CIT Group, Inc.

First Quarter 2018 Earnings Conference Call

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CORPORATE PARTICIPANTS

Barbara Callahan - *Head, Investor Relations*

Ellen Alemany - *Chairwoman and Chief Executive Officer*

John Fawcett - *Executive Vice President and Chief Financial Officer*

Robert Rowe - *Executive Vice President and Chief Risk Officer*

PRESENTATION

Operator
Good morning, and welcome to CIT's First Quarter 2018 Earnings Conference Call. My name is Denise and I will be your Operator today. At this time, all participants are in a listen-only mode. There will be a question and answer session later in the call. At that time, if you would like to ask a question, you may press star, then one on your telephone keypad. To withdraw from the question queue, please press star, then two. Please note that this call is being recorded. If at any time you require assistance, please press star, zero and an Operator will be happy to assist you.

At this time, I would like to turn the call over to Barbara Callahan, Head of Investor Relations. Please proceed, ma'am.

Barbara Callahan
Thank you, Denise. Good morning, and welcome to CIT's First Quarter 2018 Earnings Conference Call. Our call today will be hosted by Ellen Alemany, Chairwoman and CEO, and John Fawcett, our CFO. After Ellen and John's prepared remarks, we will have a question and answer session. Also joining us for the Q&A discussion is our Chief Risk Officer, Rob Rowe.

As a courtesy to others on the call, we ask that you limit yourself to one question and a follow-up, and then return to the call queue if you have additional questions. We will do our best to answer as many questions as possible in the time we have this morning.

Elements of this call are forward-looking in nature and may involve risks, uncertainties and contingencies that may cause actual results to differ materially from those anticipated. Any forward-looking statements relate only to the time and date of this call. We disclaim any duty to update these statements based on new information, future events or otherwise. For information about risk factors relating to the business, please refer to our 2017 10-K.

Any references to non-GAAP financial measures are meant to provide meaningful insights and are reconciled with GAAP in our press release.

Also, as part of the call this morning, we will be referencing a presentation that is available on the Investor Relations section of our website at www.cit.com.

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

Ellen Alemany
Thank you, Barbara. Good morning, everyone, and thank you for joining the call. The first quarter was another period for solid progress for CIT as we advanced our strategic plan. We posted strong growth in our core business, continued to expand the Direct Bank and further optimize capital. Net income in the quarter was $97 million or $0.74 per common share, and income from continuing operations was $104 million or $0.79 per share. While credit performance was generally stable, we did post an increase in provisions that was primarily driven by a single commercial exposure and that affected results. Credit reserves remain strong, and John will walk you through more details shortly.

On Slide 2, you can see an overview of our progress in the quarter. At the top of our list is to maximize the potential of our core businesses, and I'm pleased to say that in the first quarter our average core portfolios grew 2% quarter-over-quarter. This marks the second consecutive quarter of strong growth.

As I have previously shared, last year we took a number of steps to build on our core capabilities by expanding into additional market segments, adding talent and investing in our franchises. We are now beginning to see some early results of those efforts. Our originations volume was up significantly from the first quarter of last year, and part of that growth is from our new initiatives.

Let me spend a minute on each of our business areas.

Average loan and leases in the Commercial Finance business were up 4%, compared to the prior quarter, fueled mainly by the C&I, energy and healthcare verticals, as well as the newly formed Aviation Lending Group. The marketplace remains competitive and we continue to be disciplined, but we also have some distinct competitive advantages; namely, our deep industry expertise and relationships in the middle market. For example, when we decided to relaunch the Aviation business, it was built on a 30-year presence in that industry. It allows us to hit the ground running and deliver results.

Average loans and leases were up approximately 3% in the equipment financing areas within Business Capital, as customers' sentiment in the economy remained positive and spending levels remain strong. Growth was led by the capital equipment, industrial, technology and lender finance areas, as well as our Small Digital Business Lending Division.

The Real Estate Finance operation posted modest growth in the core business and continues to take a prudent approach to a highly competitive market. We have a very experienced team and we are picking our spots in this area thoughtfully.

