STATE STREET CORP
Form 10-Q
November 01, 2017
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UNITED STATES
SECURITIES AND EXCHANGE COMMISSION
Washington, DC 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, 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 No. 001-07511

STATE STREET CORPORATION
(Exact name of registrant as specified in its charter)

Massachusetts	04-2456637
(State or other jurisdiction of incorporation)	(I.R.S. Employer Identification No.)
One Lincoln Street Boston, Massachusetts	02111
(Address of principal executive office)	(Zip Code)

617-786-3000
(Registrant’s telephone number, including area code)

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 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, 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 x	Accelerated filer ¨	Non-accelerated filer ¨	Smaller reporting company ¨
Emerging growth company ¨		(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 Act). Yes ¨ No x

The number of shares of the registrant’s common stock outstanding as of October 31, 2017 was 370,836,680.

STATE STREET CORPORATION
QUARTERLY REPORT ON FORM 10-Q FOR THE QUARTERLY PERIOD ENDED
September 30, 2017

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STATE STREET CORPORATION
MANAGEMENT'S DISCUSSION AND ANALYSIS OF FINANCIAL CONDITION AND RESULTS OF OPERATIONS

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We use acronyms and other defined terms for certain business terms and abbreviations, as defined on the acronyms list and glossary following the consolidated financial statements in this Form 10-Q.

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GENERAL

State Street Corporation, referred to as the Parent Company, is a financial holding company organized in 1969 under the laws of the Commonwealth of Massachusetts. Our executive offices are located at One Lincoln Street, Boston, Massachusetts 02111 (telephone (617) 786-3000). For purposes of this Form 10-Q, unless the context requires otherwise, references to “State Street,” “we,” “us,” “our” or similar terms mean State Street Corporation and its subsidiaries on a consolidated basis. The Parent Company is a source of financial and managerial strength to our subsidiaries.

Through our subsidiaries, including our principal banking subsidiary, State Street Bank, we provide a broad range of financial products and services to institutional investors worldwide, with $32.11 trillion of AUCA and $2.67 trillion of AUM as of September 30, 2017.

As of September 30, 2017, we had consolidated total assets of $235.99 billion, consolidated total deposits of $179.26 billion, consolidated total shareholders' equity of $22.50 billion and 36,303 employees. We operate in more than 100 geographic markets worldwide, including in the U.S., Canada, Europe, the Middle East and Asia.

Our operations are organized into two lines of business, Investment Servicing and Investment Management, which are defined based on products and services provided.

Additional information about our lines of business is provided in Line of Business Information in this Management's Discussion and Analysis and Note 17 to the consolidated financial statements in this Form 10-Q.

This Management's Discussion and Analysis is part of our Quarterly Report on Form 10-Q for the quarter ended September 30, 2017, and updates the Management's Discussion and Analysis in our 2016 Form 10-K previously filed with the SEC. You should read the financial information contained in this Management's Discussion and Analysis and elsewhere in this Form 10-Q in conjunction with the financial and other information contained in our 2016 Form 10-K. Certain previously reported amounts presented in this Form 10-Q have been reclassified to conform to current-period presentation.

We prepare our consolidated financial statements in conformity with U.S. GAAP. The preparation of financial statements in conformity with U.S. GAAP requires management to make estimates and assumptions in its application of certain accounting policies that materially affect the reported amounts of assets, liabilities, equity, revenue and expenses.

The significant accounting policies that require us to make judgments, estimates and assumptions that are difficult, subjective or complex about matters that are uncertain and may change in subsequent periods include:

- accounting for fair value measurements;
- other-than-temporary impairment of investment securities;
- impairment of goodwill and other intangible assets; and
- contingencies.

These significant accounting policies require the most subjective or complex judgments, and underlying estimates and assumptions could be subject to revision as new information becomes available. For additional information about these significant accounting policies, refer to pages 119 - 122, "Significant Accounting Estimates," included under Item 7, Management's Discussion and Analysis of Financial Condition and Results of Operations, in our 2016 Form 10-K. We did not change these significant accounting policies in the first nine months of 2017.

Certain financial information provided in this Form 10-Q, including in this Management's Discussion and Analysis, is prepared on both a U.S. GAAP, or reported basis, and a non-GAAP basis, including certain non-GAAP measures used in the calculation of identified regulatory ratios. We measure and compare certain financial information on a non-GAAP basis, including information (such as capital ratios calculated under regulatory standards scheduled to be effective in the future) that management uses in evaluating our business and activities.

Non-GAAP financial information should be considered in addition to, and not as a substitute for or superior to, financial information prepared in conformity with U.S. GAAP. Any non-GAAP financial information presented in this Form 10-Q, including this Management’s Discussion and Analysis, is reconciled to its most directly comparable

currently applicable regulatory ratio or U.S. GAAP-basis measure.
We further believe that our presentation of fully taxable-equivalent NII, a non-GAAP measure, which reports non-taxable revenue, such as interest income associated with tax-exempt investment securities, on a fully taxable-equivalent basis, facilitates an investor's understanding and analysis of our underlying financial performance and trends.
We provide additional disclosures required by applicable bank regulatory standards, including supplemental qualitative and quantitative information with respect to regulatory capital (including market

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risk associated with our trading activities) and the liquidity coverage ratio, summary results of semi-annual State Street-run stress tests which we conduct under the Dodd-Frank Act, and resolution plan disclosures required under the Dodd-Frank Act. These additional disclosures are accessible on the "Investor Relations" section of our corporate website at www.statestreet.com.

We have included our website address in this report as an inactive textual reference only. Information on our website is not incorporated by reference into this Form 10-Q.

We use acronyms and other defined terms for certain business terms and abbreviations, as defined in the acronyms list and glossary following the consolidated financial statements in this Form 10-Q.

Forward-Looking Statements

This Form 10-Q, as well as other reports and proxy materials submitted by us under the Securities Exchange Act of 1934, registration statements filed by us under the Securities Act of 1933, our annual report to shareholders and other public statements we may make, may contain statements (including statements in the Management's Discussion and Analysis included in such reports, as applicable) that are considered "forward-looking statements" within the meaning of U.S. securities laws, including statements about our goals and expectations regarding our business, financial and capital condition, results of operations, strategies, financial portfolio performance, dividend and stock purchase programs, outcomes of legal proceedings, market growth, acquisitions, joint ventures and divestitures, cost savings and transformation initiatives, client growth and new technologies, services and opportunities, as well as industry, regulatory, economic and market trends, initiatives and developments, the business environment and other matters that do not relate strictly to historical facts.

Terminology such as "plan," "expect," "intend," "objective," "forecast," "outlook," "believe," "priority," "anticipate," "estimat "may," "will," "trend," "target," "strategy" and "goal," or similar statements or variations of such terms, are intended to identif forward-looking statements, although not all forward-looking statements contain such terms.

Forward-looking statements are subject to various risks and uncertainties, which change over time, are based on management's expectations and assumptions at the time the statements are made, and are not guarantees of future results. Management's expectations and assumptions, and the continued validity of the forward-looking statements, are subject to change due to a broad range of factors affecting the national and global economies, regulatory environment and the equity,

debt, currency and other financial markets, as well as factors specific to State Street and its subsidiaries, including State Street Bank. Factors that could cause changes in the expectations or assumptions on which forward-looking statements are based cannot be foreseen with certainty and include, but are not limited to:

- the financial strength and continuing viability of the counterparties with which we or our clients do business and to which we have investment, credit or financial exposure, including, for example, the direct and indirect effects on counterparties of the sovereign-debt risks in the U.S., Europe and other regions;
- increases in the volatility of, or declines in the level of, our NII, changes in the composition or valuation of the assets recorded in our consolidated statement of condition (and our ability to measure the fair value of investment securities) and the possibility that we may change the manner in which we fund those assets;
- the liquidity of the U.S. and international securities markets, particularly the markets for fixed-income securities and inter-bank credits, and the liquidity requirements of our clients;
- the level and volatility of interest rates, the valuation of the U.S. dollar relative to other currencies in which we record revenue or accrue expenses and the performance and volatility of securities, credit, currency and other markets in the U.S. and internationally; and the impact of monetary and fiscal policy in the United States and internationally on prevailing rates of interest and currency exchange rates in the markets in which we provide services to our clients;
- the credit quality, credit-agency ratings and fair values of the securities in our investment securities portfolio, a deterioration or downgrade of which could lead to other-than-temporary impairment of the respective securities and the recognition of an impairment loss in our consolidated statement of income;
-

our ability to attract deposits and other low-cost, short-term funding, our ability to manage levels of such deposits and the relative portion of our deposits that are determined to be operational under regulatory guidelines and our ability to deploy deposits in a profitable manner consistent with our liquidity needs, regulatory requirements and risk profile;

- the manner and timing with which the Federal Reserve and other U.S. and foreign regulators implement or reevaluate changes to the regulatory framework applicable to our operations, including implementation or

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modification of the Dodd-Frank Act, the Basel III final rule and European legislation (such as the Alternative Investment Fund Managers Directive, Undertakings for Collective Investment in Transferable Securities Directives and Markets in Financial Instruments Directive II); among other consequences, these regulatory changes impact the levels of regulatory capital we must maintain, acceptable levels of credit exposure to third parties, margin requirements applicable to derivatives, and restrictions on banking and financial activities. In addition, our regulatory posture and related expenses have been and will continue to be affected by changes in regulatory expectations for global systemically important financial institutions applicable to, among other things, risk management, liquidity and capital planning, resolution planning, compliance programs, and changes in governmental enforcement approaches to perceived failures to comply with regulatory or legal obligations;

- our resolution plan, submitted to the Federal Reserve and FDIC in June 2017, may not be considered to be sufficient by the Federal Reserve and the FDIC, due to a number of factors, including, but not limited to, challenges we may experience in interpreting and addressing regulatory expectations, failure to implement remediation in a timely manner, the complexities of development of a comprehensive plan to resolve a global custodial bank and related costs and dependencies. If we fail to meet regulatory expectations to the satisfaction of the Federal Reserve and the FDIC in our resolution plan submission filed in June 2017 or any future submission, we could be subject to more stringent capital, leverage or liquidity requirements, or restrictions on our growth, activities or operations;
- adverse changes in the regulatory ratios that we are required or will be required to meet, whether arising under the Dodd-Frank Act or the Basel III final rule, or due to changes in regulatory positions, practices or regulations in jurisdictions in which we engage in banking activities, including changes in internal or external data, formulae, models, assumptions or other advanced systems used in the calculation of our capital ratios that cause changes in those ratios as they are measured from period to period;
- requirements to obtain the prior approval or non-objection of the Federal Reserve or other U.S. and non-U.S. regulators for the use, allocation or distribution of our capital or other specific capital actions or corporate activities, including,

without limitation, acquisitions, investments in subsidiaries, dividends and stock purchases, without which our growth plans, distributions to shareholders, share repurchase programs or other capital or corporate initiatives may be restricted;

- changes in law or regulation, or the enforcement of law or regulation, that may adversely affect our business activities or those of our clients or our counterparties, and the products or services that we sell, including additional or increased taxes or assessments thereon, capital adequacy requirements, margin requirements and changes that expose us to risks related to the adequacy of our controls or compliance programs;
- economic or financial market disruptions in the U.S. or internationally, including those which may result from recessions or political instability; for example, the U.K.'s decision to exit from the European Union may continue to disrupt financial markets or economic growth in Europe or, similarly, financial markets may react sharply or abruptly to actions taken by the new administration in the United States;
- our ability to develop and execute State Street Beacon, our multi-year transformation program to digitize our business, deliver significant value and innovation for our clients and lower expenses across the organization, any failure of which, in whole or in part, may among other things, reduce our competitive position, diminish the cost-effectiveness of our systems and processes or provide an insufficient return on our associated investment;
- our ability to promote a strong culture of risk management, operating controls, compliance oversight, ethical behavior and governance that meets our expectations and those of our clients and our regulators, and the financial, regulatory, reputation and other consequences of our failure to meet such expectations;
- the impact on our compliance and controls enhancement programs of the appointment of a monitor under the deferred prosecution agreement with the DOJ and compliance consultant appointed under a settlement with the SEC, including the potential for such monitor and compliance consultant to require changes to our programs or to identify other issues that require substantial expenditures, changes in our operations, or payments to clients or reporting to U.S. authorities;

- the results of our review of our billing practices, including additional amounts we may be required to reimburse clients, as well as

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potential consequences of such review, including damage to our client relationships and adverse actions by governmental authorities;

- the results of, and costs associated with, governmental or regulatory inquiries and investigations, litigation and similar claims, disputes, or civil or criminal proceedings;
- changes or potential changes in the amount of compensation we receive from clients for our services, and the mix of services provided by us that clients choose;
- the large institutional clients on which we focus are often able to exert considerable market influence, and this, combined with strong competitive market forces, subjects us to significant pressure to reduce the fees we charge, to potentially significant changes in our assets under custody and administration or our assets under management in the event of the acquisition or loss of a client, in whole or in part, and to potentially significant changes in our fee revenue in the event a client re-balances or changes its investment approach or otherwise re-directs assets to lower- or higher-fee asset classes;
- the potential for losses arising from our investments in sponsored investment funds;
- the possibility that our clients will incur substantial losses in investment pools for which we act as agent, and the possibility of significant reductions in the liquidity or valuation of assets underlying those pools;
- our ability to anticipate and manage the level and timing of redemptions and withdrawals from our collateral pools and other collective investment products;
- the credit agency ratings of our debt and depositary obligations and investor and client perceptions of our financial strength;
- adverse publicity, whether specific to State Street or regarding other industry participants or industry-wide factors, or other reputational harm;
- our ability to control operational risks, data security breach risks and outsourcing risks, our ability to protect our intellectual property rights, the possibility of errors in the quantitative models we use to manage our business and the possibility that our controls will prove insufficient, fail or be circumvented;
- our ability to expand our use of technology to enhance the efficiency, accuracy and reliability of our operations and our dependencies on information technology and our ability to control related risks, including cyber-crime and other threats to our information technology

infrastructure and systems (including those of our third-party service providers) and their effective operation both independently and with external systems, and complexities and costs of protecting the security of such systems and data;

- our ability to grow revenue, manage expenses, attract and retain highly skilled people and raise the capital necessary to achieve our business goals and comply with regulatory requirements and expectations;
- changes or potential changes to the competitive environment, including changes due to regulatory and technological changes, the effects of industry consolidation and perceptions of State Street as a suitable service provider or counterparty;
- our ability to complete acquisitions, joint ventures and divestitures, including the ability to obtain regulatory approvals, the ability to arrange financing as required and the ability to satisfy closing conditions;
- the risks that our acquired businesses and joint ventures will not achieve their anticipated financial and operational benefits or will not be integrated successfully, or that the integration will take longer than anticipated, that expected synergies will not be achieved or unexpected negative synergies or liabilities will be experienced, that client and deposit retention goals will not be met, that other regulatory or operational challenges will be experienced, and that disruptions from the transaction will harm our relationships with our clients, our employees or regulators;
- our ability to recognize evolving needs of our clients and to develop products that are responsive to such trends and profitable to us, the performance of and demand for the products and services we offer, and the potential for new products and services to impose additional costs on us and expose us to increased operational risk;
- changes in accounting standards and practices; and

- changes in tax legislation and in the interpretation of existing tax laws by U.S. and non-U.S. tax authorities that affect the amount of taxes due.

Actual outcomes and results may differ materially from what is expressed in our forward- looking statements and from our historical financial results due to the factors discussed in this section and elsewhere in this Form 10-Q or disclosed in our other SEC filings. Forward-looking statements in

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this Form 10-Q should not be relied on as representing our expectations or beliefs as of any time subsequent to the time this Form 10-Q is filed with the SEC. We undertake no obligation to revise our forward-looking statements after the time they are made. The factors discussed herein are not intended to be a complete statement of all risks and uncertainties that may affect our businesses. We cannot anticipate all developments that may adversely affect our business or operations or our consolidated results of operations, financial condition or cash flows.

Forward-looking statements should not be viewed as predictions, and should not be the primary basis on which investors evaluate State Street. Any investor in State Street should consider all risks and uncertainties disclosed in our SEC filings, including our filings under the Securities Exchange Act of 1934, in particular our annual reports on Form 10-K, our quarterly reports on Form 10-Q and our current reports on Form 8-K, or registration statements filed under the Securities Act of 1933, all of which are accessible on the SEC's website at www.sec.gov or on the "Investor Relations" section of our corporate website at www.statestreet.com.

