STATE STREET CORP
Form 10-Q
August 04, 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 June 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 July 31, 2017 was 373,955,415.

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

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

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 $31.04 trillion of AUCA and $2.61 trillion of AUM as of June 30, 2017.

As of June 30, 2017, we had consolidated total assets of $238.27 billion, consolidated total deposits of $181.42 billion, consolidated total shareholders' equity of $22.07 billion and 35,606 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 June 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 six 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

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 expected to be appointed under a potential 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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MANAGEMENT'S DISCUSSION AND ANALYSIS OF FINANCIAL CONDITION AND RESULTS OF OPERATIONS

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 June 30,		
(Dollars in millions, except per share amounts)	2017	2016	% Change
Total fee revenue	$2,235	$2,053	9 %
Net interest income	575	521	10
Gains (losses) related to investment securities, net	—	(1)	nm
Total revenue	2,810	2,573	9
Provision for loan losses	3	4	(25)
Total expenses	2,031	1,860	9
Income before income tax expense	776	709	9
Income tax expense (benefit)	156	92	70
Net Income (loss) from non-controlling interest	—	2	nm
Net income	$620	$619	—
Adjustments to net income:			
Dividends on preferred stock[1]	(36)	(33)	9
Earnings allocated to participating securities[2]	—	(1)	nm
Net income available to common shareholders	$584	$585	—
Earnings per common share:			
Basic	$1.56	$1.48	5
Diluted	1.53	1.47	4
Average common shares outstanding (in thousands):			
Basic	375,395	394,160	
Diluted	380,915	398,847	
Cash dividends declared per common share	$.38	$.34	
Return on average common equity	12.6 %	12.4 %	

	Six Months Ended June 30,		
(Dollars in millions, except per share amounts)	2017	2016	% Change
Total fee revenue	$4,433	$4,023	10 %
Net interest income	1,085	1,033	5

Gains (losses) related to investment securities, net	(40)	1	nm
Total revenue	5,478	5,057	8
Provision for loan losses	1	8	(88)
Total expenses	4,117	3,910	5
Income before income tax expense	1,360	1,139	19
Income tax expense (benefit)	238	154	55
Net income from non-controlling interest	—	2	nm
Net income	$1,122	$987	14
Adjustments to net income:			
Dividends on preferred stock[1]	$(91)	$(82)	11
Earnings allocated to participating securities[2]	(1)	(1)	nm
Net income available to common shareholders	$1,030	$904	14
Earnings per common share:			
Basic	$2.72	$2.28	19
Diluted	2.69	2.25	20
Average common shares outstanding (in thousands):			
Basic	378,293	396,790	
Diluted	383,489	401,113	
Cash dividends declared per common share	$.76	$.68	
Return on average common equity	11.3 %	9.6 %	

[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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MANAGEMENT’S DISCUSSION AND ANALYSIS OF FINANCIAL CONDITION
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The following “Highlights” and “Financial Results” sections provide information related to significant events, as well as highlights of our consolidated financial results for the quarter ended June 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 quarter ended June 30, 2017 to those for the quarter ended June 30, 2016 and for the six months ended June 30, 2017 to those for the six months ended June 30, 2016, is provided under “Consolidated Results of Operations,” which follows these sections. 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 results.

Highlights

- EPS of $1.53 increased 4% in the second quarter of 2017 compared to $1.47 in the second quarter of 2016, reflecting growth in fee revenue driven by higher global equity markets, new business wins and higher client volumes, the contribution of the acquired GEAM operations and savings associated with State Street Beacon. The growth in EPS also reflected higher NII as a result of the higher market interest rates in the U.S., disciplined liability pricing and improvement of our liability mix. These increases were partially offset by restructuring costs of $62 million in the second quarter of 2017 as compared to $13 million in the second quarter of 2016.
- Second quarter 2017 ROE of 12.6% increased 20 bps compared to 12.4% in the second quarter of 2016, reflecting strong earnings and capital return via stock purchases and dividend payouts, partially offset by the aforementioned restructuring charges.
- Strength in equity markets and new business drove increases in both AUCA and AUM.

AUCA increased 12% in the second quarter of 2017 compared to the second quarter of 2016, primarily due to higher global equity markets, net new business and client flows. The AUCA growth contributed to revenue growth across the geographic regions we serve and across a range of products and client segments. In the second quarter of 2017, we secured new asset servicing mandates of approximately $135 billion. Our AUCA

pipeline of asset servicing mandates that have been won but not yet installed as of June 30, 2017 totaled approximately $370 billion.

AUM increased 13% in the second quarter of 2017 compared to the second quarter of 2016, primarily due to higher global equity markets, the impact of the acquired GEAM operations and positive ETF flows, partially offset by continuing institutional net outflows.

Additional information about AUCA and AUM is provided in "Servicing Fees" and "Management Fees," respectively, in "Line of Business - Investment Servicing" and "Line of Business - Investment Management," respectively, in this Management's Discussion and Analysis in this Form 10-Q.

- We declared a quarterly common stock dividend of $0.38 per share, totaling approximately $142 million, in the second quarter of 2017, compared to $0.34 per share, totaling $133 million in the second quarter of 2016.
- In the second quarter of 2017, we acquired approximately 2.7 million shares of common stock at an average per-share cost of $83.84 and an aggregate cost of approximately $227 million under the common stock purchase program approved by our Board in June 2016.
- Subsequent to the Federal Reserve's June 2017 non-objection to our capital plan under its 2017 CCAR process, our Board approved a new common stock purchase program, authorizing the purchase of up to $1.4 billion of common stock from July 1, 2017 through June 30, 2018 and, in July 2017, approved a third quarter quarterly common stock dividend of $0.42 per share, an increase of approximately 11% over the second quarter of 2017 quarterly common stock dividend.

Additional information with respect to our common stock purchase program and stock dividends are provided under "Capital" in "Financial Condition" in this Management's Discussion and Analysis in this Form 10-Q.

- In May 2017, we issued $750 million of fixed-to-floating rate senior notes due on May 15, 2023.

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Financial Results

- Total revenue in the second quarter of 2017 increased 9% compared to the second quarter of 2016, reflecting growth in total fee revenue and NII. The increase was primarily due to higher global equity markets, the acquired GEAM business, higher market interest rates in the U.S. and net new business. The second quarter of 2016 also included a revenue reduction of $48 million to servicing fees related to reimbursements to our clients related to the manner in which we invoiced certain expenses to our clients, as further discussed within "Investment Servicing" in "Line of Business Information" in this Management's Discussion and Analysis.
- Servicing fee revenue increased 8% in the second quarter of 2017 compared to the second quarter of 2016, primarily due to higher global equity markets, net new business and higher client volumes.
- Management fee revenue increased 36% in the second quarter of 2017 compared to the second quarter of 2016, primarily due to approximately $72 million from the acquired GEAM business, higher global equity markets and higher revenue-yielding ETF flows.
- Processing and other fee revenue decreased 68% in the second quarter of 2017 compared to the second quarter of 2016, primarily due to a pre-tax gain of approximately $53 million related to the sale of the WM/Reuters business in the second quarter of 2016 and unfavorable foreign exchange swap costs in the second quarter of 2017.
- NII increased 10% in the second quarter of 2017 compared to the second quarter of 2016, primarily due to higher market interest rates in the U.S. and disciplined liability pricing as well as improved liability mix, partially offset by lower investment portfolio securities balances.
- In the second quarter of 2017, we recorded restructuring charges of $62 million related to 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. 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. We expect to generate at least $140 million in annual pre-tax expense savings in 2017. Actual expenses may

increase or decrease in the future due to other factors.

