantly. Partially offsetting this decrease were increases in rates paid on interest-bearing deposits and short-term borrowings, primarily attributable to the 25 basis point increases in the Federal Funds rate in each of the four quarters of 2018, combined with a significant increase in short-term borrowings.

#### *Interest Income*

Taxable-equivalent interest income was \$54.2 million for the three months ended September 30, 2019, representing an increase of 7.5% from \$50.4 million in the three months ended September 30, 2018. The increase was primarily attributable to a \$351.9 million increase in average loans and leases compared to the three months ended September 30, 2018, accounting for approximately \$3.6 million of the increase in interest income during the three months ended September 30, 2019. In addition, the average yields earned on the loans and leases portfolio during the three months ended September 30, 2019 increased by 16 bp, compared to the three months ended September 30, 2018, accounting for approximately \$1.7 million of the increase in interest income. These increases were partially offset by a \$236.4 million decline in average investment securities, which decreased interest income by approximately \$1.6 million.

Taxable-equivalent interest income was \$161.9 million for the nine months ended September 30, 2019, representing an increase of 10.3% from \$146.7 million in the nine months ended September 30, 2018. The increase was primarily attributable to a \$327.3 million increase in average loans and leases compared to the nine months ended September 30, 2018, accounting for approximately \$9.9 million of the increase in interest income during the nine months ended September 30, 2019. In addition, the average yields earned on the loans and leases and investment securities portfolios during the nine months ended September 30, 2019 increased by 28 bp and 5 bp, respectively, compared to the nine months ended September 30, 2018, accounting for approximately \$8.8 million and \$0.4 million of the increase in interest income, respectively. These increases were partially offset by a \$204.4 million decline in average investment securities, which decreased interest income by approximately \$4.1 million.

#### *Interest Expense*

Interest expense for the three months ended September 30, 2019 was \$8.3 million, representing an increase of 22.3% from the three months ended September 30, 2018. The increase was primarily attributable to an increase in average short-term borrowings of \$166.4 million, resulting in higher interest expense of approximately \$1.0 million. In addition, increases in average rates paid on time deposits \$100,000 and over and savings and money market deposits of 18 bp and 24 bp, respectively, increased interest expense by approximately \$0.4 million and \$1.0 million, respectively. Time deposits \$100,000 and over primarily consists of public funds which may be opportunistic sources of funding, but fluctuate more directly with changes in the Federal Funds rate. These increases were partially offset by a \$175.3 million decline in average time deposits \$100,000 and over, which decreased interest expense by approximately \$0.7 million and a 94 bp decrease in rates paid on long-term debt, which decreased interest expense by approximately \$0.2 million.

Interest expense for the nine months ended September 30, 2019 was \$25.1 million, representing an increase of 42.2% from the nine months ended September 30, 2018. The increase was primarily attributable to 48 bp and 20 bp increases in average rates paid on time deposits \$100,000 and over and savings and money market deposits, respectively, combined with a 34 bp increase in average rates paid on short-term borrowings, which increased interest expense by approximately \$3.3 million, \$2.3 million and \$0.4 million, respectively. In addition, average short-term borrowings increased by \$153.7 million, resulting in higher interest expense of approximately \$2.5 million. These increases were partially offset by a \$121.4 million decline in average time deposits \$100,000 and over, which decreased interest expense by approximately \$1.3 million, and a 55 bp decrease in rates paid on long-term debt, which decreased interest expense by approximately \$0.4 million.

#### *Net Interest Margin*

Our net interest margin of 3.30% for the three months ended September 30, 2019 increased by 10 bp from 3.20% in the three months ended September 30, 2018. Our net interest margin of 3.32% for the nine months ended September 30, 2019 increased by 12 bp from 3.20% in the nine months ended September 30, 2018.

The average yields earned on our interest-earning assets, which increased by 20 bp and 30 bp in the three and nine months ended September 30, 2019, respectively, compared to the same prior year periods, outpaced the increase in average rates paid on our interest-bearing liabilities, which increased by 13 bp and 24 bp in the three and nine months ended September 30, 2019, respectively, compared to the same prior year periods.

The aforementioned increases in average yields earned on our loans and leases portfolio during the three and nine months ended September 30, 2019 was partially offset by the aforementioned increases in average rates paid on our time deposits \$100,000 and over and savings and money market deposits during the three and nine months ended September 30, 2019.

#### Provision for Loan and Lease Losses

Our Provision expense was \$1.5 million during the three months ended September 30, 2019, compared to a Provision reversal of \$0.1 million in the three months ended September 30, 2018. Our Provision expense was \$4.2 million during the nine months ended September 30, 2019, compared to expense of \$0.3 million in the nine months ended September 30, 2018.

Our net charge-offs were \$1.6 million during the three months ended September 30, 2019, compared to net charge-offs of \$1.3 million in the three months ended September 30, 2018. Our net charge-offs were \$4.0 million during the nine months ended September 30, 2019, compared to net charge-offs of \$3.4 million in the nine months ended September 30, 2018.

#### Other Operating Income

The following tables set forth components of other operating income for the periods indicated:

(dollars in thousands)	<b>Three Months Ended</b>			
	<b>September 30, 2019</b>	<b>September 30, 2018</b>	<b>\$ Change</b>	<b>% Change</b>
<b>Other operating income:</b>				
Mortgage banking income	\$ 1,764	\$ 1,923	\$ (159)	-8.3 %
Service charges on deposit accounts	2,125	2,189	(64)	-2.9 %
Other service charges and fees	3,724	3,286	438	13.3 %
Income from fiduciary activities	1,126	1,159	(33)	-2.8 %
Equity in earnings of unconsolidated subsidiaries	86	71	15	21.1 %
Fees on foreign exchange	170	220	(50)	-22.7 %
Investment securities gains	36	—	36	N.M. *
Income from bank-owned life insurance	645	1,055	(410)	-38.9 %
Loan placement fees	230	115	115	100.0 %
Net gain on sales of foreclosed assets	17	—	17	N.M. *
<b>Other:</b>				
Income recovered on nonaccrual loans previously charged-off	73	395	(322)	-81.5 %
Other recoveries	42	101	(59)	-58.4 %
Commissions on sale of checks	75	79	(4)	-5.1 %
Other	153	227	(74)	-32.6 %
<b>Total other operating income</b>	<b>\$ 10,266</b>	<b>\$ 10,820</b>	<b>\$ (554)</b>	<b>-5.1 %</b>

\* Not meaningful ("N.M.")

For the three months ended September 30, 2019, total other operating income of \$10.3 million decreased by \$0.6 million, or 5.1%, from \$10.8 million in the year-ago quarter. The decrease from the year-ago quarter was primarily due to lower income from bank-owned life insurance of \$0.4 million, lower income recovered on nonaccrual loans previously charged-off of \$0.3 million and lower mortgage banking income of \$0.2 million. The lower income from bank-owned life insurance was primarily attributable to fluctuations in the equity markets during the quarter. These decreases were partially offset by higher merchant and bank card fees of \$0.3 million (included in other service charges and fees).

