FIRST COMMONWEALTH FINANCIAL CORP /PA/
Form 10-Q
November 08, 2018
UNITED STATES
SECURITIES AND EXCHANGE COMMISSION
Washington, D.C. 20549
FORM 10-Q

x QUARTERLY REPORT PURSUANT TO SECTION 13 OR 15(d) OF THE SECURITIES EXCHANGE ACT OF 1934
For the quarterly period ended September 30, 2018
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 001-11138
First Commonwealth Financial Corporation
(Exact name of registrant as specified in its charter)

Pennsylvania	25-1428528
(State or other jurisdiction of incorporation or organization)	(I.R.S. Employer Identification No.)
601 Philadelphia Street, Indiana, PA	15701
(Address of principal executive offices)	(Zip Code)

724-349-7220
(Registrant's telephone number, including area code)
N/A
(Former name, former address and former fiscal year, if changed since last report)
Indicate by a 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 x No ¨.
Indicate by check mark whether the registrant has submitted electronically and posted on its corporate Web site, if any, every Interactive Data File required to be submitted and posted pursuant to Rule 405 of Regulation S-T (§232.405 of this chapter) during the preceding 12 months (or for such shorter period that the registrant was required to submit and post such files). Yes x No ¨
Indicate by check mark whether the registrant is a large accelerated filer, an accelerated filer, a non-accelerated filer, or a smaller reporting company. See the definitions of "large accelerated filer," "accelerated filer" and "smaller reporting company" in Rule 12b-2 of the Exchange Act.
Large accelerated filer x Accelerated filer ¨ Smaller reporting company ¨ Emerging growth company ¨
Non-accelerated filer ¨ (Do not check if a smaller reporting company)

If an emerging growth company, indicate by check mark if the registrant has elected not to use the extended transition period for complying with any new or revised financial accounting standards provided pursuant to Section 13(a) of the Exchange Act. ¨
Indicate by check mark whether the registrant is a shell company (as defined in Rule 12b-2 of the Exchange Act). Yes ¨ No x
The number of shares outstanding of issuer's common stock, $1.00 par value, as of November 7, 2018, was 99,423,275.

Table of Contents

FIRST COMMONWEALTH FINANCIAL CORPORATION AND SUBSIDIARIES
FORM 10-Q
INDEX

Table of Contents

ITEM 1. Financial Statements and Supplementary Data
FIRST COMMONWEALTH FINANCIAL CORPORATION AND SUBSIDIARIES
CONDENSED CONSOLIDATED STATEMENTS OF FINANCIAL CONDITION (Unaudited)

	September 30, 2018	December 31, 2017
	(dollars in thousands, except share data)	
Assets		
Cash and due from banks	$93,162	$98,624
Interest-bearing bank deposits	3,022	8,668
Securities available for sale, at fair value	889,056	731,358
Securities held to maturity, at amortized cost (Fair value of $373,933 and $418,249 at September 30, 2018 and December 31, 2017, respectively)	389,621	422,096
Other investments	25,029	29,837
Loans held for sale	8,287	14,850
Loans:		
Portfolio loans	5,662,782	5,407,376
Allowance for credit losses	(50,746)	(48,298)
Net loans	5,612,036	5,359,078
Premises and equipment, net	80,426	81,339
Other real estate owned	3,874	2,765
Goodwill	274,202	255,353
Amortizing intangibles, net	13,826	15,007
Bank owned life insurance	214,322	212,099
Other assets	79,482	77,465
Total assets	$7,686,345	$7,308,539
Liabilities		
Deposits (all domestic):		
Noninterest-bearing	$1,451,284	$1,416,771
Interest-bearing	4,443,859	4,163,934
Total deposits	5,895,143	5,580,705
Short-term borrowings	587,806	707,466
Subordinated debentures	170,249	72,167
Other long-term debt	7,706	8,161
Capital lease obligation	7,311	7,590
Total long-term debt	185,266	87,918
Other liabilities	45,199	44,323
Total liabilities	6,713,414	6,420,412
Shareholders' Equity		
Preferred stock, $1 par value per share, 3,000,000 shares authorized, none issued	—	—
Common stock, $1 par value per share, 200,000,000 shares authorized; 113,914,902 shares issued at September 30, 2018 and December 31, 2017, and 100,361,434 and 97,456,478 shares outstanding at September 30, 2018 and December 31, 2017, respectively	113,915	113,915
Additional paid-in capital	492,262	470,123
Retained earnings	493,392	437,416

Accumulated other comprehensive loss, net	(20,657)	(6,173)
Treasury stock (13,553,468 and 16,458,424 shares at September 30, 2018 and December 31, 2017, respectively)	(105,981)	(127,154)
Total shareholders’ equity	972,931	888,127
Total liabilities and shareholders’ equity	$7,686,345	$7,308,539

The accompanying notes are an integral part of these unaudited condensed consolidated financial statements.

3

Table of Contents

ITEM 1. Financial Statements and Supplementary Data (Continued)
FIRST COMMONWEALTH FINANCIAL CORPORATION AND SUBSIDIARIES
CONDENSED CONSOLIDATED STATEMENTS OF INCOME (Unaudited)

	For the Three Months Ended September 30,		For the Nine Months Ended September 30,	
	2018	2017	2018	2017
	(dollars in thousands, except share data)			
Interest Income				
Interest and fees on loans	$66,105	$57,335	$188,529	$160,548
Interest and dividends on investments:				
Taxable interest	7,899	7,219	23,031	21,577
Interest exempt from federal income taxes	410	410	1,231	1,212
Dividends	420	417	1,412	1,276
Interest on bank deposits	39	30	109	97
Total interest income	74,873	65,411	214,312	184,710
Interest Expense				
Interest on deposits	6,006	2,491	14,639	6,511
Interest on short-term borrowings	2,603	2,427	7,387	6,373
Interest on subordinated debentures	2,302	772	4,664	2,215
Interest on other long-term debt	76	81	228	245
Interest on lease obligations	73	77	221	156
Total interest expense	11,060	5,848	27,139	15,500
Net Interest Income	63,813	59,563	187,173	169,210
Provision for credit losses	2,961	1,214	11,032	2,834
Net Interest Income after Provision for Credit Losses	60,852	58,349	176,141	166,376
Noninterest Income				
Net securities gains	—	92	8,102	695
Trust income	2,206	2,147	6,014	5,275
Service charges on deposit accounts	4,589	4,803	13,418	13,858
Insurance and retail brokerage commissions	1,872	2,128	5,560	6,652
Income from bank owned life insurance	1,579	1,472	5,241	4,213
Gain on sale of mortgage loans	1,542	1,418	4,267	3,710
Gain on sale of other loans and assets	643	503	3,548	1,267
Card-related interchange income	5,044	4,780	14,929	13,873
Derivatives mark to market	—	(14)	789	(49)
Swap fee income	528	217	1,115	458
Other income	1,754	2,244	5,125	5,674
Total noninterest income	19,757	19,790	68,108	55,626
Noninterest Expense				
Salaries and employee benefits	26,553	26,169	77,580	74,933
Net occupancy expense	4,341	3,715	12,932	11,597
Furniture and equipment expense	3,424	3,342	10,611	9,753
Data processing expense	2,853	2,229	7,764	6,659
Advertising and promotion expense	1,200	941	3,185	2,735
Pennsylvania shares tax expense	1,248	1,093	3,398	3,070
Intangible amortization	817	844	2,430	2,262

Collection and repossession expense	630	402	2,060	1,342
Other professional fees and services	962	1,300	3,000	3,355
FDIC insurance	217	696	1,590	2,466
Loss on sale or write-down of assets	181	167	875	1,486
Litigation and operational losses	435	598	811	1,107
Merger and acquisition related	24	(69)	1,634	10,412
Other operating expenses	6,645	5,934	17,662	17,212
Total noninterest expense	49,530	47,361	145,532	148,389
Income Before Income Taxes	31,079	30,778	98,717	73,613
Income tax provision	5,930	9,495	18,217	22,429
Net Income	$25,149	$ 21,283	$80,500	$51,184
Average Shares Outstanding	100,226,647	97,402,816	98,998,497	94,536,472
Average Shares Outstanding Assuming Dilution	100,490,812	97,457,470	99,197,568	94,578,490
Per Share Data:				
Basic Earnings per Share	$0.25	$ 0.22	$0.81	$0.54
Diluted Earnings per Share	$0.25	$ 0.22	$0.81	$0.54
Cash Dividends Declared per Common Share	$0.09	$ 0.08	$0.26	$0.24

The accompanying notes are an integral part of these unaudited condensed consolidated financial statements.

4

Table of Contents

ITEM 1. Financial Statements and Supplementary Data (Continued)
FIRST COMMONWEALTH FINANCIAL CORPORATION AND SUBSIDIARIES
CONDENSED CONSOLIDATED STATEMENTS OF COMPREHENSIVE INCOME (Unaudited)

	For the Three Months Ended September 30,		For the Nine Months Ended September 30,	
	2018	2017	2018	2017
	(dollars in thousands)			
Net Income	$25,149	$21,283	$80,500	$51,184
Other comprehensive (loss) income, before tax benefit (expense):				
Unrealized holding (losses) gains on securities arising during the period	(5,382)	1,690	(8,704)	5,935
Less: reclassification adjustment for gains on securities included in net income	—	(92)	(8,102)	(695)
Unrealized holding gains (losses) on derivatives arising during the period	198	(49)	165	(631)
Less: reclassification adjustment for losses on derivatives included in net income	—	20	10	93
Total other comprehensive (loss) income, before tax benefit (expense)	(5,184)	1,569	(16,631)	4,702
Income tax benefit (expense) related to items of other comprehensive (loss) income	1,088	(549)	3,491	(1,646)
Total other comprehensive (loss) income	(4,096)	1,020	(13,140)	3,056
Comprehensive Income	$21,053	$22,303	$67,360	$54,240

The accompanying notes are an integral part of these unaudited condensed consolidated financial statements.

Table of Contents

ITEM 1. Financial Statements and Supplementary Data (Continued)
FIRST COMMONWEALTH FINANCIAL CORPORATION AND SUBSIDIARIES
CONDENSED CONSOLIDATED STATEMENTS OF CHANGES IN SHAREHOLDERS' EQUITY (Unaudited)

	Shares Outstanding	Common Stock	Additional Paid-in-Capital	Retained Earnings	Accumulated Other Comprehensive Income (Loss), net	Treasury Stock	Total Shareholders' Equity
	(dollars in thousands, except share and per share data)						
Balance at December 31, 2017	97,456,478	$113,915	$470,123	$437,416	$ (6,173)	$(127,154)	$888,127
Cumulative effect of adoption of ASU 2018-02				1,344	(1,344)		—
January 1, 2018	97,456,478	113,915	470,123	438,760	(7,517)	(127,154)	888,127
Net income				80,500			80,500
Other comprehensive loss					(13,140)		(13,140)
Cash dividends declared ($0.26 per share)				(25,868)			(25,868)
Treasury stock acquired	(75,778)					(1,136)	(1,136)
Treasury stock reissued	2,908,234		21,579	—		22,447	44,026
Restricted stock	72,500	—	560	—		(138)	422
Balance at September 30, 2018	100,361,434	$113,915	$492,262	$493,392	$ (20,657)	$(105,981)	$972,931

	Shares Outstanding	Common Stock	Additional Paid-in-Capital	Retained Earnings	Accumulated Other Comprehensive Income (Loss), net	Treasury Stock	Total Shareholders' Equity
	(dollars in thousands, except share and per share data)						
Balance at December 31, 2016	89,007,077	$105,563	$366,426	$412,764	$ (7,027)	$(127,797)	$749,929
Net income				51,184			51,184
Other comprehensive income					3,056		3,056
Cash dividends declared ($0.24 per share)				(22,717)			(22,717)
Treasury stock acquired	(85,160)					(1,187)	(1,187)
Treasury stock reissued	181,211		1,170	—		1,387	2,557
Restricted stock	21,000	—	138	—		600	738
Common stock issuance	8,351,447	8,352	102,389				110,741
Balance at September 30, 2017	97,475,575	$113,915	$470,123	$441,231	$ (3,971)	$(126,997)	$894,301

The accompanying notes are an integral part of these unaudited condensed consolidated financial statements.

