PNC FINANCIAL SERVICES GROUP, INC.
Form 10-Q
May 03, 2017
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UNITED STATES

SECURITIES AND EXCHANGE COMMISSION

Washington, DC 20549

FORM 10-Q

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

For the quarterly period ended March 31, 2017

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 001-09718

The PNC Financial Services Group, Inc.

(Exact name of registrant as specified in its charter)

Pennsylvania	**25-1435979**
(State or other jurisdiction of incorporation or organization)	**(I.R.S. Employer Identification No.)**

The Tower at PNC Plaza, 300 Fifth Avenue, Pittsburgh, Pennsylvania 15222-2401

(Address of principal executive offices, including zip code)

(888) 762-2265

(Registrant s telephone number, including area code)

(Former name, former address and former fiscal year, if changed since last report)

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

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

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

Large accelerated filer	Accelerated filer
Non-accelerated filer	Smaller reporting company
Emerging growth company	

If an emerging growth company, indicate by check mark if the registrant has elected not to use the extended transition period for complying with any new or revised financial accounting standards provided pursuant to Section 7(a)(2)(B) of the Securities Act.

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

As of April 21, 2017, there were 483,901,441 shares of the registrant s common stock ($5 par value) outstanding.

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FINANCIAL REVIEW

THE PNC FINANCIAL SERVICES GROUP, INC.

This Financial Review, including the Consolidated Financial Highlights, should be read together with our unaudited Consolidated Financial Statements and unaudited Statistical Information included elsewhere in this Report and with Items 6, 7, 8 and 9A of our 2016 Annual Report on Form 10-K (2016 Form 10-K). We have reclassified certain prior period amounts to conform with the current period presentation, which we believe is more meaningful to readers of our consolidated financial statements. For information regarding certain business, regulatory and legal risks, see the following: the Risk Management section of this Financial Review and of Item 7 in our 2016 Form 10-K; Item 1A Risk Factors included in our 2016 Form 10-K; and the Legal Proceedings and Commitments Notes of the Notes To Consolidated Financial Statements included in Item 1 of this Report and Item 8 of our 2016 Form 10-K. Also, see the Cautionary Statement Regarding Forward-Looking Information section in this Financial Review and the Critical Accounting Estimates And Judgments section in this Financial Review and in our 2016 Form 10-K for certain other factors that could cause actual results or future events to differ, perhaps materially, from historical performance and from those anticipated in the forward-looking statements included in this Report. See Note 14 Segment Reporting in the Notes To Consolidated Financial Statements included in this Report for a reconciliation of total business segment earnings to total PNC consolidated net income as reported on a generally accepted accounting principles (GAAP) basis. In this Report, PNC , we or us refers to The PNC Financial Services Group, Inc. and its subsidiaries on a consolidated basis. References to The PNC Financial Services Group, Inc. or to any of its subsidiaries are specifically made where applicable.

Table 1: Consolidated Financial Highlights

Dollars in millions, except per share data	Three months ended March 31	
Unaudited	2017	2016
Financial Results (a)		
Revenue		
Net interest income	$ 2,160	$ 2,098
Noninterest income	1,724	1,567
Total revenue	3,884	3,665
Provision for credit losses	88	152
Noninterest expense	2,402	2,281
Income before income taxes and noncontrolling interests	$ 1,394	$ 1,232
Net income	$ 1,074	$ 943
Less:		
Net income attributable to noncontrolling interests	17	19
Preferred stock dividends	63	63
Preferred stock discount accretion and redemptions	21	2
Net income attributable to common shareholders	$ 973	$ 859
Less:		
Dividends and undistributed earnings allocated to nonvested restricted shares	6	6
Impact of BlackRock earnings per share dilution	4	3
Net income attributable to diluted common shares	$ 963	$ 850

Diluted earnings per common share	$ 1.96	$ 1.68
Cash dividends declared per common share	$ .55	$ .51
Effective tax rate (b)	23.0%	23.5%
Performance Ratios		
Net interest margin (c)	2.77%	2.75%
Noninterest income to total revenue	44%	43%
Efficiency	62%	62%
Return on:		
Average common shareholders equity	9.50%	8.44%
Average assets	1.19%	1.07%

(a) The Executive Summary and Consolidated Income Statement Review portions of this Financial Review provide information regarding items impacting the comparability of the periods presented.

(b) The effective income tax rates are generally lower than the statutory rate due to the relationship of pretax income to tax credits and earnings that are not subject to tax.

(c) Calculated as annualized taxable-equivalent net interest income divided by average earning assets. To provide more meaningful comparisons of net interest margins, we use net interest income on a taxable-equivalent basis in calculating net interest margin by increasing the interest income earned on tax-exempt assets to make it fully equivalent to interest income earned on taxable investments. This adjustment is not permitted under GAAP in the Consolidated Income Statement. The taxable-equivalent adjustments to net interest income for the three months ended March 31, 2017 and March 31, 2016 were $52 million and $48 million, respectively. For additional information, see the Statistical Information (Unaudited) section of this Report.