- Total expenses increased 9% in the second quarter of 2017 compared to the second quarter of 2016, primarily driven by costs to support new business (including technology infrastructure), expenses associated with the acquired GEAM operations, increases in restructuring expenses related to State Street Beacon as well as incentive compensation and annual merit increases. The increases to total expenses were partially offset by savings associated with State Street Beacon.

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MANAGEMENT'S DISCUSSION AND ANALYSIS OF FINANCIAL CONDITION
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CONSOLIDATED RESULTS OF OPERATIONS
This section discusses our consolidated results of operations for the second quarter and first six months ended June 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

	Quarters Ended June 30,		
(Dollars in millions)	2017	2016	% Change
Fee revenue:			
Servicing fees	$1,339	$1,239	8 %
Management fees	397	293	36
Trading services:			
Foreign exchange trading	178	157	13
Brokerage and other trading services	111	110	1
Total trading services	289	267	8
Securities finance	179	156	15
Processing fees and other	31	98	(68)
Total fee revenue	2,235	2,053	9
Net interest income:			
Interest income	700	620	13
Interest expense	125	99	26
Net interest income	575	521	10
Gains (losses) related to investment securities, net	—	(1)	nm
Total revenue	$2,810	$2,573	9

	Six Months Ended June 30,		
(Dollars in millions)	2017	2016	% Change
Fee revenue:			
Servicing fees	$2,635	$2,481	6 %
Management fees	779	563	38
Trading services:			
Foreign exchange trading	342	313	9
Brokerage and other trading services	222	226	(2)
Total trading services	564	539	5
Securities finance	312	290	8
Processing fees and other	143	150	(5)
Total fee revenue	4,433	4,023	10
Net interest income:			
Interest income	1,350	1,249	8
Interest expense	265	216	23
Net interest income	1,085	1,033	5
Gains (losses) related to investment securities, net	(40)	1	nm
Total revenue	$5,478	$5,057	8

nm Not meaningful

Fee Revenue

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

Servicing and management fees collectively made up approximately 78% and 77% of total fee revenue in the second quarter and first six months of 2017, respectively, compared to approximately 75% and 76% in the second quarter and first six 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 are generally 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 assets under management than for passive products. Actively managed products may also include performance fee arrangements which are recorded when the performance period is complete. Performance fees are generated when the performance of certain managed portfolios exceeds benchmarks specified in the management agreements. Generally, we experience more volatility

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with performance fees than with more traditional management fees.
In light of the above, we estimate, using relevant information as of June 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. The index names listed in the table are service marks of their respective owners.
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

	Daily Averages of Indices			Averages of Month-End Indices			Quarter-End Indices		
	Quarters Ended June 30,			Quarters Ended June 30,			As of June 30,		
	2017	2016	% Change	2017	2016	% Change	2017	2016	% Change
S&P 500®	2,398	2,075	16 %	2,406	2,087	15 %	2,423	2,099	15 %
MSCI EAFE®	1,856	1,648	13	1,869	1,656	13	1,883	1,608	17
MSCI® Emerging Markets	993	819	21	998	827	21	1,011	834	21
HFRI Asset Weighted Composite®	N/A	N/A	N/A	1,339	1,250	7	1,336	1,250	7

	Daily Averages of Indices			Averages of Month-End Indices		
	Six Months Ended June 30,			Six Months Ended June 30,		
	2017	2016	% Change	2017	2016	% Change
S&P 500®	2,362	2,015	17 %	2,371	2,032	17 %
MSCI EAFE®	1,802	1,621	11	1,814	1,629	11
MSCI® Emerging Markets	960	788	22	966	800	21
HFRI Asset Weighted Composite®	N/A	N/A	N/A	1,331	1,245	7

TABLE 4: QUARTER-END DEBT INDICES

	Quarter-End Indices		
	As of June 30,		
	2017	2016	% Change
Barclays Capital U.S. Aggregate Bond Index®	2,021	2,028	— %
Barclays Capital Global Aggregate Bond Index®	471	482	(2)

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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 six months ended June 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.

Net interest margin 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 June 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	$53,146	$41	.31 %	$51,084	$30	.24 %
Securities purchased under resale agreements[1]	2,352	69	11.77	2,673	35	5.32
Trading account assets	941	—	—	870	—	—
Investment securities	94,637	466	1.97	102,391	492	1.92
Loans and leases	21,070	122	2.31	18,662	93	2.00
Other interest-earning assets	23,141	44	.76	22,563	10	.18
Average total interest-earning assets	$195,287	$742	1.52	$198,243	$660	1.34
Interest-bearing deposits:						
U.S.	$25,770	$24	.38 %	$30,363	$31	.41 %
Non-U.S.[2]	99,389	(10)	(.04)	96,446	(15)	(.06)
Securities sold under repurchase agreements[3]	4,028	—	—	4,103	—	—
Federal funds purchased	2	—	—	61	—	—
Other short-term borrowings	1,322	3	.80	1,928	2	.38
Long-term debt	11,515	75	2.61	10,998	62	2.24
Other interest-bearing liabilities	5,355	33	2.44	5,054	19	1.54
Average total interest-bearing liabilities	$147,381	$125	.34	$148,953	$99	.27
Interest-rate spread			1.18 %			1.07 %
Net interest income—fully taxable-equivalent basis		$617			$561	
Net interest margin—fully taxable-equivalent basis			1.27 %			1.14 %
Tax-equivalent adjustment		(42)			(40)	
Net interest income—GAAP basis		$575			$521	

	Six Months Ended June 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	$51,031	$76	.30 %	$49,815	$73	.29 %
Securities purchased under resale agreements[1]	2,205	115	10.52	2,581	71	5.58
Trading account assets	928	(1)	(.13)	865	1	.12
Investment securities	95,921	936	1.95	101,645	980	1.93
Loans and leases	20,607	230	2.25	18,639	184	1.98
Other interest-earning assets	22,882	78	.69	22,617	22	.20
Average total interest-earning assets	$193,574	$1,434	1.49	$196,162	$1,331	1.37
Interest-bearing deposits:						
U.S.	$25,849	$56	.44 %	$28,729	$58	.40 %
Non-U.S.[2]	97,201	1	—	94,708	(4)	(.01)
Securities sold under repurchase agreements	3,961	1	.04	4,173	1	.03
Federal funds purchased	1	—	—	38	—	—
Other short-term borrowings	1,332	5	.71	1,808	2	.24

Long-term debt	11,469	148	2.58	11,013	122	2.22
Other interest-bearing liabilities	5,298	54	2.04	5,502	37	1.37
Average total interest-bearing liabilities	$145,111	$265	.37	$145,971	$216	.30
Interest-rate spread			1.12 %			1.07 %
Net interest income—fully taxable-equivalent basis		$1,169			$1,115	
Net interest margin—fully taxable-equivalent basis			1.22 %			1.14 %
Tax-equivalent adjustment		(84)			(82)	
Net interest income—GAAP basis		$1,085			$1,033	

(1) Reflects the impact of balance sheet netting under enforceable netting agreements of approximately $33 billion and $32 billion for the second quarter and first six months of 2017, respectively, and $32 billion for both the second quarter and first six months of 2016, respectively. Excluding the impact of netting, the average interest rates would be approximately 0.79% and 0.67% for the second quarter and first six months of 2017, respectively, and 0.41% for both the second quarter and six months of 2016, respectively.
(2) Average rate includes the impact of FX swap expense of approximately $13 million and $45 million for the second quarter and first six months of 2017, respectively, and $5 million and $21 million for the same periods in 2016, respectively.
(3) Interest for the second quarter of 2016 and 2017 was less than $1 million, representing average interest rates of 0.03% and 0.04%, respectively.