**Nine Months Ended**

(dollars in thousands)	<u>September 30, 2019</u>	<u>September 30, 2018</u>	<u>\$ Change</u>	<u>% Change</u>
<b>Other operating income:</b>				
Mortgage banking income	\$ 4,789	\$ 5,545	\$ (756)	-13.6 %
Service charges on deposit accounts	6,247	6,169	78	1.3 %
Other service charges and fees	10,479	9,697	782	8.1 %
Income from fiduciary activities	3,220	3,132	88	2.8 %
Equity in earnings of unconsolidated subsidiaries	165	151	14	9.3 %
Fees on foreign exchange	539	708	(169)	-23.9 %
Investment securities gains	36	—	36	N.M. *
Income from bank-owned life insurance	2,511	1,874	637	34.0 %
Loan placement fees	486	532	(46)	-8.6 %
Net gain on sales of foreclosed assets	17	—	17	N.M.
<b>Other:</b>				
Income recovered on nonaccrual loans previously charged-off	240	621	(381)	-61.4 %
Other recoveries	94	196	(102)	-52.0 %
Commissions on sale of checks	234	249	(15)	-6.0 %
Gain on sale of MasterCard stock	2,555	—	2,555	N.M. *
Other	421	530	(109)	-20.6 %
Total other operating income	<u>\$ 32,033</u>	<u>\$ 29,404</u>	<u>\$ 2,629</u>	8.9 %

\* Not meaningful ("N.M.")

For the nine months ended September 30, 2019, total other operating income of \$32.0 million increased by \$2.6 million, or 8.9%, from \$29.4 million in the year-ago period. The increase from the year-ago period was primarily due to the conversion of MasterCard Class B common stock received during their initial public offering to Class A common stock and immediate sale of the converted shares resulting in a gain of \$2.6 million in the first quarter of 2019, combined with higher income from bank-owned life insurance of \$0.6 million, higher merchant and bank card fees of \$0.4 million (included in other service charges and fees) and higher commissions and fees on investment services of \$0.4 million (included in other service charges and fees). The higher income from bank-owned life insurance was primarily attributable to fluctuations in the equity markets. These increases were partially offset by lower mortgage banking income of \$0.8 million and lower income recovered on nonaccrual loans previously charged-off of \$0.4 million.

## Other Operating Expense

The following tables set forth components of other operating expense for the periods indicated:

(dollars in thousands)	Three Months Ended			
	September 30, 2019	September 30, 2018	\$ Change	% Change
<b>Other operating expense:</b>				
Salaries and employee benefits	\$ 20,631	\$ 19,011	\$ 1,620	8.5 %
Net occupancy	3,697	3,488	209	6.0 %
Equipment	1,067	1,048	19	1.8 %
Amortization of core deposit premium	—	669	(669)	-100.0 %
Communication expense	1,008	903	105	11.6 %
Legal and professional services	1,933	1,528	405	26.5 %
Computer software expense	2,713	2,672	41	1.5 %
Advertising expense	711	612	99	16.2 %
Foreclosed asset expense	15	212	(197)	-92.9 %
<b>Other:</b>				
Charitable contributions	230	166	64	38.6 %
FDIC insurance assessment	5	437	(432)	-98.9 %
Miscellaneous loan expenses	274	403	(129)	-32.0 %
ATM and debit card expenses	660	686	(26)	-3.8 %
Armored car expenses	220	185	35	18.9 %
Entertainment and promotions	323	185	138	74.6 %
Stationery and supplies	240	206	34	16.5 %
Directors' fees and expenses	242	263	(21)	-8.0 %
Provision for residential mortgage loan repurchase losses	—	331	(331)	-100.0 %
Increase (decrease) to the reserve for unfunded commitments	(465)	(71)	(394)	554.9 %
Other	1,430	1,091	339	31.1 %
<b>Total other operating expense</b>	<b>\$ 34,934</b>	<b>\$ 34,025</b>	<b>\$ 909</b>	<b>2.7 %</b>

For the three months ended September 30, 2019, total other operating expense was \$34.9 million and increased by \$0.9 million, or 2.7%, from \$34.0 million in the year-ago quarter. The increase was primarily due to higher salaries and employee benefits of \$1.6 million and higher legal and professional services of \$0.4 million. The increase in salaries and employee benefits was partially attributable to the addition of positions in strategic areas and higher commissions, combined with annual merit increases effective in the second quarter of 2019. These increases were partially offset by lower amortization of core deposit premium of \$0.7 million, as the intangible asset was fully amortized as of September 30, 2018, a credit to the reserve for unfunded loan commitments during the current quarter of \$0.5 million and lower FDIC insurance expense of \$0.4 million. FDIC insurance expense includes a \$0.4 million assessment credit received in the current quarter.

(dollars in thousands)	Nine Months Ended			
	September 30, 2019	September 30, 2018	\$ Change	% Change
<b>Other operating expense:</b>				
Salaries and employee benefits	\$ 61,083	\$ 56,299	\$ 4,784	8.5 %
Net occupancy	10,680	10,114	566	5.6 %
Equipment	3,211	3,160	51	1.6 %
Amortization of core deposit premium	—	2,006	(2,006)	-100.0 %
Communication expense	2,645	2,547	98	3.8 %
Legal and professional services	5,231	5,118	113	2.2 %
Computer software expense	7,870	7,244	626	8.6 %
Advertising expense	2,134	1,841	293	15.9 %
Foreclosed asset expense	223	537	(314)	-58.5 %
<b>Other:</b>				
Charitable contributions	559	497	62	12.5 %
FDIC insurance assessment	868	1,305	(437)	-33.5 %
Miscellaneous loan expenses	885	1,026	(141)	-13.7 %
ATM and debit card expenses	1,930	2,032	(102)	-5.0 %
Armored car expenses	629	584	45	7.7 %
Entertainment and promotions	1,576	617	959	155.4 %
Stationery and supplies	744	643	101	15.7 %
Directors' fees and expenses	722	777	(55)	-7.1 %
Provision for residential mortgage loan repurchase losses	(403)	331	(734)	-221.8 %
Increase (decrease) to the reserve for unfunded commitments	189	36	153	425.0 %
Other	4,613	4,326	287	6.6 %
<b>Total other operating expense</b>	<b>\$ 105,389</b>	<b>\$ 101,040</b>	<b>\$ 4,349</b>	<b>4.3 %</b>

For the nine months ended September 30, 2019, total other operating expense was \$105.4 million and increased by \$4.3 million, or 4.3%, from \$101.0 million in the year-ago quarter. The increase was primarily due to higher salaries and employee benefits of \$4.8 million, higher entertainment and promotions expense of \$1.0 million, higher computer software expense of \$0.6 million and higher net occupancy expense of \$0.6 million. The higher entertainment and promotions expense was primarily attributable to expenses related to a core deposit gathering campaign in the second quarter of 2019. These increases were partially offset by lower amortization of core deposit premium of \$2.0 million, a credit to the reserve for residential mortgage loan repurchase losses of \$0.4 million, compared to an increase to the reserve of \$0.3 million in the year-ago period, and lower FDIC insurance expense of \$0.4 million.