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Table 1: Consolidated Financial Highlights (Continued) (a)

Unaudited	March 31 2017	December 31 2016	March 31 2016
Balance Sheet Data (dollars in millions, except per share data)			
Assets	$ 370,944	$ 366,380	$ 360,985
Loans	$ 212,826	$ 210,833	$ 207,485
Allowance for loan and lease losses	$ 2,561	$ 2,589	$ 2,711
Interest-earning deposits with banks (b)	$ 27,877	$ 25,711	$ 29,478
Investment securities	$ 76,432	$ 75,947	$ 72,569
Loans held for sale	$ 1,414	$ 2,504	$ 1,541
Equity investments (c)	$ 10,900	$ 10,728	$ 10,391
Mortgage servicing rights	$ 1,867	$ 1,758	$ 1,323
Goodwill	$ 9,103	$ 9,103	$ 9,103
Other assets	$ 28,083	$ 27,506	$ 27,945
Noninterest-bearing deposits	$ 79,246	$ 80,230	$ 78,151
Interest-bearing deposits	$ 181,464	$ 176,934	$ 172,208
Total deposits	$ 260,710	$ 257,164	$ 250,359
Borrowed funds	$ 55,062	$ 52,706	$ 54,178
Total shareholders equity	$ 45,754	$ 45,699	$ 45,130
Common shareholders equity	$ 41,774	$ 41,723	$ 41,677
Accumulated other comprehensive income (loss)	$ (279)	$ (265)	$ 532
Book value per common share	$ 86.14	$ 85.94	$ 83.47
Common shares outstanding (in millions)	485	485	499
Loans to deposits	82%	82%	83%
Client Assets (in billions)			
Discretionary client assets under management	$ 141	$ 137	$ 135
Nondiscretionary client assets under administration	123	120	118
Total client assets under administration (d)	264	257	253
Brokerage account client assets	46	44	43
Total client assets	$ 310	$ 301	$ 296
Capital Ratios			
Transitional Basel III (e) (f)			
Common equity Tier 1	10.5%	10.6%	10.6%
Tier 1 risk-based	11.8%	12.0%	11.9%
Total capital risk-based	14.1%	14.3%	14.4%
Leverage	9.9%	10.1%	10.2%
Pro forma Fully Phased-In Basel III (Non-GAAP) (f)			
Common equity Tier 1	10.0%	10.0%	10.1%
Common shareholders equity to assets	11.3%	11.4%	11.5%
Asset Quality			

Nonperforming loans to total loans	.94%	1.02%	1.10%
Nonperforming assets to total loans, OREO, foreclosed and other assets	1.04%	1.12%	1.23%
Nonperforming assets to total assets	.60%	.65%	.71%
Net charge-offs to average loans (for the three months ended) (annualized)	.23%	.20%	.29%
Allowance for loan and lease losses to total loans	1.20%	1.23%	1.31%
Allowance for loan and lease losses to total nonperforming loans	128%	121%	119%
Accruing loans past due 90 days or more (in millions)	$ 699	$ 782	$ 782

(a) The Executive Summary and Consolidated Balance Sheet Review portions of this Financial Review provide information regarding items impacting the comparability of the periods presented.

(b) Amounts include balances held with the Federal Reserve Bank of Cleveland (Federal Reserve Bank) of $27.5 billion, $25.1 billion and $29.0 billion as of March 31, 2017, December 31, 2016 and March 31, 2016, respectively.

(c) Amounts include our equity interest in BlackRock.

(d) As a result of certain investment advisory services performed by one of our registered investment advisors, certain assets were previously reported as both discretionary client assets under management and nondiscretionary client assets under administration. Effective for the first quarter of 2017, these amounts are only reported as discretionary assets under management. Prior periods were adjusted to remove amounts previously included in nondiscretionary assets under administration of approximately $9 billion and $7 billion as of December 31, 2016 and March 31, 2016, respectively.

(e) Calculated using the regulatory capital methodology applicable to PNC during each period presented.

(f) See Basel III Capital discussion in the Capital Management portion of the Risk Management section of this Financial Review and the capital discussion in the Banking Regulation and Supervision section of Item 1 Business in our 2016 Form 10-K. See also the Transitional Basel III and Pro forma Fully Phased-In Basel III Common Equity Tier 1 Capital Ratios (Non-GAAP) 2016 Periods table in the Statistical Information section of this Report for a reconciliation of the 2016 periods ratios.