OVERVIEW OF FINANCIAL RESULTS

TABLE 1: OVERVIEW OF FINANCIAL RESULTS

	Quarters Ended September 30,		
(Dollars in millions, except per share amounts)	2017	2016	% Change
Total fee revenue	$2,242	$2,079	8 %
Net interest income	603	537	12
Gains (losses) related to investment securities, net	1	4	nm
Total revenue	2,846	2,620	9
Provision for loan losses	3	—	—
Total expenses	2,021	1,984	2
Income before income tax expense	822	636	29
Income tax expense (benefit)	137	72	90
Net Income (loss) from non-controlling interest	—	(1)	nm
Net income	$685	$563	22
Adjustments to net income:			
Dividends on preferred stock[1]	(55)	(55)	—
Earnings allocated to participating securities[2]	(1)	(1)	nm
Net income available to common shareholders	$629	$507	24
Earnings per common share:			
Basic	$1.69	$1.31	29
Diluted	1.66	1.29	29
Average common shares outstanding (in thousands):			
Basic	372,765	388,358	
Diluted	378,518	393,212	
Cash dividends declared per common share	$.42	$.38	
Return on average common equity	13.0 %	10.6 %	

	Nine Months Ended September 30,		
(Dollars in millions, except per share amounts)	2017	2016	% Change
Total fee revenue	$6,675	$6,102	9 %

Net interest income	1,688	1,570	8
Gains (losses) related to investment securities, net	(39)	5	nm
Total revenue	8,324	7,677	8
Provision for loan losses	4	8	(50)
Total expenses	6,138	5,894	4
Income before income tax expense	2,182	1,775	23
Income tax expense (benefit)	375	226	66
Net income from non-controlling interest	—	1	nm
Net income	$1,807	$1,550	17
Adjustments to net income:			
Dividends on preferred stock[(1)]	$(146)	$(137)	7
Earnings allocated to participating securities[(2)]	(2)	(2)	nm
Net income available to common shareholders	$1,659	$1,411	18
Earnings per common share:			
Basic	$4.41	$3.58	23
Diluted	4.35	3.54	23
Average common shares outstanding (in thousands):			
Basic	376,430	393,959	
Diluted	381,779	398,413	
Cash dividends declared per common share	$1.18	$1.06	
Return on average common equity	11.9 %	9.9 %	

(1) Additional information about our preferred stock dividends is provided in Note 12 to the consolidated financial statements in this Form 10-Q.
(2) Represents the portion of net income available to common equity allocated to participating securities, composed of unvested and fully vested SERP shares and fully vested deferred director stock awards, which are equity-based awards that contain non-forfeitable rights to dividends, and are considered to participate with the common stock in undistributed earnings.
nm Not meaningful

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The following “Financial Results and Highlights” section provides information related to significant events, as well as highlights of our consolidated financial results for the quarter ended September 30, 2017 presented in Table 1: Overview of Financial Results. More detailed information about our consolidated financial results, including comparisons of our financial results for the third quarter and first nine months ended September 30, 2017 to those for the same periods in 2016, is provided under “Consolidated Results of Operations,” "Line of Business Information" and "Capital" which follows these sections, as well as in our consolidated financial statements included in this Form 10-Q. In this Management’s Discussion and Analysis, where we describe the effects of changes in foreign exchange rates, those effects are determined by applying applicable weighted average foreign exchange rates from the relevant 2016 period to the relevant 2017 period results.

Financial Results and Highlights

- EPS of $1.66 in the third quarter of 2017 increased 29% compared to $1.29 in the third quarter of 2016.
- Third quarter 2017 ROE of 13.0% increased from 10.6% in the third quarter of 2016.
- Pre-tax margin of 28.9% in the third quarter of 2017 increased from 24.3% in the third quarter of 2016.

Revenue

- Total revenue and fee revenue increased 9% and 8%, respectively, in the third quarter of 2017 compared to the third quarter of 2016, primarily driven by higher global equity markets, net new asset servicing business and the impact of the weaker U.S. dollar, partially offset by lower trading services revenue.
- Servicing fee revenue increased 4% in the third quarter of 2017 compared to the third quarter of 2016, primarily due to higher global equity markets, net new business and the weaker U.S. dollar.
- Management fee revenue increased 14% in the third quarter of 2017 compared to the third quarter of 2016, primarily due to higher global equity markets, new business and higher revenue-yielding ETF inflows.
- NII increased 12% in the third quarter of 2017 compared to the third quarter of 2016, primarily due to higher U.S. market interest rates, loan portfolio growth, lower wholesale CD costs and disciplined liability pricing, partially offset by lower average interest earning assets.

Expenses

- Total expenses increased 2% in the third quarter of 2017 compared to the third quarter of 2016, primarily reflecting installation of new business, annual merit and performance related incentive compensation increases and the impact of the weaker U.S. dollar, partially offset by Beacon savings (including approximately $35 million of Beacon savings attributable to the third quarter of 2017).
- In the third quarter of 2017, we recorded restructuring charges of $33 million related to Beacon.

AUCA/AUM

- AUCA increased 10% in the third quarter of 2017 compared to the third quarter of 2016, primarily due to higher global equity markets and business activity. In the third quarter of 2017, we secured new asset servicing mandates of approximately $105 billion. Our AUCA pipeline of asset servicing mandates that have been won but not yet installed as of September 30, 2017 totaled approximately $390 billion.
- AUM increased 9% in the third quarter of 2017 compared to the third quarter of 2016, primarily due to higher global equity markets and positive ETF flows, partially offset by continuing institutional net outflows.

Capital

- We declared a quarterly common stock dividend of $0.42 per share, totaling approximately $156 million in the third quarter of 2017, compared to $0.38 per share, totaling $147 million in the third quarter of 2016, representing an increase of approximately 11% on a per share basis.
- In the third quarter of 2017, we acquired approximately 3.7 million shares of common stock at an average per-share cost of $93.39 and an aggregate cost of approximately $350 million under the common stock purchase program approved by our Board in June 2017.
- CET1 capital ratio under the Basel III standardized approach was 11.6% as of September 30, 2017.
- Tier 1 leverage ratio increased to 7.4% as of September 30, 2017.

MANAGEMENT'S DISCUSSION AND ANALYSIS OF FINANCIAL CONDITION AND RESULTS OF OPERATIONS

CONSOLIDATED RESULTS OF OPERATIONS

This section discusses our consolidated results of operations for the third quarter and first nine months ended September 30, 2017 compared to the same periods in 2016, and should be read in conjunction with the consolidated financial statements and accompanying condensed notes to the consolidated financial statements included in this Form 10-Q.

Total Revenue

TABLE 2: TOTAL REVENUE

(Dollars in millions)	Quarters Ended September 30, 2017	2016	% Change
Fee revenue:			
Servicing fees	$1,351	$1,303	4 %
Management fees	419	368	14
Trading services:			
Foreign exchange trading	150	159	(6)
Brokerage and other trading services	109	108	1
Total trading services	259	267	(3)
Securities finance	147	136	8
Processing fees and other	66	5	nm
Total fee revenue	2,242	2,079	8
Net interest income:			
Interest income	761	647	18
Interest expense	158	110	44
Net interest income	603	537	12
Gains (losses) related to investment securities, net	1	4	nm
Total revenue	$2,846	$2,620	9

(Dollars in millions)	Nine Months Ended September 30, 2017	2016	% Change
Fee revenue:			
Servicing fees	$3,986	$3,784	5 %
Management fees	1,198	931	29
Trading services:			
Foreign exchange trading	492	472	4
Brokerage and other trading services	331	334	(1)
Total trading services	823	806	2
Securities finance	459	426	8
Processing fees and other	209	155	35
Total fee revenue	6,675	6,102	9
Net interest income:			
Interest income	2,111	1,896	11
Interest expense	423	326	30
Net interest income	1,688	1,570	8

Gains (losses) related to investment securities, net	(39)	5	nm
Total revenue	$8,324	$7,677	8

nm Not meaningful

Fee Revenue

Table 2: Total Revenue, provides the breakout of fee revenue for the quarters and nine months ended September 30, 2017 and 2016.

Servicing and management fees collectively made up approximately 79% and 78% of total fee revenue in the third quarter and first nine months of 2017, respectively, compared to approximately 80% and 77% in the third quarter and first nine months of 2016, respectively. The level of these fees is influenced by several factors, including the mix and volume of our AUCA and our AUM, the value and type of securities positions held (with respect to assets under custody), the volume of portfolio transactions, and the types of products and services used by our clients, and is generally affected by changes in worldwide equity and fixed-income security valuations and trends in market asset class preferences.

Generally, servicing fees are affected by changes in daily average valuations of AUCA. Additional factors, such as the relative mix of assets serviced, the level of transaction volumes, changes in service level, the nature of services provided, balance credits, client minimum balances, pricing concessions, the geographical location in which services are provided and other factors, may have a significant effect on our servicing fee revenue.

Management fees generally are affected by changes in month-end valuations of AUM. Management fees for certain components of managed assets, such as ETFs, are affected by daily average valuations of AUM. Management fee revenue is more sensitive to market valuations than servicing fee revenue, as a higher proportion of the underlying services provided, and the associated management fees earned, are dependent on equity and fixed-income security valuations. Additional factors, such as the relative mix of assets managed, may have a significant effect on our management fee revenue. While certain management fees are directly determined by the values of AUM and the investment strategies employed, management fees may reflect other factors as well, including performance fee arrangements, as well as our relationship pricing for clients using multiple services.

Asset-based management fees for actively managed products are generally charged at a higher percentage of AUM than for passive products. Actively managed products may also include performance fee arrangements which are recorded when the performance period is complete.

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In light of the above, we estimate, using relevant information as of September 30, 2017 and assuming that all other factors remain constant, that:

- A 10% increase or decrease in worldwide equity valuations, on a weighted average basis, over the relevant periods for which our servicing and management fees are calculated, would result in a corresponding change in our total servicing and management fee revenues of approximately 3%; and
- A 10% increase or decrease in worldwide fixed income markets, on a weighted average basis, over the relevant periods for which our servicing and management fees are calculated, would result in a corresponding change in our total servicing and management fee revenues of approximately 1%.

See Table 3: Daily, Month-End and Quarter-End Equity Indices and Table 4: Quarter-End Debt Indices, for selected indices. While the specific indices presented are indicative of general market trends, the asset types and classes relevant to individual client portfolios can and do differ, and the performance of associated relevant indices can therefore differ from the performance of the indices presented.

Daily averages, month-end averages, and quarter-end indices demonstrate worldwide changes in equity and debt markets that affect our servicing and management fee revenue. Quarter-end indices affect the values of AUCA and AUM as of those dates.

Further discussion of fee revenue is provided under Line of Business Information in this Management's Discussion and Analysis in this Form 10-Q.

TABLE 3: DAILY, MONTH-END AND QUARTER-END EQUITY INDICES(1)

	Daily Averages of Indices			Averages of Month-End Indices			Quarter-End Indices		
	Quarters Ended September 30,			Quarters Ended September 30,			As of September 30,		
	2017	2016	% Change	2017	2016	% Change	2017	2016	% Change
S&P 500®	2,467	2,162	14 %	2,487	2,171	15 %	2,519	2,168	16 %
MSCI EAFE®	1,934	1,678	15	1,947	1,692	15	1,974	1,702	16
MSCI® Emerging Markets	1,068	887	20	1,079	890	21	1,082	903	20
HFRI Asset Weighted Composite®	NA	NA	NA	1,358	1,274	7	1,361	1,277	7

	Daily Averages of Indices			Averages of Month-End Indices		
	Nine Months Ended September 30,			Nine Months Ended September 30,		
	2017	2016	% Change	2017	2016	% Change
S&P 500®	2,397	2,065	16 %	2,410	2,078	16 %
MSCI EAFE®	1,846	1,640	13	1,859	1,650	13
MSCI® Emerging Markets	996	821	21	1,004	830	21
HFRI Asset Weighted Composite®	NA	NA	NA	1,340	1,255	7

(1) The index names listed in the table are service marks of their respective owners.
NA Not applicable

TABLE 4: QUARTER-END DEBT INDICES(1)

	Quarter-End Indices		
	As of September 30,		
	2017	2016	% Change
Barclays Capital U.S. Aggregate Bond Index®	2,038	2,037	— %

Barclays Capital Global Aggregate Bond Index®	480	486	nm

(1) The index names listed in the table are service marks of their respective owners.

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Net Interest Income

See Table 2: Total Revenue, for the breakout of interest income and interest expense for the quarters and nine months ended September 30, 2017 and 2016.

NII is defined as interest income earned on interest-earning assets less interest expense incurred on interest-bearing liabilities. Interest-earning assets, which principally consist of investment securities, interest-bearing deposits with banks, repurchase agreements, loans and leases and other liquid assets, are financed primarily by client deposits, short-term borrowings and long-term debt.

NIM represents the relationship between annualized fully taxable-equivalent NII and average total interest-earning assets for the period. It is calculated by dividing fully taxable-equivalent NII by average interest-earning assets. Revenue that is exempt from income taxes, mainly that earned from certain investment securities (state and political subdivisions), is adjusted to a fully taxable-equivalent basis using a federal statutory income tax rate of 35%, adjusted for applicable state income taxes, net of the related federal tax benefit.

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TABLE 5: AVERAGE BALANCES AND INTEREST RATES - FULLY TAXABLE-EQUIVALENT BASIS

	Quarters Ended September 30,					
	2017			2016		
(Dollars in millions; fully taxable-equivalent basis)	Average Balance	Interest Revenue/ Expense	Rate	Average Balance	Interest Revenue/ Expense	Rate
Interest-bearing deposits with banks	$45,513	$45	.40 %	$57,580	$29	.20 %
Securities purchased under resale agreements[1]	2,167	74	13.53	2,667	40	6.01
Trading account assets	991	—	—	994	—	—
Investment securities	95,311	474	1.99	100,449	505	2.01
Loans and leases	22,843	143	2.49	18,744	97	2.06
Other interest-earning assets	23,091	67	1.18	21,721	18	.30
Average total interest-earning assets	$189,916	$803	1.68	$202,155	$689	1.35
Interest-bearing deposits:						
U.S.	$25,767	$21	.32 %	$33,668	$42	.49 %
Non-U.S.[2]	96,189	18	.07	95,617	(22)	(.09)
Securities sold under repurchase agreements[3]	3,974	1	.07	3,976	—	—
Federal funds purchased	—	—	—	24	—	—
Other short-term borrowings	1,277	3	.81	1,566	2	.57
Long-term debt	11,766	78	2.67	11,885	68	2.27
Other interest-bearing liabilities	4,063	37	3.70	5,647	20	1.41
Average total interest-bearing liabilities	$143,036	$158	.44	$152,383	$110	.29
Interest-rate spread			1.24 %			1.06 %
Net interest income—fully taxable-equivalent basis		$645			$579	
Net interest margin—fully taxable-equivalent basis			1.35 %			1.14 %
Tax-equivalent adjustment		(42)			(42)	
Net interest income—GAAP basis		$603			$537	

	Nine Months Ended September 30,					
	2017			2016		
(Dollars in millions; fully taxable-equivalent basis)	Average Balance	Interest Revenue/ Expense	Rate	Average Balance	Interest Revenue/ Expense	Rate
Interest-bearing deposits with banks	$49,171	$121	.33 %	$52,423	$101	.26 %
Securities purchased under resale agreements[1]	2,192	189	11.52	2,610	112	5.73
Trading account assets	949	(1)	(.14)	908	1	.09
Investment securities	95,716	1,410	1.96	101,243	1,486	1.96
Loans and leases	21,360	373	2.33	18,674	281	2.01
Other interest-earning assets	22,952	146	.85	22,316	39	.24
Average total interest-earning assets	$192,340	$2,238	1.56	$198,174	$2,020	1.36
Interest-bearing deposits:						
U.S.	$25,821	$77	.40 %	$30,388	$99	.44 %
Non-U.S.[2]	96,860	19	.03	95,013	(26)	(.04)
Securities sold under repurchase agreements	3,965	2	.05	4,107	1	.03
Federal funds purchased	1	—	—	33	—	—
Other short-term borrowings	1,313	7	.75	1,727	4	.34

Long-term debt	11,569	227	2.61	11,306	191	2.24
Other interest-bearing liabilities	4,881	91	2.50	5,550	57	1.38
Average total interest-bearing liabilities	$ 144,410	$ 423	.39	$ 148,124	$ 326	.29
Interest-rate spread			1.17 %			1.07 %
Net interest income—fully taxable-equivalent basis		$ 1,815			$ 1,694	
Net interest margin—fully taxable-equivalent basis			1.26 %			1.14 %
Tax-equivalent adjustment		(127)			(124)	
Net interest income—GAAP basis		$ 1,688			$ 1,570	

(1) Reflects the impact of balance sheet netting under enforceable netting agreements of approximately $30 billion and $31 billion for the third quarter and first nine months of 2017, respectively, and $30 billion and $32 billion for the third quarter and first nine months of 2016, respectively. Excluding the impact of netting, the average interest rates would be approximately 0.92% and 0.76% for the third quarter and first nine months of 2017, respectively, and 0.49% and 0.44% for the third quarter and first nine months of 2016, respectively.
(2) Average rate includes the impact of FX swap expense of approximately $39 million and $84 million for the third quarter and first nine months of 2017, respectively, and $3 million and $24 million for the same periods in 2016, respectively.
(3) Interest for the third quarter of 2016 was less than $1 million, representing an average interest rate of 0.02%.

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See Table 5: Average Balances and Interest Rates - Fully Taxable-Equivalent Basis, for the breakout of NII on a fully taxable-equivalent basis for the quarters and nine months ended September 30, 2017 and 2016. NII on a fully taxable-equivalent basis increased in the third quarter of 2017 compared to the same period in 2016, as benefits due to higher U.S. market interest rates, loan portfolio growth and disciplined liability pricing were partially offset by lower average interest earning assets and a smaller amount of discount accretion related to the asset-backed commercial paper conduits. Average balances in the third quarter of 2017 reflect management actions to reduce the usage of wholesale deposit funding on our balance sheet. Average deposits were approximately $12.06 billion lower in the third quarter of 2017 compared to the third quarter of 2016, primarily due to a $14.91 billion reduction in wholesale deposit funding and were partially offset by an increase in less expensive client deposits.

We recorded aggregate discount accretion in interest income of $4 million and $15 million for the third quarter and first nine months of 2017, respectively, related to the assets we consolidated onto our balance sheet in 2009 from our asset-backed commercial paper conduits. Assuming that we hold the former conduit securities remaining in our investment portfolio until they mature or are sold, we expect to generate aggregate discount accretion in future periods of approximately $126 million over their remaining terms.

Changes in the components of interest-earning assets and interest-bearing liabilities are discussed in more detail below. Additional information about the components of interest income and interest expense is provided in Note 14 to the consolidated financial statements included in this Form 10-Q.

Average total interest-earning assets were $5.83 billion lower in the nine months ended September 30, 2017 compared to the same period in 2016, primarily due to a smaller investment portfolio.

Interest-bearing deposits with banks averaged $45.51 billion and $49.17 billion for the third quarter and first nine months of 2017, respectively, compared to $57.58 billion and $52.42 billion for the same periods in 2016. These deposits primarily reflect our maintenance of cash balances at the Federal Reserve, the ECB and other non-U.S. central banks.