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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 six months ended June 30, 2017 and 2016. NII on a fully taxable-equivalent basis increased in the second quarter of 2017 compared to the same period in 2016, as benefits due to a higher domestic rate environment and improvements in our liability mix were offset by lower investment portfolio securities balances and a smaller amount of discount accretion related to the asset-backed commercial paper conduits. Average balances in the second quarter of 2017 reflect management actions to reduce the usage of wholesale deposit funding of our balance sheet. Though average interest and non-interest bearing deposits were approximately $1.40 billion lower in the second quarter of 2017 compared to the second quarter of 2016, these management actions contributed to a $9.87 billion reduction in wholesale deposits and were offset by an increase in less expensive client deposits.

We recorded aggregate discount accretion in interest income of $6 million and $10 million for the second quarter and first six 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 $127 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 $2.59 billion lower in the six months ended June 30, 2017 compared to the same period in 2016, primarily due to a smaller investment portfolio.

Interest-bearing deposits with banks averaged $53.15 billion and $51.03 billion for the second quarter and first six months of 2017, respectively, compared to $51.08 billion and $49.82 billion for the same periods in 2016. These deposits reflected our maintenance of cash balances at the Federal Reserve, the ECB and other non-U.S. central banks.

Loans and leases averaged $21.07 billion and $20.61 billion for the second quarter and first six months of 2017, respectively, compared to $18.66 billion and $18.64 billion for the same periods in 2016. The increase in average loans and leases resulted from growth in loans to municipalities,

alternative financing, mutual fund lending, and continued investment in senior secured loans.

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

	Quarters Ended June 30,	
(Dollars in millions)	2017	2016
Average U.S. short-duration advances	$2,087	$2,144
Average non-U.S. short-duration advances	1,450	1,471
Average total short-duration advances	$3,537	$3,615
Average short-duration advances to average loans and leases	17 %	19 %

	Six Months Ended June 30,	
(Dollars in millions)	2017	2016
Average U.S. short-duration advances	$2,173	$2,187
Average non-U.S. short-duration advances	1,336	1,368
Average total short-duration advances	$3,509	$3,555
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 $23.14 billion and $22.88 billion for the second quarter and first six months of 2017, respectively, from $22.56 billion and $22.62 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 second quarter and first six months of 2017, compared to approximately 11% and 12% of our average total interest-earning assets for the same periods in 2016. The enhanced custody business, which is our principal securities financing business for our custody clients, generates securities finance revenue. The NII earned on these transactions is generally lower than the interest earned on other alternative investments.

Aggregate average U.S. and non-U.S. interest-bearing deposits decreased to $125.16 billion and $123.05 billion for the second quarter and first six months of 2017, respectively, from $126.81 billion and $123.44 billion for the same periods in 2016. The relatively flat levels in the first six months of 2017 compared to the prior year period were a result of higher U.S. and non-U.S. client deposit levels during the year, offset by management's actions to reduce more expensive wholesale certificates of deposit. 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.

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Average other short-term borrowings declined to $1.32 billion and $1.33 billion for the second quarter and first six months of 2017, respectively, from $1.93 billion and $1.81 billion for the same periods in 2016, as bonds matured in the Tax-Exempt Investment program.
Average long-term debt increased to $11.52 billion and $11.47 billion for the second quarter and first six months of 2017, respectively, from $11.00 billion and $11.01 billion for the same periods in 2016. The increases primarily reflected the issuance of $1.5 billion of senior debt in May 2016 and $750 million of senior debt in May 2017, which was partially offset by the maturity of $400 million of senior debt in January 2016, $1.0 billion of senior debt in March 2016, and $450 million of senior debt in April 2017.
Average other interest-bearing liabilities were $5.36 billion and $5.30 billion for the second quarter and first six months of 2017, respectively, compared to $5.05 billion and $5.50 billion for the same periods in 2016, primarily the result of changes in the level of cash collateral received from clients in connection with our enhanced custody business, which is presented on a net basis in accordance with enforceable netting agreements.
Several factors could affect future levels of our NII and net interest margin, including the volume and mix of client liabilities; actions of various central banks; changes in U.S. and non-U.S. interest rates; changes in the 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 requirements, 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 mortgage-backed securities and U.S. and non-U.S. mortgage- and asset-backed securities. 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, 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 net interest margin.

Expenses
Table 7: Expenses provides the breakout of expenses for the quarters and six months ended June 30, 2017 and 2016.
TABLE 7: EXPENSES

	Quarters Ended June 30,		
(Dollars in millions)	2017	2016	% Change
Compensation and employee benefits	$1,071	$989	8 %
Information systems and communications	283	270	5
Transaction processing services	207	201	3
Occupancy	116	111	5
Acquisition costs	9	7	29
Restructuring charges, net	62	13	377
Other:			
Professional services	97	82	18
Amortization of other intangible assets	54	49	10
Securities processing costs	9	6	50
Regulatory fees and assessments	18	18	—
Other	105	114	(8)
Total other	283	269	5

Total expenses	$2,031	$1,860	9
Number of employees at quarter-end	35,606	32,636	9

	Six Months Ended June 30,		
(Dollars in millions)	2017	2016	% Change
Compensation and employee benefits	$2,237	$2,096	7 %
Information systems and communications	570	542	5
Transaction processing services	404	401	1
Occupancy	226	224	1
Acquisition costs	21	14	50
Restructuring charges, net	79	110	(28)
Other:			
Professional services	191	175	9
Amortization of other intangible assets	106	98	8
Securities processing costs	16	10	60
Regulatory fees and assessments	45	38	18
Other	222	202	10
Total other	580	523	11
Total expenses	$4,117	$3,910	5

Compensation and employee benefits expenses increased 8% in the second quarter of 2017 compared to the same period of 2016, primarily due to increased costs to support new business, higher incentive compensation and annual merit increases, costs related to the acquired GEAM operations and regulatory initiatives, partially offset by State Street Beacon savings.

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

the first quarter of 2016. These increases were partially offset by State Street Beacon savings.
Headcount increased 9% in second quarter of 2017 compared to the same period of 2016. New business, including the impact of large client lift outs and new client ramp-ups, as well as regulatory initiatives and contractor conversions to full-time employees contributed to this growth. The growth was primarily within low cost locations. These increases were partially offset by reductions from State Street Beacon initiatives.
Information systems and communications expenses increased 5% in each of the second quarter and first six months of 2017 compared to the same periods of 2016. The increases were primarily related to State Street Beacon and investments supporting new business.
Other expenses increased 5% in the second quarter of 2017 compared to the same period of 2016. The increase was primarily due to higher security processing costs and professional services, partially offset by a release of litigation reserves in the second quarter of 2017.
Other expenses increased 11% in the six months ended June 30, 2017 compared to the same period in 2016. The increase was primarily due to higher securities processing costs and regulatory fees and assessments.
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.