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Executive Summary

The PNC Financial Services Group, Inc. is one of the largest diversified financial services companies in the United States and is headquartered in Pittsburgh, Pennsylvania.

We have businesses engaged in retail banking, including residential mortgage, corporate and institutional banking and asset management, providing many of our products and services nationally. Our primary geographic markets are located in Pennsylvania, Ohio, New Jersey, Michigan, Illinois, Maryland, Indiana, Florida, North Carolina, Kentucky, Washington, D.C., Delaware, Virginia, Georgia, Alabama, Missouri, Wisconsin and South Carolina. We also provide certain products and services internationally.

Key Strategic Goals

At PNC we manage our company for the long term. We are focused on the fundamentals of growing customers, loans, deposits and revenue and improving profitability, while investing for the future and managing risk, expenses and capital. We continue to invest in our products, markets and brand, and embrace our commitments to our customers, shareholders, employees and the communities where we do business.

We strive to expand and deepen customer relationships by offering a broad range of deposit, fee-based and credit products and services. We are focused on delivering those products and services to our customers with the goal of addressing their financial objectives and putting customers needs first. Our business model is built on customer loyalty and engagement, understanding our customers financial goals and offering our diverse products and services to help them achieve financial wellbeing. Our approach is concentrated on organically growing and deepening client relationships across our businesses that meet our risk/return measures.

Our strategic priorities are designed to enhance value over the long term. One of our priorities is to build a leading banking franchise in our underpenetrated geographic markets. We are focused on reinventing the retail banking experience by transforming the retail distribution network and the home lending process for a better customer experience and improved efficiency, and growing our consumer loan portfolio. In addition, we are seeking to attract more of the investable assets of new and existing clients and we continue to focus on expense management while investing in technology to bolster critical business infrastructure and streamline core processes.

Our capital priorities are to support client growth and business investment, maintain appropriate capital in light of economic conditions and the Basel III framework and return excess capital to shareholders, in accordance with the currently effective capital plan included in our Comprehensive Capital

Analysis and Review (CCAR) submission to the Board of Governors of the Federal Reserve System (Federal Reserve). For more detail, see the Capital Highlights portion of this Executive Summary and the Liquidity and Capital Management portion of the Risk Management section of this Financial Review and the Supervision and Regulation section in Item 1 Business of our 2016 Form 10-K.

Income Statement Highlights

Net income for the first quarter of 2017 was $1.1 billion, or $1.96 per diluted common share, an increase of 14%, compared to $943 million, or $1.68 per diluted common share, for the first quarter of 2016.

- Total revenue increased $219 million, or 6%, to $3.9 billion.
- Net interest income increased $62 million, or 3%, to $2.2 billion.

- Net interest margin increased to 2.77% compared to 2.75% for the first quarter of 2016.
- Noninterest income increased $157 million, or 10%, to $1.7 billion primarily due to growth in fee income.
- Provision for credit losses decreased to $88 million for the first quarter of 2017 compared to $152 million for the first quarter of 2016.
- Noninterest expense increased $121 million to $2.4 billion, reflecting overall higher levels of business activity.

For additional detail, see the Consolidated Income Statement Review section in this Financial Review.

Balance Sheet Highlights

Our balance sheet was strong and well positioned at March 31, 2017 and December 31, 2016.

- Total loans increased $2.0 billion, or 1%, to $212.8 billion.
  - Total commercial lending grew $2.7 billion, or 2%.
  - Total consumer lending decreased $.7 billion, or 1%.
- Total deposits increased $3.5 billion, or 1%, to $260.7 billion.
- Investment securities increased $.5 billion, or 1%, to $76.4 billion.

For additional detail, see the Consolidated Balance Sheet Review section of this Financial Review.

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Credit Quality Highlights

Overall credit quality remained stable with the fourth quarter of 2016.

- Nonperforming assets decreased $162 million, or 7%, to $2.2 billion at March 31, 2017 compared with December 31, 2016.
- Overall loan delinquencies decreased $192 million, or 12%, as of March 31, 2017 compared with December 31, 2016.
- Net charge-offs of $118 million in the first quarter of 2017 decreased compared to net charge-offs of $149 million for the first quarter of 2016.

For additional detail, see the Credit Risk Management portion of the Risk Management section of this Financial Review.

Capital Highlights

We maintained a strong capital position and continued to return capital to shareholders.

- The Transitional Basel III common equity Tier 1 capital ratio was 10.5% at March 31, 2017 compared to 10.6% at December 31, 2016.
- Pro forma fully phased-in Basel III common equity Tier 1 capital ratio, a non-GAAP financial measure, remained stable at an estimated 10.0% at March 31, 2017 and December 31, 2016 based on the standardized approach rules.
- In the first quarter of 2017, we returned $.9 billion of capital to shareholders through repurchases of 5.0 million common shares for $.6 billion and dividends on common shares of $.3 billion.
- On January 30, 2017, PNC announced a $300 million increase to its common stock share repurchase programs, which now provide for repurchases of up to $2.3 billion for the four-quarter period ending June 30, 2017.
- On April 4, 2017, the PNC board of directors declared a quarterly cash dividend on common stock of 55 cents per share with a payment date of May 5, 2017.