A key measure of operating efficiency tracked by management is the efficiency ratio, which is calculated by dividing total other operating expense by total pre-provision revenue (net interest income and total other operating income). Management believes that the efficiency ratio provides useful supplemental information that is important to a proper understanding of the company's core business results by investors. Our efficiency ratio should not be viewed as a substitute for results determined in accordance with GAAP, nor is it necessarily comparable to the efficiency ratio presented by other companies.

The following table sets forth a calculation of our efficiency ratio for each of the periods indicated:

(dollars in thousands)	Three Months Ended September 30,		Nine Months Ended September 30,	
	2019	2018	2019	2018
Total other operating expense	\$ 34,934	\$ 34,025	\$ 105,389	\$ 101,040
Net interest income	\$ 45,649	\$ 43,325	\$ 136,140	\$ 128,319
Total other operating income	10,266	10,820	32,033	29,404
Total pre-provision revenue	\$ 55,915	\$ 54,145	\$ 168,173	\$ 157,723
Efficiency ratio	62.48%	62.84%	62.67%	64.06%

Our efficiency ratio improved to 62.48% in the three months ended September 30, 2019 compared to 62.84% in the year-ago quarter and improved to 62.67% in the nine months ended September 30, 2019 compared to 64.06% in the year-ago period. The efficiency ratio in the nine months ended September 30, 2019 was positively impacted by the aforementioned \$2.6 million gain on sale of MasterCard stock.

#### Income Taxes

The Company recorded income tax expense of \$4.9 million and \$14.4 million for the three and nine months ended September 30, 2019, respectively, compared to \$5.0 million and \$12.7 million in the same prior year periods, respectively. The effective tax rate for the three and nine months ended September 30, 2019 was 25.2% and 24.7%, respectively, compared to 24.7% and 22.6% in the same prior year periods, respectively. The increases in income tax expense and the effective tax rate in the three and nine months ended September 30, 2019 was primarily due to higher pre-tax income in the current quarter, combined with an income tax benefit of \$0.7 million related to the finalization of the impact of H.R.1, commonly referred to as the Tax Cuts and Jobs Act, recorded in the first quarter of 2018 and an income tax benefit of \$0.6 million related to a tax accounting method change strategy recorded in the second quarter of 2018.

The valuation allowance on our net deferred tax assets ("DTA") totaled \$3.3 million at September 30, 2019 and \$3.5 million at December 31, 2018, of which \$3.2 million and \$3.3 million, respectively, related to our DTA from net apportioned net operating loss ("NOL") carryforwards for California state income tax purposes as we do not expect to generate sufficient income in California to utilize the DTA. The remaining valuation allowance of \$0.1 million and \$0.2 million as of September 30, 2019 and December 31, 2018 relates to a Hawaii capital loss carryforward balance that we do not expect to be able to utilize. Net of the valuation allowance, the Company's net DTA totaled \$14.0 million at September 30, 2019, compared to a net DTA of \$21.5 million as of December 31, 2018, and is included in other assets on our consolidated balance sheets.

#### **Financial Condition**

Total assets at September 30, 2019 of \$5.98 billion increased by \$169.7 million from \$5.81 billion at December 31, 2018.

#### Investment Securities

Investment securities of \$1.19 billion at September 30, 2019 decreased by \$166.9 million, or 12.3%, from December 31, 2018. The decrease reflects \$201.4 million in principal runoff, offset by a \$33.4 million increase in the market valuation on the available-for-sale portfolio and \$1.0 million in net purchases.

## Loans and Leases

The following table sets forth information regarding our outstanding loans and leases by category and geographic location as of the dates indicated.

(dollars in thousands)	September 30, 2019	December 31, 2018	\$ Change	% Change
<b>Hawaii:</b>				
Commercial, financial and agricultural	\$ 439,296	\$ 439,112	\$ 184	— %
Real estate:				
Construction	96,661	64,654	32,007	49.5
Residential mortgage	1,558,735	1,428,205	130,530	9.1
Home equity	475,565	468,966	6,599	1.4
Commercial mortgage	909,987	861,086	48,901	5.7
Consumer	369,511	357,908	11,603	3.2
Leases	31	124	(93)	(75.0)
Total loans and leases	3,849,786	3,620,055	229,731	6.3
Allowance for loan and lease losses	(42,286)	(42,993)	707	(1.6)
Net loans and leases	\$ 3,807,500	\$ 3,577,062	\$ 230,438	6.4
<b>U.S. Mainland:</b>				
Commercial, financial and agricultural	\$ 137,316	\$ 142,548	\$ (5,232)	(3.7)
Real estate:				
Construction	—	2,273	(2,273)	(100.0)
Residential mortgage	—	—	—	—
Home equity	—	—	—	—
Commercial mortgage	223,925	179,192	44,733	25.0
Consumer	156,835	134,298	22,537	16.8
Leases	—	—	—	—
Total loans and leases	518,076	458,311	59,765	13.0
Allowance for loan and lease losses	(5,881)	(4,923)	(958)	19.5
Net loans and leases	\$ 512,195	\$ 453,388	\$ 58,807	13.0
<b>Total:</b>				
Commercial, financial and agricultural	\$ 576,612	\$ 581,660	\$ (5,048)	(0.9)
Real estate:				
Construction	96,661	66,927	29,734	44.4
Residential mortgage	1,558,735	1,428,205	130,530	9.1
Home equity	475,565	468,966	6,599	1.4
Commercial mortgage	1,133,912	1,040,278	93,634	9.0
Consumer	526,346	492,206	34,140	6.9
Leases	31	124	(93)	(75.0)
Total loans and leases	4,367,862	4,078,366	289,496	7.1
Allowance for loan and lease losses	(48,167)	(47,916)	(251)	0.5
Net loans and leases	\$ 4,319,695	\$ 4,030,450	\$ 289,245	7.2

Loans and leases, net of deferred costs, of \$4.37 billion at September 30, 2019 increased by \$289.5 million, or 7.1%, from December 31, 2018. The increase reflects net increases in the following loan portfolios: residential mortgage of \$130.5 million, commercial mortgage of \$93.6 million, consumer of \$34.1 million, construction of \$29.7 million, and home equity of \$6.6 million. These increases were partially offset by a net decrease in the commercial, financial and agricultural portfolio of \$5.0 million.

The Hawaii loan portfolio increased by \$229.7 million, or 6.3%, from December 31, 2018. The increase reflects net increases in the following loan portfolios: residential mortgage of \$130.5 million, commercial mortgage of \$48.9 million, construction of

\$32.0 million, consumer of \$11.6 million and home equity of \$6.6 million. The increases in the portfolios were primarily due to an increased demand from both new and existing customers.

The U.S. Mainland loan portfolio increased by \$59.8 million, or 13.0% from December 31, 2018. The net increase was primarily attributable to net increases in the commercial mortgage loan portfolio of \$44.7 million and consumer loan portfolio of \$22.5 million. These increases were partially offset by net decreases in commercial, financial and agricultural and construction loan portfolios of \$5.2 million and \$2.3 million, respectively.

Through the third quarter of 2019, we purchased U.S. Mainland consumer loans with outstanding balances at the time of purchases totaling \$80.0 million for \$78.8 million, or a net discount of \$1.2 million.

In 2018, we purchased U.S Mainland consumer loans totaling \$58.6 million, which included a \$0.1 million premium over the \$58.5 million outstanding balance at the time of purchase.