Investment securities averaged $95.31 billion and $95.72 billion for the third quarter and first nine months of 2017, respectively, compared to $100.45 billion and $101.24 billion for the same periods in 2016. The decrease in average investment securities resulted from a reduction of our U.S. Treasury securities and our continued investment into loans and lease products.

Loans and leases averaged $22.84 billion and $21.36 billion for the third quarter and first nine months of 2017, respectively, compared to $18.74 billion and $18.67 billion for the same periods in 2016. The increase in average loans and leases resulted from growth in loans to municipalities, mutual fund lending, and continued investment in senior secured loans.

TABLE 6: U.S. AND NON-U.S. SHORT-DURATION ADVANCES

	Quarters Ended September 30,	
(Dollars in millions)	2017	2016
Average U.S. short-duration advances	$2,233	$2,114
Average non-U.S. short-duration advances	1,566	1,299
Average total short-duration advances	$3,799	$3,413
Average short-duration advances to average loans and leases	17 %	18 %

	Nine Months Ended September 30,	
(Dollars in millions)	2017	2016
Average U.S. short-duration advances	$2,193	$2,163
Average non-U.S. short-duration advances	1,414	1,345

Average total short-duration advances	$3,607	$3,508
Average short-duration advances to average loans and leases	17 %	19 %

Average loans and leases also includes short-duration advances. The decline in the proportion of average short-duration advances to average loans and leases is primarily due to growth in the other segments of the loan and lease portfolio. Short-duration advances provide liquidity to clients in support of their investment activities.

Average other interest-earning assets increased to $23.09 billion and $22.95 billion for the third quarter and first nine months of 2017, respectively, from $21.72 billion and $22.32 billion for the same periods in 2016. Our average other interest-earning assets, largely associated with our enhanced custody business, comprised approximately 12% of our average total interest-earning assets for both the third quarter and first nine months of 2017, compared to approximately 11% for both the third quarter and first nine months of 2016. The enhanced custody business is our securities financing business where we act as principal with respect to our custody clients and generate securities finance revenue.

Aggregate average U.S. and non-U.S. interest-bearing deposits decreased to $121.96 billion and $122.68 billion for the third quarter and first nine months of 2017, respectively, from $129.29 billion and $125.40 billion for the same periods in 2016. The lower levels in the first nine months of 2017 compared to the prior year period were a result of higher U.S. and non-U.S. interest bearing client deposit levels during the year, offset by

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management's actions to reduce more expensive wholesale deposit funding. Future deposit levels will be influenced by the underlying asset servicing business, client deposit behavior, as well as market conditions, including the general levels of U.S. and non-U.S. interest rates.

Average other short-term borrowings declined to $1.28 billion and $1.31 billion for the third quarter and first nine months of 2017, respectively, from $1.57 billion and $1.73 billion for the same periods in 2016, as bonds matured in the tax-exempt investment program.

Average long-term debt was $11.77 billion and $11.57 billion for the third quarter and first nine months of 2017, respectively, compared to $11.89 billion and $11.31 billion for the same periods in 2016. These amounts reflect issuances and maturities of senior debt during the respective periods.

Average other interest-bearing liabilities were $4.06 billion and $4.88 billion for the third quarter and first nine months of 2017, respectively, compared to $5.65 billion and $5.55 billion for the same periods in 2016. Other interest-bearing liabilities primarily reflect our level of cash collateral received from clients in connection with our enhanced custody business, which is presented on a net basis where we have enforceable netting agreements.

Several factors could affect future levels of NII and NIM, including the volume and mix of client liabilities; actions of various central banks; changes in the level of U.S. and non-U.S. interest rates and the slope of various yield curves around the world; revised or proposed regulatory capital or liquidity standards, or interpretations of those standards; the amount of discount accretion generated by the former conduit securities that remain in our investment securities portfolio; the yields earned on securities purchased compared to the yields earned on securities sold or matured; changes in the type and amount of credit or other loans we extend; and changes in our enhanced custody business.

Based on market conditions and other factors, including regulatory standards, we continue to reinvest the majority of the proceeds from pay-downs and maturities of investment securities in highly-rated securities, such as U.S. Treasury and agency securities, municipal securities, federal agency MBS and U.S. and non-U.S. mortgage- and ABS. The pace at which we continue to reinvest and the types of investment securities purchased will depend on the impact of market conditions, the implementation of regulatory standards, including interpretation of those standards and other factors over time. We expect these factors and the levels of global interest rates to influence what effect our reinvestment program will have on future levels of our NII and NIM.

Expenses

Table 7: Expenses, provides the breakout of expenses for the quarters and nine months ended September 30, 2017 and 2016.

TABLE 7: EXPENSES

	Quarters Ended September 30,		
(Dollars in millions)	2017	2016	% Change
Compensation and employee benefits	$1,090	$1,013	8 %
Information systems and communications	296	285	4
Transaction processing services	215	200	8
Occupancy	118	107	10
Acquisition costs	—	33	(100)
Restructuring charges, net	33	9	267
Other:			
Professional services	71	95	(25)
Amortization of other intangible assets	54	55	(2)
Securities processing costs	4	10	(60)
Regulatory fees and assessments	24	28	(14)

Other	116	149	(22)
Total other	269	337	(20)
Total expenses	$2,021	$1,984	2
Number of employees at quarter-end	36,303	33,332	9

	Nine Months Ended September 30,		
(Dollars in millions)	2017	2016	% Change
Compensation and employee benefits	$3,327	$3,109	7 %
Information systems and communications	866	827	5
Transaction processing services	619	601	3
Occupancy	344	331	4
Acquisition costs	21	47	(55)
Restructuring charges, net	112	119	(6)
Other:			
Professional services	262	270	(3)
Amortization of other intangible assets	160	153	5
Securities processing costs	20	20	—
Regulatory fees and assessments	77	65	18
Other	330	352	(6)
Total other	849	860	(1)
Total expenses	$6,138	$5,894	4

Compensation and employee benefits expenses increased 8% in the third quarter of 2017 compared to the same period of 2016, primarily due to increased costs to support new business, annual merit and performance based incentive compensation increases and the impact of the weaker U.S. dollar, partially offset by Beacon savings.

Compensation and employee benefits expenses increased 7% in the first nine months of 2017 compared to the same period of 2016, primarily due to higher annual merit and performance based incentive compensation increases, including higher seasonal deferred incentive compensation expense for retirement-eligible employees and payroll taxes in the first quarter of 2017 compared to the first quarter of 2016, increased costs to support new business and costs related to the acquired GEAM operations.

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These increases were partially offset by Beacon savings.
Headcount increased 9% in the third quarter of 2017 compared to the same period of 2016. New business, including the impact of large client lift outs, as well as regulatory initiatives and contractor conversions to full-time employees contributed to this growth. The growth in headcount was primarily within low cost locations. These increases were partially offset by other reductions from Beacon initiatives.
Information systems and communications expenses increased 4% in the third quarter of 2017 compared to the same period of 2016 and 5% in the first nine months of 2017 compared to the same period of 2016. The increases were primarily related to technology infrastructure costs, new business and Beacon investments.
Other expenses decreased 20% in the third quarter of 2017 compared to the same period of 2016, primarily due to lower professional services fees.
As a systemically important financial institution, we are subject to enhanced supervision and prudential standards. Our status as a G-SIB has also resulted in heightened prudential and conduct expectations of our U.S. and international regulators with respect to our capital and liquidity management and our compliance and risk oversight programs. These heightened expectations have increased our regulatory compliance costs, including personnel and systems, as well as significant additional implementation and related costs to enhance our regulatory compliance programs. We anticipate that these evolving regulatory compliance requirements and expectations will continue to affect our expenses.
Restructuring Charges
In connection with Beacon, we expect to incur aggregate pre-tax restructuring charges of approximately $300 million to $400 million beginning in 2016 through December 31, 2020. We estimate those charges will include approximately $250 million to $300 million in severance and benefits costs associated with targeted staff reductions (a substantial portion of which will result in future cash expenditures) and approximately $50 million to $100 million in information technology application rationalization and real estate actions. We expect to achieve estimated annual pre-tax net run-rate expense savings of $550 million by the end of 2020, relative to 2015, all else equal, for full effect in 2021. Actual expenses may increase or decrease in the future due to other factors.
In the third quarter and first nine months of 2017, we recorded restructuring charges of $33 million and $112 million, respectively, compared to

$10 million and $120 million in the same periods of 2016, related to Beacon.
In the third quarter of 2017, we recognized approximately $35 million in year-over-year expense savings related to Beacon. In the first nine months of 2017, we achieved approximately $100 million in expense savings relative to our 2017 target of $140 million.
The following table presents aggregate restructuring activity for the periods indicated.
TABLE 8: RESTRUCTURING CHARGES

(In millions)	Employee Related Costs	Real Estate Actions	Asset and Other Write-offs	Total
Accrual Balance at December 31, 2015	$ 9	$ 11	$ 3	$23
Accruals for Beacon	86	—	11	97
Payments and Other Adjustments	(4)	(1)	(7)	(12)
Accrual Balance at March 31, 2016	$ 91	$ 10	$ 7	$108
Accruals for Beacon	(1)	15	(1)	13
Payments and Other Adjustments	(35)	(3)	(1)	(39)
Accrual Balance at June 30, 2016	$ 55	$ 22	$ 5	$82
Accruals for Beacon	8	3	(1)	10
Payments and Other Adjustments	(14)	(3)	(1)	(18)
Accrual Balance at September 30, 2016	$ 49	$ 22	$ 3	$74

Accrual Balance at December 31, 2016	$ 37	$ 17	$ 2	$56
Accruals for Beacon	14	—	2	16
Payments and Other Adjustments	(13)	(3)	(2)	(18)
Accrual Balance at March 31, 2017	$ 38	$ 14	$ 2	$54
Accruals for Beacon	60	—	2	62
Payments and Other Adjustments	(11)	(3)	(2)	(16)
Accrual Balance at June 30, 2017	$ 87	$ 11	$ 2	$100
Accruals for Beacon	23	9	1	33
Payments and Other Adjustments	(10)	(5)	(1)	(16)
Accrual Balance at September 30, 2017	$ 100	$ 15	$ 2	$117

Income Tax Expense

Income tax expense was $137 million in the third quarter of 2017 compared to $72 million in the third quarter of 2016. In the first nine months of 2017 and 2016, income tax expense was $375 million and $226 million, respectively. Our effective tax rate for the third quarter and first nine months of 2017 was 16.7% and 17.2%, respectively, compared to 11.4% and 12.8% for the same periods in 2016. The effective tax rate for the third quarter and first nine months of 2017 reflect a decrease in alternative energy investments, partially offset by benefits from share-based compensation and the effects of the disposition of BFDS.

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LINE OF BUSINESS INFORMATION

Our operations are organized into two lines of business: Investment Servicing and Investment Management, which are defined based on products and services provided. The results of operations for these lines of business are not necessarily comparable with those of other companies, including companies in the financial services industry.

Investment Servicing provides services for institutional clients, including mutual funds, collective investment funds and other investment pools, corporate and public retirement plans, insurance companies, investment managers, foundations and endowments worldwide. Products include custody; product- and participant-level accounting; daily pricing and administration; master trust and master custody; record-keeping; cash management; foreign exchange, brokerage and other trading services; securities finance; our enhanced custody product, which integrates principal securities lending and custody; deposit and short-term investment facilities; loans and lease financing; investment manager and alternative investment manager operations

outsourcing; and performance, risk and compliance analytics to support institutional investors.

Investment Management, through SSGA, provides a broad array of investment management, investment research and investment advisory services to corporations, public funds and other sophisticated investors. SSGA offers passive and active asset management strategies across equity, fixed-income, alternative, multi-asset solutions (including OCIO) and cash asset classes. Products are distributed directly and through intermediaries using a variety of investment vehicles, including ETFs, such as the SPDR® ETF brand.

For information about our two lines of business, as well as the revenues, expenses and capital allocation methodologies associated with them, refer to pages 188 to 189 provided in Note 24 to the consolidated financial statements included under Item 8, Financial Statements and Supplementary Data, in our 2016 Form 10-K and Note 17 to the consolidated financial statements included in this Form 10-Q.

Investment Servicing

TABLE 9: INVESTMENT SERVICING LINE OF BUSINESS RESULTS

	Quarters Ended September 30,			Nine Months Ended September 30,		
(Dollars in millions)	2017	2016	% Change	2017	2016	% Change
Servicing fees	$1,351	$1,303	4 %	$3,986	$3,784	5 %
Trading services	239	248	(4)	768	760	1
Securities finance	147	136	8	459	426	8
Processing fees and other	65	12	442	203	164	24
Total fee revenue	1,802	1,699	6	5,416	5,134	5
Net interest income	606	536	13	1,691	1,567	8
Gains (losses) related to investment securities, net	1	4	nm	(39)	5	nm
Total revenue	2,409	2,239	8	7,068	6,706	5
Provision for loan losses	3	—	nm	4	8	nm
Total expenses	1,673	1,634	2	5,050	4,920	3
Income before income tax expense	$733	$605	21	$2,014	$1,778	13
Pre-tax margin	30 %	27 %		28 %	27 %	

nm Not meaningful

Servicing Fees

Servicing fees increased 4% in the third quarter of 2017 compared to the same period in 2016, primarily due to higher global equity markets, net new business and the weaker U.S. dollar, partially offset by continued outflows and liquidations from hedge funds that we service.

Servicing fees increased 5% in the first nine months of 2017 compared to the same period in 2016, primarily due to higher global equity markets and net new business, partially offset by continued outflows and liquidations from hedge funds that we service. The first nine months of 2016 included a revenue reduction of $48 million related to

reimbursements to our clients related to the manner in which we invoiced certain expenses to our clients, as further described below.

Servicing fees generated outside the U.S. were approximately 47% and 45% of total servicing fees in both the third quarter and first nine months of 2017 compared to approximately 43% and 42% for the same periods in 2016, respectively.

In December 2015, we announced a review of the manner in which we invoiced certain expenses to certain of our Investment Servicing clients, primarily in the United States, during a period going back to 1998. We have substantially completed the reimbursement to our clients of an amount equal to

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the expenses we concluded were incorrectly invoiced to them, plus interest. Additional information about the invoicing matter is provided in Note 10 to the consolidated financial statements included in this Form 10-Q.

TABLE 10: ASSETS UNDER CUSTODY AND ADMINISTRATION BY PRODUCT

(In billions)	September 30, 2017	December 31, 2016	September 30, 2016
Mutual funds	$ 7,394	$ 6,841	$ 6,906
Collective funds	9,190	7,501	7,541
Pension products	6,571	5,584	5,671
Insurance and other products	8,955	8,845	9,060
Total	$ 32,110	$ 28,771	$ 29,178

TABLE 11: ASSETS UNDER CUSTODY AND ADMINISTRATION BY ASSET CLASS

(In billions)	September 30, 2017	December 31, 2016	September 30, 2016
Equities	$ 18,423	$ 16,189	$ 16,400
Fixed-income	9,883	9,231	9,500
Short-term and other investments	3,804	3,351	3,278
Total	$ 32,110	$ 28,771	$ 29,178

TABLE 12: GEOGRAPHIC MIX OF ASSETS UNDER CUSTODY AND ADMINISTRATION[1]

(In billions)	September 30, 2017	December 31, 2016	September 30, 2016
North America	$ 23,675	$ 21,544	$ 21,561
Europe/Middle East/Africa	6,806	5,734	6,107
Asia/Pacific	1,629	1,493	1,510
Total	$ 32,110	$ 28,771	$ 29,178

(1) Geographic mix is based on the location in which the assets are serviced.

The increase in total AUCA as of September 30, 2017 compared to December 31, 2016 primarily resulted from higher global equity markets. Asset levels as of September 30, 2017 do not reflect the approximately $390 billion of new business in assets to be serviced, which was awarded to us in the first nine months of 2017 and prior periods but not installed prior to September 30, 2017, including approximately $105 billion of new asset servicing mandates awarded to us in the third quarter of 2017. This new business will be reflected in AUCA in future periods after installation and will generate servicing fee revenue in subsequent periods. The $390 billion of new business assets to be serviced does not include new business which has been contracted, but for which the client has not yet provided permission to publicly disclose and is not yet installed. Also not included is the loss of business which occurs from time to time or changes in AUCA, usually from changes in market values of customer assets, subscriptions or redemptions from our customer investment products.

With respect to these new assets, we will provide various services, including, accounting, bank loan servicing, compliance reporting and monitoring, custody, depository banking services, foreign exchange, fund administration, hedge fund servicing, middle-office outsourcing, performance and analytics, private equity administration, real estate administration, securities finance, transfer agency, and wealth management services.

As a result of a decision to diversify providers, one of our large clients will move a portion of its assets, largely common trust funds, currently with State Street to another service provider. We expect to remain a significant service provider to this client. The transition will principally occur in 2018 and represents approximately $1 trillion in assets with respect to which we will no longer derive revenue post-transition.

Trading Services

TABLE 13: TRADING SERVICES REVENUE

(Dollar in millions)	Quarters Ended September 30, 2017	2016	% Change
Foreign exchange trading:			
Direct sales and trading	$84	$94	(11)%
Indirect foreign exchange trading	66	65	2
Total foreign exchange trading	150	159	(6)
Brokerage and other trading services:			
Electronic foreign exchange services	39	41	(5)
Other trading, transition management and brokerage	50	48	4
Total brokerage and other trading services	89	89	—
Total trading services revenue	$239	$248	(4)

(Dollars in millions)	Nine Months Ended September 30, 2017	2016	% Change
Foreign exchange trading:			
Direct sales and trading	$282	$271	4 %
Indirect foreign exchange trading	210	201	4
Total foreign exchange trading	492	472	4
Brokerage and other trading services:			
Electronic foreign exchange services	119	128	(7)
Other trading, transition management and brokerage	157	160	(2)
Total brokerage and other trading services	276	288	(4)
Total trading services revenue	$768	$760	1

Trading services revenue is composed of revenue generated by FX trading, as well as revenue generated by brokerage and other trading services as noted in Table 13: Trading Services Revenue.