Table of Contents

ITEM 1. Financial Statements and Supplementary Data (Continued)
FIRST COMMONWEALTH FINANCIAL CORPORATION AND SUBSIDIARIES
CONDENSED CONSOLIDATED STATEMENTS OF CASH FLOWS (Unaudited)

	For the Nine Months Ended September 30,	
	2018	2017
Operating Activities	(dollars in thousands)	
Net income	$80,500	$51,184
Adjustment to reconcile net income to net cash provided by operating activities:		
Provision for credit losses	11,032	2,834
Deferred tax expense	2,969	3,411
Depreciation and amortization	5,620	6,711
Net gains on securities and other assets	(15,816)	(3,821)
Net amortization of premiums and discounts on securities	2,343	2,685
Income from increase in cash surrender value of bank owned life insurance	(4,364)	(4,213)
Increase in interest receivable	(2,483)	(588)
Mortgage loans originated for sale	(129,552)	(116,699)
Proceeds from sale of mortgage loans	139,685	114,819
Increase in interest payable	1,672	678
(Decrease) increase in income taxes payable	(3,412)	3,288
Distribution from unconsolidated subsidiary	9,000	—
Other-net	(3,655)	2,963
Net cash provided by operating activities	93,539	63,252
Investing Activities		
Transactions with securities held to maturity:		
Proceeds from maturities and redemptions	37,007	36,620
Purchases	(5,506)	(101,372)
Transactions with securities available for sale:		
Proceeds from sales	15,939	143,660
Proceeds from maturities and redemptions	111,800	100,620
Purchases	(292,249)	(150,892)
Purchases of FHLB stock	(38,947)	(35,346)
Proceeds from the redemption of FHLB stock	43,754	42,791
Proceeds from bank owned life insurance	2,140	—
Proceeds from sale of loans	32,745	9,986
Proceeds from sale of other assets	2,486	3,835
Acquisition, net of cash acquired	705	3,188
Net increase in loans	(109,060)	(132,079)
Purchases of premises and equipment and other assets	(6,862)	(8,960)
Net cash used in investing activities	(206,048)	(87,949)
Financing Activities		
Net increase in federal funds purchased	6,500	—
Net decrease in other short-term borrowings	(126,160)	(62,118)
Net increase in deposits	173,553	123,455
Repayments of other long-term debt	(23,443)	(440)

Repayments of capital lease obligation	(279)	(173)
Proceeds from issuance of other long-term debt	98,026	—
Dividends paid	(25,868)	(22,717)
Proceeds from reissuance of treasury stock	208	228
Purchase of treasury stock	(1,136)	(1,187)
Net cash provided by financing activities	101,401	37,048
Net (decrease) increase in cash and cash equivalents	(11,108)	12,351
Cash and cash equivalents at January 1	107,292	115,677
Cash and cash equivalents at September 30	$96,184	$128,028

The accompanying notes are an integral part of these unaudited condensed consolidated financial statements.
7

ITEM 1. Financial Statements and Supplementary Data
FIRST COMMONWEALTH FINANCIAL CORPORATION AND SUBSIDIARIES
NOTES TO THE UNAUDITED CONDENSED CONSOLIDATED FINANCIAL STATEMENTS
Note 1 Basis of Presentation

The accounting and reporting policies of First Commonwealth Financial Corporation and its subsidiaries (“First Commonwealth” or the “Company”) conform with generally accepted accounting principles in the United States of America (“GAAP”). The preparation of financial statements in conformity with GAAP requires management to make estimates, assumptions and judgments that affect the amounts reported in the financial statements and accompanying notes. Actual realized amounts could differ from those estimates. In the opinion of management, the unaudited interim condensed consolidated financial statements include all adjustments (consisting of only normal recurring adjustments) necessary for a fair presentation of First Commonwealth’s financial position, results of operations, comprehensive income, cash flows and changes in shareholders’ equity as of and for the periods presented.

The results of operations for the nine months ended September 30, 2018 are not necessarily indicative of the results that may be expected for the full year of 2018. These interim financial statements should be read in conjunction with First Commonwealth’s 2017 Annual Report on Form 10-K.

Adoption of New Accounting Standards

On January 1, 2018, First Commonwealth adopted ASU 2014-09, "Revenue from Contracts with Customers" ("ASC 606") and all subsequent amendments to the ASU, which creates a single framework for recognizing revenue from contracts with customers that fall within its scope and revises when it is appropriate to recognize a gain(loss) from the transfer of nonfinancial assets, such as OREO. The majority of the Company's revenues come from interest income and other sources, including loans and securities, that are outside the scope of ASC 606. The Company's services that fall within the scope of ASC 606 are presented within non-interest income and are recognized as revenue as the Company satisfies its obligation to the customer. Services within the scope of ASC 606 include trust income, service charges on deposits, insurance and retail brokerage commissions, interchange fees and gain(loss) on other real estate owned ("OREO"). Refer to Note 15, "Revenue Recognition" for further discussion on the Company's accounting policies for revenue sources within the scope of ASC 606. The Company adopted ASC 606 using the modified retrospective method applied to all contracts not completed as of January 1, 2018. Results for reporting periods beginning after January 1, 2018 are presented under ASC 606 while prior period amounts continue to be reported in accordance with legacy GAAP. The adoption of ASC 606 did not result in a significant change to the accounting for any of the in-scope revenue streams; as such, no cumulative effect adjustment was recorded.

On January 1, 2018, First Commonwealth elected to adopt ASU 2018-02, "Income Statement - Reporting Comprehensive Income (Topic 220)." As part of this adoption, First Commonwealth has elected to reclassify the income tax effects resulting from tax reform from accumulated other comprehensive income to retained earnings on a portfolio basis. ASU 2018-02 provides for the reclassification of the stranded tax effects resulting from the Tax Cuts and Jobs Act. As of January 1, 2018, First Commonwealth reclassified $1.3 million from accumulated other comprehensive income to retained earnings in relation to the stranded tax effect which included accumulated other comprehensive income recognized on available-for-sale investment securities, interest rate swaps and other post-retirement benefits. This reclassification is shown as an adjustment to the beginning of the year balances and can be seen in the Condensed Consolidated Statements of Changes in Shareholders' Equity.

In January 2016, the FASB issued ASU No. 2016-01, “Recognition and Measurement of Financial Assets and Financial Liabilities.” This ASU addresses certain aspects of recognition, measurement, presentation, and disclosure of financial instruments by making targeted improvements to GAAP as follows: (1) require equity investments (except those accounted for under the equity method of accounting or those that result in consolidation of the investee) to be measured at fair value with changes in fair value recognized in net income; (2) simplify the impairment assessment of equity investments without readily determinable fair values by requiring a qualitative assessment to identify impairment, and when that assessment indicates that impairment exists, requiring the entity to measure the investment at fair value; (3) eliminate the requirement to disclose the fair value of financial instruments measured at amortized cost for entities that are not public business entities; (4) eliminate the requirement for public business entities to disclose the method(s) and significant assumptions used to estimate the fair value that is required to be disclosed for financial instruments measured at amortized cost on the balance sheet; (5) require public business entities to use the exit price notion when measuring the fair value of financial instruments for disclosure purposes; (6) require an entity to present separately in other comprehensive income the portion of the total change in the fair value of a liability resulting from a change in the instrument-specific credit risk when the entity has elected to measure the liability at fair value in accordance with the fair value option for financial instruments; (7) require separate presentation of financial assets and financial liabilities by measurement category and form of financial asset (that is, securities or loans and receivables) on the balance sheet or the accompanying notes to the financial statements; and (8) clarify that an entity should evaluate the need for a

ITEM 1. Financial Statements and Supplementary Data
FIRST COMMONWEALTH FINANCIAL CORPORATION AND SUBSIDIARIES
NOTES TO THE UNAUDITED CONDENSED CONSOLIDATED FINANCIAL STATEMENTS (Continued)

valuation allowance on a deferred tax asset related to available-for-sale securities in combination with the entity's other deferred tax assets. The adoption of ASU No. 2016-01 on January 1, 2018 did not have a material impact on the Company's Consolidated Financial Statements. In accordance with this ASU, and as reflected in Note 11, "Fair Values of Assets and Liabilities," the Company measured the fair value of its loan portfolio as of September 30, 2018 using an exit price notion.

For purposes of reporting cash flows, cash and cash equivalents include cash on hand, amounts due from banks, federal funds sold and interest-bearing bank deposits. Generally, federal funds are sold for one-day periods.

Note 2 Acquisition

On May 1, 2018, the Company completed its acquisition of Garfield Acquisition Corporation ("Garfield") and its banking subsidiary, Foundation Bank, for consideration of $17.4 million in cash and 2.7 million shares of the Company's common stock. Through the acquisition, the Company obtained five full-service banking offices which are operating under the First Commonwealth name. This acquisition expands the Company's presence into the Cincinnati, Ohio market and added $184.5 million in loans and $141.3 million in deposits to the Company's balance sheet.

The table below summarizes the net assets acquired (at fair value) and consideration transferred in connection with the Garfield acquisition (dollars in thousands):

Consideration Paid		
Cash paid to shareholders	$17,400	
Shares issued to shareholders (2,745,098 shares)	41,561	
Total consideration paid		$58,961
Fair Value of Assets Acquired		
Cash and cash equivalents	18,105	
FHLB Stock	3,261	
Loans	184,506	
Premises and other equipment	409	
Intangible assets	1,248	
Other assets	1,747	
Total assets acquired	209,276	
Fair Value of Liabilities Assumed		
Deposits	141,281	
Federal Home Loan Bank borrowings	22,988	
Other liabilities	5,068	
Total liabilities assumed	169,337	
Total Fair Value of Identifiable Net Assets		39,939
Goodwill		$19,022

The goodwill of $19.0 million arising from the acquisition represents the value of synergies and economies of scale expected from combining the operations of the Company with Garfield Acquisition Corporation.