### Nonperforming Assets, Accruing Loans Delinquent for 90 Days or More, Restructured Loans Still Accruing Interest

The following table sets forth nonperforming assets, accruing loans delinquent for 90 days or more and restructured loans still accruing interest as of the dates indicated.

(dollars in thousands)	<u>September 30, 2019</u>	<u>December 31, 2018</u>	<u>\$ Change</u>	<u>% Change</u>
<b>Nonperforming Assets</b>				
Nonaccrual loans:				
Real estate:				
Residential mortgage	\$ 799	\$ 2,048	\$ (1,249)	(61.0)
Home equity	95	275	(180)	(65.5)
Total nonaccrual loans	894	2,323	(1,429)	(61.5)
Other real estate owned ("OREO"):				
Real estate:				
Residential mortgage	302	414	(112)	(27.1)
Home equity	164	—	164	—
Total OREO	466	414	52	12.6
Total nonperforming assets	1,360	2,737	(1,377)	(50.3)
<b>Accruing Loans Delinquent for 90 Days or More</b>				
Real estate:				
Home equity	—	298	(298)	(100.0)
Consumer	235	238	(3)	(1.3)
Total accruing loans delinquent for 90 days or more	235	536	(301)	(56.2)
<b>Restructured Loans Still Accruing Interest</b>				
Commercial, financial and agricultural	157	220	(63)	(28.6)
Real estate:				
Construction	—	2,273	(2,273)	(100.0)
Residential mortgage	6,717	8,026	(1,309)	(16.3)
Commercial mortgage	1,985	2,348	(363)	(15.5)
Total restructured loans still accruing interest	8,859	12,867	(4,008)	(31.1)
Total nonperforming assets, accruing loans delinquent for 90 days or more and restructured loans still accruing interest	\$ 10,454	\$ 16,140	\$ (5,686)	(35.2)
Ratio of nonaccrual loans to total loans and leases	0.02%	0.06%		(0.04)%
Ratio of nonperforming assets to total loans and leases and OREO	0.03%	0.07%		(0.04)%
Ratio of nonperforming assets and accruing loans delinquent for 90 days or more to total loans and leases and OREO	0.04%	0.08%		(0.04)%
Ratio of nonperforming assets, accruing loans delinquent for 90 days or more, and restructured loans still accruing interest to total loans and leases and OREO	0.24%	0.40%		(0.16)%

The following table sets forth year-to-date activity in nonperforming assets as of the date indicated:

(dollars in thousands)

<b>Balance at December 31, 2018</b>	<b>\$ 2,737</b>
Additions	922
Reductions:	
Payments	(2,177)
Return to accrual status	(27)
Net charge-offs, valuation and other adjustments	(95)
<b>Total reductions</b>	<b>(2,299)</b>
Net increase	(1,377)
<b>Balance at September 30, 2019</b>	<b>\$ 1,360</b>

Nonperforming assets, which includes nonaccrual loans and leases and other real estate, totaled \$1.4 million at September 30, 2019, compared to \$2.7 million at December 31, 2018. There were no nonperforming loans classified as held for sale at September 30, 2019 and December 31, 2018. The decrease in nonperforming assets from December 31, 2018 was primarily attributable to \$2.2 million in repayments of nonaccrual loans and \$0.1 million in net charge-offs, valuation and other adjustments, offset by four additions to nonperforming assets totaling \$0.9 million.

Troubled debt restructurings ("TDRs") included in nonperforming assets at September 30, 2019 consisted of one Hawaii residential mortgage loan with a combined principal balance of \$0.3 million.

Concessions made to the original contractual terms of these loans consisted primarily of the deferral of interest and/or principal payments due to deterioration in the borrowers' financial condition. The principal balances on these TDRs had matured and/or were in default at the time of restructure and we have no commitments to lend additional funds to any of these borrowers. There were \$8.9 million of TDRs still accruing interest at September 30, 2019, none of which were more than 90 days delinquent. At December 31, 2018, there were \$12.9 million of TDRs still accruing interest, none of which were more than 90 days delinquent.

## Allowance for Loan and Lease Losses

The following table sets forth certain information with respect to the Allowance as of the dates and for the periods indicated:

(dollars in thousands)	Three Months Ended September 30,		Nine Months Ended September 30,	
	2019	2018	2019	2018
<b>Allowance for Loan and Lease Losses:</b>				
Balance at beginning of period	\$ 48,267	\$ 48,181	\$ 47,916	\$ 50,001
Provision (credit) for loan and lease losses	1,532	(59)	4,219	262
Charge-offs:				
Commercial, financial and agricultural	797	731	2,099	1,971
Real estate:				
Home equity	5	—	5	—
Consumer	1,832	1,762	5,542	5,424
Total charge-offs	2,634	2,493	7,646	7,395
Recoveries:				
Commercial, financial and agricultural	362	578	910	1,017
Real estate:				
Construction	6	6	604	1,205
Residential mortgage	104	51	498	98
Home equity	24	6	42	18
Commercial mortgage	—	8	25	52
Consumer	506	548	1,599	1,568
Total recoveries	1,002	1,197	3,678	3,958
Net charge-offs	1,632	1,296	3,968	3,437
Balance at end of period	\$ 48,167	\$ 46,826	\$ 48,167	\$ 46,826
Allowance as a percentage of total loans and leases	1.10%	1.18%	1.10%	1.18%
Annualized ratio of net charge-offs to average loans and leases	0.15%	0.13%	0.13%	0.12%

Our Allowance at September 30, 2019 totaled \$48.2 million compared to \$47.9 million at December 31, 2018. During the three months ended September 30, 2019, we recorded Provision expense of \$1.5 million primarily due to the increase in our loan portfolio and reflects net charge-offs of \$1.6 million. During the nine months ended September 30, 2019, we recorded Provision expense of \$4.2 million primarily due to the increase in our loan portfolio and reflects net charge-offs of \$4.0 million.

Our Allowance as a percentage of total loans and leases decreased from 1.17% at December 31, 2018 to 1.10% at September 30, 2019. The decrease in our Allowance as a percentage of total loans and leases reflects the credit quality of the loan portfolio, real estate markets and general economic conditions both in Hawaii and the U.S. Mainland. Our Allowance as a percentage of nonperforming assets increased from 1,751% at December 31, 2018 to 3,542% at September 30, 2019.

In accordance with GAAP, loans held for sale and other real estate assets are not included in our assessment of the Allowance.

## Federal Home Loan Bank Stock

The bank is a member of the Federal Home Loan Bank of Des Moines (the "FHLB"). FHLB stock of \$17.2 million at September 30, 2019 increased by \$0.5 million, or 3.2%, from the FHLB stock balance at December 31, 2018. FHLB stock has an activity-based stock requirement, thus as borrowings increase, so will our holdings of FHLB stock. There is a minimum requirement of \$7.0 million in FHLB stock even if we have no borrowings outstanding.