Acquisition Costs

We recorded acquisition costs of $9 million and $7 million in the second quarter of 2017 and 2016, respectively, and $21 million and $14 million in the first six months of 2017 and 2016, respectively. Costs incurred in the second quarter and first six months of 2017 related to the acquired GEAM operations. For additional information about the GEAM acquisition, refer to page 132 in Note 1 to the consolidated financial statements included under Item 8, Financial Statements and Supplementary Data, in our 2016 Form 10-K.

Restructuring Charges

In October 2015, we announced State Street Beacon, a multi-year program to create cost efficiencies through changes in our operational processes and to further digitize our processes and interfaces with our clients. In connection with State Street Beacon, we expect to incur aggregate pre-tax restructuring charges of approximately $300 million to $400 million beginning in 2016 through December 31, 2020 to implement State Street Beacon. 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 second quarter and first six months of 2017, we recorded restructuring charges of $62 million and $79 million, respectively, compared to $13 million and $110 million in the same periods of 2016, primarily related to State Street Beacon.
The following table presents aggregate restructuring activity for the periods indicated.

TABLE 8: RESTRUCTURING CHARGES

(In millions)	Employee Related Costs	Real Estate Consolidation	Asset and Other Write-offs	Total
Accrual Balance at December 31, 2015	$ 9	$ 11	$ 3	$23
Accruals for State Street Beacon	86	—	11	97

Payments and Other Adjustments	(4)	(1)	(7)	(12)
Accrual Balance at March 31, 2016	$ 91	$ 10	$ 7	$ 108
Accruals for State Street Beacon	(1)	15	(1)	13
Payments and Other Adjustments	(35)	(3)	(1)	(39)
Accrual Balance at June 30, 2016	$ 55	$ 22	$ 5	$ 82
Accrual Balance at December 31, 2016	$ 37	$ 17	$ 2	$ 56
Accruals for State Street Beacon	14	—	2	16
Payments and Other Adjustments	(13)	(3)	(2)	(18)
Accrual Balance at March 31, 2017	$ 38	$ 14	$ 2	$ 54
Accruals for State Street Beacon	60	—	2	62
Payments and Other Adjustments	(11)	(3)	(2)	(16)
Accrual Balance at June 30, 2017	$ 87	$ 11	$ 2	$ 100

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Income Tax Expense
Income tax expense was $156 million in the second quarter of 2017 compared to $92 million in the second quarter of 2016. In the first six months of 2017 and 2016, income tax expense was $238 million and $154 million, respectively. Our effective tax rate for the second quarter and first six months of 2017 was 20.1% and 17.5%, respectively, compared to 12.9% and 13.5% for the same periods in 2016. The effective tax rate for the second quarter and first six months of 2017 reflect a decrease in alternative energy investments.

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 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 June 30,			Six Months Ended June 30,		
(Dollars in millions)	2017	2016	% Change	2017	2016	% Change
Servicing fees	$1,339	$1,239	8 %	$2,635	$2,481	6 %
Trading services	272	254	7	529	512	3
Securities finance	179	156	15	312	290	8
Processing fees and other	32	103	(69)	138	152	(9)
Total fee revenue	1,822	1,752	4	3,614	3,435	5
Net interest income	576	520	11	1,085	1,032	5
Gains (losses) related to investment securities, net	—	(1)	nm	(40)	1	nm
Total revenue	2,398	2,271	6	4,659	4,468	4
Provision for loan losses	3	4	nm	1	8	nm
Total expenses	1,649	1,599	3	3,377	3,286	3
Income before income tax expense	$746	$668	12	$1,281	$1,174	9
Pre-tax margin	31 %	29 %		27 %	26 %	

nm Not meaningful

Total revenue, as presented in Table 9: Investment Servicing Line of Business Results, increased 6% and 4% in the second quarter and first six months of 2017, respectively, compared to the same periods in 2016 due to increases in servicing fees, trading services, securities finance and NII, offset by a decrease in processing fees and other revenue as further described below.

Total fee revenue increased 4% and 5% in the second quarter and first six months of 2017, respectively, compared to the same periods in 2016, primarily due to higher global equity markets, net new business and higher client volumes as well as growth in our enhanced custody business. The second quarter and first six months of 2016 included a revenue reduction of $48 million related to reimbursements to our clients related to the manner

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in which we invoiced certain expenses to our clients as discussed below. The increases were partially offset by a pre-tax gain of approximately $53 million related to the sale of the WM/Reuters business in the second quarter of 2016.

NII increased 11% and 5% in the second quarter and first six months of 2017, respectively, compared to the same periods in 2016, as discussed under “Net Interest Income" in “Consolidated Results of Operations - Total Revenue" in this Management's Discussion and Analysis.

Total expenses increased 3% in the second quarter of 2017 compared to the same period in 2016, primarily due to increased costs to support new business (including technology infrastructure), incentive compensation and annual merit increases.

Total expenses increased 3% in the first six months of 2017 compared to the same period in 2016, primarily due to net new business (including technology infrastructure), incentive compensation and annual merit increases, regulatory initiatives and an increase of approximately $28 million associated with the first quarter seasonal deferred incentive compensation expense for retirement-eligible employees and payroll taxes.

The increases in total expenses were partially offset by savings related to State Street Beacon.

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

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 informed our clients that we will pay to them the expenses we concluded were incorrectly invoiced to them, plus interest. The process of reimbursing clients these amounts is substantially complete. In conjunction with the review announced in December 2015, which is ongoing, we are implementing enhancements to our billing processes and reviewing the conduct of our employees and have taken appropriate steps to address conduct inconsistent with our standards, including, in some cases, termination of employment. We are also evaluating other aspects of invoicing relating to billing our Investment Servicing clients, including calculation of asset-based fees. Additional information about the invoicing matter is provided in Note 10 to the consolidated financial statements included in this Form 10-Q.

Servicing Fees

Servicing fees increased 8% and 6% in the second quarter and first six months of 2017, respectively, compared to the same periods in 2016,

primarily due to higher global equity markets, net new business and higher client volumes. The second quarter and first six 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 discussed above within "Investment Servicing" in our "Line of Business Information" section of this Management's Discussion and Analysis.

Servicing fees generated outside the U.S. was approximately 44% of total servicing fees in both the second quarter and first six months of 2017 compared to approximately 43% and 42% for the same periods in 2016, respectively.