See the Liquidity and Capital Management portion of the Risk Management section of this Financial Review for more detail on our 2017 capital and liquidity actions as well as our capital ratios.

Our ability to take certain capital actions, including plans to pay or increase common stock dividends or to repurchase shares under current or future programs, is subject to the results of the supervisory assessment of capital adequacy undertaken by the Federal Reserve as part of the CCAR process. For additional information, see the Supervision and Regulation section in Item 1 Business of our 2016 Form 10-K.

Business Outlook

Statements regarding our business outlook are forward-looking within the meaning of the Private Securities Litigation Reform Act of 1995. Our forward-looking statements are subject to the risk that economic and financial market conditions will be substantially different than those we are currently expecting and do not take into account potential legal and regulatory contingencies. These statements are based on our current view that the U.S. economy and the labor market will grow moderately in 2017, boosted by stable oil/energy prices, improving consumer spending and housing activity, and expanded federal fiscal policy stimulus as a result of the 2016 elections. Short-term interest rates and bond yields are expected to continue rising gradually in 2017, along with inflation. Specifically, our business outlook reflects our expectation of continued steady growth in GDP and two 25 basis point increases in short-term interest rates by the Federal Reserve in June and December of 2017. We are also assuming that long-term rates rise at a slower pace than short-term rates. See the Cautionary Statement Regarding Forward-Looking Information section in this Financial Review and Item 1A Risk Factors in our 2016 Form 10-K for other factors that could cause future events to differ, perhaps materially, from those anticipated in these forward-looking statements.

For the full year 2017 compared to full year 2016, we expect:

- Loans to increase by mid-single digits, on a percentage basis;
- Revenue growth in the upper end of the mid-single digit range, on a percentage basis;
- Noninterest expense to increase by low single digits, on a percentage basis; and
- The effective tax rate to be approximately 25%, absent any tax reform.

For the remaining quarters of 2017, we expect quarterly other noninterest income to be between $225 million and $275 million.

For the second quarter of 2017 compared to the first quarter of 2017, we expect:

- Modest loan growth;
- Net interest income to increase by low single digits, on a percentage basis;
- Fee income to increase by mid-single digits, on a percentage basis. Fee income consists of asset management, consumer services, corporate services, residential mortgage and service charges on deposits;
- Provision for credit losses to be between $75 million and $125 million, and could be at the higher end of this range as a result of an initial provision for acquired loans; and
- Noninterest expense to increase by low single digits, on a percentage basis.

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Consolidated Income Statement Review

Our Consolidated Income Statement is presented in Part I, Item 1 of this Report.

Net income for the first quarter of 2017 was $1.1 billion, or $1.96 per diluted common share, an increase of 14%, compared to $943 million, or $1.68 per diluted common share, for the first quarter of 2016. The increase was driven by a 6% increase in revenue and lower provision for credit losses, partially offset by a 5% increase in noninterest expense. Higher revenue in the comparison reflected a 10% increase in noninterest income and a 3% increase in net interest income.

Net Interest Income

Table 2: Summarized Average Balances and Net Interest Income (a)

Three months ended March 31 Dollars in millions	2017 Average Balances	2017 Average Yields/ Rates	2017 Interest Income/ Expense	2016 Average Balances	2016 Average Yields/ Rates	2016 Interest Income/ Expense
Assets						
Interest-earning assets						
Investment securities	$ 76,253	2.67%	$ 508	$ 70,269	2.72%	$ 478
Loans	212,253	3.67%	1,941	207,184	3.60%	1,875
Interest-earning deposits with banks	24,192	.81%	49	25,533	.50%	32
Other	8,395	3.54%	74	7,764	3.62%	70
Total interest-earning assets/interest income	$ 321,093	3.22%	2,572	$ 310,750	3.15%	2,455
Liabilities						
Interest-bearing liabilities						
Interest-bearing deposits	$ 176,871	.28%	120	$ 168,823	.25%	105
Borrowed funds	54,942	1.74%	240	53,626	1.51%	204
Total interest-bearing liabilities/interest expense	$ 231,813	.62%	360	$ 222,449	.55%	309
Net interest margin/income (Non-GAAP)		2.77%	2,212		2.75%	2,146
Taxable-equivalent adjustments			(52)			(48)
Net interest income (GAAP)			$ 2,160			$ 2,098

(a) Interest income calculated as taxable-equivalent interest income. To provide more meaningful comparisons of interest income and yields for all interest-earning assets, as well as net interest margins, we use interest income on a taxable-equivalent basis in calculating average yields and net interest margins by increasing the interest income earned on tax-exempt assets to make it fully equivalent to interest income earned on taxable investments. This adjustment is not permitted under GAAP on the Consolidated Income Statement.