## Deposits

The following table sets forth the composition of our deposits by category for the periods indicated:

(dollars in thousands)	September 30, 2019	December 31, 2018	\$ Change	% Change
Noninterest-bearing demand deposits	\$ 1,399,200	\$ 1,436,967	\$ (37,767)	(2.6)%
Interest-bearing demand deposits	998,037	954,011	44,026	4.6
Savings and money market deposits	1,593,738	1,448,257	145,481	10.0
Time deposits less than \$100,000	165,687	176,707	(11,020)	(6.2)
Core deposits	4,156,662	4,015,942	140,720	3.5
Government time deposits	552,470	631,293	(78,823)	(12.5)
Other time deposits \$100,000 to \$250,000	103,959	106,783	(2,824)	(2.6)
Other time deposits greater than \$250,000	224,568	192,472	32,096	16.7
Total time deposits \$100,000 and greater	880,997	930,548	(49,551)	(5.3)
Total deposits	\$ 5,037,659	\$ 4,946,490	\$ 91,169	1.8

Total deposits of \$5.04 billion at September 30, 2019 increased by \$91.2 million from total deposits of \$4.95 billion at December 31, 2018. Net increases in savings and money market deposits of \$145.5 million, interest-bearing demand deposits of \$44.0 million and other time deposits greater than \$250,000 of \$32.1 million, were partially offset by net decreases in government time deposits of \$78.8 million, noninterest-bearing demand deposits of \$37.8 million and time deposits less than \$100,000 of \$11.0 million.

Core deposits, which we define as demand deposits, savings and money market deposits, and time deposits less than \$100,000, totaled \$4.16 billion at September 30, 2019 and increased by \$140.7 million, or 3.5%, from December 31, 2018. Core deposits as a percentage of total deposits was 82.5% at September 30, 2019, compared to 81.2% at December 31, 2018.

## **Capital Resources**

In order to ensure adequate levels of capital, we conduct an ongoing assessment of projected sources and uses of capital in conjunction with an analysis of the size and quality of our assets, the level of risk and regulatory capital requirements. As part of this ongoing assessment, the Board of Directors reviews our capital position on an ongoing basis to ensure it is adequate, including, but not limited to, need for raising additional capital or returning capital to our shareholders, including the ability to declare cash dividends or repurchase our securities.

## Common and Preferred Equity

Shareholders' equity totaled \$525.2 million at September 30, 2019, compared to \$491.7 million at December 31, 2018. The change in total shareholders' equity was attributable to net income of \$44.1 million and other comprehensive income of \$28.3 million, partially offset by the repurchase of 631,300 shares of common stock under our repurchase program, at a cost of \$18.0 million and cash dividends paid of \$19.2 million in the nine months ended September 30, 2019. During the nine months ended September 30, 2019, we repurchased approximately 2.2% of our common stock outstanding as of December 31, 2018.

Our total shareholders' equity to total assets ratio was 8.79% at September 30, 2019, compared to 8.47% at December 31, 2018. Our book value per share was \$18.47 and \$16.97 at September 30, 2019 and December 31, 2018, respectively.

## Holding Company Capital Resources

CPF is required to act as a source of strength to the bank under the Dodd-Frank Act. CPF is obligated to pay its expenses and payments on its junior subordinated debentures which fund payments on the outstanding trust preferred securities.

CPF relies on the bank to pay dividends to fund its obligations. As of September 30, 2019, on a stand-alone basis, CPF had an available cash balance of approximately \$11.6 million in order to meet its ongoing obligations.

As a Hawaii state-chartered bank, the bank may only pay dividends to the extent it has retained earnings as defined under Hawaii banking law ("Statutory Retained Earnings"), which differs from GAAP retained earnings. As of September 30, 2019, the bank had Statutory Retained Earnings of \$61.5 million. On October 22, 2019, the Company's Board of Directors declared a cash dividend of \$0.23 per share on the Company's outstanding common stock, which was a 9.5% increase from the \$0.21 per share a year-ago.

Dividends are payable at the discretion of the Board of Directors and there can be no assurance that the Board of Directors will continue to pay dividends at the same rate, or at all, in the future. Our ability to pay cash dividends to our shareholders is subject to restrictions under federal and Hawaii law, including restrictions imposed by the FRB and covenants set forth in various agreements we are a party to, including covenants set forth in our subordinated debentures.

In the year ended December 31, 2018, the Company repurchased 1,155,157 shares of common stock, at a cost of \$32.8 million, under the Company's repurchase plan.

In June 2019, the Company's Board of Directors authorized the repurchase of up to \$30 million of its common stock from time to time in the open market or in privately negotiated transactions, pursuant to a newly authorized share repurchase program (the "Repurchase Plan"). The Repurchase Plan replaces and supersedes in its entirety the share repurchase program previously approved by the Company's Board of Directors, which had \$6.8 million in remaining repurchase authority. In the nine months ended September 30, 2019, a total of 631,300 shares of common stock, at a cost of \$18.0 million, were repurchased under the Company's stock repurchase plans. As of September 30, 2019, \$25.9 million remained available for repurchase under the Company's Repurchase Plan. The Company's Repurchase Plan has no expiration date.

## Trust Preferred Securities

On December 17, 2018, the Company completed the redemption of \$20.0 million in floating rate trust preferred securities of CPB Statutory Trust III ("Trust III") bearing an interest rate of three-month LIBOR plus 2.85% and maturing on December 17, 2033. The redemption price was 100% of the aggregate liquidation amount of the securities plus accumulated but unpaid distributions up to but not including the redemption date. The Company also redeemed \$0.6 million of common securities issued by Trust III and held by the Company, as a result of the concurrent redemption of 100% of the principal assets of Trust III, or \$20.6 million of the Company's junior subordinated debentures with an identical interest rate and maturity as the Trust III trust preferred securities. The redemption was pursuant to the optional prepayment provisions of the indenture. On January 9, 2019, Trust III was canceled with the state of Connecticut.

On January 7, 2019, the Company completed the redemption of \$20.0 million in floating rate trust preferred securities of CPB Capital Trust II ("Trust II") bearing an interest rate of three-month LIBOR plus 2.85% and maturing on October 7, 2033. The redemption price was 100% of the aggregate liquidation amount of the securities plus accumulated but unpaid distributions up to but not including the redemption date. The Company also redeemed \$0.6 million of common securities issued by Trust II and held by the Company, as a result of the concurrent redemption of 100% of the principal assets of Trust II, or \$20.6 million of the Company's junior subordinated debentures with an identical interest rate and maturity as the Trust II trust preferred securities. The redemption was pursuant to the optional prepayment provisions of the indenture. On January 22, 2019, Trust II was canceled with the state of Delaware.

As of September 30, 2019, we have two remaining statutory trusts, CPB Capital Trust IV ("Trust IV") and CPB Statutory Trust V ("Trust V"), which issued a total of \$50.0 million in floating rate trust preferred securities. The trust preferred securities, the underlying floating rate junior subordinated debentures that are the assets of Trusts IV and V, and the common securities issued by Trusts IV and V are redeemable in whole or in part on any interest payment date on or after December 15, 2009 for Trust IV and V, or at any time in whole but not in part within 90 days following the occurrence of certain events. Our obligations with respect to the issuance of the trust preferred securities constitute a full and unconditional guarantee by the Company of each trust's obligations with respect to its trust preferred securities. Subject to certain exceptions and limitations, we may elect from time to time to defer subordinated debenture interest payments, which would result in a deferral of dividend payments on the related trust preferred securities, for up to 20 consecutive quarterly periods without default or penalty.