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Foreign Exchange Trading Revenue

We primarily earn FX trading revenue by acting as a principal market-maker. We offer a range of FX products, services and execution models. Most of our FX products and execution services can be grouped into two broad categories, which are further explained below: “direct sales and trading” and “indirect foreign exchange trading.” Total FX trading revenue decreased 6% and increased 4% in the third quarter and first nine months of 2017, respectively, compared to the same periods in 2016. The decrease in the third quarter of 2017 was primarily due to lower foreign exchange volatility, partially offset by higher client-related volumes. The increase in the first nine months of 2017 was primarily due to higher client-related volumes.

We also offer a range of brokerage and other trading products tailored specifically to meet the needs of the global pension community, including transition management and commission recapture. These products and services are generally offered by us as agent of the institutional investor. Revenue earned from these services is recorded in other trading, transition management and brokerage revenue within brokerage and other trading services revenue.

Our FX trading revenue is influenced by multiple factors, including: the volume and type of client FX transactions and related spreads; currency volatility, reflecting market conditions; and our management of exchange rate, interest rate and other market risks associated with our foreign exchange activities. The relative impact of these factors on our total FX trading revenues often differs from period to period. For example, assuming all other factors remain constant, increases or decreases in volumes or bid-offer spreads across product mix tend to result in increases or decreases, as the case may be, in client-related FX revenue. Revenue earned from direct sales and trading and indirect FX trading is recorded in FX trading revenue.

Total FX trading revenue is comprised of:

- Direct sales and trading: We enter into FX transactions with clients and investment managers that contact our trading desk directly. These trades are all executed at negotiated rates. We refer to this activity, and our principal market-making activities, as “direct sales and trading” and it includes many transactions for funds serviced by third party custodians or prime brokers, as well as those funds under custody at State Street. Direct sales and trading revenue represents all of the FX trading revenue other than the revenue attributed to indirect FX trading. Direct sales and trading revenue represented

56% and 57% of total FX trading revenue in the third quarter and first nine months of 2017, respectively, compared to 59% and 57% for the same periods in 2016.

- Indirect FX trading: Clients or their investment managers may elect to route FX transactions to our FX desk through our asset-servicing operation; we refer to this activity as “indirect FX trading” and, in all cases, we are the funds' custodian. We execute indirect FX trades as a principal at rates disclosed to our clients. Estimated indirect sales and trading revenue represented 44% and 43% of total FX trading revenue in the third quarter and first nine months of 2017, respectively, compared to 41% and 43% for the same periods in 2016. We calculate revenue for indirect FX trading using an attribution methodology. This methodology takes into consideration estimated mark-ups/downs and observed client volumes.

Our clients that utilize indirect FX trading can, in addition to executing their FX transactions through dealers not affiliated with us, transition from indirect FX trading to either direct sales and trading execution, including our “Street FX” service, or to one of our electronic trading platforms. Street FX, in which we continue to act as a principal market-maker, enables our clients to define their FX execution strategy and automate the FX trade execution process, both for funds under custody with us as well as those under custody at another bank.

We continue to expect that some clients may choose, over time, to reduce their level of indirect FX trading transactions in favor of other execution methods, including either direct sales and trading transactions or electronic FX services which we provide. To the extent that clients shift to other execution methods that we provide, our FX trading revenue may decrease, even if volumes remain constant.

Total brokerage and other trading services revenue was flat in the third quarter of 2017 and decreased 4% in the first nine months of 2017 compared to the same periods in 2016, primarily due to lower foreign exchange volatility compared to 2016, as well as the absence of revenue associated with the WM/ Reuters business, which we disposed of in the second quarter of 2016. Total brokerage and other trading services revenue comprises:

- Electronic FX services: Our clients may choose to execute FX transactions through one of our electronic trading platforms. These transactions generate revenue through a “click” fee.

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- Other trading, transition management and brokerage revenue: As our clients look to State Street to enhance and preserve portfolio values, they may choose to utilize our Transition or Currency Management capabilities or transact with our Equity Trade execution group. These transactions generate revenue via commissions charged for trades transacted during the management of these portfolios.

In recent years, our transition management revenue was adversely affected by compliance issues in our U.K. business during 2010 and 2011, including settlements with the FCA in 2014 and the DOJ in 2017, the latter including a deferred prosecution agreement. The reputational and regulatory impact of those compliance issues continues and may adversely affect our results in future periods.

Securities Finance

Our securities finance business consists of three components:

(1) an agency lending program for SSGA-managed investment funds with a broad range of investment objectives, which we refer to as the SSGA lending funds;

(2) an agency lending program for third-party investment managers and asset owners, which we refer to as the agency lending funds; and

(3) security lending transactions which we enter into as principal, which we refer to as our enhanced custody business.

Securities finance revenue earned from our agency lending activities, which is composed of our split of both the spreads related to cash collateral and the fees related to non-cash collateral, is principally a function of the volume of securities on loan, the interest-rate spreads and fees earned on the underlying collateral, and our share of the fee split.

As principal, our enhanced custody business borrows securities from the lending client and then lends such securities to the subsequent borrower, either a State Street client or a broker/dealer. We act as principal when the lending client is unable to, or elects not to, transact directly with the market and execute the transaction and furnish the securities. In our role as principal, we provide support to the transaction through our credit rating. While we source a significant proportion of the securities furnished by us in our role as principal from third parties, we have the ability to source securities through our assets under custody and administration from clients who have designated State Street as an eligible borrower.

Securities finance revenue as presented in Table 9: Investment Servicing Line of Business Results, increased 8% in both the third quarter and first nine months of 2017 compared to the same periods in 2016, primarily the result of higher revenue in our enhanced custody business.

Market influences may continue to affect client demand for securities finance, and as a result our revenue from, and the profitability of, our securities lending activities in future periods. In addition, the constantly evolving regulatory environment, including revised or proposed capital and liquidity standards, and interpretations of those standards, may influence modifications to the way in which we deliver our agency lending or enhanced custody businesses, the volume of our securities lending activity and related revenue and profitability in future periods.

Processing Fees and Other

Processing fees and other revenue includes diverse types of fees and revenue, including fees from our structured products business, fees from software licensing and maintenance, equity income from our joint venture investments, gains and losses on sales of other assets, derivative financial instruments to support our clients' needs and to manage our interest-rate and currency risk, and amortization of our tax-advantaged investments.

Processing fees and other revenue, presented in Table 9: Investment Servicing Line of Business Results, increased 442% and 24% in the third quarter and first nine months of 2017, respectively, compared to the same periods in 2016. The increase in the third quarter of 2017 compared to the third quarter of 2016 is primarily due to a pre-tax gain of approximately $26 million on the sale of an equity trading platform business in the third quarter of 2017. The increase in the first nine months of 2017 is primarily due to a pre-tax gain of $30 million on the dispositions of our joint venture interests in IFDS U.K. and BFDS in the first quarter of 2017 and the aforementioned sale of an equity trading platform business in the third quarter of 2017, partially offset by a pre-tax gain of approximately $53 million related to the sale of WM/Reuters in 2016.

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Expenses

Total expenses for Investment Servicing increased 2% in the third quarter of 2017 compared to the same period in 2016, primarily reflecting installation of new business, annual merit and performance related incentive compensation expenses and the impact of the weaker U.S. dollar.

Total expenses increased 3% in the first nine months of 2017 compared to the same period in 2016, primarily due to higher annual merit and performance based incentive compensation increases, including higher seasonal deferred incentive compensation expense for retirement

eligible employees and payroll taxes of approximately $28 million in the first quarter of 2017 compared to the first quarter of 2016, and increased costs to support new business.

The increases for both the three- and nine-month periods were partially offset by Beacon savings.

Additional information about expenses is provided under "Expenses" in this Management's Discussion and Analysis in this Form 10-Q.

Investment Management

TABLE 14: INVESTMENT MANAGEMENT LINE OF BUSINESS RESULTS

	Quarters Ended September 30,			Nine Months Ended September 30,		
(Dollars in millions)	2017	2016	% Change	2017	2016	% Change
Management fees	$419	$368	14 %	$1,198	$931	29 %
Trading services[1]	20	19	5	55	46	20
Processing fees and other	1	(7)	nm	6	(9)	nm
Total fee revenue	440	380	16	1,259	968	30
Net interest income	(3)	1	nm	(3)	3	nm
Total revenue	437	381	15	1,256	971	29
Total expenses	314	317	(1)	954	817	17
Income before income tax expense	$123	$64	92	$302	$154	96
Pre-tax margin	28 %	17 %		24 %	16 %	

[1] Includes revenues associated with the SPDR® Gold ETF and SPDR® Long Dollar Gold Trust ETF, for which we act as the marketing agent.

nm Not meaningful

Management Fees

Through SSGA, we provide a broad range of investment management strategies, specialized investment management advisory services, OCIO and other financial services for corporations, public funds, and other sophisticated investors. SSGA offers an array of investment management strategies, including passive and active, such as enhanced indexing, using quantitative and fundamental methods for both U.S. and global equity and fixed income securities. SSGA also offers ETFs, such as the SPDR® ETF brand. While certain management fees are directly determined by the values of AUM and the investment strategies employed, management fees reflect other factors as well, including our relationship pricing for clients who use multiple services, and the benchmarks specified in the respective management agreements related to performance fees.

Management fees increased 14% in the third quarter of 2017 compared to the same period in 2016, primarily due to higher global equity markets, net new business and positive ETF flows, partially offset by institutional net outflows.

Management fees increased 29% in the first nine months of 2017 compared to the same period in 2016, primarily due to the acquired GEAM operations, higher global equity markets and higher revenue yielding ETF inflows. Management fees generated outside the U.S. were approximately 28% of total management fees in both the third quarter and first nine months of 2017, compared to 29% and 33% in the same periods in 2016, respectively. The percentage of management fees generated outside the U.S. for the first nine months of 2017 decreased from the same period in 2016 primarily due to the acquired GEAM operations.

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TABLE 15: ASSETS UNDER MANAGEMENT BY ASSET CLASS AND INVESTMENT APPROACH

(In billions)	September 30, 2017	December 31, 2016	September 30, 2016
Equity:			
Active	$ 95	$ 73	$ 70
Passive	1,545	1,401	1,340
Total Equity	1,640	1,474	1,410
Fixed-Income:			
Active	73	70	73
Passive	326	308	318
Total Fixed-Income	399	378	391
Cash[(1)]	347	333	351
Multi-Asset-Class Solutions:			
Active	18	19	19
Passive	116	107	106
Total Multi-Asset-Class Solutions	134	126	125
Alternative Investments[(2)]:			
Active	24	28	29
Passive	129	129	140
Total Alternative Investments	153	157	169
Total	$ 2,673	$ 2,468	$ 2,446

(1) Includes both floating- and constant-net-asset-value portfolios held in commingled structures or separate accounts.
(2) Includes real estate investment trusts, currency and commodities, including SPDR® Gold ETF and SPDR® Long Dollar Gold Trust ETF. State Street is not the investment manager for the SPDR® Gold ETF and SPDR® Long Dollar Gold Trust ETF, but acts as the marketing agent.

TABLE 16: EXCHANGE - TRADED FUNDS BY ASSET CLASS[(1)]

(In billions)	September 30, 2017	December 31, 2016	September 30, 2016
Alternative Investments[(2)]	$ 48	$ 42	$ 54
Cash	2	2	2
Equity	478	426	370
Fixed-income	61	51	52
Total Exchange-Traded Funds	$ 589	$ 521	$ 478

(1) ETFs are a component of AUM presented in the preceding table.
(2) Includes real estate investment trusts, currency and commodities, including SPDR® Gold ETF and SPDR® Long Dollar Gold Trust ETF. State Street is not the investment manager for the SPDR® Gold ETF and SPDR® Long Dollar Gold Trust ETF, but acts as the marketing agent.

TABLE 17: GEOGRAPHIC MIX OF ASSETS UNDER MANAGEMENT[(1)]

(In billions)	September 30, 2017	December 31, 2016	September 30, 2016
North America	$ 1,845	$ 1,691	$ 1,641
Europe/Middle East/Africa	510	482	495

Asia/Pacific	318	295	310
Total	$ 2,673	$ 2,468	$ 2,446

(1) Geographic mix is based on client location or fund management location.

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TABLE 18: ACTIVITY IN ASSETS UNDER MANAGEMENT BY PRODUCT CATEGORY

(In billions)	Equity	Fixed-Income	Cash[1]	Multi-Asset-Class Solutions	Alternative Investments[2]	Total
Balance as of December 31, 2015	$1,326	$ 312	$ 368	$ 103	$ 136	$2,245
Long-term institutional inflows[3]	161	62	—	34	9	266
Long-term institutional outflows[3]	(206)	(71)	—	(26)	(16)	(319)
Long-term institutional flows, net	(45)	(9)	—	8	(7)	(53)
ETF flows, net	(3)	7	(1)	—	13	16
Cash fund flows, net	—		(21)	—	—	(21)
Total flows, net	(48)	(2)	(22)	8	6	(58)
Market appreciation	84	19	1	11	15	130
Foreign exchange impact	10	6	—	—	1	17
Total market/foreign exchange impact	94	25	1	11	16	147
Acquisitions and transfers[4]	38	56	4	3	11	112
Balance as of September 30, 2016	$1,410	$ 391	$ 351	$ 125	$ 169	$2,446
Balance as of December 31, 2016	$1,474	$ 378	$ 333	$ 126	$ 157	$2,468
Long-term institutional inflows[3]	182	65	—	30	16	293
Long-term institutional outflows[3]	(242)	(73)	—	(33)	(32)	(380)
Long-term institutional flows, net	(60)	(8)	—	(3)	(16)	(87)
ETF flows, net	(1)	8	—	—	3	10
Cash fund flows, net	—	—	13	—	—	13
Total flows, net	(61)	—	13	(3)	(13)	(64)
Market appreciation	203	12	(2)	6	4	223
Foreign exchange impact	24	9	3	5	5	46
Total market/foreign exchange impact	227	21	1	11	9	269
Balance as of September 30, 2017	$1,640	$ 399	$ 347	$ 134	$ 153	$2,673

[1] Includes both floating- and constant-net-asset-value portfolios held in commingled structures or separate accounts.
[2] Includes real estate investment trusts, currency and commodities, including SPDR® Gold ETF and SPDR® Long Dollar Gold Trust ETF. State Street is not the investment manager for the SPDR® Gold ETF and SPDR® Long Dollar Gold Trust ETF, but acts as the marketing agent.
[3] Amounts represent long-term portfolios, excluding ETFs.
[4] Includes AUM acquired as part of the acquisition of GEAM on July 1, 2016.

The preceding table does not include approximately $29 billion of new asset management business which was awarded but not installed as of September 30, 2017. New business will be reflected in AUM in future periods after installation, and will generate management fee revenue in subsequent periods. Total AUM as of September 30, 2017 included managed assets lost but not liquidated. Lost business occurs from time to time and it is difficult to predict the timing of client behavior in transitioning these assets. This timing can vary significantly.

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Expenses

Total expenses for Investment Management remained flat in the third quarter of 2017 compared to the same period in 2016.

Total expenses for Investment Management increased 17% in the first nine months of 2017 compared to the same period in 2016 primarily due to higher annual merit and performance based incentive compensation increases, including higher seasonal deferred incentive compensation expense for retirement eligible employees and payroll taxes in the first quarter of 2017 compared to the first quarter of 2016 and increased costs to support new business. These increases were partially offset by Beacon savings.

Additional information about expenses is provided under "Expenses" in “Consolidated Results of Operations” in this Management's Discussion and Analysis in this Form 10-Q.

FINANCIAL CONDITION

The structure of our consolidated statement of condition is primarily driven by the liabilities generated by our Investment Servicing and Investment Management lines of business. Our clients' needs and our operating objectives determine balance sheet volume, mix, and currency denomination. As our clients execute their worldwide cash management and investment activities, they utilize deposits and short-term investments that constitute the majority of our liabilities. These liabilities are generally in the form of interest-bearing transaction account deposits, which are denominated in a variety of currencies; non-interest-bearing demand deposits; and repurchase agreements, which generally serve as short-term investment alternatives for our clients.

Deposits and other liabilities resulting from client initiated transactions are invested in assets that generally have contractual maturities significantly longer than our liabilities; however, we evaluate the operational nature of our deposits and seek to maintain appropriate short-term liquidity of those liabilities that are not operational in nature and maintain longer-termed assets for our operational deposits. Our assets consist primarily of securities held in our AFS or HTM portfolios and short-duration financial instruments, such as interest-bearing deposits with banks and securities purchased under resale agreements. The actual mix of assets is determined by the characteristics of the client liabilities and our desire to maintain a well-diversified portfolio of high-quality assets.

TABLE 19: AVERAGE STATEMENT OF CONDITION[(1)]

	Nine Months Ended September 30,	
	2017	2016
(In millions)	Average Balance	Average Balance
Assets:		
Interest-bearing deposits with banks	$49,171	$52,423
Securities purchased under resale agreements	2,192	2,610
Trading account assets	949	908
Investment securities	95,716	101,243
Loans and leases	21,360	18,674
Other interest-earning assets	22,952	22,316
Average total interest-earning assets	192,340	198,174
Cash and due from banks	3,181	3,402
Other non-interest-earning assets	24,973	27,052
Average total assets	$220,494	$228,628
Liabilities and shareholders’ equity:		
Interest-bearing deposits:		
U.S.	$25,821	$30,388

Non-U.S.	96,860	95,013
Total interest-bearing deposits	122,681	125,401
Securities sold under repurchase agreements	3,965	4,107
Federal funds purchased	1	33
Other short-term borrowings	1,313	1,727
Long-term debt	11,569	11,306
Other interest-bearing liabilities	4,881	5,550
Average total interest-bearing liabilities	144,410	148,124
Non-interest-bearing deposits	42,043	43,806
Other non-interest-bearing liabilities	12,130	14,697
Preferred shareholders’ equity	3,197	3,015
Common shareholders’ equity	18,714	18,986
Average total liabilities and shareholders’ equity	$220,494	$228,628

(1) Additional information about our average statement of condition, primarily our interest-earning assets and interest-bearing liabilities, is provided in "Net Interest Income" in this Management's Discussion and Analysis included in this Form 10-Q.

