CIT Group, Inc.

Discussion of Third Quarter 2020 Financial Results

PREPARED REMARKS

We returned to profitability and reported net income of $83 million or 84 cents per diluted common share. We had two noteworthy items that substantially offset. Costs associated with the Mutual of Omaha Bank integration offset the reversal of compensation, as the achievement of certain performance conditions related to the Company's stock-based compensation has been negatively impacted by the current environment.

While our financial results continue to reflect the ongoing global pandemic and lower rate environment, we returned to profitability as PPNR improved and credit costs continued to decline. Average loans and leases were down modestly as business activity picked up in sectors where we have strong capabilities and are mostly unimpacted by the current environment, while we continued to reduce risk in industries that have been more impacted.

We grew lower cost HOA and Commercial deposits and continued to aggressively lower deposit costs in our retail channels, driving improvement in net finance revenue and margin expansion. Average deposit costs are now less than 1 percent.

Non-interest income grew with higher factoring commissions as retailers rebuilt inventory levels. We resumed our portfolio management activities, reducing risk and recognizing a gain on the sale of legacy consumer mortgage loans as the bid for those assets normalized.

We remain vigilant in managing operating expenses, which declined this quarter as we have immediately started to see the benefits of the restructuring actions taken last quarter. We continue to outperform our expense reduction commitments and remain on track to deliver lower operating costs this year when compared to our original 2020 outlook.

Our credit provision continued to decline with lower net charge-offs. The level of deferrals declined substantially, and the ACL was essentially unchanged at $1.2 billion as we built significant reserves in the first half of the year.

Our credit reserves, capital and liquidity remain strong. Our CET1 level ended the quarter at 9.9%, well in excess of the capital conservation buffer and our ACL coverage ratio remained at 3.2%. Assuming there is no significant change to the forecasted macro environment, or in the expected credit performance of our portfolio, we expect to see further improvement in our financial performance next quarter as we continue to manage through the environment.

I will now provide some additional details on our operating trends and refer to our earnings presentation starting with Net finance revenue and margin on slides 6 and 7.

As I mentioned, net finance revenue improved, and margin expanded by thirteen basis points, driven by our actions to reduce deposit costs. The most significant impact was from the Direct Bank where we took the savings builder product offer rate down 120 basis points over the second and third quarters to now an offer rate of 55 basis points without experiencing any notable attrition. We also had about $1.2 billion of time deposits in this channel with an average rate of 2.3% that either rolled off or repriced down at significantly lower rates. The decline in loan yields reflecting lower average quarterly LIBOR levels and a higher mix of cash and investment securities partially offset the benefit of lower deposit costs.

Rail market trends continue to recover from the second quarter lows but remain below prior year levels. Rail utilization rates held steady, forming a soft floor, and leases repriced down 35% this quarter driven by the sand and coal markets. Lower maintenance costs more than offset lower lease repricing, improving net portfolio yields and benefitting the margin. As with other areas, we have been proactive in our efforts to improve efficiencies in the rail business and the prior investments we made in technology, people and processes are helping to manage our profitability as the rail market recovers.

Looking into the fourth quarter, assuming LIBOR levels remain relatively constant, we expect margin to improve another 5-10 basis points as we continue to manage through the cycle, reduce deposit costs and deploy excess liquidity.

Turning to Other Non-Interest Income on slide 8. Other non-interest income benefited from higher factoring commissions mentioned earlier and a $24 million gain on the sale of about $65 million in LCM assets from our portfolio management activities. We suspended our portfolio management activities in the second quarter given the market disruption and resumed in the third quarter as valuations normalized. Recall the mortgage loans in the LCM portfolio carry an average discount of about 20% to UPB along with an average portfolio LTV of 66%. Further, this quarter, we recognized about $8 million in additional BOLI income from elevated insurance payouts.

Looking into the fourth quarter, we think factoring commissions will remain relatively constant as activity continues with holiday season inventory building. We expect to continue to opportunistically sell LCM assets as part of our portfolio management and de-risking activity, although I would expect the gains to be lower given this quarter's activity reflected a catch up from the lack of activity in the second quarter.