## Regulatory Capital Ratios

General capital adequacy regulations adopted by the FRB and FDIC require an institution to maintain minimum leverage capital, Tier 1 risk-based capital, total risk-based capital, and common equity Tier 1 ("CET1") capital ratios. In addition to these uniform risk-based capital guidelines and leverage ratios that apply across the industry, the regulators have the discretion to set individual minimum capital requirements for specific institutions at rates significantly above the minimum guidelines and ratios. For a further discussion of the effect of forthcoming changes in required regulatory capital ratios, see the discussion in the "Business — Supervision and Regulation" sections of our 2018 Form 10-K.

The Company's and the bank's leverage capital, tier 1 risk-based capital, total risk-based capital, and CET1 risk-based capital ratios as of September 30, 2019 were above the levels required for a "well capitalized" regulatory designation.

The following table sets forth the Company's and the bank's capital ratios, as well as the minimum capital adequacy requirements applicable to all financial institutions as of the dates indicated.

(dollars in thousands)	Actual		Minimum Required for Capital Adequacy Purposes		Minimum Required to be Well Capitalized	
	Amount	Ratio	Amount	Ratio	Amount	Ratio
<b>Company</b>						
<b>At September 30, 2019:</b>						
Leverage capital	\$ 561,478	9.5%	\$ 235,781	4.0%		N/A
Tier 1 risk-based capital	561,478	12.6	267,821	6.0		N/A
Total risk-based capital	611,076	13.7	357,094	8.0		N/A
CET1 risk-based capital	511,478	11.5	200,865	4.5		N/A
<b>At December 31, 2018:</b>						
Leverage capital	\$ 570,260	9.9%	\$ 230,847	4.0%		N/A
Tier 1 risk-based capital	570,260	13.5	252,921	6.0		N/A
Total risk-based capital	619,419	14.7	337,228	8.0		N/A
CET1 risk-based capital	500,260	11.9	189,691	4.5		N/A
<b>Central Pacific Bank</b>						
<b>At September 30, 2019:</b>						
Leverage capital	\$ 550,913	9.4%	\$ 235,625	4.0%	\$ 294,531	5.0%
Tier 1 risk-based capital	550,913	12.4	267,577	6.0	356,770	8.0
Total risk-based capital	600,511	13.5	356,770	8.0	445,962	10.0
CET1 risk-based capital	550,913	12.4	200,683	4.5	289,875	6.5
<b>At December 31, 2018:</b>						
Leverage capital	\$ 533,166	9.3%	\$ 230,638	4.0%	\$ 288,298	5.0%
Tier 1 risk-based capital	533,166	12.7	252,667	6.0	336,889	8.0
Total risk-based capital	582,325	13.8	336,889	8.0	421,111	10.0
CET1 risk-based capital	533,166	12.7	189,500	4.5	273,722	6.5

## Asset/Liability Management and Interest Rate Risk

Our earnings and capital are sensitive to risk of interest rate fluctuations. Interest rate risk arises when rate-sensitive assets and rate-sensitive liabilities mature or reprice during different periods or in differing amounts. In the normal course of business, we are subjected to interest rate risk through the activities of making loans and taking deposits, as well as from our investment securities portfolio and other interest-bearing funding sources. Asset/liability management attempts to coordinate our rate-sensitive assets and rate-sensitive liabilities to meet our financial objectives.

Our Asset/Liability Management Policy seeks to maximize the risk-adjusted return to shareholders while maintaining consistently acceptable levels of liquidity, interest rate risk and capitalization. Our Asset/Liability Management Committee, or ALCO, monitors interest rate risk through the use of interest rate sensitivity gap, net interest income and market value of portfolio equity simulation and rate shock analyses. This process is designed to measure the impact of future changes in interest rates on net interest income and market value of portfolio equity. Adverse interest rate risk exposures are managed through the shortening or lengthening of the duration of assets and liabilities.

ALCO utilizes a detailed and dynamic simulation model to measure and manage interest rate risk exposures. The simulation process is designed to measure the impact of future changes in interest rates on net interest income and market value of portfolio equity and to allow ALCO to model alternative balance sheet strategies.

The following reflects our net interest income sensitivity analysis as of September 30, 2019, over a one-year horizon, assuming no balance sheet growth and given both a 100 bp upward and 100 bp downward parallel shift in interest rates.

Rate Change	Estimated Net Interest Income Sensitivity
+100 bp	1.99 %
-100 bp	(3.90)%

### Liquidity and Borrowing Arrangements

Our objective in managing liquidity is to maintain a balance between sources and uses of funds in order to economically meet the cash requirements of customers for loans and deposit withdrawals and participate in lending and investment opportunities as they arise. We monitor our liquidity position in relation to changes in loan and deposit balances on a daily basis to ensure maximum utilization, maintenance of an adequate level of readily marketable assets and access to short-term funding sources.

Core deposits have historically provided us with a sizable source of relatively stable and low cost funds, but are subject to competitive pressure in our market. In addition to core deposit funding, we also have access to a variety of other short-term and long-term funding sources, which include proceeds from maturities of our investment securities, as well as secondary funding sources such as the FHLB, secured repurchase agreements and the Federal Reserve discount window, available to meet our liquidity needs. While we historically have had access to these other funding sources, access to these sources may not be guaranteed and can be restricted in the future as a result of market conditions or the Company's and bank's financial position.

The bank maintained a \$1.80 billion line of credit with the FHLB as of September 30, 2019, compared to \$1.43 billion at December 31, 2018. We had \$205.0 million in short-term borrowings under this arrangement at September 30, 2019, compared to \$197.0 million at December 31, 2018. Letters of credit under this arrangement that are used to collateralize certain government deposits totaled \$118.9 million at September 30, 2019, compared to \$4.6 million at December 31, 2018. Long-term borrowings under this arrangement totaled \$50.0 million at September 30, 2019 and December 31, 2018. FHLB advances and standby letters of credit available at September 30, 2019 were secured by certain real estate loans with a carrying value of \$2.42 billion in accordance with the collateral provisions of the Advances, Security and Deposit Agreement with the FHLB. At September 30, 2019, \$1.43 billion was undrawn under this arrangement, compared to \$1.18 billion at December 31, 2018.

At September 30, 2019 and December 31, 2018, our bank had additional unused borrowings available at the Federal Reserve discount window of \$65.6 million and \$73.9 million, respectively. As of September 30, 2019 and December 31, 2018, certain commercial and commercial real estate loans with a carrying value totaling \$118.9 million and \$123.3 million, respectively, were pledged as collateral on our line of credit with the Federal Reserve discount window. The Federal Reserve does not have the right to sell or repledge these loans.

Our ability to maintain adequate levels of liquidity is dependent on our ability to continue to maintain our strong risk profile and capital base. Our liquidity may also be negatively impacted by weakness in the financial markets and industry-wide reductions in liquidity.

### Contractual Obligations

Information regarding our contractual obligations is provided in "Part II, Item 7. Management's Discussion and Analysis of Financial Condition and Results of Operations" of our Annual Report on Form 10-K for the year ended December 31, 2018. During the first quarter of 2019, the Company signed an extension to its existing agreement with a computer software vendor.