In the Rail business, we continue to manage through the cycle. We did see utilization rates tick up in the quarter to 97%, but lease renewal rates continue to be impacted by oversupply in certain industries. We have a young and diverse fleet and are focused on our strengths in portfolio management and customer service.

Overall, our Commercial businesses are well positioned in their respective segments of the marketplace and our plan is advancing.

In addition, the strategic transactions continue to progress. We expect the NACCO sale to close in the second half of the year, and this transaction supports our efforts to exit overseas operations. We are targeting the end of the second quarter for the Financial Freedom sale, pending regulatory approval. This transaction supports our plan to simplify the Company and focus on our core strengths.

We remain committed to achieving our operating expense target despite elevated annual benefit costs and higher legal expenses this quarter.

Our deposit strategy has seen positive results despite the rising rate environment. On average, deposits grew more than $400 million and average deposit costs are up to just five basis points from last quarter. We are thoughtfully managing deposit pricing and achieving a more balanced mix of products, with a greater focus on non-maturity products. The Direct Bank is an important driver of our deposit strategy and this was a very strong quarter for the franchise, with $1.5 billion in deposit growth and 28,000 new customers. The high yield savings account continues to be successful and we just launched the new money market account that is off to a strong start. The Southern California retail branch network provided additional balance to the deposit mix and posted modest growth quarter-over-quarter.

We took several positive steps to optimize the capital structure during the quarter. In February, we received a non-objection to our amended capital plan, which will allow us to increase the capital return in the first half of the year by up to $900 million. Part of that plan was conditioned on the issuance of $400 million of sub-debt, and that has been completed. In addition, we repurchased 3.7 million shares of common stock for $195 million in the first quarter. We are committed to returning the remaining capital in the plan as prudently and efficiently as possible by the end of the second quarter. Lastly, we remain focused on a disciplined approach to risk management.

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

John Fawcett
Thank you, Ellen, and good morning, everyone. Turning to our results on Page 3 of the presentation, we posted GAAP net income for the quarter of $97 million, or $0.74 per common share, and income from continuing operations of $104 million, or $0.79 per common share. Operating performance this quarter reflected strong new business volume in all our core lending businesses and lower prepayments, which resulted in 1.7% total average loan and lease growth and 2.3% growth in our core portfolios, compared to the prior quarter. Net income was negatively impacted this quarter from the charge-off of a single commercial exposure and a higher level of reserves, primarily within our Commercial Finance Division.

As shown on Page 4 of the presentation, our financial results included a single noteworthy item, which was a $7 million after-tax benefit from suspended depreciation related to the pending NACCO disposition. With regard to the NACCO disposition, all remaining antitrust approvals were received by the buyer from the European regulators this quarter, which includes a condition to sell approximately 30% of the NACCO cars to other parties. This additional requirement does not impact the overall economics to us and we expect to close the sale in the second half of 2018.

Turning to Page 5, income from continuing operations available to common shareholders, excluding noteworthy items, was $97 million or $0.74 per common share this quarter. This is down from $130 million or $0.99 per common share last quarter and from $109 million or $0.54 per common share in the year ago quarter.

I will now go into further detail on our financial results for the quarter. Please note that in this discussion I will refer to our results from continuing operations excluding noteworthy items, unless otherwise noted.

Turning to Page 6 of the presentation, net finance revenue was down $9 million from the prior quarter and net finance margin declined by 14 basis points. Compared to the year ago quarter, net finance revenue was down $35 million and the margin was down 20 basis points. Purchase accounting accretion net of negative interest income on the indemnification asset, or net PAA, declined from both the year ago quarter and the prior quarter. We expect the purchase accounting accretion to continue to decline as the portfolio runs off. This quarter, we recognized about $32 million in purchase accounting accretion, down from $40 million last quarter and $56 million in the year ago quarter. The reduction is primarily in Commercial Banking, where assets have a shorter remaining life than in Consumer Banking. This quarter, Commercial Banking recognized $11 million of purchase accounting accretion, compared to $16 million last quarter and $24 million in the year ago quarter. We continue to see a reduction in PAA as the portfolios run off. We now have approximately $700 million in total PAA remaining, of which almost $650 million relates to the legacy consumer mortgage portfolio, which runs off at about 10% to 15% annually. The remaining $85 million relates to Commercial Finance and Real Estate Finance, and we are forecasting 40% to 50% of it to accrete over the next four quarters.