The Company determined that this acquisition constitutes a business combination as defined in FASB ASC Topic 805, "Business Combinations." Accordingly, as of the date of the acquisition, the Company recorded the assets acquired and liabilities assumed at fair value. The Company determined fair values in accordance with the guidance provided in FASB ASC Topic 820, "Fair Value Measurements and Disclosures." Acquired loans were recorded at fair value with no carryover of the related allowance for loan losses. Fair value is established by discounting the expected future cash flows with a market discount

9

ITEM 1. Financial Statements and Supplementary Data
FIRST COMMONWEALTH FINANCIAL CORPORATION AND SUBSIDIARIES
NOTES TO THE UNAUDITED CONDENSED CONSOLIDATED FINANCIAL STATEMENTS (Continued)

rate for like maturities and risk instruments. At the date of acquisition, none of the loans were accounted for under the guidance of ASC Topic 310-30, “Receivables-Loans and Debt Securities Acquired with Deteriorated Credit Quality.” The $184.5 million fair value of acquired loans is the result of $183.7 million in net loans acquired from Garfield, the recognition of a net combined yield and credit mark adjustment of $4.3 million and the $5.1 million reversal of Garfield's allowance as well as prior fair value marks recorded by Garfield.

The fair value of the 2,745,098 common shares issued was determined based on the market price of the Company's common shares on the acquisition date.

Costs related to the acquisition totaled $1.6 million. These amounts were expensed as incurred and are recorded as a merger and acquisition related expense in the Condensed Consolidated Statements of Income.

As a result of the full integration of the operations of Garfield, it is not practicable to determine revenue or net income included in the Company's operating results relating to Garfield since the date of acquisition as Garfield’s results cannot be separately identified.

Note 3 Supplemental Comprehensive Income Disclosures

The following table identifies the related tax effects allocated to each component of other comprehensive income (“OCI”) in the Condensed Consolidated Statements of Comprehensive Income. Reclassification adjustments related to securities available for sale are included in the "Net securities gains" line and reclassification adjustments related to losses on derivatives are included in the "Other operating expenses" line in the Condensed Consolidated Statements of Income.

	For the Nine Months Ended September 30,					
	2018			2017		
	Pretax Amount	Tax (Expense) Benefit	Net of Tax Amount	Pretax Amount	Tax (Expense) Benefit	Net of Tax Amount
	(dollars in thousands)					
Unrealized (losses) gains on securities:						
Unrealized holding (losses) gains on securities arising during the period	$(8,704)	$ 1,828	$(6,876)	$5,935	$ (2,077)	$3,858
Reclassification adjustment for gains on securities included in net income	(8,102)	1,701	(6,401)	(695)	243	(452)
Total unrealized (losses) gains on securities	(16,806)	3,529	(13,277)	5,240	(1,834)	3,406
Unrealized gains (losses) on derivatives:						
Unrealized holding gains (losses) on derivatives arising during the period	165	(35)	130	(631)	221	(410)
Reclassification adjustment for losses on derivatives included in net income	10	(3)	7	93	(33)	60
Total unrealized gains (losses) on derivatives	175	(38)	137	(538)	188	(350)
Total other comprehensive (loss) income	$(16,631)	$ 3,491	$(13,140)	$4,702	$ (1,646)	$3,056

ITEM 1. Financial Statements and Supplementary Data
FIRST COMMONWEALTH FINANCIAL CORPORATION AND SUBSIDIARIES
NOTES TO THE UNAUDITED CONDENSED CONSOLIDATED FINANCIAL STATEMENTS (Continued)

	For the Three Months Ended September 30,					
	2018			2017		
	Pretax Amount	Tax (Expense) Benefit	Net of Tax Amount	Pretax Amount	Tax (Expense) Benefit	Net of Tax Amount
	(dollars in thousands)					
Unrealized (losses) gains on securities:						
Unrealized holding (losses) gains on securities arising during the period	$(5,382)	$ 1,130	$(4,252)	$1,690	$ (591)	$1,099
Reclassification adjustment for gains on securities included in net income	—	—	—	(92)	32	(60)
Total unrealized (losses) gains on securities	(5,382)	1,130	(4,252)	1,598	(559)	1,039
Unrealized gains (losses) on derivatives:						
Unrealized holding gains (losses) on derivatives arising during the period	198	(42)	156	(49)	17	(32)
Reclassification adjustment for losses on derivatives included in net income	—	—	—	20	(7)	13
Total unrealized gains (losses) on derivatives	198	(42)	156	(29)	10	(19)
Total other comprehensive (loss) income	$(5,184)	$ 1,088	$(4,096)	$1,569	$ (549)	$1,020

The following table details the change in components of OCI for the nine months ended September 30:

	2018				2017			
	Securities Available for Sale	Post-Retirement Obligation	Derivatives	Accumulated Other Comprehensive Income (Loss)	Securities Available for Sale	Post-Retirement Obligation	Derivatives	Accumulated Other Comprehensive Income (Loss)
	(dollars in thousands)							
Balance at December 31	$(6,166)	$ 299	$ (306)	$ (6,173)	$(7,455)	$ 225	$ 203	$ (7,027)
Cumulative effect of adoption of ASU 2018-02	(1,344)	—	—	(1,344)	—	—	—	—
Balance at January 1	(7,510)	299	(306)	(7,517)	(7,455)	225	203	(7,027)
Other comprehensive (loss) income before reclassification adjustment	(6,876)	—	130	(6,746)	3,858	—	(410)	3,448
Amounts reclassified from accumulated other comprehensive (loss) income	(6,401)	—	7	(6,394)	(452)	—	60	(392)
Net other comprehensive (loss) income during the period	(13,277)	—	137	(13,140)	3,406	—	(350)	3,056
Balance at September 30	$(20,787)	$ 299	$ (169)	$ (20,657)	$(4,049)	$ 225	$ (147)	$ (3,971)

ITEM 1. Financial Statements and Supplementary Data
FIRST COMMONWEALTH FINANCIAL CORPORATION AND SUBSIDIARIES
NOTES TO THE UNAUDITED CONDENSED CONSOLIDATED FINANCIAL STATEMENTS (Continued)

Note 4 Supplemental Cash Flow Disclosures

The following table presents information related to cash paid during the period for interest and income taxes, as well as detail on non-cash investing and financing activities for the nine months ended September 30:

	2018	2017
	(dollars in thousands)	
Cash paid during the period for:		
Interest	$25,780	$14,995
Income taxes	18,750	17,394
Non-cash investing and financing activities:		
Loans transferred to other real estate owned and repossessed assets	3,346	2,154
Loans transferred from held to maturity to held for sale	29,765	13,292
Gross (decrease) increase in market value adjustment to securities available for sale	(16,806)	5,240
Gross increase (decrease) in market value adjustment to derivatives	175	(538)
Noncash treasury stock reissuance	2,257	2,258
Net assets acquired through acquisition	21,834	36,926
Proceeds from death benefit on bank-owned life insurance not received	—	897

Note 5 Earnings per Share

The following table summarizes the composition of the weighted-average common shares (denominator) used in the basic and diluted earnings per share computations:

	For the Three Months Ended September 30,		For the Nine Months Ended September 30,	
	2018	2017	2018	2017
Weighted average common shares issued	113,914,902	113,914,902	113,914,902	111,100,495
Average treasury stock shares	(13,550,710)	(16,436,228)	(14,783,078)	(16,465,984)
Average deferred compensation shares	(37,411)	—	(37,411)	—
Average unearned nonvested shares	(100,134)	(75,858)	(95,916)	(98,039)
Weighted average common shares and common stock equivalents used to calculate basic earnings per share	100,226,647	97,402,816	98,998,497	94,536,472
Additional common stock equivalents (nonvested stock) used to calculate diluted earnings per share	226,754	54,654	161,660	42,018
Additional common stock equivalents (deferred compensation) used to calculate diluted earnings per share	37,411	—	37,411	—
Weighted average common shares and common stock equivalents used to calculate diluted earnings per share	100,490,812	97,457,470	99,197,568	94,578,490

The following table shows the number of shares and the price per share related to common stock equivalents that were not included in the computation of diluted earnings per share for the nine months ended September 30 because to do so would have been antidilutive.

	2018			2017		
		Price Range			Price Range	
	Shares	From	To	Shares	From	To
Restricted Stock	66,332	$8.84	$14.49	22,802	$8.55	$13.96
Restricted Stock Units	—	$—	$—	22,750	$15.09	$15.09

ITEM 1. Financial Statements and Supplementary Data
FIRST COMMONWEALTH FINANCIAL CORPORATION AND SUBSIDIARIES
NOTES TO THE UNAUDITED CONDENSED CONSOLIDATED FINANCIAL STATEMENTS (Continued)

Note 6 Commitments and Contingent Liabilities
Commitments and Letters of Credit
Standby letters of credit and commercial letters of credit are conditional commitments issued by First Commonwealth to guarantee the performance of a customer to a third party. The contract or notional amount of these instruments reflects the maximum amount of future payments that First Commonwealth could be required to pay under the guarantees if there were a total default by the guaranteed parties, without consideration of possible recoveries under recourse provisions or from collateral held or pledged. In addition, many of these commitments are expected to expire without being drawn upon; therefore, the total commitment amounts do not necessarily represent future cash requirements.
The following table identifies the notional amount of those instruments at:

	September 30, 2018	December 31, 2017
	(dollars in thousands)	
Financial instruments whose contract amounts represent credit risk:		
Commitments to extend credit	$1,846,575	$1,840,180
Financial standby letters of credit	18,486	17,946
Performance standby letters of credit	21,460	20,472
Commercial letters of credit	927	1,149

The notional amounts outstanding as of September 30, 2018 include amounts issued in 2018 of $1.1 million in financial standby letters of credit and $0.7 million in performance standby letters of credit. There were no commercial letters of credit issued in 2018. A liability of $0.2 million has been recorded as of September 30, 2018 and December 31, 2017, which represents the estimated fair value of letters of credit issued. The fair value of letters of credit is estimated based on the unrecognized portion of fees received at the time the commitment was issued.
Unused commitments and letters of credit provide exposure to future credit loss in the event of nonperformance by the borrower or guaranteed parties. Management's evaluation of the credit risk related to these commitments resulted in the recording of a liability of $5.2 million as of both September 30, 2018 and December 31, 2017. This liability is reflected in "Other liabilities" in the Condensed Consolidated Statements of Financial Condition. The credit risk evaluation incorporated probability of default, loss given default and estimated utilization for the next twelve months for each loan category and the letters of credit.
Legal Proceedings
First Commonwealth and its subsidiaries are subject in the normal course of business to various pending and threatened legal proceedings in which claims for monetary damages are asserted. As of September 30, 2018, management, after consultation with legal counsel, does not anticipate that the aggregate ultimate liability arising out of litigation pending or threatened against First Commonwealth or its subsidiaries will be material to First Commonwealth's consolidated financial position. On at least a quarterly basis, First Commonwealth assesses its liabilities and contingencies in connection with such legal proceedings. For those matters where it is probable that First Commonwealth will incur losses and the amounts of the losses can be reasonably estimated, First Commonwealth records an expense and corresponding liability in its consolidated financial statements. To the extent the pending or threatened litigation could result in exposure in excess of that liability, the amount of such excess is not currently estimable. Although not considered probable, the range of reasonably possible losses for such matters in the aggregate, beyond the existing recorded liability (if any), is between $0 and $1 million. Although First Commonwealth does not believe that the outcome of pending litigation will be material to First Commonwealth's consolidated financial position, it cannot rule out the possibility that such outcomes will be material to the consolidated results of operations and cash flows for a particular reporting period in the future.