Slide 11 provides more detail on average loans and leases by division. Average loans and leases were down modestly this quarter with the run-off and sale of LCM loans and the impact on average client receivables from the slowdown in the factoring business last quarter. In addition, we had higher prepayments in both Commercial and Consumer Banking.

Commercial Banking activity picked up in the third quarter in certain verticals within Commercial Finance although still below prior year levels. We continue to see opportunities and deal flow in certain industry verticals such as Power & renewable energy, Healthcare, technology and telecom which are less impacted by COVID 19. Heading into the fourth quarter, overall pipelines in Commercial Finance are better than 90 days ago.

In Real Estate Finance, we focus on partnering with strong sponsors and new business activity has primarily been related to industrial, distribution and multifamily properties as well as in support of our CRA commitments.

In Business Capital, overall business activity moderated from the increase we saw in June as we moved through the summer, which tends to be seasonally slower. And, while we have tightened our underwriting and pulled back from certain industries given the current environment, we continue to see good opportunities as we originate lower risk assets.

Our differentiating technology, industry expertise and unique knowledge of residual values gives us a strong market position. Overall, we expect average loans and leases will be relatively flat next quarter and expect to start to see modest growth as we head into the first quarter of 2021.

Turning to Deposit Trends on Slide 13. Average deposits were relatively flat while costs declined to 91 basis points, down 32 basis points from the prior quarter and 107 basis points from the year-ago quarter. A key part of our deposit strategy has been to build longer relationships which includes segmentation and targeted marketing to attract generation x, y & z customers who have proven to be less rate sensitive and exhibit lower churn rates as well as investing in products and tools that enhance the digital experience.

Our strategy also included reducing our higher cost term deposits while growing the savings and money market deposits where there is more flexibility to reduce rates. And, the diversification of our deposit sources gives us the ability to optimize our costs while meeting our funding and liquidity needs. The merits of this strategy are proving out in the current cycle.

Since the end of the first quarter, we reduced the savings builder rate by 120 basis points, an 80% beta when comparing to the 150 basis point Fed Funds rate reduction this year with minimal attrition in our target market. In the Branch channel, where the average relationship is about 13 years, deposit costs continued to decline as we grew non-maturity deposits and reduced higher cost time deposits from more rate sensitive customers.

The investments we are making in Treasury and Payments Services are providing new opportunities to grow commercial customer deposits at lower rates than our branch and online channels. Here, our relationship focused approach to gathering deposits has enabled us to increase deposits at more efficient pricing from new and existing relationships, including both the legacy CIT customer base as well as our new middle market customers.

Average deposits in this channel grew by $550 million in the third quarter and now make up 10 percent of total deposits with an average cost of 47 basis points. We are also pleased with the performance of the lower cost, HOA channel. Typically, deposits decline in the third and fourth quarters as HOA outflows exceed inflows in the second half of the year.

That said, even with this seasonal dynamic, average deposits this quarter increased $260 million as we added over 700 new HOA deposit accounts, essentially reversing that historical trend. Overall, we expect deposit costs to reduce further in the fourth quarter as we look for opportunities to further optimize our costs and we realize a full quarter benefit of the reductions made this quarter.

Slide 14 and 15 highlights our credit trends and provision. We are proactively managing our credit risk and the provision declined further this quarter, although remained elevated from pre-COVID levels.

Net charge-offs were down $104 million from last quarter. Excluding the one factoring bankruptcy last quarter that increased net charge offs by $73 million, net-charge offs were down $31 million, to $66 million, reflecting an annualized net charge off rate of 71 bps.

The retail sector continues to be challenged. Retailers, to varying degrees of success, have re-opened stores and continue to take actions to manage liquidity for the fall season. Factored volume and receivable balances increased as retailers restocked for school and the upcoming holiday season, although they remain below prior year levels. With the increased activity, we have been able to take a number of actions to further mitigate our risks including managing down exposures to more troubled retailers as well as converting to secured positions or adding collateral where we can and when appropriate. We are also seeking price enhancements where applicable to reflect the current risk environment.

