

NORTHERN TRUST CORP
Form 10-Q
April 28, 2015
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UNITED STATES
SECURITIES AND EXCHANGE COMMISSION
Washington, D.C. 20549

FORM 10-Q

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

For the Quarterly Period Ended March 31, 2015

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. 0-5965

NORTHERN TRUST CORPORATION

(Exact name of registrant as specified in its charter)

Delaware
(State or other jurisdiction of
incorporation or organization)

50 South LaSalle Street

36-2723087
(I.R.S. Employer
Identification No.)

60603

Chicago, Illinois
(Address of principal executive offices) (Zip Code)
Registrant's telephone number, including area code: (312) 630-6000

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

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

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

Large accelerated filer Accelerated filer
Non-accelerated filer (Do not check if a smaller reporting company) Smaller reporting company

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

233,368,512 Shares \$1.66 2/3 Par Value

(Shares of Common Stock Outstanding on March 31, 2015)

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FOR THE QUARTERLY PERIOD ENDED MARCH 31, 2015
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CONSOLIDATED FINANCIAL HIGHLIGHTS

(UNAUDITED)

CONDENSED INCOME STATEMENT (In Millions)	2015	Three Months Ended March 31,	
		2014	% Change (*)
Noninterest Income	\$ 873.9	\$ 794.8	10%
Net Interest Income	260.6	245.7	6
Provision for Credit Losses	(4.5)	3.0	N/M
Noninterest Expense	789.0	768.0	3
Income before Income Taxes	350.0	269.5	30
Provision for Income Taxes	119.3	88.1	36
Net Income	\$ 230.7	\$ 181.4	27%

PER COMMON SHARE

Net Income Basic	\$ 0.95	\$ 0.75	27%
Diluted	0.94	0.75	25
Cash Dividends Declared Per Common Share	0.33	0.31	6
Book Value End of Period (EOP)	35.22	33.61	5
Market Price EOP	69.65	65.56	6

SELECTED BALANCE SHEET DATA (In Millions)

	March 31, 2015	December 31, 2014	% Change (*)
<i>End of Period:</i>			
Assets	\$ 106,952.0	\$ 109,946.5	(3)%
Earning Assets	97,203.9	100,889.8	(4)
Deposits	86,736.5	90,757.0	(4)
Stockholders Equity	8,607.6	8,448.9	2

	2015	Three Months Ended March 31, 2014	% Change (*)
<i>Average Balances:</i>			
Assets	\$ 107,513.2	\$ 100,243.5	7%
Earning Assets	98,693.1	91,840.7	7
Deposits	86,526.1	80,747.8	7
Stockholders Equity	8,472.7	7,926.4	7

Table of Contents**SELECTED RATIOS AND METRICS**

	2015	Three Months Ended March 31, 2014	% Change (*)
<i>Financial Ratios:</i>			
Return on Average Common Equity	11.28%	9.28%	22%
Return on Average Assets	0.87	0.73	19
Dividend Payout Ratio	35.1	41.3	(15)
Net Interest Margin (**)	1.10	1.12	(2)

	March 31, 2015		December 31, 2014	
	Advanced (a) Approach	Standardized (b) Approach	Advanced (a) Approach	Standardized (c) Approach
<i>Capital Ratios:</i>				
Northern Trust Corporation				
Common Equity Tier 1	11.8%	10.5%	12.4%	12.5%
Tier 1	12.4	11.1	13.2	13.3
Total	14.2	13.1	15.0	15.5
Tier 1 Leverage	7.8	7.8	n/a	7.8
Supplementary Leverage (d)	6.4	n/a	n/a	n/a
The Northern Trust Company				
Common Equity Tier 1	11.3%	10.0%	12.0%	11.8%
Tier 1	11.3	10.0	12.0	11.8
Total	13.0	11.8	13.8	14.0
Tier 1 Leverage	6.9	6.9	n/a	6.9
Supplementary Leverage (d)	5.7	n/a	n/a	n/a

CLIENT ASSETS (In Billions)	March 31, 2015	December 31, 2014	% Change (*)
Assets Under Custody	\$ 6,090.8	\$ 5,968.8	2%
Assets Under Management	960.1	934.1	3

(*) Percentage calculations are based on actual balances rather than the rounded amounts presented in the Consolidated Financial Highlights.

(**) Net interest margin is presented on a fully taxable equivalent (FTE) basis, a non-generally-accepted-accounting-principle (GAAP) financial measure that facilitates the analysis of asset yields. The net interest margin on a GAAP basis and a reconciliation of net interest income on a GAAP basis to net interest income on an FTE basis are presented on page 19.

(a) Effective with the second quarter of 2014, Northern Trust exited parallel run. Accordingly, the March 31, 2015, and December 31, 2014, ratios were calculated in compliance with the Basel III Advanced Approach final rules released by the Board of Governors of the Federal Reserve on July 2, 2013.