First Commonwealth Financial Corporation and First Commonwealth Bank were named defendants in an action commenced August 27, 2015 by eight named plaintiffs that filed in the Court of Common Pleas of Jefferson County, Pennsylvania. The plaintiffs alleged that the Bank repossessed motor vehicles, sold the vehicles and sought to collect deficiency balances in a manner that did not comply with the notice requirements of the Pennsylvania Uniform Commercial Code (UCC), charged inappropriate costs and fees, including storage costs for dates that a repossessed vehicle was not in storage, and wrongly filed forms with the Department of Motor Vehicles asserting that the Bank had complied with applicable laws relating to the repossession of the vehicles. First Commonwealth Financial Corporation, First Commonwealth Bank, the plaintiffs, the plaintiffs' counsel and First Commonwealth's liability insurer entered into a Class Action Settlement Agreement and Release in

ITEM 1. Financial Statements and Supplementary Data
FIRST COMMONWEALTH FINANCIAL CORPORATION AND SUBSIDIARIES
NOTES TO THE UNAUDITED CONDENSED CONSOLIDATED FINANCIAL STATEMENTS (Continued)

which, among other things, First Commonwealth and its insurer agreed to pay certain amounts into a settlement fund to be distributed among the class members and class counsel, First Commonwealth agreed to satisfy the remaining deficiency balances of the class members and request that credit reporting agencies delete the tradeline relating to the repossession from each class member's credit report, and the class members released all claims against First Commonwealth and its insurer. At a hearing on July 23, 2018, the Court granted final approval of the settlement and dismissed all claims against First Commonwealth. In August 2018, this settlement was completed. The cost of the settlement to First Commonwealth was recorded as a liability in the second quarter of 2016.

Note 7 Investment Securities

Securities Available for Sale

Below is an analysis of the amortized cost and estimated fair values of securities available for sale at:

	September 30, 2018				December 31, 2017			
	Amortized Cost	Gross Unrealized Gains	Gross Unrealized Losses	Estimated Fair Value	Amortized Cost	Gross Unrealized Gains	Gross Unrealized Losses	Estimated Fair Value
	(dollars in thousands)							
Obligations of U.S. Government Agencies:								
Mortgage-Backed Securities – Residential	$9,276	$ 484	$(132)	$9,628	$10,556	$ 789	$(7)	$11,338
Mortgage-Backed Securities – Commercial	170,086	—	(2,675)	167,411	24,611	—	(462)	24,149
Obligations of U.S. Government-Sponsored Enterprises:								
Mortgage-Backed Securities – Residential	685,721	987	(25,079)	661,629	632,422	2,622	(9,489)	625,555
Other Government-Sponsored Enterprises	100	—	—	100	1,098	—	(1)	1,097
Obligations of States and Political Subdivisions	27,590	56	(129)	27,517	27,083	327	—	27,410
Corporate Securities	20,907	473	(279)	21,101	15,907	590	(4)	16,493
Pooled Trust Preferred Collateralized Debt Obligations	—	—	—	—	27,499	526	(4,379)	23,646
Total Debt Securities	913,680	2,000	(28,294)	887,386	739,176	4,854	(14,342)	729,688
Equities	1,670	—	—	1,670	1,670	—	—	1,670
Total Securities Available for Sale	$915,350	$ 2,000	$(28,294)	$889,056	$740,846	$ 4,854	$(14,342)	$731,358

Mortgage-backed securities include mortgage-backed obligations of U.S. Government agencies and obligations of U.S. Government-sponsored enterprises. These obligations have contractual maturities ranging from less than one year to approximately 30 years with lower anticipated lives to maturity due to prepayments. All mortgage-backed securities contain a certain amount of risk related to the uncertainty of prepayments of the underlying mortgages. Interest rate changes have a direct impact upon prepayment speeds; therefore, First Commonwealth uses computer simulation models to test the average life and yield volatility of all mortgage-backed securities under various interest rate scenarios to monitor the potential impact on earnings and interest rate risk positions.

Expected maturities will differ from contractual maturities because issuers may have the right to call or repay obligations with or without call or prepayment penalties. Other fixed income securities within the portfolio also contain prepayment risk.

ITEM 1. Financial Statements and Supplementary Data
FIRST COMMONWEALTH FINANCIAL CORPORATION AND SUBSIDIARIES
NOTES TO THE UNAUDITED CONDENSED CONSOLIDATED FINANCIAL STATEMENTS (Continued)

The amortized cost and estimated fair value of debt securities available for sale at September 30, 2018, by contractual maturity, are shown below.

	Amortized Cost	Estimated Fair Value
	(dollars in thousands)	
Due within 1 year	$4,099	$4,089
Due after 1 but within 5 years	15,730	15,464
Due after 5 but within 10 years	26,342	26,269
Due after 10 years	2,426	2,896
	48,597	48,718
Mortgage-Backed Securities (a)	865,083	838,668
Total Debt Securities	$913,680	$887,386

(a) Mortgage-Backed Securities include an amortized cost of $179.4 million and a fair value of $177.0 million for Obligations of U.S. Government agencies issued by Ginnie Mae and an amortized cost of $685.7 million and a fair value of $661.6 million for Obligations of U.S. Government-sponsored enterprises issued by Fannie Mae and Freddie Mac.

Proceeds from sales, gross gains (losses) realized on sales, maturities and other-than-temporary impairment charges related to securities available for sale were as follows for the nine months ended September 30:

	2018	2017
	(dollars in thousands)	
Proceeds from sales	$15,939	$143,660
Gross gains (losses) realized:		
Sales Transactions:		
Gross gains	$4,719	$359
Gross losses	—	(316)
	4,719	43
Maturities and impairment		
Gross gains	3,383	712
Gross losses	—	(60)
	3,383	652
Net gains and impairment	$8,102	$695

Gross gains from sales transactions of $4.7 million were recognized in 2018 as a result of the sale of the remaining pooled trust preferred security portfolio. Gross gains from maturities and impairment of $3.4 million were recognized in 2018 as a result of successful auction calls on PreSTL XIV and PreSTL IX, two of our pooled trust preferred securities. Gross gains of $0.7 million were recognized in 2017 due to the early redemption of another of our trust preferred securities, PreSTL VII.

Securities available for sale with an estimated fair value of $680.9 million and $569.0 million were pledged as of September 30, 2018 and December 31, 2017, respectively, to secure public deposits and for other purposes required or permitted by law.

ITEM 1. Financial Statements and Supplementary Data
FIRST COMMONWEALTH FINANCIAL CORPORATION AND SUBSIDIARIES
NOTES TO THE UNAUDITED CONDENSED CONSOLIDATED FINANCIAL STATEMENTS (Continued)

Securities Held to Maturity
Below is an analysis of the amortized cost and fair values of debt securities held to maturity at:

	September 30, 2018				December 31, 2017			
	Amortized Cost	Gross Unrealized Gains	Gross Unrealized Losses	Estimated Fair Value	Amortized Cost	Gross Unrealized Gains	Gross Unrealized Losses	Estimated Fair Value
	(dollars in thousands)							
Obligations of U.S. Government Agencies:								
Mortgage-Backed Securities – Residential	$3,663	$ —	$(156)	$3,507	$3,925	$ —	$(14)	$3,911
Mortgage-Backed Securities-Commercial	55,726	—	(2,742)	52,984	58,249	—	(1,394)	56,855
Obligations of U.S. Government-Sponsored Enterprises:								
Mortgage-Backed Securities – Residential	273,972	—	(11,468)	262,504	305,126	10	(2,552)	302,584
Mortgage-Backed Securities – Commercial	13,413	—	(427)	12,986	14,056	—	(71)	13,985
Obligations of States and Political Subdivisions	42,447	5	(895)	41,557	40,540	335	(161)	40,714
Debt Securities Issued by Foreign Governments	400	—	(5)	395	200	—	—	200
Total Securities Held to Maturity	$389,621	$ 5	$(15,693)	$373,933	$422,096	$ 345	$(4,192)	$418,249

The amortized cost and estimated fair value of debt securities held to maturity at September 30, 2018, by contractual maturity, are shown below. Expected maturities will differ from contractual maturities because borrowers may have the right to call or repay obligations with or without call or prepayment penalties.

	Amortized Cost	Estimated Fair Value
	(dollars in thousands)	
Due within 1 year	$85	$85
Due after 1 but within 5 years	3,814	3,778
Due after 5 but within 10 years	37,329	36,491
Due after 10 years	1,619	1,598
	42,847	41,952
Mortgage-Backed Securities (a)	346,774	331,981
Total Debt Securities	$389,621	$373,933

(a) Mortgage-Backed Securities include an amortized cost of $59.4 million and a fair value of $56.5 million for Obligations of U.S. Government agencies issued by Ginnie Mae and an amortized cost of $287.4 million and a fair value of $275.5 million for Obligations of U.S. Government-sponsored enterprises issued by Fannie Mae and Freddie Mac.

Securities held to maturity with an amortized cost of $298.9 million and $338.3 million were pledged as of September 30, 2018 and December 31, 2017, respectively, to secure public deposits and for other purposes required or permitted by law.

ITEM 1. Financial Statements and Supplementary Data
FIRST COMMONWEALTH FINANCIAL CORPORATION AND SUBSIDIARIES
NOTES TO THE UNAUDITED CONDENSED CONSOLIDATED FINANCIAL STATEMENTS (Continued)

Note 8 Impairment of Investment Securities
Securities Available for Sale and Held to Maturity
As required by FASB ASC Topic 320, “Investments – Debt and Equity Securities,” credit-related other-than-temporary impairment on debt securities is recognized in earnings, while non-credit related other-than-temporary impairment on debt securities not expected to be sold is recognized in OCI. During the nine months ended September 30, 2018 and 2017, no other-than-temporary impairment charges were recognized.
First Commonwealth utilizes the specific identification method to determine the net gain or loss on debt securities and the average cost method to determine the net gain or loss on equity securities.
We review our investment portfolio on a quarterly basis for indications of impairment. This review includes analyzing the length of time and the extent to which the fair value has been lower than the cost, the financial condition and near-term prospects of the issuer, including any specific events which may influence the operations of the issuer and whether we are more likely than not to sell, or be required to sell, the security. We evaluate whether we are more likely than not to sell debt securities based upon our investment strategy for the particular type of security, our cash flow needs, liquidity position, capital adequacy, tax position and interest rate risk position. In addition, the risk of future other-than-temporary impairment may be influenced by weakness in the U.S. economy or changes in real estate values.
The following table presents the gross unrealized losses and estimated fair values at September 30, 2018 for both available for sale and held to maturity securities by investment category and time frame for which securities have been in a continuous unrealized loss position:

	Less Than 12 Months		12 Months or More		Total	
	Estimated Fair Value	Gross Unrealized Losses	Estimated Fair Value	Gross Unrealized Losses	Estimated Fair Value	Gross Unrealized Losses
	(dollars in thousands)					
Obligations of U.S. Government Agencies:						
Mortgage-Backed Securities – Residential	$7,267	$(288)	$—	$—	$7,267	$(288)
Mortgage-Backed Securities – Commercial	144,211	(1,538)	76,183	(3,879)	220,394	(5,417)
Obligations of U.S. Government-Sponsored Enterprises:						
Mortgage-Backed Securities – Residential	399,505	(10,329)	489,431	(26,218)	888,936	(36,547)
Mortgage-Backed Securities – Commercial	12,986	(427)	—	—	12,986	(427)
Other Government-Sponsored Enterprises	—	—	100	—	100	—
Obligations of States and Political Subdivisions	44,422	(635)	5,781	(389)	50,203	(1,024)
Debt securities issued by foreign governments	395	(5)	—	—	395	(5)
Corporate Securities	18,702	(279)	—	—	18,702	(279)
Total Securities	$627,488	$(13,501)	$571,495	$(30,486)	$1,198,983	$(43,987)

At September 30, 2018, fixed income securities issued by U.S. Government-sponsored enterprises and U.S. Government agencies comprised 84% and 13%, respectively, of total unrealized losses due to changes in market interest rates. At September 30, 2018, there are 183 debt securities in an unrealized loss position.