This extension increases the Company's contractual obligations for the years 2022 through 2024 by approximately \$6 million per year. There have been no other material changes in our contractual obligations since December 31, 2018.

### **Item 3. Quantitative and Qualitative Disclosures about Market Risk**

Market risk is the risk of loss in a financial instrument arising from adverse changes in market rates/prices such as interest rates, foreign currency rates, commodity prices and equity prices. Our primary market risk exposure is interest rate risk that occurs when rate-sensitive assets and rate-sensitive liabilities mature or reprice during different periods or in differing amounts. Asset/liability management attempts to coordinate our rate-sensitive assets and rate-sensitive liabilities to meet our financial objectives. The Asset/Liability Committee ("ALCO") monitors interest rate risk through the use of interest rate sensitivity gap, net interest income and market value of portfolio equity simulation, and rate shock analyses. Adverse interest rate risk exposures are managed through the shortening or lengthening of the duration of assets and liabilities.

The primary analytical tool we use to measure and manage our interest rate risk is a simulation model that projects changes in net interest income ("NII") as market interest rates change. Our ALCO policy requires that simulated changes in NII should be within certain specified ranges, or steps must be taken to reduce interest rate risk. The results of the model indicate that the mix of rate-sensitive assets and liabilities at September 30, 2019 would not result in a fluctuation of NII that would exceed the established policy limits.

### **Item 4. Controls and Procedures**

#### **Evaluation of Disclosure Controls and Procedures**

As of the end of the period covered by this report and pursuant to Rule 13a-15 of the Securities Exchange Act of 1934, as amended, (the "Exchange Act"), the Company's management, including the principal executive officer and principal financial officer, conducted an evaluation of the effectiveness and design of the Company's disclosure controls and procedures (as that term is defined in Rules 13a-15(e) and 15d-15(e) of the Exchange Act). Based upon that evaluation, the Company's principal executive officer and principal financial officer concluded, as of the end of the period covered by this report, that the Company's disclosure controls and procedures were effective.

#### **Changes in Internal Control Over Financial Reporting**

As of the end of the period covered by this report, there have been no changes in the Company's internal control over financial reporting (as defined in Rule 13a-15(f) and 15d-15(f) of the Exchange Act) during the quarter to which this report relates that have materially affected or are reasonably likely to materially affect, our internal control over financial reporting.

## PART II. OTHER INFORMATION

### Item 1A. Risk Factors

There have been no material changes from the Risk Factors as previously disclosed in our Annual Report on Form 10-K for the year ended December 31, 2018, as filed with the SEC on February 28, 2019, except as described below.

#### *Our RISE2020 initiative may not be successful.*

During the second half of 2019 and throughout 2020, we intend to invest an aggregate of approximately \$40 million to upgrade our branch spaces, digital banking platforms and ATM network through a new initiative we call RISE2020. RISE2020 is intended to enhance customer experience, drive stronger long-term growth and profitability, improve shareholder returns and lower our efficiency ratio. However, we cannot provide any assurance that RISE2020 will achieve any of our objectives or will achieve our objectives to the extent we have forecasted. In particular, the costs of RISE2020 may exceed our expectations; we may not be able to attract new business from existing customers; new customers may not be attracted to our platform despite the amount of expense we incur; and implementation of RISE2020 initiatives may disrupt our operations. If our RISE2020 initiative is not successful, our overall noninterest expense will have increased without a corresponding increase in revenue and growth which could have a material adverse effect on our business, financial condition or results of operations.

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

#### Issuer Purchases of Equity Securities

In June 2019, the Company's Board of Directors authorized the repurchase of up to \$30 million of its common stock from time to time in the open market or in privately negotiated transactions, pursuant to a newly authorized share repurchase program (the "Repurchase Plan"). The Repurchase Plan replaces and supersedes in its entirety the share repurchase program previously approved by the Company's Board of Directors, which had \$6.8 million in remaining repurchase authority.

In the three months ended September 30, 2019, the Company repurchased 140,600 shares of common stock, at an aggregate cost of \$4.0 million, under the Company's stock repurchase plans. As of September 30, 2019, a total of \$25.9 million remained available for repurchase under the Company's Repurchase Plan. There is no expiration date on the Repurchase Plan.

Period	Issuer Purchases of Equity Securities			
	Total Number of Shares Purchased	Average Price Paid per Share	Total Shares Purchased as Part of Publicly Announced Programs	Maximum Dollar Value of Shares That May Yet Be Purchased Under the Program
July 1-31, 2019	11,100	\$ 29.74	11,100	\$ 29,612,363
August 1-31, 2019	67,000	28.34	67,000	27,713,654
September 1-30, 2019	62,500	28.58	62,500	25,927,436
Total	140,600	\$ 28.56	140,600	25,927,436

**Item 6. Exhibits**

<b>Exhibit No.</b>	<b>Document</b>
31.1	<a href="#">Rule 13a-14(a) Certification of Chief Executive Officer in accordance with Section 302 of the Sarbanes-Oxley Act of 2002 *</a>
31.2	<a href="#">Rule 13a-14(a) Certification of Chief Financial Officer in accordance with Section 302 of the Sarbanes-Oxley Act of 2002 *</a>
32.1	<a href="#">Section 1350 Certification of Chief Executive Officer in accordance with Section 906 of the Sarbanes-Oxley Act of 2002 **</a>
32.2	<a href="#">Section 1350 Certification of Chief Financial Officer in accordance with Section 906 of the Sarbanes-Oxley Act of 2002 **</a>
101.INS	XBRL Instance Document*
101.SCH	XBRL Taxonomy Extension Schema Document*
101.CAL	XBRL Taxonomy Extension Calculation Linkbase Document*
101.LAB	XBRL Taxonomy Extension Label Linkbase Document*
101.PRE	XBRL Taxonomy Extension Presentation Linkbase Document*
101.DEF	XBRL Taxonomy Extension Definition Linkbase Document*

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\* Filed herewith.

\*\* Furnished herewith.

**SIGNATURES**

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

CENTRAL PACIFIC FINANCIAL CORP.  
(Registrant)

Date: November 5, 2019

/s/ Paul K. Yonamine

Paul K. Yonamine  
Chairman and Chief Executive Officer

Date: November 5, 2019

/s/ David S. Morimoto

David S. Morimoto  
Executive Vice President and Chief Financial Officer

**Rule 13a-14(a) Certification of Chief Executive Officer in  
Accordance with Section 302 of the Sarbanes-Oxley Act of 2002**

I, Paul K. Yonamine, Chairman and Chief Executive Officer of Central Pacific Financial Corp. (the "Company"), certify that:

- (1) I have reviewed this quarterly report on Form 10-Q of the Company;
- (2) Based on my knowledge, this quarterly report does not contain any untrue statement of a material fact or omit to state a material fact necessary to make the statements made, in light of the circumstances under which such statements were made, not misleading with respect to the period covered by this quarterly report;
- (3) Based on my knowledge, the financial statements, and other financial information included in this quarterly report, fairly present in all material respects the financial condition, results of operations and cash flows of the Company as of, and for, the periods presented in this quarterly report;
- (4) The Company's other certifying officer and I are responsible for establishing and maintaining disclosure controls and procedures (as defined in Exchange Act Rules 13a-15(e) and 15d-15(e)) and internal control over financial reporting (as defined in Exchange Act Rules 13a-15(f) and 15d-15(e)) for the Company and we have:
  - (a) designed such disclosure controls and procedures, or caused such disclosure controls and procedures to be designed under our supervision to ensure that material information relating to the Company, including its consolidated subsidiaries, is made known to us by others within those entities, particularly during the period in which this quarterly report is being prepared;
  - (b) designed such internal control over financial reporting, or caused such internal control over financial reporting to be designed under our supervision, to provide reasonable assurance regarding the reliability of financial reporting and the preparation of financial statements for external purposes in accordance with generally accepted accounting principles;
  - (c) evaluated the effectiveness of the Company's disclosure controls and procedures and presented in this report our conclusions about the effectiveness of the disclosure controls and procedures as of the end of the period covered by this quarterly report based on such evaluation; and
  - (d) disclosed in this quarterly report any change in the Company's internal control over financial reporting that occurred during the Company's most recent fiscal quarter that has materially affected, or is reasonably likely to materially affect, the Company's internal control over financial reporting; and
- (5) The Company's other certifying officer and I have disclosed, based on our most recent evaluation of internal control over financial reporting, to the Company's auditors and the audit committee of the Company's board of directors (or persons performing the equivalent functions):
  - (a) all significant deficiencies and material weaknesses in the design or operation of internal control over financial reporting which are reasonably likely to adversely affect the Company's ability to record, process, summarize and report financial information; and
  - (b) any fraud, whether or not material, that involves management or other employees who have a significant role in the Company's internal control over financial reporting.

Date: November 5, 2019

/s/ Paul K. Yonamine

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Paul K. Yonamine

Chairman and Chief Executive Officer

**Rule 13a-14(a) Certification of Chief Financial Officer in  
Accordance with Section 302 of the Sarbanes-Oxley Act of 2002**

I, David S. Morimoto, Executive Vice President and Chief Financial Officer of Central Pacific Financial Corp. (the "Company"), certify that:

- (1) I have reviewed this quarterly report on Form 10-Q of the Company;
- (2) Based on my knowledge, this quarterly report does not contain any untrue statement of a material fact or omit to state a material fact necessary to make the statements made, in light of the circumstances under which such statements were made, not misleading with respect to the period covered by this quarterly report;
- (3) Based on my knowledge, the financial statements, and other financial information included in this quarterly report, fairly present in all material respects the financial condition, results of operations and cash flows of the Company as of, and for, the periods presented in this quarterly report;
- (4) The Company's other certifying officer and I are responsible for establishing and maintaining disclosure controls and procedures (as defined in Exchange Act Rules 13a-15(e) and 15d-15(e)) and internal control over financial reporting (as defined in Exchange Act Rules 13a-15(f) and 15d-15(e)) for the Company and we have:
  - (a) designed such disclosure controls and procedures, or caused such disclosure controls and procedures to be designed under our supervision to ensure that material information relating to the Company, including its consolidated subsidiaries, is made known to us by others within those entities, particularly during the period in which this quarterly report is being prepared;
  - (b) designed such internal control over financial reporting, or caused such internal control over financial reporting to be designed under our supervision, to provide reasonable assurance regarding the reliability of financial reporting and the preparation of financial statements for external purposes in accordance with generally accepted accounting principles;
  - (c) evaluated the effectiveness of the Company's disclosure controls and procedures and presented in this report our conclusions about the effectiveness of the disclosure controls and procedures as of the end of the period covered by this quarterly report based on such evaluation; and
  - (d) disclosed in this quarterly report any change in the Company's internal control over financial reporting that occurred during the Company's most recent fiscal quarter that has materially affected, or is reasonably likely to materially affect, the Company's internal control over financial reporting; and
- (5) The Company's other certifying officer and I have disclosed, based on our most recent evaluation of internal control over financial reporting, to the Company's auditors and the audit committee of the Company's board of directors (or persons performing the equivalent functions):
  - (a) all significant deficiencies and material weaknesses in the design or operation of internal control over financial reporting which are reasonably likely to adversely affect the Company's ability to record, process, summarize and report financial information; and
  - (b) any fraud, whether or not material, that involves management or other employees who have a significant role in the Company's internal control over financial reporting.

Date: November 5, 2019

/s/ David S. Morimoto

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David S. Morimoto

Executive Vice President and Chief Financial Officer  
(Principal Financial and Accounting Officer)

**Section 1350 Certification of Chief Executive Officer in  
Accordance with Section 906 of the Sarbanes-Oxley Act of 2002**

In connection with the Quarterly Report of Central Pacific Financial Corp. (the "Company") on Form 10-Q for the period ended September 30, 2019 as filed with the Securities and Exchange Commission on the date hereof (the "Report"), I, Paul K. Yonamine, Chairman and Chief Executive Officer, certify, pursuant to 18 U.S.C. Section 1350, as adopted pursuant to Section 906 of the Sarbanes-Oxley Act of 2002, that to my knowledge:

- (1) The Report fully complies with the requirements of Section 13(a) or 15(d) of the Securities Exchange Act of 1934; and
- (2) The information contained in the Report fairly presents, in all material aspects, the financial condition and results of operations of the Company.

Date: November 5, 2019

/s/ Paul K. Yonamine

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Paul K. Yonamine

Chairman and Chief Executive Officer

A signed original of this written statement required by Section 906 has been provided to the Company and will be retained by the Company and furnished to the Securities and Exchange Commission or its staff upon request.

This certification accompanies the Report pursuant to Section 906 of the Sarbanes-Oxley Act of 2002 and shall not be deemed filed by the Company for purposes of Section 18 of the Securities Exchange Act of 1934, as amended.

**Section 1350 Certification of Chief Financial Officer in  
Accordance with Section 906 of the Sarbanes-Oxley Act of 2002**

In connection with the Quarterly Report of Central Pacific Financial Corp. (the "Company") on Form 10-Q for the period ended September 30, 2019 as filed with the Securities and Exchange Commission on the date hereof (the "Report"), I, David S. Morimoto, Executive Vice President and Chief Financial Officer, certify, pursuant to 18 U.S.C. Section 1350, as adopted pursuant to Section 906 of the Sarbanes-Oxley Act of 2002, that to my knowledge:

- (1) The Report fully complies with the requirements of Section 13(a) or 15(d) of the Securities Exchange Act of 1934; and
- (2) The information contained in the Report fairly presents, in all material aspects, the financial condition and results of operations of the Company.

Date: November 5, 2019

/s/ David S. Morimoto

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David S. Morimoto

Executive Vice President and Chief Financial Officer

(Principal Financial and Accounting Officer)

A signed original of this written statement required by Section 906 has been provided to the Company and will be retained by the Company and furnished to the Securities and Exchange Commission or its staff upon request.

This certification accompanies the Report pursuant to Section 906 of the Sarbanes-Oxley Act of 2002 and shall not be deemed filed by the Company for purposes of Section 18 of the Securities Exchange Act of 1934, as amended.