TABLE 10: ASSETS UNDER CUSTODY AND
ADMINISTRATION BY PRODUCT

(In billions)	June 30, 2017	December 31, 2016	June 30, 2016
Mutual funds	$7,123	$ 6,841	$6,734
Collective funds	8,560	7,501	7,234
Pension products	5,937	5,584	5,496
Insurance and other products	9,417	8,845	8,322
Total	$31,037	$ 28,771	$27,786

TABLE 11: ASSETS UNDER CUSTODY AND
ADMINISTRATION BY ASSET CLASS

(In billions)

	June 30, 2017	December 31, 2016	June 30, 2016
Equities	$17,304	$ 15,833	$14,960
Fixed-income	10,117	9,665	9,530
Short-term and other investments	3,616	3,273	3,296
Total	$31,037	$ 28,771	$27,786

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

(In billions)	June 30, 2017	December 31, 2016	June 30, 2016
North America	$23,020	$ 21,544	$21,072
Europe/Middle East/Africa	6,464	5,734	5,356
Asia/Pacific	1,553	1,493	1,358
Total	$31,037	$ 28,771	$27,786

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

The increase in total AUCA as of June 30, 2017 compared to December 31, 2016 primarily resulted from higher global equity markets. Asset levels as of June 30, 2017 do not reflect the approximately $370 billion of new business in assets to be serviced, which was awarded to us in the first six months of 2017 and prior periods but not installed prior to June 30, 2017. This new business will be reflected in AUCA in future periods after installation and will generate servicing fee revenue in subsequent periods. This does not include 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.

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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 June 30, 2017	2016	% Change
Foreign exchange trading:			
Direct sales and trading	$100	$87	15 %
Indirect foreign exchange trading	78	70	11
Total foreign exchange trading	178	157	13
Brokerage and other trading services:			
Electronic foreign exchange services	39	43	(9)
Other trading, transition management and brokerage	55	54	2
Total brokerage and other trading services	94	97	(3)
Total trading services revenue	$272	$254	7

(Dollars in millions)	Six Months Ended June 30, 2017	2016	% Change
Foreign exchange trading:			
Direct sales and trading	$198	$177	12 %
Indirect foreign exchange trading	144	136	6
Total foreign exchange trading	342	313	9
Brokerage and other trading services:			
Electronic foreign exchange services	80	87	(8)
Other trading, transition management and brokerage	107	112	(4)
Total brokerage and other trading services	187	199	(6)
Total trading services revenue	$529	$512	3

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.

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 three broad categories, which are further explained below: “direct sales and trading,” “indirect FX trading” and “electronic FX services.” With respect to electronic FX services, we provide an execution venue, but do not act as agent or principal.

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 differentiated by our role as an 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 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 increased 13% and 9% in the second quarter and first six months of 2017, respectively, compared to the same periods in 2016, primarily due to higher volumes. Total FX trading revenue comprises:

- 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 58% of total foreign exchange trading revenue in the second quarter and first six months of 2017, respectively,

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compared to 55% and 57% for the same periods in 2016. Our direct sales and trading revenue increased by 15% and 12% in the second quarter and first six months of 2017, respectively, compared to the same periods in 2016. The increases were primarily due to higher volumes.

- 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 42% of total foreign exchange trading revenue in the second quarter and first six months of 2017, respectively, compared to 45% 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 estimated indirect FX trading revenue increased 11% and 6% in the second quarter and first six months of 2017, respectively, compared to the same periods in 2016, primarily due to higher 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 decreased 3% and 6% in the second quarter and first six months of 2017, respectively, compared to the same periods in 2016, primarily due to lower electronic foreign exchange trading revenue 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. Revenue from such electronic FX services decreased 9% and 8% in the second quarter and first six months of 2017, respectively, compared to the same periods in 2016.
- Other trading, transition management and brokerage revenue: Revenue remained flat in the second quarter of 2017 compared to the same period in 2016. Revenue decreased 4% in the first six months of 2017 compared to the same period in 2016, primarily due to the disposition of the WM/Reuters business.

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. Information about contingencies is provided in Note 10 to the consolidated financial statements included in this Form 10-Q.

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.

See Table 9: Investment Servicing Line of Business Results, for the comparison of securities finance revenue in the second quarter and first six months of 2017 compared to the same periods in 2016.
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.

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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 increased 15% and 8% in the second quarter and first six months of 2017, respectively, 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 may affect 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 leased equipment and 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, decreased 69% and 9% in the second quarter and first six months of 2017, respectively, compared to the same periods in 2016. The decrease in the second quarter of 2017 compared to the second quarter of 2016 is primarily due to a pre-tax gain of approximately $53 million related to the sale of WM/Reuters in the second quarter of 2016 as well as unfavorable foreign exchange swap costs in the second quarter of 2017. The decrease in the first six months of 2017 is primarily due to the aforementioned pre-tax gain on the sale of WM/Reuters in 2016, partially offset by 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.

Investment Management

TABLE 14: INVESTMENT MANAGEMENT LINE OF BUSINESS RESULTS

	Quarters Ended June 30,			Six Months Ended June 30,		
(Dollars in millions)	2017	2016	% Change	2017	2016	% Change
Management fees	$397	$293	35 %	$779	$563	38 %
Trading services[1]	17	13	31	35	27	30
Processing fees and other	(1)	(5)	nm	5	(2)	nm
Total fee revenue	413	301	37	819	588	39
Net interest income	(1)	1	nm	—	1	nm
Total revenue	412	302	36	819	589	39
Total expenses	311	244	27	640	500	28
Income before income tax expense	$101	$58	74	$179	$89	101
Pre-tax margin	25 %	19 %		22 %	15 %	

[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

Total revenue, as presented in Table 14: Investment Management Line of Business Results, increased 36% and 39% in the second quarter and first six months of 2017, respectively, compared to the same periods in 2016, primarily due to approximately $72 million and $143 million, respectively, from the acquired GEAM operations, higher global equity markets and higher revenue-yielding ETF flows.

Total expenses increased 27% and 28% in the second quarter and first six months of 2017, respectively, compared to the same periods in 2016 primarily due to approximately $51 million and $102 million, respectively, in incremental costs related to the acquired GEAM operations, as well as higher incentive compensation and annual merit increases. These increases were partially offset by savings related to State Street Beacon.

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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.

In July 2016, we completed our acquisition of GEAM, including $110 billion of acquired AUM. AUM associated with the acquired GEAM operations totaled $125 billion as of June 30, 2017, including the impact of global equity markets, assets from acquired clients and new business from these clients since the acquisition date. Our consolidated financial statements include the operating results for the acquired business from the date of acquisition, July 1, 2016.

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 assets under management 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 35% and 38% in the second quarter and first six months 2017, respectively, compared to the same periods in 2016, primarily due to approximately $72 million and $143 million, respectively, from the acquired GEAM operations, higher global equity markets, and higher revenue-yielding ETF flows.

Management fees generated outside the U.S. was approximately 28% of total management fees in both the second quarter and first six months of 2017, respectively, compared to 34% and 35% in the same periods in 2016, respectively.