We expect continued pressure in this industry. We are monitoring the developments in this sector closely and remain in constant contact with our customers and clients. The level of criticized and classified loans increased modestly this quarter as we prudently adjusted our risk ratings in the second quarter.

The increase in consumer banking non-accruals this quarter was largely driven by the Legacy Consumer Mortgage portfolio where loans are heavily discounted, and we do not expect any notable losses. The increase in commercial non-accruals were from a few loans that included sectors more impacted by the COVID environment.

We are also monitoring deferral trends. Outstanding Deferrals have come down significantly in both our consumer and commercial portfolios. As of the end of the quarter about 3% of total loans were on deferral declining by more than 50% since the end of June.

Within Commercial Banking, the reduction in deferrals trends so far have been better than we anticipated. Within our larger ticket businesses in Commercial Finance and Real Estate Finance, we continue to underwrite each modification and extension request to ensure there is a path to recovery. Approximately 10% of loans coming off deferral have extended with the majority being in the gaming and commercial air industries.

Within Business Capital, which are the small ticket equipment loans, only 2 percent of loans remain on deferral, a reduction of ~$400 million from June 30th. We have been staying in touch with our customers, including a robust calling effort to ensure we continue to understand our customers' needs. We have been encouraged to see that at the end of the September, over 95% of loans that are no longer on deferral are less than 30 days past due and when analyzing the data related to loans that exited from their deferral at least three months ago, almost 80% have made three consecutive payments.

In our consumer mortgage book, we are seeing a higher percentage of deferrals in our legacy consumer mortgage portfolio that have either extended or have not yet made a payment post deferral and therefore we have increased the level of non-accruals. That said, we do not expect losses in this portfolio given the purchase accounting discount that remains on the portfolio along with the low LTVs mentioned earlier.

Overall, we are maintaining an active dialog with our customers as we closely monitor the activity and evolving environment. We have updated our slides in the appendix to include current deferral information. Our reserves remain strong at approximately 3.2% of total loans and 3.6% of commercial loans. We had a significant reserve build in the first quarter with the adoption of CECL and the onset of COVID. We bolstered reserves in the second quarter, although at a much lower level as we were proactive in our implementation of CECL and appropriately added substantial reserves reflecting the uncertainty from COVID in the first quarter. In the third quarter, we increased specific reserves on our commercial loans while reducing reserves on our consumer loans, including about $10 million related to the sale of the LCM portfolio.

We continue to use scenarios developed by a well-known provider as a baseline for our quantitative reserve and applied qualitative adjustments for areas that we believe reflect risks not covered by quantitative models, model limitations given unprecedented activity in inputs such as the unemployment rate as well as general uncertainty in the trajectory of the economy.

We just completed our annual capital stress testing process and leveraged hypothetical scenarios from the same top industry provider used for our CECL modeling. The hypothetical scenarios selected for capital stress testing were comparable in severity to the FRB's Severely Adverse scenario published in September. Based on the results using the most severe scenario, the current ACL of $1.2 billion represents about 70% of the cumulative net losses over a 10-quarter projection period.

Given the results of our latest capital stress testing along with the additional insights we have gained from the actual performance and continued discussions with our customers as each quarter passes, we believe our reserve position is strong. In addition, we believe our capital position remains strong even after the stress experienced this year and can remain well above regulatory minimums if additional stress were to materialize. And assuming no significant change in the outlook, we expect the provision to decline further next quarter.

Turning to Slide 17. Our CET1 ratio is well in excess of the Federal Reserve's minimum levels including the capital conservation buffer at 9.9%. The decline in the ratio this quarter was driven by an increase in risk weighted assets primarily due to the seasonal increase in off balance sheet factoring receivables. Assuming there is no significant change in the forecasted macro environment, we expect our CET1 level to remain in the 9.8% to 10.0% range depending on the mix of lower risk weighted assets.