Changes in net interest income and margin result from the interaction of the volume and composition of interest-earning assets and related yields, interest-bearing liabilities and related rates paid, and noninterest-bearing sources of funding. See the Statistical Information (Unaudited) Average Consolidated Balance Sheet And Net Interest Analysis section of this Report for additional information.

Net interest income increased by $62 million, or 3%, in the first quarter of 2017 compared with the first quarter of 2016, and net interest margin increased to 2.77% compared with 2.75% in the prior year quarter. Both increases reflected higher loan yields, partially offset by an increase in borrowing and deposit costs. The increase in net interest income also was driven by growth in loans and securities balances.

Average investment securities increased $6.0 billion, or 9%, due to higher average U.S. Treasury and government agency securities and average agency residential mortgage-backed securities, partially offset by decreases in average commercial

mortgage-backed securities and non-agency residential mortgage-backed securities. Total investment securities increased to 24% of average interest-earning assets for the first quarter of 2017 compared to 23% for the first quarter of 2016.

Average loans grew $5.1 billion, or 2%, consisting of growth in average commercial loans of $4.0 billion and average commercial real estate loans of $1.2 billion, driven by our Corporate Banking and Real Estate businesses within our Corporate & Institutional Banking segment. Additionally, average residential real estate loans increased $1.1 billion. These increases were partially offset by a decline in consumer loans of $1.4 billion, which reflected decreases in the non-strategic runoff consumer loan portfolios of brokered home equity and government guaranteed education loans. Average loans represented 66% of average interest-earning assets for the first quarter of 2017 and 67% of average interest-earning assets for the first quarter of 2016.

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Average total deposits of $254.9 billion grew $8.8 billion, or 4%, in the first quarter of 2017 compared to the first quarter of 2016. Average interest-bearing deposits increased $8.0 billion primarily due to higher average savings deposits, which largely reflected a shift from money market deposits to relationship-based savings products, as well as higher average interest-bearing demand deposits. Average interest-bearing deposits represented 76% of average interest-bearing liabilities in both quarters in the comparison.

Noninterest Income

Table 3: Noninterest Income

Three months ended March 31			Change	
Dollars in millions	2017	2016	$	%
Noninterest income				
Asset management	$ 403	$ 341	$ 62	18%
Consumer services	332	337	(5)	(1)%
Corporate services	393	325	68	21%
Residential mortgage	113	100	13	13%
Service charges on deposits	161	158	3	2%
Other	322	306	16	5%
Total noninterest income	$ 1,724	$ 1,567	$ 157	10%

Noninterest income as a percentage of total revenue was 44% in the first quarter of 2017 compared to 43% in the first quarter of 2016.

Asset management revenue growth in the comparison reflected higher earnings from BlackRock and the impact of higher average equity markets as well as net new business activity in our asset management business. Discretionary client assets under management increased $6 billion to $141 billion at March 31, 2017 compared to March 31, 2016.

Corporate services revenue increased due to higher merger and acquisition advisory fees and other capital markets revenue, higher commercial mortgage servicing rights valuation, net of economic hedge, and higher treasury management revenue.

Residential mortgage revenue was higher in the comparison as a result of an increased benefit from residential mortgage servicing rights valuation, net of economic hedge.

Other noninterest income for the first quarter of 2017 increased over the first quarter of 2016 largely attributable to higher revenue from private equity investments, including positive valuation adjustments of $47 million associated with

our receipt of a five-year extension of the prior July 2017 deadline to conform certain equity investments subject to the Volcker Rule provisions of the Dodd-Frank Act. The increase was partially offset by the impact of first quarter 2016 net gains on the sale of Visa Class B common shares.

Provision For Credit Losses

The provision for credit losses was $88 million for the first quarter of 2017 compared with $152 million for the first quarter of 2016, which included a higher provision for energy related loans in the oil, gas and coal sectors.

The Credit Risk Management portion of the Risk Management section of this Financial Review includes additional information regarding factors impacting the provision for credit losses.

Noninterest Expense

Table 4: Noninterest Expense

Three months ended March 31			Change	
Dollars in millions	2017	2016	$	%
Noninterest expense				
Personnel	$ 1,249	$ 1,145	$ 104	9%
Occupancy	222	221	1	
Equipment	251	234	17	7%
Marketing	55	54	1	2%
Other	625	627	(2)	
Total noninterest expense	$ 2,402	$ 2,281	$ 121	5%

Higher noninterest expense in the comparison reflected the impact of overall higher levels of business activity on personnel and equipment expense. We remained focused on disciplined expense management while continuing to invest in technology and business infrastructure.