- (b) Effective with the first quarter of 2015, Standardized Approach risk weighted assets are calculated in compliance with the Basel III Standardized Approach final rules released by the Board of Governors of the Federal Reserve on July 2, 2013.
- (c) Standardized Approach capital components in 2014 were determined by Basel III phased in requirements and risk weighted assets were determined by Basel I requirements. The December 31, 2014, ratios calculated under the Standardized Approach comply with the final rules released by the Board of Governors of the Federal Reserve on July 2, 2013.
- (d) Advanced Approaches banking organizations must calculate and report their supplementary leverage ratio beginning with the first quarter of 2015. Northern Trust must maintain a minimum supplementary leverage ratio of 3 percent beginning with the first quarter of 2018.

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PART I FINANCIAL INFORMATION

Items 2. and 3. Management's Discussion and Analysis of Financial Condition and Results of Operations and Quantitative and Qualitative Disclosures about Market Risk

FIRST QUARTER CONSOLIDATED RESULTS OF OPERATIONS

General

Northern Trust Corporation (Corporation) is a financial holding company that is a leading provider of asset servicing, fund administration, asset management, fiduciary and banking solutions for corporations, institutions, families and individuals worldwide. Northern Trust focuses on managing and servicing client assets through its two client-focused reporting segments: Corporate & Institutional Services (C&IS) and Wealth Management (WM). Asset management and related services are provided to C&IS and Wealth Management clients primarily by the Asset Management business. Except where the context requires otherwise, the term Northern Trust, we, us, our or similar terms mean the Corporation and its subsidiaries on a consolidated basis.

The following should be read in conjunction with the consolidated financial statements and related footnotes included in this report. Investors should also read the section entitled Forward-Looking Statements.

Overview

Net income per diluted common share in the current quarter was \$0.94, up from \$0.75 in the first quarter of 2014. Net income was \$230.7 million in the current quarter as compared to \$181.4 million in the prior-year quarter. Annualized return on average common equity in the quarter was 11.3% as compared to 9.3% in the prior-year quarter. The annualized return on average assets was 0.9% as compared to 0.7% in the prior-year quarter.

Revenue of \$1.13 billion in the current quarter was up \$94.0 million, or 9%, from \$1.04 billion in the prior-year quarter. Noninterest income increased \$79.1 million, or 10%, to \$873.9 million from \$794.8 million in the prior-year quarter, primarily reflecting higher trust, investment and other servicing fees and foreign exchange trading income.

Net interest income increased \$14.9 million, or 6%, to \$260.6 million in the current quarter as compared to \$245.7 million in the prior-year quarter, due to growth in earning assets, offset partially by a lower net interest margin.

Net investment security gains totaled \$0.1 million in the current quarter compared to net investment security losses of \$4.0 million in the prior-year quarter. The prior-year quarter included \$3.9 million of charges relating to the other-than-temporary impairment (OTTI) of certain Community Reinvestment Act (CRA) eligible securities.

The provision for credit losses was a credit of \$4.5 million in the current quarter, reflecting improved credit quality across the loan portfolio. A provision of \$3.0 million was recorded in the prior-year quarter.

Noninterest expense totaled \$789.0 million, up \$21.0 million, or 3%, from \$768.0 million in the prior-year quarter, primarily attributable to higher compensation, equipment and software and employee benefits expense, partially offset by lower outside services expense.

Table of Contents**FIRST QUARTER CONSOLIDATED RESULTS OF OPERATIONS (continued)****Noninterest Income**

The components of noninterest income are provided below.

Table 1: Noninterest Income

Noninterest Income (\$ In Millions)	Three Months Ended March 31,		Change	
	2015	2014		
Trust, Investment and Other Servicing Fees	\$ 727.5	\$ 679.5	\$ 48.0	7%
Foreign Exchange Trading Income	71.6	50.1	21.5	43
Treasury Management Fees	16.3	16.8	(0.5)	(3)
Security Commissions and Trading Income	19.8	14.7	5.1	35
Other Operating Income	38.6	37.7	0.9	2
Investment Security Gains (Losses), net	0.1	(4.0)	4.1	104
Total Noninterest Income	\$ 873.9	\$ 794.8	\$ 79.1	10%

Trust, investment and other servicing fees are based primarily on: the market value of assets held in custody, managed and serviced; the volume of transactions; securities lending volume and spreads; and fees for other services rendered. Certain market value calculations on which fees are based are performed on a monthly or quarterly basis in arrears. For a further discussion of trust, investment and other servicing fees and how they are derived, refer to the Reporting Segments section.

The following table presents Northern Trust's assets under custody by reporting segment.