The negative interest income on the indemnification asset declined slightly to $14 million this quarter. We expect the negative interest income to continue to decline modestly each quarter, until the loss share agreement expires in the first quarter of 2019.

Excluding the impact of net PAA, our core net finance revenue was down modestly, reflecting higher yields on our loans and investments, which was more than offset by lower prepayment-related fees and higher interest expense. Net finance revenue also included approximately $2 million in negative carry from the senior unsecured debt issuance and the corresponding redemption activity that required 30 days notice.

In early March, we issued $1 billion of senior unsecured debt in two $500 million tranches, including a three-year tranche with a 4⅛% coupon and a seven-year tranche with a 5.25% coupon, for a weighted average net coupon of 4.69%. On April 9, we used the proceeds to redeem almost $900 million of senior unsecured debt due in early 2019 that had an average coupon of 4.58%. While the refinancing modestly increased our overall senior unsecured debt costs to 4.83% from 4.81%, we extended our 2019 maturities into 2021 and 2025. We will continue to look for opportunities to further repay or refinance unsecured debt. In March, we also issued $400 million of Tier 2 qualifying subordinated debt with a 10-year maturity at 6⅛% related to our amended capital plan. We expect to deploy the proceeds over the course of this quarter as we return excess capital to shareholders.

Turning to Page 7, net finance margin declined by 14 basis points this quarter to 3.37%. Nine basis points of the decline were from lower net purchase accounting accretion and lower net prepayments, which mostly impacted Commercial Banking. Higher borrowing costs reduced margin by five basis points, most of which was driven by the aforementioned unsecured debt issuance. Deposit rates increased across all of the channels this quarter, reducing margin by three basis points, while higher yields on loans, investments and mix increased margin by six basis points.

Lower net operating lease revenue from our Rail business continues to reduce our margin. Rail utilization in our North American business increased to almost 97% this quarter, while rail renewal rates, on average, repriced down 32%, reflecting the mix of cars renewing. We continue to expect leases to reprice down an average of 20% to 30% through 2018 and into 2019, reflecting continued pressure from tank car lease rates, which are renewing at a faster pace. The team is doing a good job finding new opportunities for our tank cars and, while lease rates have stabilized, they are coming off peak levels.

Compared to the year ago quarter, the decline in net finance margin was primarily due to the same trends I just described.

Turning to Page 8, other non-interest income was down slightly from a seasonally strong fourth quarter, as lower fees, factoring commissions and gains on investment securities were mostly offset by higher gains on sales of leasing equipment and other revenue. Compared to last year, other non-interest income is up significantly, reflecting higher gains on sales of leasing equipment, income from BOLI and gains on derivative activity. Fee income was down from the prior and year ago quarters, resulting from prior capital markets fees, which can be uneven throughout the year. While factoring volumes have increased year-over-year, commissions were down, reflecting the mix of services provided and lower pricing.

We are now presenting the gains on leasing equipment and investment securities lines net of any impairments. The increase in gains on leasing equipment this quarter reflected modestly higher gains on rail equipment and higher end-of-lease activity in our Capital Equipment Finance business. Gains on investment securities declined this quarter, as we have worked through about two-thirds of the optimization of higher risk-weighted investment securities acquired with the OneWest acquisition.

Consistent with last quarter, we had $7 million in net gains in other revenue related to the reverse mortgage portfolio that is being sold with the Financial Freedom servicing operations. When the reverse mortgages were moved to held-for-sale in the third quarter of last year, we stopped accreting the related purchase discount in interest income. This reduction, however, was more than offset by gains from loan payoffs, liquidations and sales recognized in other revenue, which will continue until the portfolio is sold. The buyer is continuing to work to obtain the required regulatory and investor approvals. We are still working to close the sale of Financial Freedom in the second quarter, but the timing is now targeted to be closer to the end of the second quarter.