ITEM 1. Financial Statements and Supplementary Data
FIRST COMMONWEALTH FINANCIAL CORPORATION AND SUBSIDIARIES
NOTES TO THE UNAUDITED CONDENSED CONSOLIDATED FINANCIAL STATEMENTS (Continued)

The following table presents the gross unrealized losses and estimated fair values at December 31, 2017 by investment category and time frame for which securities have been in a continuous unrealized loss position:

	Less Than 12 Months		12 Months or More		Total	
	Estimated Fair Value	Gross Unrealized Losses	Estimated Fair Value	Gross Unrealized Losses	Estimated Fair Value	Gross Unrealized Losses
	(dollars in thousands)					
Obligations of U.S. Government Agencies:						
Mortgage-Backed Securities – Residential	$5,584	$(21)	$—	$—	$5,584	$(21)
Mortgage-Backed Securities - Commercial	48,322	(962)	32,683	(894)	81,005	(1,856)
Obligations of U.S. Government-Sponsored Enterprises:						
Mortgage-Backed Securities – Residential	351,222	(2,295)	400,984	(9,746)	752,206	(12,041)
Mortgage-Backed Securities – Commercial	13,985	(71)	—	—	13,985	(71)
Other Government-Sponsored Enterprises	997	(1)	99	—	1,096	(1)
Obligation of States and Political Subdivisions	7,144	(32)	3,653	(129)	10,797	(161)
Corporate Securities	3,993	(4)	—	—	3,993	(4)
Pooled Trust Preferred Collateralized Debt Obligations	—	—	19,120	(4,379)	19,120	(4,379)
Total Securities	$431,247	$(3,386)	$456,539	$(15,148)	$887,786	$(18,534)

As of September 30, 2018, our corporate securities had an amortized cost and an estimated fair value of $20.9 million and $21.1 million, respectively. As of December 31, 2017, our corporate securities had an amortized cost and estimated fair value of $15.9 million and $16.5 million, respectively. Corporate securities are comprised of debt for large regional banks. There were four corporate securities in an unrealized loss position as of September 30, 2018 and one corporate security in an unrealized loss position as of December 31, 2017. When unrealized losses exist on these investments, management reviews each of the issuer’s asset quality, earnings trends and capital position, to determine whether issues in an unrealized loss position were other-than-temporarily impaired. All interest payments on the corporate securities are being made as contractually required.

During the first six months of 2018, all of our pooled trust preferred collateralized debt obligations were liquidated either through a successful auction call or sale. At December 31, 2017, the pooled trust preferred securities had an amortized cost and estimated fair value of $27.5 million and $23.6 million, respectively. Other-than-temporary impairment charges were recognized on the pooled trust preferred securities in 2008, 2009 and 2010. The following table provides a cumulative roll forward of credit losses recognized in earnings for the trust preferred securities:

	For the Three Months Ended September 30,		For the Nine Months Ended September 30,	
	2018	2017	2018	2017
	(dollars in thousands)			
Balance, beginning (a)	$—	$16,610	$12,208	$17,056
Credit losses on debt securities for which other-than-temporary impairment was not previously recognized	—	—	—	—
	—	—	—	—

Additional credit losses on debt securities for which other-than-temporary impairment was previously recognized				
Increases in cash flows expected to be collected, recognized over the remaining life of the security (b)	—	(219)	(223)	(665)
Reduction for debt securities sold during the period	—	—	(9,164)	—
Reduction for debt securities called during the period	—	—	(2,821)	—
Balance, ending	$—	$16,391	$—	$16,391

(a) The beginning balance represents credit related losses included in other-than-temporary impairment charges recognized on debt securities in prior periods.

(b) Represents the increase in cash flows recognized in interest income during the period.

During the nine-months ended September 30, 2018, there were no gains or losses recognized through earnings on equity securities. During the nine-months ended September 30, 2017, no other-than-temporary impairment charges were recorded on equity securities. On a quarterly basis, management evaluates equity securities for other-than-temporary impairment by reviewing the severity and duration of decline in estimated fair value, research reports, analysts' recommendations, credit rating changes, news stories, annual reports, regulatory filings, impact of interest rate changes and other relevant information. As of September 30, 2018 and 2017, there were no equity securities in an unrealized loss position.

Other Investments

As a member of the Federal Home Loan Bank ("FHLB"), First Commonwealth is required to purchase and hold stock in the FHLB to satisfy membership and borrowing requirements. The level of stock required to be held is dependent on the amount of First Commonwealth's mortgage-related assets and outstanding borrowings with the FHLB. This stock is restricted in that it can only be sold to the FHLB or to another member institution, and all sales of FHLB stock must be at par. As a result of these restrictions, FHLB stock is unlike other investment securities insofar as there is no trading market for FHLB stock and the transfer price is determined by FHLB membership rules and not by market participants. As of September 30, 2018 and December 31, 2017, our FHLB stock totaled $25.0 million and $29.8 million, respectively, and is included in “Other investments” on the Condensed Consolidated Statements of Financial Condition.

FHLB stock is held as a long-term investment and its value is determined based on the ultimate recoverability of the par value. First Commonwealth evaluates impairment quarterly and has concluded that the par value of its investment in FHLB stock will be recovered. Accordingly, no impairment charge was recorded on these securities during the three and nine months ended September 30, 2018.

Note 9 Loans and Allowance for Credit Losses

The following table provides outstanding balances related to each of our loan types:

	September 30, 2018			December 31, 2017		
	Originated	Acquired	Total	Originated	Acquired	Total
	(dollars in thousands)					
Commercial, financial, agricultural and other	$1,079,537	$36,667	$1,116,204	$1,122,741	$40,642	$1,163,383
Real estate construction	291,645	6,750	298,395	242,905	5,963	248,868
Residential real estate	1,277,427	255,911	1,533,338	1,206,119	220,251	1,426,370
Commercial real estate	1,929,219	207,212	2,136,431	1,892,185	126,911	2,019,096
Loans to individuals	572,696	5,718	578,414	543,411	6,248	549,659
Total loans	$5,150,524	$512,258	$5,662,782	$5,007,361	$400,015	$5,407,376

ITEM 1. Financial Statements and Supplementary Data
FIRST COMMONWEALTH FINANCIAL CORPORATION AND SUBSIDIARIES
NOTES TO THE UNAUDITED CONDENSED CONSOLIDATED FINANCIAL STATEMENTS (Continued)

Credit Quality Information

As part of the on-going monitoring of credit quality within the loan portfolio, the following credit worthiness categories are used in grading our loans:

Pass	Acceptable levels of risk exist in the relationship. Includes all loans not classified as OAEM, substandard or doubtful.
Other Assets Especially Mentioned (OAEM)	Potential weaknesses that deserve management's close attention. The potential weaknesses may result in deterioration of the repayment prospects or weaken the Company's credit position at some future date. The credit risk may be relatively minor, yet constitute an undesirable risk in light of the circumstances surrounding the specific credit. No loss of principal or interest is expected.
Substandard	Well-defined weakness or a weakness that jeopardizes the repayment of the debt. A loan may be classified as substandard as a result of deterioration of the borrower's financial condition and repayment capacity. Loans for which repayment plans have not been met or collateral equity margins do not protect the Company may also be classified as substandard.
Doubtful	Loans with the characteristics of substandard loans with the added characteristic that collection or liquidation in full, on the basis of presently existing facts and conditions, is highly improbable.

The use of creditworthiness categories to grade loans permits management's use of migration analysis to estimate a portion of credit risk. The Company's internal creditworthiness grading system provides a measurement of credit risk based primarily on an evaluation of the borrower's cash flow and collateral. Movement between these rating categories provides a predictive measure of credit losses and therefore assists in determining the appropriate level for the loan loss reserves. Category ratings are reviewed each quarter, at which time management analyzes the results, as well as other external statistics and factors related to loan performance. Loans that migrate towards higher risk rating levels generally have an increased risk of default, whereas loans that migrate toward lower risk ratings generally will result in a lower risk factor being applied to those related loan balances.

The following tables represent our credit risk profile by creditworthiness:

	September 30, 2018					
	Commercial, financial, agricultural and other	Real estate construction	Residential real estate	Commercial real estate	Loans to individuals	Total
	(dollars in thousands)					
Originated loans						
Pass	$1,023,855	$ 282,713	$1,266,805	$1,876,336	$ 572,504	$5,022,213
Non-Pass						
OAEM	40,624	8,932	1,135	32,825	—	83,516
Substandard	10,740	—	9,487	20,058	192	40,477
Doubtful	4,318	—	—	—	—	4,318
Total Non-Pass	55,682	8,932	10,622	52,883	192	128,311
Total	$1,079,537	$ 291,645	$1,277,427	$1,929,219	$ 572,696	$5,150,524
Acquired loans						
Pass	$30,328	$ 6,104	$252,769	$204,074	$ 5,703	$498,978
Non-Pass						
OAEM	6,238	646	652	460	—	7,996
Substandard	101	—	2,490	2,678	15	5,284
Doubtful	—	—	—	—	—	—

Total Non-Pass	6,339	646	3,142	3,138	15	13,280
Total	$36,667	$ 6,750	$255,911	$207,212	$ 5,718	$512,258

ITEM 1. Financial Statements and Supplementary Data
FIRST COMMONWEALTH FINANCIAL CORPORATION AND SUBSIDIARIES
NOTES TO THE UNAUDITED CONDENSED CONSOLIDATED FINANCIAL STATEMENTS (Continued)

	December 31, 2017 Commercial, financial, agricultural and other	Real estate construction	Residential real estate	Commercial real estate	Loans to individuals	Total
	(dollars in thousands)					
Originated loans						
Pass	$1,061,147	$ 242,905	$1,194,352	$1,855,253	$ 543,175	$4,896,832
Non-Pass						
OAEM	26,757	—	1,435	13,326	—	41,518
Substandard	30,431	—	10,332	23,606	236	64,605
Doubtful	4,406	—	—	—	—	4,406
Total Non-Pass	61,594	—	11,767	36,932	236	110,529
Total	$1,122,741	$ 242,905	$1,206,119	$1,892,185	$ 543,411	$5,007,361
Acquired loans						
Pass	$34,573	$ 5,963	$217,824	$121,536	$ 6,231	$386,127
Non-Pass						
OAEM	5,567	—	798	3,517	—	9,882
Substandard	502	—	1,629	1,858	17	4,006
Doubtful	—	—	—	—	—	—
Total Non-Pass	6,069	—	2,427	5,375	17	13,888
Total	$40,642	$ 5,963	$220,251	$126,911	$ 6,248	$400,015

Portfolio Risks

The credit quality of our loan portfolio can potentially represent significant risk to our earnings, capital and liquidity. First Commonwealth devotes substantial resources to managing this risk primarily through our credit administration department that develops and administers policies and procedures for underwriting, maintaining, monitoring and collecting loans. Credit administration is independent of our lending departments and oversight is provided by the credit committee of the First Commonwealth Board of Directors.