Table 2: Assets Under Custody

Assets Under Custody (\$ In Billions)	March 31,	December 31,	March 31,	Change	Change
	2015	2014	2014	Q1-15/ Q4-14	Q1-15/ Q1-14
Corporate & Institutional	\$ 5,566.2	\$ 5,453.1	\$ 5,249.9	2%	6%
Wealth Management	524.6	515.7	503.6	2	4
Total Assets Under Custody	\$ 6,090.8	\$ 5,968.8	\$ 5,753.5	2%	6%

Custodied assets by reporting segment were invested as follows at March 31, 2015, and 2014:

Table 3: Allocations of Assets Under Custody

Assets Under Custody	March 31, 2015			March 31, 2014		
	C&IS	WM	Consolidated	C&IS	WM	Consolidated
Equities	45%	55%	46%	45%	55%	46%
Fixed Income Securities	37	23	35	37	22	35
Cash and Other Assets	18	22	19	18	23	19

C&IS assets under custody totaled \$5.6 trillion as of March 31, 2015, and included \$3.4 trillion of global custody assets, 6% and 5% higher compared to March 31, 2014, respectively.

Table of Contents**FIRST QUARTER CONSOLIDATED RESULTS OF OPERATIONS (continued)****Noninterest Income (continued)**

The following table presents Northern Trust's assets under management by reporting segment.

Table 4: Assets Under Management

Assets Under Management	March 31, 2015	December 31, 2014	March 31, 2014	Change Q1-15/ Q4-14	Change Q1-15/ Q1-14
(\$ In Billions)					
Corporate & Institutional	\$ 727.0	\$ 709.6	\$ 698.2	2%	4%
Wealth Management	233.1	224.5	217.2	4	7
Total Assets Under Management	\$ 960.1	\$ 934.1	\$ 915.4	3%	5%

The following table presents consolidated assets under management as of March 31, 2015, and March 31, 2014, by investment type.

Table 5: Assets Under Management by Investment Type

(\$ In Billions)	March 31, 2015	March 31, 2014
Equities	\$ 495.8	\$ 485.5
Fixed Income Securities	168.0	150.1
Cash and Other Assets	173.1	163.3
Securities Lending Collateral	123.2	116.5
Total Assets Under Management	\$ 960.1	\$ 915.4

The 5% increase in consolidated assets under management from \$915.4 billion at March 31, 2014, to \$960.1 billion as of March 31, 2015, primarily reflected higher equity and bond markets and net new business from institutional clients, primarily in fixed income and cash.

Custodied and managed assets by reporting segment were invested as follows at March 31, 2015, and 2014:

Table 6: Allocations of Assets Under Management

Assets Under Management	March 31, 2015			March 31, 2014		
	C&IS	WM	Consolidated	C&IS	WM	Consolidated
Equities	53%	46%	52%	55%	46%	53%

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Fixed Income Securities	14	28	17	13	28	16
Securities Lending	17		13	17		13
Cash and Other Assets	16	26	18	15	26	18

Changes in assets under custody and under management are in comparison to the twelve month increase in the S&P 500[®] index of 10.4% and decline in the MSCI EAFE[®] index (USD) of 3.5%.

Foreign exchange trading income totaled \$71.6 million in the current quarter, up \$21.5 million, or 43%, compared to \$50.1 million in the prior-year quarter. The increase was primarily attributable to higher currency volatility and client volumes as compared to the prior-year quarter.

Security commissions and trading income totaled \$19.8 million, up \$5.1 million, or 35%, compared with \$14.7 million in the prior-year quarter. The increase is attributable to higher income from interest rate protection products sold to clients as well as higher core brokerage revenues.

Table of Contents**FIRST QUARTER CONSOLIDATED RESULTS OF OPERATIONS (continued)****Noninterest Income (continued)**

Other operating income totaled \$38.6 million in the current quarter, up 2%, from \$37.7 million in the prior-year quarter. The components of other operating income are provided below.

Table 7: Other Operating Income

Other Operating Income (\$ In Millions)	Three Months Ended March 31,		Change	
	2015	2014		
Loan Service Fees	\$ 14.9	\$ 15.7	\$ (0.8)	(5)%
Banking Service Fees	11.9	12.3	(0.4)	(4)
Other Income	11.8	9.7	2.1	21
Total Other Operating Income	\$ 38.6	\$ 37.7	\$ 0.9	2%

The increase in the other income component of other operating income was primarily attributable to additional income in the current quarter associated with a third-party servicing agreement modified in the prior quarter.

Net Interest Income

Net interest income on an FTE basis totaled \$266.8 million, up \$12.4 million, or 5%, compared to \$254.4 million in the prior-year quarter. The increase was primarily the result of growth in earning assets, partially offset by a lower net interest margin. Earning assets for the current quarter averaged \$98.7 billion, up \$6.9 billion, or 7%, from \$91.8 billion in the prior-