Also, as I had previously indicated, we anticipated recognizing a pre-tax gain at closing of $25 million of $35 million net of transaction costs and before any incremental indemnification obligation, but that amount may vary depending on the timing of the close and the performance of the portfolio. Given that we are now targeting a close later in the second quarter, the projected gain may be reduced by the income recognized from the continued runoff of the portfolio.

Turning to Page 9, operating expenses increased from the prior quarter and reflect approximately $10 million from payroll and benefit restarts, and legal accruals. In addition, you may recall I mentioned that last quarter benefited from a reversal of a litigation provision, as well as a true-up of FDIC insurance costs. Compared to a year ago, operating expenses declined, reflecting lower professional fees, while the reduction in occupancy costs, insurance costs and other expenses were mostly offset by higher advertising and marketing costs and compensation and benefits. The increase in compensation and benefits was driven by a number of factors, including higher revenue-generating business costs and higher benefit costs. While costs this quarter were higher than our target run rate, we remain on track to achieve our 2018 annual operating expense target of $1.050 billion. We expect operating expenses to decline modestly next quarter and more significantly in the second half of the year, with most of the reduction resulting from lower professional fees and lower compensation and benefit costs.

Page 10 describes our consolidated average balance sheet. Average earning assets were up $700 million, reflecting higher loans and leases. The increase in liabilities reflects deposit growth and our unsecured debt actions. The decline in equity reflects our stock repurchases and the impact of unrealized losses in our investment securities book that runs through OCI.

Page 11 provides more detail on average loans and leases by division.

Excluding NACCO, Commercial Banking's average loans and leases increased about 1.5% from the prior quarter, reflecting strong growth in Commercial Finance and a little over 1% from the year ago quarter, driven by Business Capital. In addition, while North American rail assets remained flat, growth in Rail was driven from the NACCO portfolio, as we continued to take delivery of cars from their order book.

The middle market, where we focus, continues to be challenging and we remain disciplined in a highly competitive environment, while finding opportunities where we can grow. In Commercial Finance, average loans and leases were up 4% this quarter, with strong volumes in healthcare, energy, C&I and aviation finance verticals, as well as overall lower prepayments.

While origination volumes were down from a strong fourth quarter, they were up significantly from the year ago quarter. In addition, asset-based originations remain over 50% of total new business volume, up from 40% last year, partially driven by our re-entry into Aviation Finance and our repositioning efforts.

Real Estate Finance remained flat this quarter and up 1%, excluding runoff from the legacy non-SFR portfolio. The market has become more competitive as CMBS and debt funds are more active. We are remaining disciplined in our new business originations.

North American Rail assets remained flat, as modest new deliveries were offset by depreciation. We increased our order book slightly this quarter to over $100 million and continue to expect new deliveries to be offset by portfolio management activities and depreciation.

Business Capital is flat compared to the prior quarter, with 3% growth across the equipment lending businesses, offset by a seasonal reduction in factored assets.

In Consumer Banking, growth in our other Consumer Banking businesses more than offset the runoff of the legacy consumer mortgage portfolio. Average loans in the mortgage lending business increased due to strong originations in the retail and correspondent lending channels. We also experienced an increase in loans from our SBA lending platform.

Page 12 highlights our average funding mix. Compared to the prior quarter, total borrowed funds and deposits increased, while the overall mix remained the same. Funding costs as a percent of average earning assets increased this quarter by eight basis points. Higher deposit costs contributed three basis points, while our debt actions in March and higher FHLB costs added five basis points to our borrowing costs. As I previously mentioned, we are taking a comprehensive approach to address the impact from the sale of NACCO, as well as other actions, including further reducing unsecured debt using excess liquidity and/or refinancing with lower cost debt, in order to improve our overall funding costs.

Page 13 illustrates the deposit mix by type and channel. Quarter-over-quarter, our average deposits increased approximately $400 million to $30.1 billion, reflecting 6% growth in our online channel, offset by a reduction in brokered and commercial deposits. We also increased the mix of non-maturity deposits in conjunction with our strategy to optimize deposits costs, while working within our risk management discipline. The cost of our deposits increased five basis points in the quarter. Cumulative deposit betas have remained low at approximately 10% since the Fed started raising rates at the end of 2015, and 20% over the last 12 months. We think deposit betas will continue to increase and we are modeling 65% to 75% through the cycle for non-maturity deposits, which are currently a little over 50% of our deposit base, and expected to grow over time.