Criticized loans have been evaluated when determining the appropriateness of the allowance for credit losses, which we believe is adequate to absorb losses inherent to the portfolio as of September 30, 2018. However, changes in economic conditions, interest rates, borrower financial condition, delinquency trends or previously established fair values of collateral factors could significantly change those judgmental estimates.

ITEM 1. Financial Statements and Supplementary Data
FIRST COMMONWEALTH FINANCIAL CORPORATION AND SUBSIDIARIES
NOTES TO THE UNAUDITED CONDENSED CONSOLIDATED FINANCIAL STATEMENTS (Continued)

Age Analysis of Past Due Loans by Segment
The following tables delineate the aging analysis of the recorded investments in past due loans as of September 30, 2018 and December 31, 2017. Also included in these tables are loans that are 90 days or more past due and still accruing because they are well-secured and in the process of collection.

	September 30, 2018						
	30 - 59 days past due	60 - 89 days past due	90 days and greater and still accruing	Nonaccrual	Total past due and nonaccrual	Current	Total
	(dollars in thousands)						
Originated loans							
Commercial, financial, agricultural and other	$340	$—	$ 66	$ 11,506	$ 11,912	$1,067,625	$1,079,537
Real estate construction	—	—	—	—	—	291,645	291,645
Residential real estate	2,994	1,084	486	5,890	10,454	1,266,973	1,277,427
Commercial real estate	1,351	383	270	9,805	11,809	1,917,410	1,929,219
Loans to individuals	2,204	644	573	193	3,614	569,082	572,696
Total	$6,889	$2,111	$ 1,395	$ 27,394	$ 37,789	$5,112,735	$5,150,524
Acquired loans							
Commercial, financial, agricultural and other	$—	$—	$ 20	$ 73	$ 93	$36,574	$36,667
Real estate construction	1,126	—	—	—	1,126	5,624	6,750
Residential real estate	391	95	191	2,395	3,072	252,839	255,911
Commercial real estate	43	—	—	1,920	1,963	205,249	207,212
Loans to individuals	25	22	41	15	103	5,615	5,718
Total	$1,585	$117	$ 252	$ 4,403	$ 6,357	$505,901	$512,258

22

ITEM 1. Financial Statements and Supplementary Data
FIRST COMMONWEALTH FINANCIAL CORPORATION AND SUBSIDIARIES
NOTES TO THE UNAUDITED CONDENSED CONSOLIDATED FINANCIAL STATEMENTS (Continued)

	December 31, 2017						
	30 - 59 days past due	60 - 89 days past due	90 days and greater and still accruing	Nonaccrual	Total past due and nonaccrual	Current	Total
	(dollars in thousands)						
Originated loans							
Commercial, financial, agricultural and other	$378	$61	$ 40	$ 18,741	$ 19,220	$1,103,521	$1,122,741
Real estate construction	199	—	—	—	199	242,706	242,905
Residential real estate	4,618	1,025	1,076	6,225	12,944	1,193,175	1,206,119
Commercial real estate	2,198	28	6	3,240	5,472	1,886,713	1,892,185
Loans to individuals	1,899	769	623	236	3,527	539,884	543,411
Total	$9,292	$1,883	$ 1,745	$ 28,442	$ 41,362	$4,965,999	$5,007,361
Acquired loans							
Commercial, financial, agricultural and other	$6	$7	$ —	$ 436	$ 449	$40,193	$40,642
Real estate construction	—	—	—	—	—	5,963	5,963
Residential real estate	148	9	83	705	945	219,306	220,251
Commercial real estate	—	—	—	1,077	1,077	125,834	126,911
Loans to individuals	36	20	26	17	99	6,149	6,248
Total	$190	$36	$ 109	$ 2,235	$ 2,570	$397,445	$400,015

Nonaccrual Loans

The previous tables summarize nonaccrual loans by loan segment. The Company generally places loans on nonaccrual status when the full and timely collection of interest or principal becomes uncertain, when part of the principal balance has been charged off and no restructuring has occurred, or the loans reach a certain number of days past due. Generally, loans 90 days or more past due are placed on nonaccrual status, except for consumer loans, which are placed on nonaccrual status at 150 days past due.

When a loan is placed on nonaccrual, the accrued unpaid interest receivable is reversed against interest income and all future payments received are applied as a reduction to the loan principal. Generally, the loan is returned to accrual status when (a) all delinquent interest and principal becomes current under the terms of the loan agreement or (b) the loan is both well-secured and in the process of collection and collectability is no longer in doubt.

Impaired Loans

Management considers loans to be impaired when, based on current information and events, it is determined that the Company will not be able to collect all amounts due according to the loan contract, including scheduled interest payments. Determination of impairment is treated the same across all loan categories. When management identifies a loan as impaired, the impairment is measured based on the present value of expected future cash flows, discounted at the loan's effective interest rate, except when the sole source for repayment of the loan is the operation or liquidation of collateral. When the loan is collateral dependent, the appraised value less estimated cost to sell is utilized. If management determines the value of the impaired loan is less than the recorded investment in the loan, impairment is recognized through an allowance estimate or a charge-off to the allowance. Troubled debt restructured loans on accrual status are also considered to be impaired loans.

When the ultimate collectability of the total principal of an impaired loan is in doubt and the loan is on nonaccrual status, all payments are applied to principal under the cost recovery method. When the ultimate collectability of the total principal of an impaired loan is not in doubt and the loan is on nonaccrual status, contractual interest is credited to interest income when received under the cash basis method.

At September 30, 2018 and December 31, 2017, there were no nonaccrual loans held for sale. During the nine months ended, September 30, 2018, a gain of $1.2 million was recognized on the sale of an impaired commercial, financial, agricultural and

ITEM 1. Financial Statements and Supplementary Data
FIRST COMMONWEALTH FINANCIAL CORPORATION AND SUBSIDIARIES
NOTES TO THE UNAUDITED CONDENSED CONSOLIDATED FINANCIAL STATEMENTS (Continued)

other relationship. There were $21 thousand in gains recognized in the same period in 2017 on the sale of an impaired commercial, financial, agricultural and other loan.
The following tables include the recorded investment and unpaid principal balance for impaired loans with the associated allowance amount, if applicable, as of September 30, 2018 and December 31, 2017. Also presented are the average recorded investment in impaired loans and the related amount of interest recognized while the loan was considered impaired. Average balances are calculated using month-end balances of the loans for the period reported and are included in the table below based on their period-end allowance position.

	September 30, 2018			December 31, 2017		
	Recorded investment	Unpaid principal balance	Related allowance	Recorded investment	Unpaid principal balance	Related allowance
	(dollars in thousands)					
Originated loans:						
With no related allowance recorded:						
Commercial, financial, agricultural and other	$3,177	$9,585		$5,548	$12,153	
Real estate construction	—	—		—	—	
Residential real estate	10,302	12,163		10,625	12,470	
Commercial real estate	4,951	7,559		5,155	5,489	
Loans to individuals	287	414		347	383	
Subtotal	18,717	29,721		21,675	30,495	
With an allowance recorded:						
Commercial, financial, agricultural and other	9,998	10,219	$ 3,474	16,866	21,094	$ 3,478
Real estate construction	—	—	—	—	—	—
Residential real estate	596	602	167	456	478	107
Commercial real estate	6,094	6,161	1,722	954	954	128
Loans to individuals	—	—	—	—	—	—
Subtotal	16,688	16,982	5,363	18,276	22,526	3,713
Total	$35,405	$46,703	$ 5,363	$39,951	$53,021	$ 3,713

ITEM 1. Financial Statements and Supplementary Data
FIRST COMMONWEALTH FINANCIAL CORPORATION AND SUBSIDIARIES
NOTES TO THE UNAUDITED CONDENSED CONSOLIDATED FINANCIAL STATEMENTS (Continued)

	September 30, 2018			December 31, 2017		
	Recorded investment	Unpaid principal balance	Related allowance	Recorded investment	Unpaid principal balance	Related allowance
	(dollars in thousands)					
Acquired loans						
With no related allowance recorded:						
Commercial, financial, agricultural and other	$73	$ 73		$436	$ 449	
Real estate construction	—	—		—	—	
Residential real estate	2,436	3,006		666	965	
Commercial real estate	1,920	2,919		940	1,842	
Loans to individuals	15	17		17	17	
Subtotal	4,444	6,015		2,059	3,273	
With an allowance recorded:						
Commercial, financial, agricultural and other	—	—	$ —	—	—	$ —
Real estate construction	—	—	—	—	—	—
Residential real estate	—	—	—	93	122	4
Commercial real estate	—	—	—	137	150	29
Loans to individuals	—	—	—	—	—	—
Subtotal	—	—	—	230	272	33
Total	$4,444	$ 6,015	$ —	$2,289	$ 3,545	$ 33

	For the Nine Months Ended September 30,							
	2018				2017			
	Originated Loans		Acquired Loans		Originated Loans		Acquired Loans	
	Average recorded investment	Interest income recognized	Average recorded investment	Interest income recognized	Average recorded investment	Interest income recognized	Average recorded investment	Interest income recognized
	(dollars in thousands)							
With no related allowance recorded:								
Commercial, financial, agricultural and other	$17,838	$ 576	$261	$ 10	$11,627	$ 142	$48	$ 1
Real estate construction	—	—	—	—	—	—	33	—
Residential real estate	10,639	191	1,779	3	11,417	245	487	—
Commercial real estate	7,632	146	1,558	—	6,439	522	2,076	—
Loans to individuals	322	6	16	—	350	16	2	—
Subtotal	36,431	919	3,614	13	29,833	925	2,646	1
With an allowance recorded:								
Commercial, financial, agricultural and other	5,979	16	—	—	8,984	77	316	—
Real estate construction	—	—	—	—	—	—	—	—
Residential real estate	532	11	—	—	266	—	68	—
Commercial real estate	1,787	3	—	—	354	14	159	—
Loans to individuals	—	—	—	—	—	—	—	—
Subtotal	8,298	30	—	—	9,604	91	543	—

Total	$44,729	$ 949	$3,614	$ 13	$39,437	$ 1,016	$3,189	$ 1

25

ITEM 1. Financial Statements and Supplementary Data
FIRST COMMONWEALTH FINANCIAL CORPORATION AND SUBSIDIARIES
NOTES TO THE UNAUDITED CONDENSED CONSOLIDATED FINANCIAL STATEMENTS (Continued)

	For the Three Months Ended September 30,							
	2018				2017			
	Originated Loans		Acquired Loans		Originated Loans		Acquired Loans	
	Average recorded investment	Interest Income Recognized	Average recorded investment	Interest Income Recognized	Average recorded investment	Interest Income Recognized	Average recorded investment	Interest Income Recognized
	(dollars in thousands)							
With no related allowance recorded:								
Commercial, financial, agricultural and other	$5,697	$ 8	$73	$ 10	$7,106	$ 62	$72	$ 1
Real estate construction	—	—	—	—	—	—	—	—
Residential real estate	10,627	59	2,541	2	11,217	82	653	—
Commercial real estate	6,810	59	1,955	—	5,928	452	3,078	—
Loans to individuals	320	2	16	—	366	5	6	—
Subtotal	23,454	128	4,585	12	24,617	601	3,809	1
With an allowance recorded:								
Commercial, financial, agricultural and other	10,298	4	—	—	8,510	32	786	—
Real estate construction	—	—	—	—	—	—	—	—
Residential real estate	565	2	—	—	377	—	95	—
Commercial real estate	4,342	1	—	—	315	4	154	—
Loans to individuals	—	—	—	—	—	—	—	—
Subtotal	15,205	7	—	—	9,202	36	1,035	—
Total	$38,659	$ 135	$4,585	$ 12	$33,819	$ 637	$4,844	$ 1

Unfunded commitments related to nonperforming loans were $1.5 million at September 30, 2018 and $2.4 million at December 31, 2017. After consideration of the requirements to draw and available collateral related to these commitments, a reserve of $12 thousand and $0.2 million was established for these off balance sheet exposures at September 30, 2018 and December 31, 2017, respectively.