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Investment Securities
TABLE 20: CARRYING VALUES OF INVESTMENT SECURITIES

(In millions)	September 30, 2017	December 31, 2016
Available-for-sale:		
U.S. Treasury and federal agencies:		
Direct obligations	$ 620	$ 4,263
Mortgage-backed securities	11,000	13,257
Asset-backed securities:		
Student loans[1]	4,826	5,596
Credit cards	1,548	1,351
Sub-prime	—	272
Other	1,221	905
Total asset-backed securities	7,595	8,124
Non-U.S. debt securities:		
Mortgage-backed securities	7,074	6,535
Asset-backed securities	2,839	2,516
Government securities	6,658	5,836
Other	5,818	5,613
Total non-U.S. debt securities	22,389	20,500
State and political subdivisions	9,738	10,322
Collateralized mortgage obligations	1,528	2,593
Other U.S. debt securities	2,928	2,469
U.S. equity securities	46	42
Non-U.S. equity securities	—	3
U.S. money-market mutual funds	394	409
Non-U.S. money-market mutual funds	—	16
Total	$ 56,238	$ 61,998
Held-to-maturity[2]:		
U.S. Treasury and federal agencies:		
Direct obligations	$ 17,456	$ 17,527
Mortgage-backed securities	12,375	10,334
Asset-backed securities:		
Student loans[1]	3,116	2,883
Credit cards	798	897
Other	1	35
Total asset-backed securities	3,915	3,815
Non-U.S. debt securities:		
Mortgage-backed securities	1,000	1,150
Asset-backed securities	325	531
Government securities	483	286
Other	47	113
Total non-U.S. debt securities	1,855	2,080
Collateralized mortgage obligations	1,249	1,413
Total	$ 36,850	$ 35,169

(1) Primarily composed of securities guaranteed by the federal government with respect to at least 97% of defaulted principal and accrued interest on the underlying loans.
(2) Includes securities at amortized cost or fair value on the date of transfer from AFS.
Additional information about our investment securities portfolio is provided in Note 3 to the consolidated financial statements included in this Form 10-Q.

We manage our investment securities portfolio to align with the interest-rate and duration characteristics of our client liabilities that we consider to be operational deposits and in the context of the overall structure of our consolidated statement of condition, in consideration of the global interest-rate environment. We consider a well-diversified, high-credit quality investment securities portfolio to be an important element in the management of our consolidated statement of condition.
In the first quarter of 2017, we sold $2.7 billion of AFS, primarily Agency MBS and U.S. Treasury securities in our investment portfolio, in response to the current interest rate environment resulting in a pre-tax loss of $40 million.
Approximately 91% of the carrying value of the portfolio was rated "AAA" or "AA" as of September 30, 2017 and December 31, 2016.

TABLE 21: INVESTMENT PORTFOLIO BY EXTERNAL CREDIT RATING

	September 30, 2017		December 31, 2016	
AAA(1)	76	%	78	%
AA	15		13	
A	5		5	
BBB	3		3	
Below BBB	1		1	
	100	%	100	%

(1) Includes U.S. Treasury and federal agency securities that are split-rated, "AAA" by Moody's Investors Service and "AA+" by Standard & Poor's.
As of September 30, 2017, the investment portfolio of 10,703 securities was diversified with respect to asset class. Approximately 53% of the aggregate carrying value of the portfolio as of September 30, 2017 was composed of MBS and ABS, compared to 52% as of December 31, 2016. The ABS portfolio, of which approximately 96% and 93% of the carrying value as of September 30, 2017 and December 31, 2016, respectively, was floating-rate, consisted primarily of student loan-backed and credit card-backed securities. MBS were composed of securities issued by FNMA and FHLMC, as well as U.S. and non-U.S. large-issuer collateralized mortgage obligations.

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Non-U.S. Debt Securities
Approximately 26% of the aggregate carrying value of our investment securities portfolio was non-U.S. debt securities as of September 30, 2017, compared to approximately 23% as of December 31, 2016.
TABLE 22: NON-U.S. DEBT SECURITIES

(In millions)	September 30, 2017	December 31, 2016
Available-for-sale:		
United Kingdom	$ 5,320	$ 5,093
Australia	4,461	4,272
Canada	3,749	2,989
France	1,658	1,013
Netherlands	1,338	1,283
Japan	1,020	1,388
Italy	999	676
Belgium	774	360
Hong Kong	633	664
Germany	488	713
Sweden	479	188
Spain	424	266
Norway	419	508
South Korea	201	634
Finland	124	223
Other[1]	302	230
Total	$ 22,389	$ 20,500
Held-to-maturity:		
United Kingdom	$ 452	$ 504
Netherlands	390	473
Singapore	364	180
Australia	250	374
Germany	171	329
Spain	104	98
Other[2]	124	122
Total	$ 1,855	$ 2,080

[1] Included approximately $182 million and $164 million as of September 30, 2017 and December 31, 2016, respectively, related to Ireland, Austria and Portugal, all of which were related to MBS and auto loans.
[2] Included approximately $76 million and $80 million as of September 30, 2017 and December 31, 2016, respectively, related to Italy, Portugal and Norway all of which were related to MBS and auto loans.
Approximately 88% of the aggregate carrying value of these non-U.S. debt securities was rated "AAA" or "AA" as of both September 30, 2017 and December 31, 2016. The majority of these securities comprised senior positions within the security structures; these positions have a level of protection provided through subordination and other forms of credit protection. As of September 30, 2017 and December 31, 2016, approximately 65% of the aggregate carrying value of these non-U.S. debt securities was floating-rate, and accordingly, we consider these securities to have minimal interest-rate risk.

As of September 30, 2017, our non-U.S. debt securities had an average market-to-book ratio of 100.6%, and an aggregate pre-tax net unrealized gain of approximately $146 million, composed of gross unrealized gains of $176

million and gross unrealized losses of $30 million. These unrealized amounts included a pre-tax net unrealized gain of $66 million, composed of gross unrealized gains of $89 million and gross unrealized losses of $23 million, associated with non-U.S. debt securities available-for-sale.
As of September 30, 2017, the underlying collateral for non-U.S. MBS and ABS primarily included Australian, Dutch, Italian and U.K. prime mortgages and German auto loans. The securities listed under “Canada” were composed of Canadian government securities and corporate debt and covered bonds. The securities listed under “France” were composed of auto loans, prime mortgages, and corporate debt and covered bonds. The securities listed under “Japan” were substantially composed of Japanese government securities and corporate debt.
Municipal Obligations
We carried approximately $9.74 billion of municipal securities classified as state and political subdivisions in our investment securities portfolio as of September 30, 2017 as shown in Table 20: Carrying Values of Investment Securities, all of which were classified as AFS. As of the same date, we also provided approximately $9.52 billion of credit and liquidity facilities to municipal issuers.
TABLE 23: STATE AND MUNICIPAL OBLIGORS[1]

(Dollars in millions)	Total Municipal Securities	Credit and Liquidity Facilities[2]	Total	% of Total Municipal Exposure	
As of September 30, 2017					
State of Issuer:					
Texas	$ 1,774	$ 1,764	$3,538	18	%
California	461	2,266	2,727	14	
New York	743	1,288	2,031	11	
Massachusetts	891	992	1,883	10	
Washington	682	327	1,009	5	
Total	$ 4,551	$ 6,637	$11,188		
As of December 31, 2016					
State of Issuer:					
Texas	$ 1,781	$ 1,685	$3,466	18	%
California	523	2,298	2,821	14	
New York	740	1,293	2,033	10	
Massachusetts	916	1,071	1,987	10	
Washington	708	234	942	5	
Maryland	488	411	899	5	
Total	$ 5,156	$ 6,992	$12,148		

[1] Represented 5% or more of our aggregate municipal credit exposure of approximately $19.26 billion and $19.57 billion across our businesses as of September 30, 2017 and December 31, 2016, respectively.
[2] Includes municipal loans which are also presented within Table 25.

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Our aggregate municipal securities exposure presented in Table 23: State and Municipal Obligors, was concentrated primarily with highly-rated counterparties, with approximately 92% of the obligors rated “AAA” or “AA” as of September 30, 2017. As of that date, approximately 49% and 50% of our aggregate municipal securities exposure was associated with general obligation and revenue bonds, respectively. The portfolios are also diversified geographically, with the states that represent our largest exposures widely dispersed across the U.S.

Impairment

Impairment exists when the fair value of an individual security is below its amortized cost basis. Impairment of a security is further assessed to determine whether such impairment is other-than-temporary. When the impairment is deemed to be other-than-temporary, we record the loss in our consolidated statement of income. In addition, for AFS and HTM debt securities, we record impairment in our consolidated statement of income when management intends to sell (or may be required to sell) the securities before they recover in value, or when management expects the present value of cash flows expected to be collected from the securities to be less than the amortized cost of the impaired security (a credit loss).

The change in the net unrealized gain/(loss) position as of September 30, 2017 compared to December 31, 2016, presented in Table 24: Amortized Cost, Fair Value and Net Unrealized Gains (Losses) of Investment Securities, was primarily attributable to higher interest rates.

TABLE 24: AMORTIZED COST, FAIR VALUE AND NET UNREALIZED GAINS (LOSSES) OF INVESTMENT SECURITIES

	September 30, 2017		
(In millions)	Amortized Cost	Net Unrealized Gains (Losses)	Fair Value
Available-for-sale[1]	$55,882	$ 356	$56,238
Held-to-maturity[2]	36,850	(14)	36,836
Total investment securities	$92,732	$ 342	$93,074
Net after-tax unrealized gain (loss)		$ 205	

	December 31, 2016		
(In millions)	Amortized Cost	Net Unrealized Gains (Losses)	Fair Value
Available-for-sale[1]	$62,056	$ (58)	$61,998
Held-to-maturity[2]	35,169	(175)	34,994
Total investment securities	$97,225	$ (233)	$96,992
Net after-tax unrealized gain (loss)		$ (140)	

(1) AFS securities are carried at fair value, with after-tax net unrealized gains and losses recorded in AOCI.
(2) HTM securities are carried at amortized cost, and unrealized gains and losses are not recorded in our consolidated financial statements, other than for those that have been impaired.

We conduct periodic reviews of individual securities to assess whether OTTI exists. Our assessment of OTTI involves an evaluation of economic and security-specific factors. Such factors are based on estimates, derived by management, which contemplate current market conditions and security-specific performance. To the extent that market conditions are worse than management's expectations or due to idiosyncratic bond performance, OTTI could increase, in

particular the credit-related component that would be recorded in our consolidated statement of income.
We recorded less than $1 million of OTTI in the third quarter of 2017 and $2 million in the third quarter of 2016. Management considers the aggregate decline in fair value of the remaining investment securities and the resulting gross unrealized losses of $434 million as of September 30, 2017 to be temporary and not the result of any material changes in the credit characteristics of the securities. Additional information with respect to OTTI, net impairment losses and gross unrealized losses is provided in Note 3 to the consolidated financial statements included in this Form 10-Q.
Our evaluation of potential OTTI of structured credit securities with collateral in the U.K. and Italy takes into account the outcome from the Brexit referendum and the Italian constitutional referendum, and assumes no disruption of payments on these securities.

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Loans and Leases

TABLE 25: U.S. AND NON- U.S. LOANS AND LEASES

(In millions)	September 30, 2017	December 31, 2016
Domestic:		
Commercial and financial	$ 18,273	$ 16,412
Commercial real estate	—	27
Lease financing	283	338
Total domestic	18,556	16,777
Non-U.S.:		
Commercial and financial	4,652	2,476
Lease financing	430	504
Total non-U.S.	5,082	2,980
Total loans and leases	$ 23,638	$ 19,757

The increase in loans in the commercial and financial segment as of September 30, 2017 compared to December 31, 2016 was primarily driven by higher levels of loans to investment funds and loans to municipalities.

As of September 30, 2017 and December 31, 2016, our investment in senior secured loans totaled approximately $3.9 billion and $3.5 billion, respectively. In addition, we had binding unfunded commitments as of September 30, 2017 and December 31, 2016 of $332 million and $76 million, respectively, to participate in such syndications.

These senior secured loans, which are primarily rated “speculative” under our internal risk-rating framework, are externally rated “BBB,” “BB” or “B,” with approximately 90% of the loans rated “BB” or “B” as of September 30, 2017 and December 31, 2016. Information about our internal risk-rating framework is provided in Note 4 to the consolidated financial statements included in this Form 10-Q. Our investment strategy involves generally limiting our investment to larger, more liquid credits underwritten by major global financial institutions, applying our internal credit analysis process to each potential investment, and diversifying our exposure by counterparty and industry segment. However, these loans have significant exposure to credit losses relative to higher-rated loans.

Loans to municipalities included in the commercial and financial segment were $2.0 billion and $1.4 billion as of September 30, 2017 and December 31, 2016, respectively.

As of September 30, 2017 and December 31, 2016, unearned income deducted from our investment in leveraged lease financing was $77 million and $94 million, respectively, for U.S. leases and $161 million and $192 million, respectively, for non-U.S. leases.

Additional information about all of our loan-and-leases segments, as well as underlying classes, is

provided in Note 4 to the consolidated financial statements included in this Form 10-Q.

No loans were modified in troubled debt restructurings during the nine months ended September 30, 2017 and the year ended December 31, 2016.

TABLE 26: ALLOWANCE FOR LOAN AND LEASE LOSSES

(In millions)	Nine Months Ended September 30, 2017	2016
Allowance for loan and lease losses:		
Beginning balance	$ 53	$ 46

Provision for loan and lease losses[1]	4	8
Charge-offs[2]	—	(3)
Ending balance	$ 57	$ 51

[1] The provision for loan and lease losses is related to commercial and financial loans in the quarters ended September 30, 2017 and 2016.
[2] The charge-offs are related to commercial and financial loans.

As of September 30, 2017, approximately $49 million of our allowance for loan and lease losses were related to senior secured loans included in the commercial and financial segment. As this portfolio grows and matures, our allowance for loan and lease losses related to these loans may increase through additional provisions for credit losses. The remaining $9 million was related to other components of commercial and financial loans.

Cross-Border Outstandings

Cross-border outstandings are amounts payable to us by non-U.S. counterparties which are denominated in U.S. dollars or other non-local currency, as well as non-U.S. local currency claims not funded by local currency liabilities. Our cross-border outstandings consist primarily of deposits with banks; loans and lease financing, including short-duration advances; investment securities; amounts related to foreign exchange and interest-rate contracts; and securities finance. In addition to credit risk, cross-border outstandings have the risk that, as a result of political or economic conditions in a country, borrowers may be unable to meet their contractual repayment obligations of principal and/or interest when due because of the unavailability of, or restrictions on, foreign exchange needed by borrowers to repay their obligations.

As market and economic conditions change, the major independent credit rating agencies may downgrade U.S. and non-U.S. financial institutions and sovereign issuers which have been, and may in the future be, significant counterparties to us, or whose financial instruments serve as collateral on which we rely for credit risk mitigation purposes, and may do so again in the future. As a result, we may be exposed to increased counterparty risk, leading to negative ratings volatility.

The cross-border outstandings presented in Table 27: Cross-Border Outstandings, represented approximately 30% and 28% of our consolidated total assets as of September 30, 2017 and December 31, 2016, respectively.

TABLE 27: CROSS-BORDER OUTSTANDINGS[1]

(In millions)	Investment Securities and Other Assets	Derivatives and Securities on Loan	Total Cross-Border Outstandings
September 30, 2017			
United Kingdom	$ 17,808	$ 1,225	$ 19,033
Germany	18,727	267	18,994
Japan	15,607	674	16,281
Australia	5,344	631	5,975
Canada	4,334	1,060	5,394
France	2,273	300	2,573
Switzerland	2,023	457	2,480
December 31, 2016			
United Kingdom	$ 18,712	$ 1,761	$ 20,473
Japan	17,922	1,171	19,093
Germany	13,812	484	14,296
Australia	5,122	986	6,108
Luxembourg	3,389	762	4,151
Canada	3,179	781	3,960

[1] Cross-border outstandings included countries in which we do business, and which amounted to at least 1% of our consolidated total assets as of the dates indicated.

As of September 30, 2017, aggregate cross-border outstandings in countries which amounted to between 0.75% and 1% of our consolidated assets totaled approximately $2.15 billion to Netherlands. As of December 31, 2016, aggregate cross-border outstandings in countries which amounted to between 0.75% and 1% of our consolidated assets totaled approximately $1.84 billion and $2.38 billion to France and the Netherlands, respectively.

Risk Management

In the normal course of our global business activities, we are exposed to a variety of risks, some inherent in the financial services industry, others more specific to our business activities. Our risk management framework focuses on material risks, which include the following:

- credit and counterparty risk;
- liquidity risk, funding and management;
- operational risk;
- information technology risk;
- market risk associated with our trading activities;
- market risk associated with our non-trading activities, which we refer to as asset-and-liability management, and which consists primarily of interest-rate risk;
- strategic risk;
- model risk; and
- reputational, fiduciary and business conduct risk.

Many of these risks, as well as certain of the factors underlying each of these risks that could affect our businesses and our consolidated financial statements, are discussed in detail included under Item 1A, Risk Factors, in our 2016 Form

10-K.

For additional information about our risk management, including our risk appetite framework and risk governance committee structure, refer to pages 80 to 85 included under Item 7, Management's Discussion and Analysis of Financial Condition and Results of Operations, in our 2016 Form 10-K.