Page 14 highlights our credit trends. The credit provision this quarter of $69 million was up from $30 million last quarter and $50 million compared to the year ago quarter. The increase reflects a $22 million charge-off of a single commercial exposure, primarily within Commercial Finance, that was episodic in nature. The provision also reflects a higher level of reserves, also within Commercial Finance Division. I would also point out that we are not seeing any overall deterioration in the credit environment. The increase in reserves this quarter were not concentrated within any particular industry or geography and we continue to originate new loans at a better risk rating than that of the overall performing portfolio.

As we have indicated in the past, given the low level of losses that we have been experiencing, a higher expected loss for a single credit can create significant volatility in our quarterly credit costs. Over the past five quarters, our provision has averaged approximately $35 million and we believe $30 million to $40 million is a more normalized level in the near term.

Net charge-offs were 68 basis points in the quarter, above our outlook range of 35 to 45 basis points. However, excluding the $22 million discrete charge-off mentioned, net charge-offs would have been 39 basis points, in line with our guidance. Non-accrual loans of $236 million, or 84 basis points of loans, remained low at the end of the quarter and were slightly higher than prior quarter, but down from the year ago quarter. Our reserves within Commercial Banking remain strong at 1.79% of finance receivables, which is about four times our annualized net charge-offs over the past five quarters.

Turning to capital, on Page 15, we received a non-objection to our amended capital plan in February, which enabled us to increase our capital return in the first half of this year by $800 million, of which $400 million was predicated on the issuance of Tier 2 qualifying subordinated debt. When added to the $100 million remaining at the end of 2017, we had up to $900 million of capital that can be returned to shareholders through June 3019. In the first quarter, we bought back $195 million, or 3.7 million shares at an average price of $53.16 per share. In the second quarter, through Friday, April 20, we've repurchased an additional 1.4 million shares at an average price of $51.86 per share. We intend to return the remaining capital of up to $635 million, inclusive of $25 million originally to be repurchased associated with employee stock plans, by the end of June, and we'll continue to review options to return the capital as efficiently and as prudently as possible.

Pro forma, for the remaining capital we expect to return through June 2018, our common equity Tier 1 ration will be around 12.5%, still above our target ratio of 10% to 11%, but much improved from our current common equity Tier ratio of 14%. We submitted our capital plan earlier this month. The results will become public by the end of June. We designed a plan to bring our common equity Tier 1 ratio closer to the targets we discussed last quarter, which were 11.5% to 12% by the end of 2018, and the upper end of our 10% to 11% target range by the end of 2019, while working within our risk management discipline.

Page 16 highlights our key performance metrics both on a reported basis, as well as excluding noteworthy items.

Our effective tax rate, excluding discrete items, was 27% this quarter, slightly higher than the 25% to 26% we guided to last quarter. The increase was mostly driven by higher forecasted state and local taxes as a result of the impact of U.S. tax reform and state tax law changes during the quarter. As a result, we are now forecasting the effective tax rate to be in the 26% to 28% range for 2018.

Our return on tangible common equity, excluding noteworthy items, of 6.4% was negatively impacted by our higher credit costs. Normalizing for the higher credit provision, ROTCE would have been around 8%.

Before I turn it back to Ellen, I wanted to give you some thoughts on the second quarter outlook, which is on Page 17. We expect total average earning assets to be relatively flat with low-single-digit quarterly growth in our core portfolios, mostly offset by runoff of the legacy consumer mortgage portfolio and sale of the reverse mortgage portfolio; we expect net finance margin to remain in the mid to upper end of the 2018 target range, depending upon the timing of the sale of the reverse mortgages; we expect operating expenses to be down, as it included about $10 million of elevated costs this quarter; we continue to expect net charge-offs to be within the annual target of 35 to 45 basis points, excluding any discrete items; and, as I mentioned, we expect the effective tax rate before the impact of discrete items to be 26% to 28%.

With that, let me turn it back to Ellen.