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

(In billions)	June 30, 2017	December 31, 2016	June 30, 2016
Equity:			
Active	$ 82	$ 73	$ 32
Passive	1,512	1,401	1,275
Total Equity	1,594	1,474	1,307
Fixed-Income:			
Active	71	70	17
Passive	327	308	318
Total Fixed-Income	398	378	335
Cash[1]	334	333	380
Multi-Asset-Class Solutions:			
Active	18	19	17
Passive	113	107	100
Total Multi-Asset-Class Solutions	131	126	117
Alternative Investments[2]:			
Active	27	28	18
Passive	122	129	144
Total Alternative Investments	149	157	162
Total	$ 2,606	$ 2,468	$ 2,301

(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)	June 30, 2017	December 31, 2016	June 30, 2016
Alternative Investments(2)	$ 46	$ 42	$ 54
Cash	2	2	2
Equity	460	426	348
Fixed-income	58	51	48
Total Exchange-Traded Funds	$ 566	$ 521	$ 452

(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)	June 30, 2017	December 31, 2016	June 30, 2016
North America	$ 1,802	$ 1,691	$ 1,501
Europe/Middle East/Africa	496	482	492
Asia/Pacific	308	295	308
Total	$ 2,606	$ 2,468	$ 2,301

(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[2]	Multi-Asset-Class Solutions	Alternative Investments[3]	Total
Balance as of June 30, 2016	$1,307	$ 335	$ 380	$ 117	$ 162	$2,301
Long-term institutional inflows[1]	138	54	—	27	7	226
Long-term institutional outflows[1]	(157)	(56)	—	(17)	(16)	(246)
Long-term institutional flows, net	(19)	(2)	—	10	(9)	(20)
ETF flows, net	49	4	1	—	(6)	48
Cash fund flows, net	—	—	(49)	—	—	(49)
Total flows, net	30	2	(48)	10	(15)	(21)
Market appreciation	118	(7)	(1)	(1)	2	111
Foreign exchange impact	(19)	(8)	(2)	(3)	(3)	(35)
Total market/foreign exchange impact	99	(15)	(3)	(4)	(1)	76
Acquisitions and transfers[4]	38	56	4	3	11	112
Balance as of December 31, 2016	$1,474	$ 378	$ 333	$ 126	$ 157	$2,468
Long-term institutional inflows[1]	134	45	—	21	12	212
Long-term institutional outflows[1]	(163)	(45)	—	(23)	(29)	(260)
Long-term institutional flows, net	(29)	—	—	(2)	(17)	(48)
ETF flows, net	1	5	—	—	2	8
Cash fund flows, net	—	—	1	—	—	1
Total flows, net	(28)	5	1	(2)	(15)	(39)
Market appreciation	131	8	(2)	3	4	144
Foreign exchange impact	17	7	2	4	3	33
Total market/foreign exchange impact	148	15	—	7	7	177
Balance as of June 30, 2017	$1,594	$ 398	$ 334	$ 131	$ 149	$2,606

[1] Amounts represent long-term portfolios, excluding ETFs.
[2] Includes both floating- and constant-net-asset-value portfolios held in commingled structures or separate accounts.
[3] 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.
[4] Includes AUM acquired as part of the acquisition of GEAM on July 1, 2016.

The preceding table does not include approximately $14 billion of new asset management business which was awarded but not installed as of June 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 June 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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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 available-for-sale or held-to-maturity 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]

(In millions)	Six Months Ended June 30, 2017 Average Balance	2016 Average Balance
Assets:		
Interest-bearing deposits with banks	$51,031	$49,815
Securities purchased under resale agreements	2,205	2,581
Trading account assets	928	865
Investment securities	95,921	101,645
Loans and leases	20,607	18,639
Other interest-earning assets	22,882	22,617
Average total interest-earning assets	193,574	196,162
Cash and due from banks	3,224	3,317
Other non-interest-earning assets	24,779	26,932
Average total assets	$221,577	$226,411
Liabilities and shareholders' equity:		
Interest-bearing deposits:		
U.S.	$25,849	$28,729
Non-U.S.	97,201	94,708
Total interest-bearing deposits	123,050	123,437
Securities sold under repurchase agreements	3,961	4,173
Federal funds purchased	1	38
Other short-term borrowings	1,332	1,808
Long-term debt	11,469	11,013
Other interest-bearing liabilities	5,298	5,502
Average total interest-bearing liabilities	145,111	145,971
Non-interest-bearing deposits	43,241	43,495
Other non-interest-bearing liabilities	11,539	15,049
Preferred shareholders' equity	3,197	2,923

Common shareholders' equity	18,489	18,973
Average total liabilities and shareholders' equity	$221,577	$226,411

[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)	June 30, 2017	December 31, 2016
Available-for-sale:		
U.S. Treasury and federal agencies:		
Direct obligations	$633	$ 4,263
Mortgage-backed securities	11,414	13,257
Asset-backed securities:		
Student loans[1]	5,887	5,596
Credit cards	1,556	1,351
Sub-prime	243	272
Other	1,160	905
Total asset-backed securities	8,846	8,124
Non-U.S. debt securities:		
Mortgage-backed securities	6,962	6,535
Asset-backed securities	2,891	2,516
Government securities	6,600	5,836
Other	6,276	5,613
Total non-U.S. debt securities	22,729	20,500
State and political subdivisions	10,038	10,322
Collateralized mortgage obligations	2,443	2,593
Other U.S. debt securities	2,799	2,469
U.S. equity securities	45	42
Non-U.S. equity securities	1	3
U.S. money-market mutual funds	77	409
Non-U.S. money-market mutual funds	—	16
Total	$59,025	$ 61,998
Held-to-maturity[2]:		
U.S. Treasury and federal agencies:		
Direct obligations	$17,479	$ 17,527
Mortgage-backed securities	11,937	10,334
Asset-backed securities:		
Student loans[1]	2,738	2,883
Credit cards	858	897
Other	5	35
Total asset-backed securities	3,601	3,815
Non-U.S. debt securities:		
Mortgage-backed securities	1,084	1,150
Asset-backed securities	365	531
Government securities	357	286
Other	122	113
Total non-U.S. debt securities	1,928	2,080
Collateralized mortgage obligations	1,285	1,413
Total	$36,230	$ 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] At amortized cost or fair value on the date of transfer from available-for- sale.
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 June 30, 2017 and December 31, 2016.

TABLE 21: INVESTMENT PORTFOLIO BY EXTERNAL CREDIT RATING

	June 30, 2017		December 31, 2016	
AAA[1]	77	%	78	%
AA	14		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 June 30, 2017, the investment portfolio of 11,517 securities was diversified with respect to asset class. Approximately 53% of the aggregate carrying value of the portfolio as of June 30, 2017 was composed of mortgage-backed and asset-backed securities, compared to 52% as of December 31, 2016. The asset-backed securities portfolio, of which approximately 95% and 93% of the carrying value as of June 30, 2017 and December 31, 2016, respectively, was floating-rate, consisted primarily of student loan-backed and credit card-backed securities. Mortgage-backed securities were composed of securities issued by the Federal National Mortgage Association and Federal Home Loan Mortgage Corporation, 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 June 30, 2017, compared to approximately 23% as of December 31, 2016.
TABLE 22: NON-U.S. DEBT SECURITIES

(In millions)	June 30, 2017	December 31, 2016
Available-for-sale:		
United Kingdom	$5,593	$ 5,093
Australia	4,607	4,272
Canada	3,646	2,989
France	1,575	1,013
Netherlands	1,302	1,283
Japan	1,149	1,388
Italy	795	676
Belgium	745	360
Hong Kong	616	664
Germany	566	713
Norway	543	508
Spain	431	266
Sweden	430	188
Finland	213	223
South Korea	201	634
Ireland	140	85
Other[1]	177	145
Total	$22,729	$ 20,500
Held-to-maturity:		
United Kingdom	$468	$ 504
Netherlands	455	473
Australia	337	374
Singapore	242	180
Germany	201	329
Spain	102	98
Other[2]	123	122
Total	$1,928	$ 2,080