As of March 31, 2017, we were on track to achieve our full-year 2017 goal of $350 million in cost savings through our continuous improvement program, which we expect will substantially fund our 2017 business and technology investments.

Effective Income Tax Rate

The effective income tax rate was 23.0% in the first quarter of 2017 compared with 23.5% in the first quarter of 2016. Income taxes for first quarter 2017 included higher tax deductions for stock-based compensation related to vesting of restricted shares and options exercised at a higher common stock price.

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CONSOLIDATED BALANCE SHEET REVIEW

Table 5: Summarized Balance Sheet Data

	March 31	December 31	Change	
Dollars in millions	2017	2016	$	%
Assets				
Interest-earning deposits with banks	$ 27,877	$ 25,711	$ 2,166	8%
Loans held for sale	1,414	2,504	(1,090)	(44)%
Investment securities	76,432	75,947	485	1%
Loans	212,826	210,833	1,993	1%
Allowance for loan and lease losses	(2,561)	(2,589)	28	1%
Mortgage servicing rights	1,867	1,758	109	6%
Goodwill	9,103	9,103		
Other, net	43,986	43,113	873	2%
Total assets	$ 370,944	$ 366,380	$ 4,564	1%
Liabilities				
Deposits	$ 260,710	$ 257,164	$ 3,546	1%
Borrowed funds	55,062	52,706	2,356	4%
Other	9,269	9,656	(387)	(4)%
Total liabilities	325,041	319,526	5,515	2%
Equity				
Total shareholders equity	45,754	45,699	55	
Noncontrolling interests	149	1,155	(1,006)	(87)%
Total equity	45,903	46,854	(951)	(2)%
Total liabilities and equity	$ 370,944	$ 366,380	$ 4,564	1%

The summarized balance sheet data in Table 5 is based upon our Consolidated Balance Sheet in Part 1, Item 1 of this Report.

Our balance sheet was strong and well positioned at both March 31, 2017 and December 31, 2016.

Total assets increased primarily driven by loan growth and higher interest-earning deposits with banks;

Total liabilities increased due to deposit growth and higher borrowed funds;

Total equity decreased due to a decline in noncontrolling interests related to the redemption of Perpetual Trust Securities.

The following discussion provides additional information about the major components of our balance sheet. Information regarding our capital and regulatory compliance is included in the Liquidity and Capital Management portion of the Risk Management section of this Financial Review and in Note 18 Regulatory Matters in the Notes To Consolidated Financial Statements included in our 2016 Form 10-K.

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Loans

Table 6: Details of Loans

Dollars in millions	March 31 2017	December 31 2016	Change $	Change %
Commercial lending				
Commercial				
Manufacturing	$ 20,054	$ 18,891	$ 1,163	6%
Retail/wholesale trade	17,446	16,752	694	4%
Service providers	14,185	14,707	(522)	(4)%
Real estate related (a)	11,690	11,920	(230)	(2)%
Health care	9,603	9,491	112	1%
Financial services	7,710	7,241	469	6%
Other industries	23,077	22,362	715	3%
Total commercial	103,765	101,364	2,401	2%
Commercial real estate	29,435	29,010	425	1%
Equipment lease financing	7,462	7,581	(119)	(2)%
Total commercial lending	140,662	137,955	2,707	2%
Consumer lending				
Home equity	29,577	29,949	(372)	(1)%
Residential real estate	15,781	15,598	183	1%
Credit card	5,112	5,282	(170)	(3)%
Other consumer				
Automobile	12,337	12,380	(43)	
Education	4,974	5,159	(185)	(4)%
Other	4,383	4,510	(127)	(3)%
Total consumer lending	72,164	72,878	(714)	(1)%
Total loans	$ 212,826	$ 210,833	$ 1,993	1%

(a) Includes loans to customers in the real estate and construction industries.

Growth in commercial lending was driven by increased utilization from manufacturing, retail/wholesale trade and financial services customers. Lower consumer lending was driven by declines in home equity loans, education loans and credit cards. The decreases in home equity and education reflected runoff in the non-strategic brokered home equity and government guaranteed education loan portfolios.

See the Credit Risk Management portion of the Risk Management section of this Financial Review and Note 1 Accounting Policies, Note 3 Asset Quality and Note 4 Allowances for Loan and Lease Losses in our Notes To

Consolidated Financial Statements included in this Report for additional information regarding our loan portfolio.