Ellen Alemany
Thank you, John. In closing, I want to say that we remain committed to achieving an 11% return on tangible common equity at the end of 2019. We are encouraged by the performance of our core businesses and believe CIT has a distinct value proposition in the markets we service. We are focused on continued progress on our plan and have demonstrated that we can consistently deliver on our objectives.

Now, let me turn it back to the Operator for question and answer.

QUESTIONS AND ANSWERS

Operator
Thank you, Ms. Alemany. We will now begin the question and answer session. To ask a question, you may press star, then one on your telephone keypad. If you are using a speaker-phone, please pick up your handset before pressing the keys. If your question has been addressed, you may withdraw from the queue by pressing star, then two.

The first question will come from Moshe Orenbuch of Credit Suisse. Please go ahead. Mr. Orenbuch, your line is open for your question.

James Ulan
Hey, guys. This is James Ulan on for Moshe. I was wondering if you can go into greater detail on growth in the Commercial Finance segment, as well as in Business Capital. I can see that Rail and Real Estate are roughly flat and I'm curious what your strategy is to grow those other two verticals, Commercial Finance and Business Capital.

Ellen Alemany
Sure, James. This is Ellen. Business Capital, I would say, if you look at our year-over-year growth, it's been very strong, and it really is reflecting overall confidence in market conditions. I think, overall, we're seeing positive sentiment from small business customers and that's really driving our growth. We also, just in Equipment Finance, which are all our vendor programs, we doubled volume in the last 12 months, mainly due to our investments in technology and industrial. We're also continuing to expand out our front end integration capabilities with major technology companies, and we think this is really unique proprietary technology. So, we are very optimistic and we believe that Business Capital should be one of our strongest growth areas this year.

In Commercial Finance, the fourth quarter of ’17 was really the inflection point for the asset levels in this business. We have a solid pipeline and we’re making continued progress against our new business initiatives. Most of the asset growth we saw this quarter was in healthcare real estate, aviation lending, energy and C&I. But, that being said, the competition for quality credits is very intense, there’s a lot of non-bank lenders out there that are taking market share, and, as we’ve mentioned in the past, leverage lending levels have moved above the guidance for banks. So, I think, overall, in Commercial Finance, the asset growth is really going to depend on market conditions, especially prepayments. I would also say that a lot of our volume comes from financial sponsors and M&A was down in the first quarter, but the pipeline is strong.

Then, Real Estate Finance, we’re just being really selective there. We recently had a reception where we had a lot of our real estate customers there. The price of real estate, just raw land is very, very high, and high end in New York, we’re not doing right now. But prepayments slowed in the first quarter for us, and I would say that we’re really just focusing on the core Northeast and Southern California.

Moshe Orenbuch
Okay, that’s very helpful, thank you, and if I could just ask a follow-up on credit. Can you go into a little bit of greater detail on not the specific credit item, but just more the increase in reserves for the broader portfolio, what’s causing that and what are your expectations for those drivers going forward?

Robert Rowe
In terms of the increase beyond the discrete event, which I would like to mention, to follow on from what John was saying, there were irregularities that were episodic in nature to that event, but in terms of the broader increase that we had, there’s no one industry, no one product type, so there’s no correlations that we’re seeing across the portfolio. It was just a number of names in our performing book that we decided to build reserves on during the first quarter. And that’s why decided to give guidance beyond just the charge-offs, but to give it to the provision, as well, to make it clear, from our perspective and from what we’re interpreting, that we think credit quality remains stable and what we think the expectations are for the balance of the year.

Moshe Orenbuch
Great. Thank you very much.

Robert Rowe
You’re welcome.

Operator
The next question will come from Chris Kotowski of Oppenheimer & Company. Please go ahead.

Chris Kotowski
On the capital repurchase plans, I guess I think the $635 million is a lot to do in the remaining time in the quarter. Previously, when you had a large amount of authorization, obviously, you did this kind of structured solution, and I’m wondering if you can talk a bit more about how you plan to get this done by the end of the quarter.