[1] Included approximately $93 million and $79 million as of June 30, 2017 and December 31, 2016, respectively, related to Portugal and Austria, all of which were related to mortgage-backed securities and auto loans.
[2] Included approximately $76 million and $80 million as of June 30, 2017 and December 31, 2016, respectively, related to Italy, Portugal and Norway, all of which were related to mortgage-backed securities and auto loans.
Approximately 89% and 88% of the aggregate carrying value of these non-U.S. debt securities was rated "AAA" or "AA" as of June 30, 2017 and December 31, 2016, respectively. 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 June 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 June 30, 2017, our non-U.S. debt securities had an average market-to-book ratio of 100.5%, and an aggregate pre-tax net unrealized gain of approximately $132 million, composed of gross unrealized gains of $170 million and gross unrealized losses of $38 million. These unrealized amounts included a pre-tax net unrealized gain of $59 million, composed of gross unrealized gains of $87 million and gross unrealized losses of $28 million, associated with non-U.S. debt securities available-for- sale.

As of June 30, 2017, the underlying collateral for non-U.S. mortgage- and asset-backed securities primarily included Australian, Dutch, Italian and U.K. prime mortgages and German automobile 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 automobile loans, prime mortgages, and corporate debt and covered bonds. The securities listed under “Japan” were substantially composed of Japanese government securities and corporate debt. The securities listed under “South Korea” were composed of South Korean government securities.

Municipal Obligations

We carried approximately $10.04 billion of municipal securities classified as state and political subdivisions in our investment securities portfolio as of June 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 $9.69 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 June 30, 2017					
State of Issuer:					
Texas	$ 1,745	$ 1,764	$3,509	18	%
California	488	2,268	2,756	14	
New York	759	1,288	2,047	10	
Massachusetts	903	1,093	1,996	10	
Washington	686	333	1,019	5	
Total	$ 4,581	$ 6,746	$11,327		
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 $19.73 billion and $19.57 billion across our businesses as of June 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 June 30, 2017. As of that date, approximately 38% and 58% of our aggregate municipal securities exposure was associated with general obligation and revenue bonds, respectively. In addition, we had no exposures associated with industrial development or land development bonds. 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 June 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

	June 30, 2017		
(In millions)	Amortized Cost	Net Unrealized Gains (Losses)	Fair Value
Available-for-sale[1]	$58,714	$ 311	$59,025
Held-to-maturity[1]	36,230	(61)	36,169
Total investment securities	$94,944	$ 250	$95,194
Net after-tax unrealized gain (loss)		$ 150	

	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[1]	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. HTM securities are carried at amortized cost, and unrealized gains and losses are not recorded in our consolidated financial statements.

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 second quarter of 2017 and $1 million in the second quarter of 2016.
Management considers the aggregate decline in fair value of the remaining investment securities and the resulting gross unrealized losses of $527 million as of June 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.
Our evaluation of potential OTTI of mortgage-backed securities with collateral in Spain, Italy, Ireland, and Portugal takes into account slow economic growth, austerity measures, and government intervention in the corresponding mortgage markets and assumes a conservative baseline macroeconomic environment. Our baseline view assumes a recessionary period characterized by high unemployment and by additional declines in housing prices between 3% and 23%. Our evaluation of OTTI in our base case does not assume a disorderly sovereign debt restructuring or a break-up of the Eurozone.

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Loans and Leases

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

(In millions)	June 30, 2017	December 31, 2016
Domestic:		
Commercial and financial	$19,227	$ 16,412
Commercial real estate	—	27
Lease financing	297	338
Total domestic	19,524	16,777
Non-U.S.:		
Commercial and financial	4,374	2,476
Lease financing	463	504
Total non-U.S.	4,837	2,980
Total loans and leases	$24,361	$ 19,757

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

As of June 30, 2017 and December 31, 2016, our investment in senior secured loans totaled approximately $3.8 billion and $3.5 billion, respectively. In addition, we had binding unfunded commitments as of June 30, 2017 and December 31, 2016 of $349 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 91% of the loans rated "BB" or "B" as of June 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 $1.9 billion and $1.4 billion as of June 30, 2017 and December 31, 2016, respectively.

As of June 30, 2017 and December 31, 2016, unearned income deducted from our investment in leveraged lease financing was $78 million and $94 million, respectively, for U.S. leases and $165 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 six months ended June 30, 2017 and the year ended December 31, 2016.

TABLE 26: ALLOWANCE FOR LOAN AND LEASE LOSSES

	Six Months Ended June 30,	
(In millions)	2017	2016
Allowance for loan and lease losses:		
Beginning balance	$53	$46
Provision for loan and lease losses[(1)]	1	8

Charge-offs[2]	—	(3)
Ending balance	$54	$51

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

As of June 30, 2017 approximately $46 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 $8 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.

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

TABLE 27: CROSS-BORDER OUTSTANDINGS[1]

(In millions)	Investment Securities and Other Assets	Derivatives and Securities on Loan	Total Cross-Border Outstandings
June 30, 2017			
United Kingdom	$ 19,110	$ 1,560	$ 20,670
Germany	16,336	465	16,801
Japan	10,845	544	11,389
Australia	5,450	319	5,769
Canada	4,250	929	5,179
Luxembourg	3,766	597	4,363
France	2,106	487	2,593
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 June 30, 2017, aggregate cross-border outstandings in countries which amounted to between 0.75% and 1% of our consolidated assets totaled approximately $2.20 billion to Switzerland. 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.

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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 June 30, 2017, the value of our Parent Company's net liquid assets decreased to $1.10 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. As of June 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.

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 in "Supervision and Regulation" 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 mortgage-backed securities), 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 June 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. Our average HQLA under the LCR final rule definition was $78.44 billion and $87.20 billion, post-prescribed haircuts, as of June 30, 2017 and December 31, 2016, respectively.

TABLE 28: COMPONENTS OF AVERAGE HQLA
BY TYPE OF ASSET

	Quarters Ended	
(In millions)	June 30, 2017	December 31, 2016
Excess Central Bank Balances	$47,464	$ 48,407
U.S. Treasuries	13,022	17,770
Other Investment securities	12,612	15,442
Foreign government	5,344	5,585
Total	$78,442	$ 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 $47.46 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 June 30, 2017 compared to quarter-end December 31, 2016 was due to normal deposit volatility. The decrease in other investment securities as of June 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 June 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 $45.77 billion as of June 30, 2017, compared to $65.64 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. We had unfunded commitments to extend credit with gross contractual amounts totaling $26.71 billion and $26.99 billion as of June 30, 2017 and December 31, 2016, respectively. These amounts do not reflect the value of any collateral. As of June 30, 2017, approximately 72% 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 to the Federal Reserve and FDIC on June 30, 2017.

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 in "Business-Supervision and Regulation-Resolution Planning" 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 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. State Street Bank’s next IDI plan is due in October 2017.

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. We invest these client deposits in a combination of investment securities and short-duration financial instruments whose mix is determined by the characteristics of the deposits.