Credit Risk Management

We define credit risk as the risk of financial loss if a counterparty, borrower or obligor, collectively referred to as a counterparty, is either unable or unwilling to repay borrowings or settle a transaction in accordance with underlying contractual terms. We assume credit risk in our traditional non-trading lending activities, such as loans and contingent commitments, in our investment securities portfolio, where recourse to a counterparty exists, and in our direct and indirect trading activities, such as principal securities lending and foreign exchange and indemnified agency securities lending. We also assume credit risk in our day-to-day treasury and securities and other settlement operations, in the form of deposit placements and other cash balances, with central banks or private sector institutions.

For additional information about our credit risk management, including our core policies and principles, structure and organization, credit ratings, risk parameter estimates, credit risk mitigation, credit limits, reporting, monitoring, controls and reserve for credit losses, refer to pages 85 to 90 included under Item 7, Management's Discussion and Analysis of Financial Condition and Results of Operations, in our 2016 Form 10-K.

Liquidity Risk Management

Our liquidity framework contemplates areas of potential risk based on our activities, size, and other appropriate risk-related factors. In managing liquidity risk we employ limits, maintain established metrics and early warning indicators, and perform routine stress testing to identify potential liquidity needs. This process involves the evaluation of a combination of internal and external scenarios which assist us in measuring our liquidity position and in identifying potential increases in cash needs or decreases in available sources of cash, as well as the potential impairment of our ability to access the global capital markets.

We manage our liquidity on a global, consolidated basis. We also manage liquidity on a stand-alone basis at the Parent Company, as well as at certain branches and subsidiaries of State Street Bank. State Street Bank generally has access to markets and funding sources limited to banks, such as the federal funds market and the Federal Reserve's discount window. Our Parent Company is managed to a more conservative liquidity profile, reflecting narrower market access. Our Parent Company typically holds, or has direct access to, primarily through SSIF and the support agreement, as discussed in the "Uses of Liquidity" section of this Management's Discussion and Analysis, enough cash to meet its current debt maturities and cash needs, as well as those projected over the next one-year period. As of September 30, 2017, the value of our Parent Company's net liquid assets decreased to $0.57 billion from $3.64 billion as of December 31, 2016. The decrease was due to the funding of SSIF in connection with our SPOE Strategy as discussed in the "Uses of Liquidity" section of this Management's Discussion and Analysis. Absent certain triggers reflecting financial distress at the Parent Company, the liquidity transferred to SSIF continues to be available to the Parent Company. As of September 30, 2017, our Parent Company and State Street Bank had approximately $1 billion of senior notes and junior subordinated debentures outstanding that will mature in the next twelve months.

As a systemically important financial institution, our liquidity risk management activities are subject to heightened and evolving regulatory requirements, including interpretations of those requirements, under specific U.S. and international regulations and also resulting from published and unpublished guidance, supervisory activities, such as stress tests, resolution planning, examinations and other regulatory interactions. Satisfaction of these requirements could, in some cases, result in changes in the composition of our investment portfolio, reduced NII or NIM, a reduction in the level of certain business activities or modifications to the way in which we deliver our products and services. If we fail to meet regulatory requirements to the satisfaction of our regulators, we could receive negative regulatory stress test results, incur a resolution plan deficiency or determination of a non-credible resolution plan or otherwise receive an adverse regulatory finding. Our efforts to satisfy, or our failure to satisfy, these regulatory requirements could materially adversely affect our business, financial condition or results of operations.

For additional information on our liquidity risk management, as well as liquidity risk metrics, refer to page 91 included under Item 7, Management's

Discussion and Analysis of Financial Condition and Results of Operation, in our 2016 Form 10-K. For additional information on our liquidity ratios, including LCR and NSFR, refer to pages 7 and 8 included under Item 1, Business, in our 2016 Form 10-K.

Asset Liquidity

Central to the management of our liquidity is asset liquidity, which consists primarily of unencumbered highly liquid securities, cash and cash equivalents reported on our consolidated statement of condition. We restrict the eligibility of securities to be characterized as asset liquidity to U.S. Government and federal agency securities (including MBS), selected non-U.S. Government and supranational securities as well as certain other high-quality securities which generally are more liquid than other types of assets even in times of stress. In 2014, U.S. banking regulators issued a final rule to implement the BCBS' LCR in the United States. The LCR is intended to promote the short-term resilience of internationally active banking organizations, like State Street, to improve the banking industry's ability to absorb shocks arising from market stress over a 30 calendar day period and improve the measurement and management of liquidity risk. The LCR measures an institution’s HQLA against its net cash outflows. The LCR was fully implemented beginning on January 1, 2017. We report LCR to the Federal Reserve daily. In addition, in December 2016, the Federal Reserve issued a final rule requiring large banking organizations, including us, to publicly disclose certain qualitative and quantitative information about their LCR. We were required to comply with the disclosure requirements beginning on April 1, 2017. As of September 30, 2017 and December 31, 2016, our LCR was in excess of 100%. With the release of the new disclosure requirements, we are now presenting average quarterly HQLA balances versus our historical presentation of the period end balances. The average HQLA for our Parent Company under the LCR final rule was $67.23 billion and $87.20 billion, post-prescribed haircuts, as of September 30, 2017 and December 31, 2016, respectively.

TABLE 28: COMPONENTS OF AVERAGE HQLA BY TYPE OF ASSET

(In millions)	Quarters Ended September 30, 2017	December 31, 2016
Excess central bank balances	$38,222	$ 48,407
U.S. Treasuries	10,804	17,770
Other investment securities	11,796	15,442
Foreign government	6,409	5,585
Total	$67,231	$ 87,204

With respect to highly liquid short-term investments presented in the preceding table, we maintained cash balances in excess of regulatory requirements governing deposits with the Federal Reserve of approximately $38.22 billion at the Federal Reserve, the ECB and other non-U.S. central banks, compared to $48.41 billion as of December 31, 2016. The lower levels of deposits with central banks as of quarter-end September 30, 2017 compared to quarter-end December 31, 2016 was due to normal deposit volatility. The decrease in other investment securities as of September 30, 2017 compared to December 31, 2016, presented in the table above, was primarily associated with repositioning the investment portfolio in light of the liquidity requirements of the LCR.

Liquid securities carried in our asset liquidity include securities pledged without corresponding advances from the FRBB, the FHLB, and other non-U.S. central banks. State Street Bank is a member of the FHLB. This membership allows for advances of liquidity in varying terms against high-quality collateral, which helps facilitate asset-and-liability management.

Access to primary, intra-day and contingent liquidity provided by these utilities is an important source of contingent liquidity with utilization subject to underlying conditions. As of September 30, 2017 and December 31, 2016, we had no outstanding primary credit borrowings from the FRBB discount window or any other central bank facility, and as of the same dates, no FHLB advances were outstanding.

In addition to the securities included in our asset liquidity, we have significant amounts of other unencumbered investment securities. The aggregate fair value of those securities was $38.05 billion as of September 30, 2017, compared to $54.40 billion as of December 31, 2016. These securities are available sources of liquidity, although not as rapidly deployed as those included in our asset liquidity.

Uses of Liquidity

Significant uses of our liquidity could result from the following: withdrawals of client deposits; draw-downs by our custody clients of lines of credit; advances to clients to settle securities transactions; or other permitted purposes. Such circumstances would generally arise under stress conditions including deterioration in credit ratings. A recurring significant use of our liquidity involves our deployment of HQLA from our investment portfolio to post collateral to financial institutions serving as sources of securities under our enhanced custody program.

We had unfunded commitments to extend credit with gross contractual amounts totaling $27.01 billion and $26.99 billion as of September 30, 2017 and December 31, 2016, respectively. These amounts do not reflect the value of any collateral. As of September 30, 2017, approximately 73% of our

unfunded commitments to extend credit expire within one year. Since many of our commitments are expected to expire or renew without being drawn upon, the gross contractual amounts do not necessarily represent our future cash requirements.

Resolution Planning

State Street, like other bank holding companies with total consolidated assets of $50 billion or more, periodically submits a plan for rapid and orderly resolution in the event of material financial distress or failure-commonly referred to as a resolution plan or a living will-to the Federal Reserve and the FDIC under Section 165(d) of the Dodd-Frank Act. Through resolution planning, we seek, in the event of the insolvency of State Street, to maintain State Street Bank's role as a key infrastructure provider within the financial system, while minimizing risk to the financial system and maximizing value for the benefit of our stakeholders. We have and will continue to focus management attention and resources to meet regulatory expectations with respect to resolution planning.

We submitted our 2017 resolution plan describing our preferred resolution strategy to the Federal Reserve and FDIC on June 30, 2017. Subsequently, the Federal Reserve and FDIC extended the next resolution plan filing deadline for eight large domestic banks, including State Street, to July 1, 2019. The agencies' review of the 2017 resolution plans is on-going and the extension does not affect any actions the agencies may take concerning our resolution plan.

In the event of material financial distress or failure, our preferred resolution strategy is the SPOE Strategy. For additional information about the SPOE Strategy, refer to pages 11 and 12 included under Item 1, Business, in our 2016 Form 10-K. The SPOE Strategy provides that prior to the bankruptcy of the Parent Company and pursuant to a support agreement among the Parent Company, SSIF (a recently formed direct subsidiary of the Parent Company), State Street's Beneficiary Entities (as defined below) and certain other State Street entities, SSIF is obligated, up to its available resources, to recapitalize and/or provide liquidity to State Street Bank and the other State Street entities benefiting from such capital and/or liquidity (collectively with State Street Bank, "Beneficiary Entities"), in amounts designed to prevent the Beneficiary Entities from themselves entering into resolution proceedings. Following the recapitalization of, or provision of liquidity to the Beneficiary Entities, the Parent Company would enter into a bankruptcy proceeding under the U.S. Bankruptcy Code. The Beneficiary Entities and other State Street subsidiaries would be transferred to a newly organized holding company held by a reorganization trust for the benefit of the Parent Company’s claimants.

Under the support agreement, the Parent Company has pre-funded SSIF by contributing certain of its assets (primarily its liquid assets, cash deposits, debt investments, investments in marketable securities and other cash and non-cash equivalent investments) to SSIF contemporaneous with entering into the support agreement and will continue to contribute such assets, to the extent available, on an on-going basis. In consideration for these contributions, SSIF has agreed in the support agreement to provide capital and liquidity support to the Parent Company and all of the Beneficiary Entities in accordance with the Parent Company’s capital and liquidity policies. Under the support agreement, the Parent Company is only permitted to retain certain amounts of cash needed to meet its upcoming obligations and to fund expenses during a potential bankruptcy proceeding. SSIF has provided the Parent Company with a committed credit line and issued (and may issue) one or more promissory notes to the Parent Company (the "Parent Company Funding Notes") that together are intended to allow State Street to continue to meet its obligations throughout the period prior to the occurrence of a "Recapitalization Event" (as defined below). The support agreement does not contemplate that SSIF is obligated to maintain any specific level of resources and SSIF may not have sufficient resources to implement the SPOE Strategy.

In the event a Recapitalization Event occurs, the obligations outstanding under the Parent Company Funding Notes would automatically convert into or be exchanged for capital contributed to SSIF. The obligations of the Parent Company and SSIF under the support agreement are secured through a security agreement that grants a lien on the assets that the Parent Company and SSIF would use to fulfill their obligations under the support agreement to the Beneficiary Entities. SSIF is a distinct legal entity separate from the Parent Company and the Parent Company’s other affiliates.

In accordance with its policies, State Street is required to monitor, on an ongoing basis, the capital and liquidity needs of State Street Bank and the other Beneficiary Entities. To support this process, State Street has established a trigger framework that identifies key actions that would need to be taken or decisions that would need to be made if certain events tied to State Street’s financial condition occur. In the event that State Street experiences material financial distress, the support agreement requires State Street to model and calculate certain capital and liquidity triggers on a regular basis to determine whether or not the Parent Company should

commence preparations for a bankruptcy filing and whether or not a Recapitalization Event has occurred.

Upon the occurrence of a Recapitalization Event: (1) SSIF would not be authorized to provide any further liquidity to the Parent Company; (2) the Parent Company would be required to contribute to SSIF any remaining assets it is required to contribute to SSIF under the support agreement; (3) the Parent Company would be expected to commence Chapter 11 proceedings under the U.S. Bankruptcy Code; and (4) SSIF would be required to provide capital and liquidity support to the Beneficiary Entities to support such entities’ continued operation. No person or entity, other than a party to the support agreement, should rely, including in evaluating any State Street entity from a creditor's perspective or determining whether to enter into a contractual relationship with any State Street entity, on any State Street affiliate being or remaining a Beneficiary Entity or receiving capital or liquidity support pursuant to the support agreement.

A “Recapitalization Event” is defined under the support agreement as the earlier occurrence of one or more capital and liquidity thresholds being breached or the authorization by the Parent Company's Board of Directors for the Parent Company to commence bankruptcy proceedings. These thresholds are set at levels intended to provide for the availability of sufficient capital and liquidity to enable an orderly resolution without extraordinary government support. The SPOE Strategy and the obligations under the support agreement may result in the recapitalization of State Street Bank and the commencement of bankruptcy proceedings by the Parent Company at an earlier stage of financial stress than might otherwise occur without such mechanisms in place. An expected effect of the SPOE Strategy and applicable TLAC regulatory requirements is that State Street’s losses will be imposed on the Parent Company shareholders and the holders of long-term debt and other forms of TLAC securities currently outstanding or issued in the future by the Parent Company, as well as on any other Parent Company creditors, before any of its losses

are imposed on the holders of the debt securities of the Parent Company's operating subsidiaries or any of their depositors or creditors, or before U.S. taxpayers are put at risk.
There can be no assurance that credit rating agencies, in response to our 2017 resolution plan or the support agreement, will not downgrade, place on negative watch or change their outlook on our debt credit ratings, generally or on specific debt securities. Any such downgrade, placement on negative watch or change in outlook could adversely affect our cost of borrowing, limit our access to the capital markets or result in restrictive covenants in future debt

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agreements and could also adversely impact the trading prices, or the liquidity, of our outstanding debt securities. State Street Bank is also required to submit annually to the FDIC a plan for resolution in the event of its failure, referred to as an IDI plan. The FDIC has extended the date for the next IDI plan submission to July 1, 2018. This IDI plan will satisfy the annual plan submission requirements under the IDI Rule for 2016, 2017 and 2018.

Funding

Deposits

We provide products and services including custody, accounting, administration, daily pricing, foreign exchange services, cash management, financial asset management, securities finance and investment advisory services. As a provider of these products and services, we generate client deposits, which have generally provided a stable, low-cost source of funds. As a global custodian, clients place deposits with State Street entities in various currencies. As of September 30, 2017 and December 31, 2016, approximately 60% of our average client deposit balances were denominated in U.S. dollars.

For the past several years, we have frequently experienced higher client deposit inflows toward the end of each fiscal quarter or the end of the fiscal year. As a result, we believe average client deposit balances are more reflective of ongoing funding than period-end balances.

TABLE 29: TOTAL DEPOSITS

	September 30,		Average Balance Nine Months Ended September 30,	
(In millions)	2017	2016	2017	2016
Client deposits	$176,263	$183,900	$159,564	$153,612
Wholesale CDs	3,000	14,865	5,160	15,595
Total deposits	$179,263	$198,765	$164,724	$169,207

Short-Term Funding

Our on-balance sheet liquid assets are also an integral component of our liquidity management strategy. These assets provide liquidity through maturities of the assets, but more importantly, they provide us with the ability to raise funds by pledging the securities as collateral for borrowings or through outright sales. In addition, our access to the global capital markets gives us the ability to source incremental funding at reasonable rates of interest from wholesale investors. As discussed earlier under "Asset Liquidity," State Street Bank's membership in the FHLB allows for advances of liquidity with varying terms against high-quality collateral.

Short-term secured funding also comes in the form of securities lent or sold under agreements to repurchase. These transactions are short-term in nature, generally overnight, and are collateralized by high-quality investment securities. These balances were $3.86 billion and $4.40 billion as of September 30, 2017 and December 31, 2016, respectively.

State Street Bank currently maintains a line of credit with a financial institution of CAD 1.40 billion, or approximately $1.12 billion as of September 30, 2017, to support its Canadian securities processing operations. The line of credit has no stated termination date and is cancelable by either party with prior notice. As of September 30, 2017, there was no balance outstanding on this line of credit.

Long-Term Funding

State Street Corporation maintains an effective universal shelf registration statement that allows for the public offering and sale of debt securities, capital securities, common stock, depositary shares and preferred stock, and warrants to purchase such securities, including any shares into which the preferred stock and depositary shares may be convertible, or any combination thereof. We have issued in the past, and we may issue in the future, securities pursuant to our shelf registration statement. The issuance of debt or equity securities will depend on future market conditions, funding needs and other factors.

As of September 30, 2017, State Street Bank had Board authority to issue unsecured senior debt securities from time to time, provided that the aggregate principal amount of such unsecured senior debt outstanding at any one time does not exceed $5 billion. As of September 30, 2017, $3.25 billion was available for issuance pursuant to this authority. As of September 30, 2017, State Street Bank also had Board authority to issue an additional $500 million of subordinated debt.

Agency Credit Ratings

Our ability to maintain consistent access to liquidity is fostered by the maintenance of high investment-grade ratings as measured by the major independent credit rating agencies. Factors essential to maintaining high credit ratings include:

- diverse and stable core earnings;
- relative market position;
- strong risk management;
- strong capital ratios;
- diverse liquidity sources, including the global capital markets and client deposits;
- strong liquidity monitoring procedures; and

- preparedness for current or future regulatory developments.

High ratings limit borrowing costs and enhance our liquidity by:

- providing assurance for unsecured funding and depositors;
- increasing the potential market for our debt and improving our ability to offer products;
- serving markets; and
- engaging in transactions in which clients value high credit ratings.

A downgrade or reduction of our credit ratings could have a material adverse effect on our liquidity by restricting our ability to access the capital markets, which could increase the related cost of funds. In turn, this could cause the sudden and large-scale withdrawal of unsecured deposits by our clients, which could lead to draw-downs of unfunded commitments to extend credit or trigger requirements under securities purchase commitments; or require additional collateral or force terminations of certain trading derivative contracts.