Troubled debt restructured loans are those loans whose terms have been renegotiated to provide a reduction or deferral of principal or interest as a result of the financial difficulties experienced by the borrower, who could not obtain comparable terms from alternate financing sources.

The following table provides detail as to the total troubled debt restructured loans and total commitments outstanding on troubled debt restructured loans:

	September 30, 2018	December 31, 2017
	(dollars in thousands)	
Troubled debt restructured loans		
Accrual status	$8,052	$ 11,563
Nonaccrual status	13,876	11,222
Total	$21,928	$ 22,785
Commitments		
Letters of credit	$60	$ 60
Unused lines of credit	895	54

Total	$955	$ 114

26

ITEM 1. Financial Statements and Supplementary Data
FIRST COMMONWEALTH FINANCIAL CORPORATION AND SUBSIDIARIES
NOTES TO THE UNAUDITED CONDENSED CONSOLIDATED FINANCIAL STATEMENTS (Continued)

The following tables provide detail, including specific reserves and reasons for modification, related to loans identified as troubled debt restructurings:

	For the Nine Months Ended September 30, 2018						
		Type of Modification					
	Number of Contracts	Extend Maturity	Modify Rate	Modify Payments	Total Pre-Modification Outstanding Recorded Investment	Post-Modification Outstanding Recorded Investment	Specific Reserve
	(dollars in thousands)						
Commercial, financial, agricultural and other	3	$74	$ —	$ 8,250	$ 8,324	$ 7,393	$ 2,811
Residential real estate	24	85	145	959	1,189	1,108	—
Commercial real estate	2	—	—	966	966	943	—
Loans to individuals	13	—	77	44	121	103	—
Total	42	$ 159	$ 222	$ 10,219	$ 10,600	$ 9,547	$ 2,811

	For the Nine Months Ended September 30, 2017						
		Type of Modification					
	Number of Contracts	Extend Maturity	Modify Rate	Modify Payments	Total Pre-Modification Outstanding Recorded Investment	Post-Modification Outstanding Recorded Investment	Specific Reserve
	(dollars in thousands)						
Commercial, financial, agricultural and other	6	$6,768	$ 1,786	$ 47	$ 8,601	$ 6,307	$ 669
Residential real estate	15	129	204	513	846	777	2
Commercial real estate	4	179	—	111	290	280	—
Loans to individuals	8	—	17	60	77	62	—
Total	33	$7,076	$ 2,007	$ 731	$ 9,814	$ 7,426	$ 671

The troubled debt restructurings included in the above tables are also included in the impaired loan tables provided earlier in this note. Loans defined as modified due to a change in rate may include loans that were modified for a change in rate as well as a re-amortization of the principal and an extension of the maturity. For the nine months ended September 30, 2018 and 2017, $0.2 million and $0.3 million, respectively, of total rate modifications represent loans with modifications to the rate as well as payment as a result of re-amortization. For both 2018 and 2017 the changes in loan balances between the pre-modification balance and the post-modification balance are due to customer payments.

ITEM 1. Financial Statements and Supplementary Data
FIRST COMMONWEALTH FINANCIAL CORPORATION AND SUBSIDIARIES
NOTES TO THE UNAUDITED CONDENSED CONSOLIDATED FINANCIAL STATEMENTS (Continued)

The following tables provide detail, including specific reserves and reasons for modification, related to loans identified as troubled debt restructurings:

	For the Three Months Ended September 30, 2018						
		Type of Modification					
	Number of Contracts	Extend Maturity	Modify Rate	Modify Payments	Total Pre-Modification Outstanding Recorded Investment	Post-Modification Outstanding Recorded Investment	Specific Reserve
	(dollars in thousands)						
Commercial, financial, agricultural and other	1	$74	$ —	$ —	$ 74	$ 74	$ —
Residential real estate	7	65	70	230	365	338	—
Loans to individuals	6	—	26	17	43	40	—
Total	14	$139	$ 96	$ 247	$ 482	$ 452	$ —

	For the Three Months Ended, September 30, 2017						
		Type of Modification					
	Number of Contracts	Extend Maturity	Modify Rate	Modify Payments	Total Pre-Modification Outstanding Recorded Investment	Post-Modification Outstanding Recorded Investment	Specific Reserve
	(dollars in thousands)						
Commercial, financial, agricultural and other	1	$—	$ —	$ 47	$ 47	$ 47	$ —
Residential real estate	4	—	17	100	117	106	—
Commercial real estate	1	—	—	27	27	25	—
Loans to individuals	1	—	—	12	12	11	—
Total	7	$—	$ 17	$ 186	$ 203	$ 189	$ —

The troubled debt restructurings included in the above tables are also included in the impaired loan tables provided earlier in this note. Loans defined as modified due to a change in rate may include loans that were modified for a change in rate as well as a re-amortization of the principal and an extension of the maturity. For the three months ended September 30, 2018 and 2017, $96 thousand and $17 thousand, respectively, of total rate modifications represent loans with modifications to the rate as well as payment as a result of re-amortization. For both 2018 and 2017 the changes in loan balances between the pre-modification balance and the post-modification balance are due to customer payments.

A troubled debt restructuring is considered to be in default when a restructured loan is 90 days or more past due. The following table provides information related to loans that were restructured within the past twelve months and that were considered to be in default during the nine months ended September 30:

	2018		2017	
	Number of Contracts	Recorded Investment	Number of Contracts	Recorded Investment
	(dollars in thousands)			
Commercial, financial, agricultural and other	1	$ 272	—	$ —
Residential real estate	1	$ 49	1	$ 9
Loans to individuals	1	8	1	2

Total	3	$	329	2	$	11

28

ITEM 1. Financial Statements and Supplementary Data
FIRST COMMONWEALTH FINANCIAL CORPORATION AND SUBSIDIARIES
NOTES TO THE UNAUDITED CONDENSED CONSOLIDATED FINANCIAL STATEMENTS (Continued)

The following table provides information related to loans that were restructured within the past twelve months and that were considered to be in default during the three months ended September 30:

	2018		2017	
	Number of Contracts	Recorded Investment	Number of Contracts	Recorded Investment
	(dollars in thousands)			
Residential real estate	1	$ 49	—	$ —
Loans to individuals	1	$ 8	1	$ 2
Total	2	$ 57	1	$ 2

The following tables provide detail related to the allowance for credit losses:

	For the Nine Months Ended September 30, 2018					
	Commercial, financial, agricultural and other	Real estate construction	Residential real estate	Commercial real estate	Loans to individuals	Total
	(dollars in thousands)					
Allowance for credit losses:						
Originated loans:						
Beginning balance	$23,418	$ 1,349	$ 2,753	$ 17,328	$ 3,404	$48,252
Charge-offs	(3,443)	—	(949)	(2,411)	(3,321)	(10,124)
Recoveries	671	93	222	123	460	1,569
Provision (credit)	1,343	150	1,584	4,623	3,274	10,974
Ending balance	21,989	1,592	3,610	19,663	3,817	50,671
Acquired loans:						
Beginning balance	11	—	6	29	—	46
Charge-offs	(93)	—	(57)	—	(15)	(165)
Recoveries	31	6	75	—	24	136
Provision (credit)	71	(6)	23	(21)	(9)	58
Ending balance	20	—	47	8	—	75
Total ending balance	$22,009	$ 1,592	$ 3,657	$ 19,671	$ 3,817	$50,746
Ending balance: individually evaluated for impairment	$3,474	$ —	$ 167	$ 1,722	$ —	$5,363
Ending balance: collectively evaluated for impairment	18,535	1,592	3,490	17,949	3,817	45,383
Loans:						
Ending balance	1,116,204	298,395	1,533,338	2,136,431	578,414	5,662,782
Ending balance: individually evaluated for impairment	12,864	—	4,522	12,012	—	29,398
Ending balance: collectively evaluated for impairment	1,103,340	298,395	1,528,816	2,124,419	578,414	5,633,384

ITEM 1. Financial Statements and Supplementary Data
FIRST COMMONWEALTH FINANCIAL CORPORATION AND SUBSIDIARIES
NOTES TO THE UNAUDITED CONDENSED CONSOLIDATED FINANCIAL STATEMENTS (Continued)

	For the Nine Months Ended September 30, 2017					
	Commercial, financial, agricultural and other	Real estate construction	Residential real estate	Commercial real estate	Loans to individuals	Total
	(dollars in thousands)					
Allowance for credit losses:						
Originated loans:						
Beginning balance	$35,974	$ 577	$ 2,492	$ 6,619	$ 4,504	$50,166
Charge-offs	(5,776)	—	(954)	(95)	(3,185)	(10,010)
Recoveries	3,819	465	259	206	355	5,104
Provision (credit)	(11,353)	299	1,095	10,593	1,752	2,386
Ending balance	22,664	1,341	2,892	17,323	3,426	47,646
Acquired loans:						
Beginning balance	—	—	19	—	—	19
Charge-offs	—	—	(26)	—	(17)	(43)
Recoveries	1	5	45	4	51	106
Provision (credit)	479	(5)	(32)	40	(34)	448
Ending balance	480	—	6	44	—	530
Total ending balance	$23,144	$ 1,341	$ 2,898	$ 17,367	$ 3,426	$48,176
Ending balance: individually evaluated for impairment	$1,818	$ —	$ 102	$ 261	$ —	$2,181
Ending balance: collectively evaluated for impairment	21,326	1,341	2,796	17,106	3,426	45,995
Loans:						
Ending balance	1,154,225	259,129	1,423,422	1,990,264	548,807	5,375,847
Ending balance: individually evaluated for impairment	15,995	—	7,142	8,189	—	31,326
Ending balance: collectively evaluated for impairment	1,138,230	259,129	1,416,280	1,982,075	548,807	5,344,521