John Fawcett
Yes, I think we’re still working through the dynamics. I think there are two imperatives associated with the return of capital, the first is that we return the capital and the second is that

we return the capital by June 30, and so both of those things have to happen. In terms of the tools, we're obviously looking at everything, and have been looking at everything. We're looking, obviously, at the tender. We're looking at ASRs. We've been doing OMRs. I think the complication with OMRs, on a go-forward basis, is there's not enough average daily trading volume for us to actually get it out. If you look at where our stock is trading, or the number of shares that are actually trading on a daily basis, we'd probably need, on a good day, probably 90 trading days to actually move it, so we'll manage around the edges with OMR. Then, I would expect that at some point there might be a cash cleanup to the extent that a tender and ASR doesn't get everything out, but it's obviously something that we're looking at very closely. We understand that time is not on our side and we're going to have to make some decisions.

I would say that also, just in the context of timing, the capital plan was actually approved February 1' I think we announced it on February 2. There were some challenges in the market post February 2, and it wasn't until March 6 that we were actually able to get the sub-debt out the door, which was a large component of this, and then we went right into blackout. So, we're pretty mindful of what we have to do and how much time we have to do it.

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

Operator
The next question will come from Eric Wasserstrom of UBS. Please go ahead.

Eric Wasserstrom
Thanks. John, just a couple of follow-ups. What was your deposit beta in the period, because I was just doing some quick calculation on the change in average deposit balance and it looks like on the incremental it might have been about 35 basis points and Fed funds are moving about 34, so obviously that would imply a much higher beta than the 20 that you cited. So, could you just give some clarity to the beta in the period?

John Fawcett
Yes. So, on an overall basis, it's probably around—it's up, but it depends on product, it depends on channel, it depends on whether you're looking at brokered or commercial. I mean, clearly, the betas are much higher associated with the non-maturity deposits, and I think to the extent that a lot of growth that you're seeing is in our non-maturity portfolio, you would expect higher, more elevated betas. Beyond that, I don't know that's there much more that I want to say.

Eric Wasserstrom
Okay. Just so I understand, that 65 to 75 beta that you've cited, that's, on average, over the course of a year, or how do I interpret that figure?

John Fawcett
No, that's over the entire cycle. So, that's from the start of the Fed tightening through the entire cycle. I think on non-maturity deposits, you can imagine betas getting up to probably 75% in the non-maturity portfolio. I think, look, betas are going to move. It's going to be a function of competition in the marketplace. It's going to be a function of what happens on the left-hand side of the balance sheet and where we need the funding, so it really is a balancing act. I'm not trying to be evasive, but we're living in real time and it's just kind of hard to project where this is all is going to go, but I would say I think we've been pretty effective thus far in terms of when you look at the overall change in deposits. Clearly. I think last year our overall deposit costs grew five basis points and we saw five basis points just in the first quarter, so things are starting

to move, there's no question about it. We don't have our head in the sand about it, but it's very fluid in terms of the way we think about the mix of products.

I think the other thing, too, that helps us a little bit is that to the extent that we've been aggressively winding down brokered and to the extent that we're underweight commercial, where you typically find higher betas, it feels like we're in a good place in those spaces. On the brokered cost to deposits, that's money still at 250 [basis points]. So, when you think about rotating out 250 [basis point] deposits into NMD, which I think our offer rate is now like 175 [basis points], you're still picking up 75 basis points, so there's still potentially opportunity for us to be doing things in the deposit space. I hope that's a little bit more helpful.

Eric Wasserstrom
No, that's very helpful, and if I could just follow up with one question on capital. Putting aside the capital actions for the near term, can you just help me understand how you achieve that longer term target? I guess what I'm really trying to understand is how much capital you're anticipating being consumed by growth versus how much incremental capital you feel you need to return in order to achieve the secular target.

John Fawcett
Well, I think it's always—it's a constant trade-off. I mean, I'm coming up on my first year here. I think the first two quarters I was here, there wasn't a lot of growth. In fact, when the rest of the market was growing quarter-on-quarter 1.5%, 2%, we were kind of flattish. I think the fourth quarter was very strong. I think the first quarter was similarly very strong, and if you look at originations in the first quarter, they were better than every quarter almost across the board, except for the fourth quarter of last year. So, actually growing into our capital by building out the balance sheet would be a nice problem to have.