A majority of our derivative contracts have been entered into under bilateral agreements with counterparties who may require us to post collateral or terminate the transactions based on changes in our credit ratings. We assess the impact of these arrangements by determining the collateral that would be required assuming a downgrade by all rating agencies. The additional collateral or termination payments related to our net derivative liabilities under these arrangements that could have been called by counterparties in the event of a downgrade in our credit ratings below levels specified in the agreements is disclosed in Note 7 to the consolidated financial statements included in this Form 10-Q. Other funding sources, such as secured financing transactions and other margin requirements, for which there are no explicit triggers, could also be adversely affected.

Operational Risk Management

Operational risk is the risk of loss resulting from inadequate or failed internal processes, people and systems or from external events. Operational risk encompasses fiduciary risk and legal risk. Fiduciary risk is defined as the risk that State Street fails to properly exercise its fiduciary duties in its provision of products or services to clients. Legal risk is the risk of loss resulting from failure to comply with laws and contractual obligations as well as prudent ethical standards in business practices in addition to exposure to litigation from all aspects of State Street's activities.

For additional information about our operational risk framework, refer to pages 95 to 98 included under Item 7, Management's Discussion and Analysis of Financial Condition and Results of Operations, in our 2016 Form 10-K.

Market Risk Management

Market risk is defined by U.S. banking regulators as the risk of loss that could result from broad market movements, such as changes in the general level of interest rates, credit spreads, foreign exchange rates or commodity prices. We are exposed to market risk in both our trading and certain of our non-trading, or asset-and-liability management, activities.

Information about the market risk associated with our trading activities is provided below under "Trading Activities." Information about the market risk associated with our non-trading activities, which consists primarily of interest-rate risk, is provided below under "Asset-and-Liability Management Activities."

Trading Activities

In the conduct of our trading activities, we assume market risk, the level of which is a function of our overall risk appetite, business objectives and liquidity needs, our clients' requirements and market volatility, and our execution against those factors.

For additional information about the market risk associated with our trading activities, refer to pages 98 to 99 included under Item 7, Management's Discussion and Analysis of Financial Condition and Results of Operations, in our 2016 Form 10-K.

As part of our trading activities, we assume positions in the foreign exchange and interest-rate markets by buying and selling cash instruments and entering into derivative instruments, including foreign exchange forward contracts, foreign exchange and interest-rate options and interest-rate swaps, interest-rate forward contracts, and interest-rate futures. As of September 30, 2017, the notional amount of these derivative contracts was $1.67 trillion, of which $1.65 trillion was composed of foreign exchange forward, swap and spot contracts. We seek to match positions closely with the objective of minimizing related currency and interest-rate risk. All foreign exchange contracts are valued daily at current market rates.

Value-at-Risk, Stress Testing and Stressed VaR

We use a variety of risk measurement tools and methodologies, including VaR, which is an estimate of potential loss for a given period within a stated statistical confidence interval. We use a risk measurement methodology to measure trading-related VaR daily. We have adopted standards for measuring trading-related VaR, and we maintain regulatory capital for market risk associated with our trading activities in conformity with currently applicable bank regulatory market risk requirements.

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For additional information about our VaR measurement tools and methodologies, refer to pages 101 to 104 included under Item 7, Management's Discussion and Analysis of Financial Condition and Results of Operations, in our 2016 Form 10-K.

Stress Testing and Stressed VaR

We have a corporate-wide stress testing program in place that incorporates an array of techniques to measure the potential loss we could suffer in a hypothetical scenario of adverse economic and financial conditions. We also monitor concentrations of risk such as concentration by branch, risk component, and currency pairs. We conduct stress testing on a daily basis based on selected historical stress events that are relevant to our positions in order to estimate the potential impact to our current portfolio should similar market conditions recur, and we also perform stress testing as part of the Federal Reserve's CCAR process. Stress testing is conducted, analyzed and reported at the corporate, trading desk, division and risk-factor level (for example, exchange risk, interest-rate risk and volatility risk).

We calculate a stressed VaR-based measure using the same model we use to calculate VaR, but with model inputs calibrated to historical data from a range of continuous twelve-month periods that reflect significant financial stress. The stressed VaR model identifies the second-worst outcome occurring in the worst continuous one-year rolling period since July 2007. This stressed VaR meets the regulatory requirement as the rolling ten-day period with an outcome that is worse than 99% of other outcomes during that twelve-month period of financial stress. For each portfolio, the stress period is determined algorithmically by seeking the one-year time horizon that produces the largest ten-business-day VaR from within the available historical data. This historical data set includes the financial crisis of 2008, the highly volatile period surrounding the Eurozone

sovereign debt crisis and the Standard & Poor's downgrade of U.S. Treasury debt in August 2011. As the historical data set used to determine the stress period expands over time, future market stress events will be automatically incorporated.

Stress testing results and limits are actively monitored on a daily basis by ERM and reported to the TMRC. Limit breaches are addressed by ERM risk managers in conjunction with the business units, escalated as appropriate, and reviewed by the TMRC if material. In addition, we have established several action triggers that prompt immediate review by management and the implementation of a remediation plan.

Validation and Back-Testing

We perform frequent back-testing to assess the accuracy of our VaR-based model in estimating loss at the stated confidence level. This back-testing involves the comparison of estimated VaR model outputs to daily, actual profit-and-loss outcomes, or P&L, observed from daily market movements. We back-test our VaR model using “clean” P&L, which excludes non-trading revenue such as fees, commissions and NII, as well as estimated revenue from intra-day trading.

Our VaR definition of trading losses excludes items that are not specific to the price movement of the trading assets and liabilities themselves, such as fees, commissions, changes to reserves and gains or losses from intra-day activity. We had no back-testing exceptions in the quarters ended September 30, 2017 and June 30, 2017.

The following tables present VaR and stressed VaR associated with our trading activities for covered positions held during the quarters ended September 30, 2017 and June 30, 2017, and as of September 30, 2017 and June 30, 2017, as measured by our VaR methodology:

TABLE 30: TEN-DAY VaR ASSOCIATED WITH TRADING ACTIVITIES FOR COVERED POSITIONS

	Quarter Ended September 30, 2017			Quarter Ended June 30, 2017			As of September 30, 2017	As of June 30, 2017
(In thousands)	Average	Maximum	Minimum	Average	Maximum	Minimum	VaR	VaR
Global Markets	$7,592	$ 13,703	$ 3,295	$7,759	$ 16,160	$ 4,590	$ 9,524	$7,577

Global Treasury	342	790	145	433	1,408	89	723	528
Total VaR	$7,546	$ 13,652	$ 3,337	$7,740	$ 16,119	$ 4,598	$ 9,463	$7,481

TABLE 31: TEN-DAY STRESSED VaR ASSOCIATED WITH TRADING ACTIVITIES FOR COVERED POSITIONS

	Quarter Ended September 30, 2017			Quarter Ended June 30, 2017			As of September 30, 2017	As of June 30, 2017
(In thousands)	Average	Maximum	Minimum	Average	Maximum	Minimum	Stressed VaR	Stressed VaR
Global Markets	$23,981	$ 45,399	$ 13,363	$26,691	$ 44,875	$ 14,301	$ 24,755	$15,192
Global Treasury	5,309	10,549	2,584	4,814	12,329	1,321	5,150	6,223
Total Stressed VaR	$24,382	$ 44,364	$ 13,887	$26,934	$ 43,754	$ 14,646	$ 24,362	$14,943

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The three month average of our stressed VaR-based measure was approximately $24 million for the quarter ended September 30, 2017, compared to an average of approximately $27 million for the quarter ended June 30, 2017.
The decrease in the total stressed VaR-based measures as of September 30, 2017, compared to June 30, 2017, was mainly driven by lower interest rate risk in emerging market currencies as of September 30, 2017 as compared to June 30, 2017.
The VaR-based measures presented in the preceding tables are primarily a reflection of the overall level of market volatility and our appetite for taking market risk in our trading activities. Overall

levels of volatility have been low both on an absolute basis and relative to the historical information observed at the beginning of the period used for the calculations. Both the ten-day VaR-based measures and the stressed VaR-based measures are based on historical changes observed during rolling ten-day periods for the portfolios as of the close of business each day over the past one-year period.
We may in the future modify and adjust our models and methodologies used to calculate VaR and stressed VaR, subject to regulatory review and approval, and these modifications and adjustments may result in changes in our VaR-based and stressed VaR-based measures.
The following tables present the VaR and stressed-VaR associated with our trading activities attributable to foreign exchange risk, interest-rate risk and volatility risk as of September 30, 2017 and June 30, 2017. The totals of the VaR-based and stressed VaR-based measures for the three attributes in total exceeded the related total VaR and total stressed VaR presented in the foregoing tables as of each period-end, primarily due to the benefits of diversification across risk types.

TABLE 32: TEN-DAY VaR ASSOCIATED WITH TRADING ACTIVITIES BY RISK FACTOR[1]

	As of September 30, 2017			As of June 30, 2017		
(In thousands)	Foreign Exchange Risk	Interest Rate Risk	Volatility Risk	Foreign Exchange Risk	Interest Rate Risk	Volatility Risk
By component:						
Global Markets	$7,876	$2,930	$ 201	$6,167	$3,042	$ 506
Global Treasury	62	736	—	59	552	—
Total VaR	$7,883	$2,564	$ 201	$6,186	$3,035	$ 506

TABLE 33: TEN-DAY STRESSED VaR ASSOCIATED WITH TRADING ACTIVITIES BY RISK FACTOR[1]

	As of September 30, 2017			As of June 30, 2017		
(In thousands)	Foreign Exchange Risk	Interest Rate Risk	Volatility Risk	Foreign Exchange Risk	Interest Rate Risk	Volatility Risk
By component:						
Global Markets	$16,864	$20,608	$ 214	$10,514	$13,782	$ 520
Global Treasury	98	5,273	—	104	6,439	—
Total Stressed VaR	$16,862	$21,940	$ 214	$10,570	$15,036	$ 520

[1] For purposes of risk attribution by component, foreign exchange refers only to the risk from market movements in period-end rates. Forwards, futures, options and swaps with maturities greater than period-end have embedded interest-rate risk that is captured by the measures used for interest-rate risk. Accordingly, the interest-rate risk embedded in these foreign exchange instruments is included in the interest-rate risk component.

Asset-and-Liability Management Activities

The primary objective of asset-and-liability management is to provide sustainable NII under varying economic conditions, while protecting the economic value of the assets and liabilities carried in our consolidated statement of condition from the adverse effects of changes in interest rates. While many market factors affect the level of NII and the economic value of our assets and liabilities, one of the most significant factors is our exposure to movements in interest rates. Most of our NII is earned from the investment of client deposits generated by our businesses. We invest these client deposits in assets that conform generally to the characteristics of our balance sheet liabilities, including the currency composition of our significant non-U.S. dollar denominated client liabilities.

We quantify NII sensitivity using an earnings simulation model that includes our expectations for new business growth, changes in balance sheet mix and investment portfolio positioning. This measure compares our baseline view of NII over a twelve-month horizon, based on our internal forecast of interest rates, to a wide range of instantaneous and gradual rate shocks. Economic value of equity sensitivity is a discounted cash flow model designed to estimate the fair value of assets and liabilities under a series of interest rate shocks over a long-term horizon. Each approach is routinely monitored as market conditions change and within internally-approved risk limits and guidelines.
For additional information about our Asset-and-Liability Management Activities, refer to pages 104 to 105 included under Item 7, Management's Discussion

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and Analysis of Financial Condition and Results of Operations, in our 2016 Form 10-K.

In the table below, we report the expected change in NII over the next twelve months from +/-100 bps instantaneous and gradual parallel rate shocks. Each scenario assumes no management action is taken to mitigate the adverse effects of interest rate changes on our financial performance. While investment securities balances can fluctuate with the level of rates as prepayment assumptions change, our deposit balances remain consistent with the baseline.

We also routinely measure NII sensitivity to non-parallel rate shocks to isolate the impact of short-term or long-term market rates. In the up 100 bps instantaneous shock, approximately 80% of the expected benefit stems from the short-end of the yield curve. Additionally, we quantify how much of the change is a result of shifts in U.S. and non-U.S. rates. In the up 100 bps instantaneous shock, approximately 50% of the expected benefit is driven by U.S. rates.

TABLE 34: NII SENSITIVITY

(In millions)	September 30, 2017	December 31, 2016
Rate change:	Benefit (Exposure)	
+100 bps shock	$ 515	$ 585
–100 bps shock	(352)	(265)
+100 bps ramp	198	284
–100 bps ramp	(119)	(161)

As of September 30, 2017, NII sensitivity remains positioned to benefit from rising interest rates. Compared to December 31, 2016, the decreased benefit to the up 100 bps instantaneous shock is driven by a mix shift in client deposits and the repricing characteristics of other wholesale liabilities, partially offset by investment portfolio activity. The increased exposure to the down 100 bps instantaneous shock is driven by higher observed short-term interest rates relative to year-end and investment portfolio activity, partially offset by a mix shift in client deposits. Gradual rate shocks have a similar asset sensitive positioning, but are less impactful due to the severity and timing of the rate shift.

The following table highlights our economic value of equity sensitivity to a +/-200 bps instantaneous rate shock, relative to spot interest rates. Management compares the change in EVE sensitivity against State Street's aggregate tier 1 and tier 2 risk-based capital, calculated in conformity with current applicable regulatory requirements. Economic value of equity sensitivity is dependent on the timing of interest and principal cash flows. Also, the measure only evaluates the spot balance sheet and does not include the impact of new business assumptions.

TABLE 35: EVE SENSITIVITY

(In millions)	September 30, 2017	December 31, 2016
Rate change:	Benefit (Exposure)	
+200 bps shock	$ (924)	$ (1,092)
–200 bps shock	118	877

As of September 30, 2017, economic value of equity sensitivity remains exposed to upward shifts in interest rates. The change in each scenario was primarily driven by investment portfolio repositioning and the mix of client deposits. The -200 bps scenario is also impacted by the low level of interest rates, which limits the size of the rate shock.

Model Risk Management

The use of quantitative models is widespread throughout the financial services industry, with large and complex organizations relying on sophisticated models to support numerous aspects of their financial decision making. The models contemporaneously represent both a significant advancement in financial management and a new source of risk. In large banking organizations like State Street, model results influence business decisions, and model failure could have a harmful effect on our financial performance. As a result, the Model Risk Management Framework seeks to mitigate model risk at State Street.

For additional information about our model risk management, including our governance and model validation, refer to pages 105 to 106 included under Item 7, Management's Discussion and Analysis of Financial Condition and Results of Operations, in our 2016 Form 10-K.

Capital

Managing our capital involves evaluating whether our actual and projected levels of capital are commensurate with our risk profile, are in compliance with all applicable regulatory requirements, and are sufficient to provide us with the financial flexibility to undertake future strategic business initiatives. We assess capital adequacy based on relevant regulatory capital requirements, as well as our own internal capital goals, targets and other relevant metrics.

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We have a hierarchical structure supporting appropriate committee review of relevant risk and capital information. The ongoing responsibility for capital management rests with our Treasurer. The Capital Management group within Global Treasury is responsible for the Capital Policy and guidelines, capital forecasting, development of the Capital Plan, the management of global capital, capital optimization and net investment hedging. The Capital Management group is also responsible for enterprise stress testing, including stress revenue and expense modeling and information technology related matters associated with stress testing models.

MRAC provides oversight of our capital management, our capital adequacy, our internal targets and the expectations of the major independent credit rating agencies. In addition, MRAC approves our balance sheet strategy and related activities. The Board’s RC assists the Board in fulfilling its oversight responsibilities related to the assessment and management of risk and capital. Our Capital Policy is reviewed and approved at least annually by the Board's RC.

For additional information about our capital, refer to pages 107 to 117 included under Item 7, Management's Discussion and Analysis of Financial Condition and Results of Operations, in our 2016 Form 10-K.

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Global Systemically Important Bank

We are one among a group of 30 institutions worldwide that have been identified by the FSB and the BCBS as G-SIBs. Our designation as a G-SIB requires us to maintain an additional capital buffer above the Basel III final rule minimum CET1 capital ratio of 4.5%, based on a number of factors, as evaluated by banking regulators.

In addition to the U.S. Basel III final rule, the Dodd-Frank Act requires the Federal Reserve to establish more stringent capital requirements for large bank holding companies, including State Street. On August 14, 2015, the Federal Reserve published a final rule on the implementation of capital requirements that impose a capital surcharge on U.S. G-SIBs. The surcharge requirements within the final rule began to phase-in on January 1, 2016 and will be fully effective on January 1, 2019. The eight U.S. banks deemed to be G-SIBs, including State Street, are required to calculate the G-SIB surcharge according to two methods, and be bound by the higher of the two:

- Method 1: Assesses systemic importance based upon twelve indicators across: size, interconnectedness, complexity, cross-jurisdictional activity and substitutability
- Method 2: Alters the calculation from Method 1 by factoring in a wholesale funding score in place of substitutability and applying a coefficient to the nine systemic indicators across size, interconnectedness, complexity and cross jurisdictional activity

As part of the final rule, the Federal Reserve published estimated G-SIB surcharges for the eight U.S. G-SIBs based on relevant data from 2012 to 2014. Method 2 is identified as the binding methodology for State Street and the applicable surcharge on January 1, 2017 was calculated to be 1.5%. Assuming a countercyclical buffer of 0%, a capital conservation buffer of 2.5%, and a G-SIB surcharge of 1.5% in 2019, the minimum fully phased-in capital ratios State Street would be required to have as of January 1, 2019 are: 8.5% for CET1 Capital, 10.0% for tier 1 risk-based capital and 12.0% for total risk-based capital, in order to make capital distributions and discretionary bonus payments without limitation.

Not all of our competitors have similarly been designated as systemically important, and therefore some of our competitors may not be subject to the same additional capital requirements.