	For the Three Months Ended September 30, 2018					
	Commercial, financial, agricultural and other	Real estate construction	Residential real estate	Commercial real estate	Loans to individuals	Total
	(dollars in thousands)					
Allowance for credit losses:						
Originated loans:						
Beginning balance	$25,082	$ 1,262	$ 3,556	$ 17,731	$ 3,527	$51,158
Charge-offs	(2,582)	—	(268)	—	(1,076)	(3,926)
Recoveries	53	92	26	36	153	360
Provision (credit)	(564)	238	296	1,896	1,213	3,079
Ending balance	21,989	1,592	3,610	19,663	3,817	50,671
Acquired loans:						
Beginning balance	23	—	127	6	—	156

Charge-offs	—	—	(9)	—	(4)	(13)
Recoveries	13	—	25	—	12	50
Provision (credit)	(16)	—	(96)	2	(8)	(118)
Ending balance	20	—	47	8	—	75
Total ending balance	$22,009	$ 1,592	$ 3,657	$ 19,671	$ 3,817	$50,746

30

ITEM 1. Financial Statements and Supplementary Data
FIRST COMMONWEALTH FINANCIAL CORPORATION AND SUBSIDIARIES
NOTES TO THE UNAUDITED CONDENSED CONSOLIDATED FINANCIAL STATEMENTS (Continued)

	For the Three Months Ended, September 30, 2017					
	Commercial, financial, agricultural and other	Real estate construction	Residential real estate	Commercial real estate	Loans to individuals	Total
	(dollars in thousands)					
Allowance for credit losses:						
Originated loans:						
Beginning balance	$33,372	$ 768	$ 2,116	$ 7,307	$ 4,332	$47,895
Charge-offs	(499)	—	(344)	(35)	(1,015)	(1,893)
Recoveries	183	369	67	60	107	786
Provision (credit)	(10,392)	204	1,053	9,991	2	858
Ending balance	22,664	1,341	2,892	17,323	3,426	47,646
Acquired loans:						
Beginning balance	118	—	4	50	—	172
Charge-offs	—	—	(17)	—	(9)	(26)
Recoveries	1	4	18	—	5	28
Provision (credit)	361	(4)	1	(6)	4	356
Ending balance	480	—	6	44	—	530
Total ending balance	$23,144	$ 1,341	$ 2,898	$ 17,367	$ 3,426	$48,176

Note 10 Income Taxes

At September 30, 2018 and December 31, 2017, First Commonwealth had no material unrecognized tax benefits or accrued interest and penalties. If applicable, First Commonwealth will record interest and penalties as a component of noninterest expense. Federal and state returns for tax years 2014 and forward remain open for examination as of September 30, 2018.

During the first quarter of 2018, First Commonwealth adopted ASU No. 2018-02, "Income Statement - Reporting Comprehensive Income (Topic 220)". Adoption of this ASU reclassified the stranded other accumulated income of $1.3 million resulting from the tax reform passed in December 2017 from accumulated other comprehensive income to retained earnings. There was no impact to total equity as a result of the adoption of this update. During the first quarter of 2017, First Commonwealth adopted ASU No. 2016-09, "Compensation-Stock Compensation (Topic 718)." Adoption of this ASU resulted in a $0.1 million tax benefit.

Note 11 Fair Values of Assets and Liabilities

FASB ASC Topic 820, “Fair Value Measurements and Disclosures,” requires disclosures for non-financial assets and non-financial liabilities, except for items that are recognized or disclosed at fair value in the financial statements on a recurring basis (at least annually). All non-financial assets are included either as a separate line item on the Condensed Consolidated Statements of Financial Condition or in the “Other assets” category of the Condensed Consolidated Statements of Financial Condition. Currently, First Commonwealth does not have any non-financial liabilities to disclose.

FASB ASC Topic 825, “Financial Instruments”, permits entities to irrevocably elect to measure select financial instruments and certain other items at fair value. The unrealized gains and losses are required to be included in earnings each reporting period for the items that fair value measurement is elected. First Commonwealth has elected not to measure any existing financial instruments at fair value under FASB ASC Topic 825; however, in the future we may elect to adopt this guidance for select financial instruments.

In accordance with FASB ASC Topic 820, First Commonwealth groups financial assets and financial liabilities measured at fair value in three levels based on the principal markets in which the assets and liabilities are transacted and the observability of the data points used to determine fair value. These levels are:

ITEM 1. Financial Statements and Supplementary Data
FIRST COMMONWEALTH FINANCIAL CORPORATION AND SUBSIDIARIES
NOTES TO THE UNAUDITED CONDENSED CONSOLIDATED FINANCIAL STATEMENTS (Continued)

- Level 1 – Valuations for assets and liabilities traded in active exchange markets, such as the New York Stock Exchange (“NYSE”). Valuations are obtained from readily available pricing sources for market transactions involving identical assets or liabilities.
- Level 2 – Valuations for assets and liabilities traded in less active dealer or broker markets. Valuations are obtained for identical or comparable assets or liabilities from alternative pricing sources with reasonable levels of price transparency. Level 2 includes Obligations of U.S. Government securities issued by Agencies and Sponsored Enterprises, Obligations of States and Political Subdivisions, corporate securities, FHLB stock, loans held for sale, interest rate derivatives (including interest rate caps, interest rate swaps and risk participation agreements), certain other real estate owned and certain impaired loans.

Level 2 investment securities are valued by a recognized third party pricing service using observable inputs. The model used by the pricing service varies by asset class and incorporates available market, trade and bid information as well as cash flow information when applicable. Because many fixed-income investment securities do not trade on a daily basis, the model uses available information such as benchmark yield curves, benchmarking of like investment securities, sector groupings and matrix pricing. The model will also use processes such as an option adjusted spread to assess the impact of interest rates and to develop prepayment estimates. Market inputs normally used in the pricing model include benchmark yields, reported trades, broker/dealer quotes, issuer spreads, two-sided markets, benchmark securities, bids, offers and reference data including market research publications.

Management validates the market values provided by the third party service by having another recognized pricing service price 100% of the securities on an annual basis and a random sample of securities each quarter, monthly monitoring of variances from prior period pricing and, on a monthly basis, evaluating pricing changes compared to expectations based on changes in the financial markets.

Other investments recorded in the Condensed Consolidated Statements of Financial Condition are comprised of FHLB stock whose estimated fair value is based on its par value. Additional information on FHLB stock is provided in Note 8, “Impairment of Investment Securities.”

Loans held for sale primarily include residential mortgage loans originated for sale in the secondary mortgage market. The estimated fair value for these loans was determined on the basis of rates obtained in the respective secondary market. Loans held for sale could also include commercial loans for which fair value is determined using an executed trade or market bid obtained from potential buyers.

Interest rate derivatives are reported at an estimated fair value utilizing Level 2 inputs and are included in other assets and other liabilities, and consist of interest rate swaps where there is no significant deterioration in the counterparties' (loan customers') credit risk since origination of the interest rate swap as well as interest rate caps and risk participation agreements. First Commonwealth values its interest rate swap and cap positions using a yield curve by taking market prices/rates for an appropriate set of instruments. The set of instruments currently used to determine the U.S. Dollar yield curve includes cash LIBOR rates from overnight to one year, Eurodollar futures contracts and swap rates from one year to thirty years. These yield curves determine the valuations of interest rate swaps. Interest rate derivatives are further described in Note 12, “Derivatives.”

For purposes of potential valuation adjustments to our derivative positions, First Commonwealth evaluates the credit risk of its counterparties as well as our own credit risk. Accordingly, we have considered factors such as the likelihood of default, expected loss given default, net exposures and remaining contractual life, among other things, in determining if any fair value adjustments related to credit risk are required. We review our counterparty exposure quarterly, and when necessary, appropriate adjustments are made to reflect the exposure.

We also utilize this approach to estimate our own credit risk on derivative liability positions. In 2018, we have not realized any losses due to a counterparty's inability to pay any uncollateralized positions.

Interest rate derivatives also include interest rate forwards entered into to hedge residential mortgage loans held for sale and the related interest-rate lock commitments. This includes forward commitments to sell mortgage loans. The fair value of these derivative financial instruments are based on derivative market data inputs as of the valuation date and the underlying value of mortgage loans for rate lock commitments.

In addition, the Company hedges foreign currency risk through the use of foreign exchange forward contracts. The fair value of foreign exchange forward contracts is based on the differential between the contract price and the market-based forward rate.

ITEM 1. Financial Statements and Supplementary Data
FIRST COMMONWEALTH FINANCIAL CORPORATION AND SUBSIDIARIES
NOTES TO THE UNAUDITED CONDENSED CONSOLIDATED FINANCIAL STATEMENTS (Continued)

The estimated fair value for other real estate owned included in Level 2 is determined by either an independent market-based appraisal less estimated costs to sell or an executed sales agreement.

- Level 3 – Valuations for assets and liabilities that are derived from other valuation methodologies, including option pricing models, discounted cash flow models and similar techniques, and not based on market exchange, dealer or broker traded transactions. If the inputs used to provide the valuation are unobservable and/or there is very little, if any, market activity for the security or similar securities, the securities would be considered Level 3 securities. Level 3 valuations incorporate certain assumptions and projections in determining the fair value assigned to such assets or liabilities. The assets included in Level 3 are pooled trust preferred collateralized debt obligations, non-marketable equity investments, certain interest rate derivatives, certain other real estate owned and certain impaired loans.

Level 3 assets at December 31, 2017 included pooled trust preferred collateralized debt obligations with an estimated fair value of $23.6 million. During the first six-months of 2018, the entire portfolio of trust preferred securities were liquidated either by a successful auction call or by sale. These securities were considered level 3 because there was little or no active trading since 2009; therefore, it is more appropriate to determine estimated fair value using a discounted cash flow analysis. When determining the fair value of these securities, the discount rate applied to the cash flows was determined by evaluating the current market yields for comparable corporate and structured credit products along with an evaluation of the risks associated with the cash flows of the comparable security.

The estimated fair value of the non-marketable equity investments included in Level 3 is based on par value.

The estimated fair value of limited partnership investments included in Level 3 is based on par value.

For interest rate derivatives included in Level 3, the fair value incorporates credit risk by considering such factors as likelihood of default and expected loss given default based on the credit quality of the underlying counterparties (loan customers).

In accordance with ASU 2011-4, the following table provides information related to quantitative inputs and assumptions used in September 30, 2018 Level 3 fair value measurements.

	Fair Value (dollars in thousands)		Valuation Technique	Unobservable Inputs	Range / (weighted average)
Equities	1,670		Par Value	N/A	N/A
Impaired Loans	1,184	(a)	Reserve study	Discount rate	10.00%
				Gas per MMBTU	$2.81 - $3.35 (b)
				Oil per BBL/d	$51.59 - $59.55 (b)
	7,883	(a)	Discounted Cash Flow	Discount Rate	1.9% - 9.5%
Limited Partnership Investments	2,521		Par Value	N/A	N/A

(a) The remainder of impaired loans valued using Level 3 inputs are not included in this disclosure as the values of those loans are based on bankruptcy agreement documentation.

(b) Unobservable inputs are defined as follows: MMBTU - million British thermal units; BBL/d - barrels per day.

The discount rate is the significant unobservable input used in the fair value measurement of impaired loans. Significant increases in this rate would result in a decrease in the estimated fair value of the loans, while a decrease in this rate would result in a higher fair value measurement. Other unobservable inputs in the fair value measurement of impaired loans relate to gas, oil and natural gas prices. Increases in these prices would result in an increase in the estimated fair value of the loans, while a decrease in these prices would result in a lower fair value measurement.

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