Investment Securities

Table 7: Investment Securities

					Ratings (a)				
	March 31, 2017		December 31, 2016		As of March 31, 2017				
Dollars in millions	Amortized Cost	Fair Value	Amortized Cost	Fair Value	AAA/ AA	A	BBB	BB and Lower	No Rating
U.S. Treasury and government agencies	$ 13,318	$ 13,459	$ 13,627	$ 13,714	100%				
Agency residential mortgage-backed	38,673	38,427	37,319	37,109	100				
Non-agency residential mortgage-backed	3,196	3,394	3,382	3,564	11		4%	76%	9%
Agency commercial mortgage-backed	2,919	2,906	3,053	3,046	100				
Non-agency commercial mortgage-backed (b)	4,407	4,434	4,590	4,602	85	4%	1	1	9
Asset-backed (c)	6,486	6,532	6,496	6,524	85	5	3	7	
Other debt (d)	6,610	6,782	6,679	6,810	73	15	8	1	3
Corporate stock and other	517	515	603	601					100
Total investment securities (e)	$ 76,126	$ 76,449	$ 75,749	$ 75,970	91%	2%	1%	4%	2%

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(a) Ratings percentages allocated based on amortized cost.
(b) Collateralized primarily by retail properties, office buildings, lodging properties and multi-family housing.
(c) Collateralized primarily by corporate debt, government guaranteed education loans and other consumer credit products.
(d) Includes state and municipal securities.
(e) Includes available for sale and held to maturity securities.

Investment securities increased $.5 billion at March 31, 2017 compared to December 31, 2016. Growth in investment securities was driven by net purchases of agency residential mortgage-backed securities, partially offset by maturities and prepayments of U.S. Treasury and government agencies, non-agency commercial mortgage-backed and non-agency residential mortgage-backed securities.

Table 7 presents the distribution of our investment securities portfolio by credit rating. We have included credit ratings information because we believe that the information is an indicator of the degree of credit risk to which we are exposed, which could affect our risk-weighted assets and, therefore, our risk-based regulatory capital ratios under the regulatory capital rules. Changes in credit ratings classifications could indicate increased or decreased credit risk and could be accompanied by a reduction or increase in the fair value of our investment securities portfolio.

At least quarterly, we conduct a comprehensive security-level impairment assessment on all securities. If economic conditions, including home prices, were to deteriorate from current levels, and if market volatility and liquidity were to deteriorate from current levels, or if market interest rates were to increase or credit spreads were to widen appreciably, the valuation of our investment securities portfolio would likely be adversely affected and we could incur additional OTTI credit losses that would impact our Consolidated Income Statement.

The duration of investment securities was 3.2 years at March 31, 2017. We estimate that at March 31, 2017 the effective duration of investment securities was 3.3 years for an immediate 50 basis points parallel increase in interest rates and 3.1 years for an immediate 50 basis points parallel decrease in interest rates.

Based on expected prepayment speeds, the weighted-average expected maturity of the investment securities portfolio (excluding corporate stock and other) was 5.1 years at March 31, 2017 compared to 5.0 years at December 31, 2016.

Table 8: Weighted-Average Expected Maturities of Mortgage and Other Asset-Backed Debt Securities

March 31, 2017	Years
Agency residential mortgage-backed	5.4
Non-agency residential mortgage-backed	5.8
Agency commercial mortgage-backed	3.5
Non-agency commercial mortgage-backed	3.7
Asset-backed	2.5

Additional information regarding our investment securities is included in Note 5 Investment Securities and Note 6 Fair Value in the Notes To Consolidated Financial Statements included in this Report.

Funding Sources

Table 9: Details of Funding Sources

	March 31	December 31	Change	
Dollars in millions	2017	2016	$	%
Deposits				
Money market	$ 105,230	$ 105,849	$ (619)	(1)%
Demand	97,076	96,799	277	
Savings	41,428	36,956	4,472	12%
Time deposits	16,976	17,560	(584)	(3)%
Total deposits	260,710	257,164	3,546	1%
Borrowed funds				
FHLB borrowings	19,549	17,549	2,000	11%
Bank notes and senior debt	23,745	22,972	773	3%
Subordinated debt	6,889	8,009	(1,120)	(14)%
Other	4,879	4,176	703	17%
Total borrowed funds	55,062	52,706	2,356	4%
Total funding sources	$ 315,772	$ 309,870	$ 5,902	2%

Growth in total deposits was driven by higher consumer savings and demand deposits, partially offset by seasonal declines in commercial deposits. The overall increase in savings deposits reflected in part a shift from money market deposits to relationship-based savings products. The decline in time deposits reflected the net runoff of maturing accounts.

The increase in total borrowed funds reflected net increases in FHLB borrowings and bank notes and senior debt, as new issuances outpaced maturities and calls. These increases were partially offset by subordinated debt maturities.

See the Liquidity and Capital Management portion of the Risk Management section of this Financial Review for additional information regarding our 2017 capital and liquidity activities.