Total Loss Absorbing Capacity

On December 15, 2016, the Federal Reserve released its final rule on TLAC, LTD and clean holding company requirements for U.S. domiciled G-SIBs, such as State Street, that are intended to improve the resiliency and resolvability of certain U.S. banking organizations through new enhanced prudential standards. The TLAC final rule imposes: (1) TLAC requirements (i.e., combined eligible tier 1 regulatory capital and eligible LTD); (2) separate eligible LTD requirements; and (3) clean holding company requirements designed to make short-term unsecured debt (including deposits) and most other ineligible liabilities structurally senior to eligible LTD.

Among other things, the TLAC final rule requires State Street to comply with minimum requirements for external TLAC and external LTD, plus an external TLAC buffer. Specifically, State Street must hold (1) combined eligible tier 1 regulatory capital and eligible LTD in the amount equal to at least 21.5% of total risk-weighted assets (using an estimated G-SIB method 1 surcharge of 1%) and 9.5% (7.5% SLR plus eSLR buffer of 2%) of total leverage exposure, as defined by the SLR final rule, and (2) qualifying external LTD equal to the greater of 7.5% of risk-weighted assets (using an estimated G-SIB method 2 surcharge of 1.5%) and 4.5% of total leverage exposure, as defined by the SLR final rule.

In forecasting our compliance with these requirements, we presently include our junior subordinated debentures maturing in 2028 and 2047 as TLAC and LTD eligible debt. Based upon current estimates, assumptions and guidance, we project that compliance with TLAC and LTD will result in increasing our outstanding long-term debt by approximately $2 billion at December 31, 2018 compared to the TLAC eligible debt outstanding at September 30, 2017.

For additional information on our TLAC requirements, refer to page 7 under "Regulatory Capital Adequacy and Liquidity Standards" in "Total Loss-Absorbing Capacity (TLAC)" included under Item 1, Business, in our 2016 Form 10-K

State Street must comply with the TLAC final rule starting on January 1, 2019.

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Regulatory Capital

We and State Street Bank, as advanced approaches banking organizations, are subject to the current Basel III minimum risk-based capital and leverage ratio guidelines. The Basel III final rule incorporates several multi-year transition provisions for capital components and minimum ratio requirements for CET1 capital, tier 1 capital and total capital. The transition period started in January 2014 and will be completed by January 1, 2019, which is concurrent with the full implementation of the Basel III final rule in the U.S.

Among other things, the Basel III final rule introduced a minimum CET1 risk-based capital ratio of 4.5% and raises the minimum tier 1 risk-based capital ratio from 4% to 6%. In addition, for advanced approaches banking organizations such as State Street, the Basel III final rule imposes a minimum supplementary tier 1 leverage ratio of 3%, the numerator of which is tier 1 capital and the denominator of which includes both on-balance sheet assets and certain off-balance sheet exposures.

The Basel III final rule also introduced a capital conservation buffer and a countercyclical capital buffer that add to the minimum risk-based capital ratios. Specifically, the final rule limits a banking organization’s ability to make capital distributions and discretionary bonus payments to executive officers if it fails to maintain a common equity tier 1 capital conservation buffer of more than 2.5% of total risk-weighted assets and, if deployed during periods of excessive credit growth, a common equity tier 1 countercyclical capital buffer of up to 2.5% of total risk-weighted assets, above each of the minimum common equity tier 1, and tier 1 and total risk-based capital ratios. The countercyclical capital buffer is currently set at zero by U.S. banking regulators.

To maintain the status of our Parent Company as a financial holding company, we and our insured depository institution subsidiaries are required to be “well-capitalized” by maintaining capital ratios above the minimum requirements. Effective on January 1, 2015, the “well-capitalized” standard for our banking subsidiaries was revised to reflect the higher capital requirements in the Basel III final rule.

Under the Basel III final rule, certain new items are deducted from CET1 capital and certain regulatory capital deductions were modified as compared to the previously applicable capital regulations. Among other things, the final rule requires significant investments in the common stock of unconsolidated financial institutions, as defined, and certain deferred tax assets that exceed specified individual and aggregate thresholds to be deducted from common equity tier 1 capital. As an advanced approaches banking organization, after-tax unrealized

gains and losses on AFS investment securities flow through to and affect State Street’s and State Street Bank's CET1 capital, subject to a phase-in schedule.

We are required to use the advanced approaches framework as provided in the Basel III final rule to determine our risk-based capital requirements. The Dodd-Frank Act applies a "capital floor" to advanced approaches banking organizations, such as State Street and State Street Bank. We are subject to the more stringent of the risk-based capital ratios calculated under the standardized approach and those calculated under the advanced approaches in the assessment of our capital adequacy under the PCA framework.

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The following table sets forth the transition to full implementation and the minimum risk-based capital ratio requirements under the Basel III final rule. This does not include the potential imposition of an additional countercyclical capital buffer.

TABLE 36: BASEL III FINAL RULES TRANSITION ARRANGEMENTS AND MINIMUM RISK-BASED CAPITAL RATIOS[1]

	2015	2016	2017	2018	2019
Capital conservation buffer (CET1)	— %	0.625 %	1.250 %	1.875 %	2.500 %
G-SIB surcharge (CET1)[2]	—	0.375	0.750	1.125	1.500
Minimum common equity tier 1[3]	4.500	5.500	6.500	7.500	8.500
Minimum tier 1 capital[3]	6.000	7.000	8.000	9.000	10.000
Minimum total capital[3]	8.000	9.000	10.000	11.000	12.000

(1) Minimum ratios shown above do not reflect the countercyclical buffer, currently set at zero by U.S. banking regulators.

(2) As part of the G-SIB Surcharge final rule, the Federal Reserve published estimated G-SIB surcharges for the eight U.S. G-SIBs based on relevant data from 2012-2014 and the estimated resulting G-SIB surcharge for State Street is 1.5%. Including the 1.5% surcharge, State Street's minimum risk-based capital ratio requirements, as of January 1, 2019 would be 8.5% for CET1, 10.0% for tier 1 capital and 12.0% for total capital.

(3) Minimum CET1 capital, minimum tier 1 capital and minimum total capital presented include the transitional capital conservation buffer as well as the estimated transitional G-SIB surcharge being phased-in beginning January 1, 2016 through January 1, 2019 based on an estimated 1.5% surcharge in all periods.

The specific calculation of State Street's and State Street Bank's risk-based capital ratios will change as the provisions of the Basel III final rule related to the numerator (capital) and denominator (risk-weighted assets) are phased in, and as our risk-weighted assets calculated using the advanced approaches change due to potential changes in methodology. These ongoing methodological changes will result in differences in our reported capital ratios from one reporting period to the next that are independent of applicable changes to our capital base, our asset composition, our off-balance sheet exposures or our risk profile.

The following table presents the regulatory capital structure and related regulatory capital ratios for State Street and State Street Bank as of the dates indicated. We are subject to the more stringent of the risk-based capital ratios calculated under the standardized approach and those calculated under the advanced approaches in the assessment of our capital adequacy under applicable bank regulatory standards.

As a result of changes in the methodologies used to calculate our regulatory capital ratios from period to period, as the provisions of the Basel III final rule are phased in, the ratios presented in the table for each period are not directly comparable. Refer to the footnotes following the table.

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TABLE 37: REGULATORY CAPITAL STRUCTURE AND RELATED REGULATORY CAPITAL RATIOS

	State Street				State Street Bank			
(In millions)	Basel III Advanced Approaches September 30, 2017[1]	Basel III Standardized Approach September 30, 2017[2]	Basel III Advanced Approaches December 31, 2016[1]	Basel III Standardized Approach December 31, 2016[2]	Basel III Advanced Approaches September 30, 2017[1]	Basel III Standardized Approach September 30, 2017[2]	Basel III Advanced Approaches December 31, 2016[1]	Basel III Standardized Approach December 31, 2016[2]
Common shareholders' equity:								
Common stock and related surplus	$10,307	$10,307	$10,286	$10,286	$11,382	$11,382	$11,376	$11,376
Retained earnings	18,675	18,675	17,459	17,459	12,286	12,286	12,285	12,285
Accumulated other comprehensive income (loss)	(985)	(985)	(1,936)	(1,936)	(808)	(808)	(1,648)	(1,648)
Treasury stock, at cost	(8,697)	(8,697)	(7,682)	(7,682)	—	—	—	—
Total	19,300	19,300	18,127	18,127	22,860	22,860	22,013	22,013
Regulatory capital adjustments:								
Goodwill and other intangible assets, net of associated deferred tax liabilities[3]	(6,739)	(6,739)	(6,348)	(6,348)	(6,447)	(6,447)	(6,060)	(6,060)
Other adjustments	(122)	(122)	(155)	(155)	(90)	(90)	(148)	(148)
Common equity tier 1 capital	12,439	12,439	11,624	11,624	16,323	16,323	15,805	15,805
Preferred stock	3,196	3,196	3,196	3,196	—	—	—	—
Trust preferred capital securities subject to phase-out from tier 1 capital	—	—	—	—	—	—	—	—
Other adjustments	(29)	(29)	(103)	(103)	—	—	—	—
Tier 1 capital	15,606	15,606	14,717	14,717	16,323	16,323	15,805	15,805
Qualifying subordinated long-term debt	1,072	1,072	1,172	1,172	1,076	1,076	1,179	1,179
Trust preferred capital securities phased out of tier 1 capital	—	—	—	—	—	—	—	—
ALLL and other	5	79	19	77	—	79	15	77
Other adjustments	1	1	1	1	—	—	—	—
Total capital	$16,684	$16,758	$15,909	$15,967	$17,399	$17,478	$16,999	$17,061
Risk-weighted assets:								
Credit risk	$50,197	$106,377	$50,900	$98,125	$47,282	$103,024	$47,383	$94,413
Operational risk[4]	45,795	NA	44,579	NA	45,270	NA	44,043	NA
Market risk[5]	3,005	1,203	3,822	1,751	3,005	1,203	3,822	1,751
	$98,997	$107,580	$99,301	$99,876	$95,557	$104,227	$95,248	$96,164

Capital Ratios[1]:	2017 Minimum Requirements Including Capital Conservation Buffer and G-SIB Surcharge[6]	2016 Minimum Requirements Including Capital Conservation Buffer and G-SIB Surcharge[7]								
Total risk-weighted assets										
Adjusted quarterly average assets			$211,396	$211,396	$226,310	$226,310	$208,308	$208,308	$222,584	$222,584
Common equity tier 1 capital	6.5 %	5.5 %	12.6 %	11.6 %	11.7 %	11.6 %	17.1 %	15.7 %	16.6 %	16.4 %
Tier 1 capital	8.0	7.0	15.8	14.5	14.8	14.7	17.1	15.7	16.6	16.4
Total capital	10.0	9.0	16.9	15.6	16.0	16.0	18.2	16.8	17.8	17.7
Tier 1 leverage	4.0	4.0	7.4	7.4	6.5	6.5	7.8	7.8	7.1	7.1

(1) CET1 capital, tier 1 capital and total capital ratios as of September 30, 2017 and December 31, 2016 were calculated in conformity with the advanced approaches provisions of the Basel III final rule. Tier 1 leverage ratio as of September 30, 2017 and December 31, 2016 were calculated in conformity with the Basel III final rule.

(2) CET1 capital, tier 1 capital and total capital ratios as of September 30, 2017 and December 31, 2016 were calculated in conformity with the standardized approach provisions of the Basel III final rule. Tier 1 leverage ratio as of September 30, 2017 and December 31, 2016 were calculated in conformity with the Basel III final rule.

(3) Amounts for State Street and State Street Bank as of September 30, 2017 consisted of goodwill, net of associated deferred tax liabilities, and 80% of other intangible assets, net of associated deferred tax liabilities. Amounts for State Street and State Street Bank as of December 31, 2016 consisted of goodwill, net of deferred tax liabilities and 60% of other intangible assets, net of associated deferred tax liabilities. Intangible assets, net of associated deferred tax liabilities is phased in as a deduction from capital, in conformity with the Basel III final rule.

(4) Under the current advanced approaches rules and regulatory guidance concerning operational risk models, RWA attributable to operational risk can vary substantially from period-to-period, without direct correlation to the effects of a particular loss event on our results of operations and financial condition and impacting dates and periods that may differ from the dates and periods as of and during which the loss event is reflected in our financial statements, with the timing and categorization dependent on the processes for model updates and, if applicable, model revalidation and regulatory review and related supervisory processes. An individual loss event can have a significant effect on the output of our operational risk RWA under the advanced approaches depending on the severity of the loss event and its categorization among the seven Basel-defined UOMs.

(5) Market risk risk-weighted assets reported in conformity with the Basel III advanced approaches included a CVA which reflected the risk of potential fair value adjustments for credit risk reflected in our valuation of over-the-counter derivative contracts. The CVA was not provided for in the final market risk capital rule; however, it was required by the advanced approaches provisions of the Basel III final rule. We used a simple CVA approach in conformity with the Basel III advanced approaches.

(6) Minimum requirements will be phased in up to full implementation beginning on January 1, 2019; minimum requirements listed are as of September 30, 2017. See Table 36: Basel III Final Rules Transition Arrangements and

Minimum Risk Based Capital Ratios.

(7) Minimum requirements will be phased in up to full implementation beginning on January 1, 2019; minimum requirements listed are as of December 31, 2016. See Table 36: Basel III Final Rules Transition Arrangements and Minimum Risk Based Capital Ratios.

NA Not applicable

MANAGEMENT'S DISCUSSION AND ANALYSIS OF FINANCIAL CONDITION AND RESULTS OF OPERATIONS

As of January 1, 2015, we used the standardized provisions of the Basel III final rule in addition to the advanced approaches provisions which were previously implemented in the second quarter of 2014, and the lower of our regulatory capital ratios calculated under the advanced approaches and those ratios calculated under the standardized approach are applied in the assessment of our capital adequacy for regulatory capital purposes. Beginning in the second quarter of 2014, until January 1, 2015, we used the advanced approaches provisions in the Basel III final rule, and transitional provisions of the Basel III final rule, and the lower of our regulatory capital ratios calculated under the advanced approaches and those ratios calculated under the transitional provisions were applied in the assessment of our capital adequacy for regulatory capital purposes.

Our CET1 capital increased $815 million as of September 30, 2017 compared to December 31, 2016 primarily due to net income of $1.81 billion and an increase in accumulated other comprehensive income of $951 million. The increases in CET1 capital were partially offset by capital distributions of $1.69 billion from common stock purchases and dividends, and the impact from the 2017 phase-in of the deduction of intangibles (80% in 2017 compared to 60% in 2016). In the same comparative period, our tier 1 capital increased $889 million, due to the increase in CET1 capital. Total capital increased $775 million under advanced approaches and increased $791 million under standardized approach due to the changes to tier 1 capital. State Street Bank's tier 1 capital increased $518 million, and total capital increased $400 million and $417 million under the advanced and standardized approaches, respectively, as of September 30, 2017, compared to December 31, 2016. The increase is a result of higher CET1.

The table below presents a roll-forward of CTE1 capital, tier 1 capital and total capital for the quarter ended September 30, 2017 and for the year ended December 31, 2016.

TABLE 38: CAPITAL ROLL-FORWARD

(In millions)	State Street Basel III Advanced Approaches September 30, 2017	Basel III Standardized Approach September 30, 2017	Basel III Advanced Approaches December 31, 2016	Basel III Standardized Approach December 31, 2016
Common equity tier 1 capital:				
Common equity tier 1 capital balance, beginning of period	$11,624	$ 11,624	$ 12,433	$ 12,433
Net income	1,807	1,807	2,143	2,143
Changes in treasury stock, at cost	(1,015)	(1,015)	(1,225)	(1,225)
Dividends declared	(588)	(588)	(732)	(732)
Goodwill and other intangible assets, net of associated deferred tax liabilities	(391)	(391)	(421)	(421)
Effect of certain items in accumulated other comprehensive income (loss)	951	951	(514)	(514)
Other adjustments	51	51	(60)	(60)
Changes in common equity tier 1 capital	815	815	(809)	(809)
Common equity tier 1 capital balance, end of period	12,439	12,439	11,624	11,624
Additional tier 1 capital:				
Tier 1 capital balance, beginning of period	14,717	14,717	15,264	15,264
Change in common equity tier 1 capital	815	815	(809)	(809)
Net issuance of preferred stock	—	—	493	493
Trust preferred capital securities phased out of tier 1 capital	—	—	(237)	(237)
Other adjustments	74	74	6	6
Changes in tier 1 capital	889	889	(547)	(547)
Tier 1 capital balance, end of period	15,606	15,606	14,717	14,717

Tier 2 capital:				
Tier 2 capital balance, beginning of period	1,192	1,250	2,085	2,139
Net issuance and changes in long-term debt qualifying as tier 2	(100)	(100)	(186)	(186)
Trust preferred capital securities phased into tier 2 capital	—	—	(713)	(713)
Changes in ALLL and other	(14)	2	7	11
Change in other adjustments	—	—	(1)	(1)
Changes in tier 2 capital	(114)	(98)	(893)	(889)
Tier 2 capital balance, end of period	1,078	1,152	1,192	1,250
Total capital:				
Total capital balance, beginning of period	15,909	15,967	17,349	17,403
Changes in tier 1 capital	889	889	(547)	(547)
Changes in tier 2 capital	(114)	(98)	(893)	(889)
Total capital balance, end of period	$16,684	$ 16,758	$ 15,909	$ 15,967

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The following table presents a roll-forward of the Basel III advanced approaches risk-weighted assets for the quarter ended September 30, 2017 and for the year ended December 31, 2016.

TABLE 39: ADVANCED APPROACHES RWA ROLL-FORWARD

	State Street	
(In millions)	September 30, 2017	December 31, 2016
Total risk-weighted assets, beginning of period	$99,301	$99,552
Changes in credit risk-weighted assets:		
Net increase (decrease) in investment securities-wholesale	1,477	(1,027)
Net increase (decrease) in loans and leases	1,432	