I think we've been very clear in terms of the glide path down. I think about it in terms of— at the end of last year we were at 14.5% common equity Tier 1. At the end of the first quarter, it was 14%. We're targeting to get down to 11.5% to 12% at the end of this year, and then at the high end of the range, 10% to 11% into next year. Now, a lot of things can happen between now and then and we've got to continue to operate within the regulatory framework. but being a non-SIFI, relaxed supervisory expectations all weigh into these things. But until any of that stuff happens, I think we're still on our glide path to get to between 11.5% and 12% at the end of this year and down to the high end of 10% to 11% at the end of '19, and that still feels right to me.

Eric Wasserstrom
Thanks very much.

John Fawcett
You're welcome.

Operator
As a reminder, if you would like to ask a question, please press star, then one. The next question will come from Vincent Caintic of Stephens. Please go ahead.

Vincent Caintic
Okay, thanks. Good morning, guys. I appreciate the color you've given so far on the growth in the specific segments, but I was wondering if you could broadly talk about the competitive environment you're seeing in commercial lending. I think we've heard from a couple of banks about the competitiveness of the space and I'm kind of wondering if you maybe could go

through some of your product sets, probably, and talk about where you might be seeing competition or you might have a particular edge, and in terms of competition, if you're maybe seeing yield pressure or people are taking more credit risk, or covenants might be loosening. Thanks.

Ellen Alemany
Sure. Good morning, Vincent. I think we're seeing the most competition in the commercial finance and the real estate segments of the market. It's really from the non-bank space and commercial finance, where there's just so much liquidity out in the marketplace, and, as I mentioned before, where the leverage lending levels and covenant-light transactions are being done. But, that being said, I think we're—in particular, our strategy is really going after certain industry niches. We had most of our growth this quarter in healthcare real estate, aviation lending, energy and some C&I. In real estate, the same thing, where the non-traditional lenders and debt funds, there's just a lot of liquidity out there, andwe haven't really seen change in the cap rates, it's roughly about 5% on the high quality properties, 4% to 7% on others, and we're also seeing spreads tightening there, because there's just so much cash in the system that the spreads have tightened a little there.

In business capital, I think it's basically the same traditional lenders out there in the marketplace, and where we're really differentiating ourselves is leading with industry expertise, proprietary technology, and then on the small business direct capital lending, we're one of the few fintec companies that's regulated within a bank. There's a lot of small business confidence out there, and so we have good growth in that segment.

Rob or John, I don't know if you have anything to add.

Robert Rowe
No, I thought that covered it pretty well. I would just be looking to add, in terms of commercial real estate, the banks, including ourselves, have been pretty disciplined around loan to cost and loan to value and having skin in the game, so that's why you see slower growth rates for commercial real estate across the board.

Vincent Caintic
Okay, thanks, that's helpful, and actually a related question there. You talked about a lot of excess liquidity, particularly in the non-bank space. In your experience, what changes that liquidity, what causes that liquidity to maybe go away, and maybe does the rising rates have a positive benefit for you in that regard?

Robert Rowe
Really, it would have to be kind of the cycle happening. So, if you think about commercial finance and then you think about the non-banks, whether it's the CLO money that's come on-board or the credit funds that actually have money, as well, it would really have to be a deterioration in the credit cycle, otherwise they're going to be able to provide returns to their investor base that are reasonable, and I would imagine that that would continue on. I don't think it's as much interest rate driven, unless the Fed got really aggressive on tightening, and then it was just really pulling liquidity out of the system, but, overall, interest rates are still relatively low.

Vincent Caintic
Yes, thanks very much.

Robert Rowe

You’re welcome.

Operator
Ladies and gentlemen, this will conclude our question and answer session. I would like to hand the conference back over to Management for any closing remarks.

CONCLUSION

Barbara Callahan
Great. Thank you, everyone, for joining this morning. If you have any follow-up questions, please feel free to contact me or any member of the Investor Relations Team. You can find our contact information, along with other information on CIT, in the Investor Relations section of our website at www.cit.com. Thanks again for your time and have a great day.

Operator
Thank you. Ladies and gentlemen, that concludes today’s conference call. Thank you for your participation. At this time, you may disconnect your lines.