Shareholders   Equity

Total shareholders   equity as of March 31, 2017 remained relatively stable compared to December 31, 2016. Increased retained earnings, driven by net income of $1.1 billion partially offset by $.3 billion of common and preferred dividends, was largely offset by common share repurchases of $.6 billion and lower capital surplus.

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Common shares outstanding were 485 million at both March 31, 2017, and December 31, 2016, as repurchases of 5.0 million shares during the first quarter of 2017 were largely offset by share issuances from treasury stock related to warrants exercised and stock based compensation activity.

BUSINESS SEGMENTS REVIEW

Effective for the first quarter of 2017, as a result of changes to how we manage our businesses, we realigned our segments and, accordingly, have changed the basis of presentation of our segments, resulting in four reportable business segments:

- Retail Banking
- Corporate & Institutional Banking
- Asset Management Group
- BlackRock

Our changes in business segment presentation resulting from the realignment included the following:

- The Residential Mortgage Banking segment was combined into Retail Banking as a result of our strategic initiative to transform the home lending process by integrating mortgage and home equity lending to enhance product capability and speed of delivery for a better customer experience and to improve efficiency. In conjunction with this shift, residential mortgages previously reported within the Other category were also moved to Retail Banking.

- The Non-Strategic Assets Portfolio segment was eliminated. The segment s remaining consumer assets were moved to the Other category as they are unrelated to the ongoing strategy of any segment, while its commercial assets were transferred to Corporate & Institutional Banking in order to continue the relationships we have with those customers.

- A portion of business banking clients was moved from Retail Banking to Corporate & Institutional Banking to facilitate enhanced product offerings to meet the financial needs of our business banking clients.

Net interest income in business segment results reflects our internal funds transfer pricing methodology. Assets receive a funding charge and liabilities and capital receive a funding credit based on a transfer pricing methodology that incorporates product repricing characteristics, tenor and other factors. Effective for the first quarter of 2017, we made certain adjustments to our internal funds transfer pricing methodology primarily relating to weighted average lives of certain non-maturity deposits based on our recent historical experience. These changes in methodology affected business segment results, primarily adversely impacting net interest income for Corporate & Institutional Banking and Retail Banking, offset by increased net interest income in the Other category.

The prior period presented was revised to conform to the new segment alignment and to our change in internal funds transfer pricing methodology.

Business segment results and a description of each business are included in Note 14 Segment Reporting included in the Notes To Consolidated Financial Statements in this Report. Certain amounts included in this Business Segments Review differ from those amounts shown in Note 14, primarily due to the presentation in this Financial Review of business net interest revenue on a taxable-equivalent basis.

Total business segment financial results differ from total consolidated net income. The impact of these differences is reflected in the Other category in the business segment tables. Other includes residual activities that do not meet the criteria for disclosure as a separate reportable business, such as gains or losses related to BlackRock transactions, integration costs, asset and liability management activities including net securities gains or losses, other-than-temporary impairment of investment securities and certain trading activities, exited businesses, certain non-strategic runoff consumer loan portfolios, private equity investments, intercompany eliminations, most corporate overhead, tax adjustments that are not allocated to business segments and differences between business segment performance reporting and financial statement reporting (GAAP), including the presentation of net income attributable to noncontrolling interests as the segments results exclude their portion of net income attributable to noncontrolling interests.

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Retail Banking

(Unaudited)

Table 10: Retail Banking Table

Three months ended March 31			Change	
Dollars in millions, except as noted	2017	2016	$	%
Income Statement				
Net interest income	$ 1,121	$ 1,122	$ (1)	
Noninterest income	603	633	(30)	(5)%
Total revenue	1,724	1,755	(31)	(2)%
Provision for credit losses	71	72	(1)	(1)%
Noninterest expense	1,315	1,299	16	1%
Pretax earnings	338	384	(46)	(12)%
Income taxes	125	141	(16)	(11)%
Earnings	$ 213	$ 243	$ (30)	(12)%
Average Balance Sheet				
Loans held for sale	$ 843	$ 801	$ 42	5%
Loans				
Consumer				
Home equity	$ 25,601	$ 26,743	$ (1,142)	(4)%
Automobile	12,146	10,787	1,359	13%
Education	5,131	5,865	(734)	(13)%
Credit cards	5,121	4,722	399	8%
Other	1,756	1,823	(67)	(4)%
Total consumer	49,755	49,940	(185)	
Commercial and commercial real estate	11,006	11,801	(795)	(7)%
Residential mortgage	11,688	10,268	1,420	14%
Total loans	$ 72,449	$ 72,009	$ 440	1%
Total assets	$ 87,109	$ 86,213	$ 896	1%
Deposits				
Noninterest-bearing demand	$ 29,010	$ 26,980	$ 2,030	