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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: CLIENT DEPOSITS

	June 30,		Average Balance Six Months Ended June 30,	
(In millions)	2017	2016	2017	2016
Client deposits[1]	$179,743	$177,065	$159,664	$152,143

[1] Balances as of June 30, 2017 and 2016 excluded term wholesale CDs of $1.67 billion and $16.06 billion, respectively; average balances for the quarters ended June 30, 2017 and 2016 excluded average CDs of $6.63 billion and $14.79 billion, respectively.

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 June 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 $1.07 billion as of June 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 June 30, 2017, there was no balance outstanding on this line of credit.

Long-Term Funding

As of June 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 June 30, 2017, $3.25 billion was available for issuance pursuant to this authority. As of June 30, 2017, State Street Bank also had Board

authority to issue an additional $500 million of subordinated debt.

State Street Corporation maintains an effective universal shelf registration 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. The issuance of debt or equity securities will depend on future market conditions, funding needs and other factors.

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 June 30, 2017, the notional amount of these derivative contracts was $1.61 trillion, of which $1.59 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.

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

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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 June 30, 2017 and March 31, 2017.

The following tables present VaR and stressed VaR associated with our trading activities for covered positions held during the quarters ended June 30, 2017 and March 31, 2017, and as of June 30, 2017 and March 31, 2017, as measured by our VaR methodology:

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

	Quarter Ended June 30, 2017			Quarter Ended March 31, 2017			As of June 30, 2017	As of March 31, 2017
(In thousands)	Average	Maximum	Minimum	Average	Maximum	Minimum	VaR	VaR
Global Markets	$7,759	$ 16,160	$ 4,590	$6,614	$ 13,090	$ 2,566	$7,577	$8,599
Global Treasury	433	1,408	89	645	832	421	528	421
Total VaR	$7,740	$ 16,119	$ 4,598	$6,595	$ 12,971	$ 2,544	$7,481	$8,475

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

	Quarter Ended June 30, 2017			Quarter Ended March 31, 2017			As of June 30, 2017	As of March 31, 2017
(In thousands)	Average	Maximum	Minimum	Average	Maximum	Minimum	Stressed VaR	Stressed VaR
Global Markets	$26,691	$ 44,875	$ 14,301	$31,676	$ 43,001	$ 13,704	$15,192	$32,115
Global Treasury	4,814	12,329	1,321	10,892	17,019	6,609	6,223	7,396
Total Stressed VaR	$26,934	$ 43,754	$ 14,646	$34,846	$ 46,895	$ 18,119	$14,943	$33,745

The three month average of our stressed VaR-based measure was approximately $27 million for the quarter ended June 30, 2017, compared to an average of approximately $35 million for the quarter ended March 31, 2017.
The decrease in the total stressed VaR-based measures as of June 30, 2017, compared to March 31, 2017, was mainly driven by lower interest rate risk in emerging market currencies as of June 30, 2017 as compared to March 31, 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.

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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 June 30, 2017 and March 31, 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]

(In thousands)	As of June 30, 2017			As of March 31, 2017		
	Foreign Exchange Risk	Interest Rate Risk	Volatility Risk	Foreign Exchange Risk	Interest Rate Risk	Volatility Risk
By component:						
Global Markets	$6,167	$3,042	$ 506	$6,107	$3,682	$ 263
Global Treasury	59	552	—	53	436	—
Total VaR	$6,186	$3,035	$ 506	$6,134	$3,579	$ 263

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

(In thousands)	As of June 30, 2017			As of March 31, 2017		
	Foreign Exchange Risk	Interest Rate Risk	Volatility Risk	Foreign Exchange Risk	Interest Rate Risk	Volatility Risk
By component:						
Global Markets	$10,514	$13,872	$ 520	$6,750	$34,006	$ 324
Global Treasury	104	6,439	—	78	7,489	—
Total Stressed VaR	$10,570	$15,036	$ 520	$6,770	$35,574	$ 324

[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 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 basis point 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 basis point instantaneous shock, approximately 80% of the 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 basis point instantaneous shock, approximately 50% of the benefit is driven by U.S. rates.

TABLE 34: NII SENSITIVITY

(In millions)	June 30, 2017	December 31, 2016
Rate change:	Benefit (Exposure)	
+100 bps shock	$523	$ 585
–100 bps shock	(356)	(265)
+100 bps ramp	228	284
–100 bps ramp	(146)	(161)

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As of June 30, 2017, NII sensitivity remains positioned to benefit from rising interest rates. Compared to December 31, 2016, the decreased benefit to the up 100 basis point 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 basis point 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 basis point 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)	June 30, 2017	December 31, 2016
Rate change:	Benefit (Exposure)	
+200 bps shock	$(945)	$ (1,092)
–200 bps shock	135	877

As of June 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 level and mix of client deposits. The -200 basis point 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.

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 common equity tier 1 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 five equally-weighted components: 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 2x multiplier to the sum of the five components

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, 2016 is calculated to be 1.5%. Assuming completion of the phase-in period for the capital conservation buffer, and a countercyclical buffer of 0%, the minimum capital ratios as of January 1, 2019, including a capital conservation buffer of 2.5% and G-SIB surcharge of 1.5% in 2019, would be 10.0% for tier 1 risk-based capital, 12.0% for total risk-based capital, and 8.5% for common equity tier 1 capital, in order for State Street 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% 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 2047 and 2028 as TLAC eligible debt. Based upon current estimates, assumptions and guidance, we project that compliance with TLAC will result in increasing our outstanding TLAC eligible long-term debt by approximately $1 billion at December 31, 2018 compared to the TLAC eligible debt outstanding at June 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.

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 common equity tier 1 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 common equity tier 1 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 common equity tier 1 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 common equity tier 1 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.

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) (2)]

	2015	2016	2017	2018	2019
Capital conservation buffer (Common Equity Tier 1)	— %	0.625 %	1.250 %	1.875 %	2.500 %
G-SIB surcharge (CET1)[(1)]	—	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)] 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 common equity tier 1, 10.0% for tier 1 capital and 12.0% for total capital.
[(2)] Minimum ratios shown above do not reflect the countercyclical buffer, currently set at zero by U.S. banking regulators.
[(3)] Minimum common equity tier 1 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 June 30, 2017(1)	Basel III Standardized Approach June 30, 2017(2)	Basel III Advanced Approaches December 31, 2016(1)	Basel III Standardized Approach December 31, 2016(2)	Basel III Advanced Approaches June 30, 2017(1)	Basel III Standardized Approach June 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	18,202	18,202	17,459	17,459	12,188	12,188	12,285	12,285
Accumulated other comprehensive income (loss)	(1,266)	(1,266)	(1,936)	(1,936)	(1,060)	(1,060)	(1,648)	(1,648)
Treasury stock, at cost	(8,367)	(8,367)	(7,682)	(7,682)	—	—	—	—
Total	18,876	18,876	18,127	18,127	22,510	22,510	22,013	22,013
Regulatory capital adjustments:								
Goodwill and other intangible assets, net of associated deferred tax liabilities(3)	(6,714)	(6,714)	(6,348)	(6,348)	(6,417)	(6,417)	(6,060)	(6,060)
Other adjustments	(155)	(155)	(155)	(155)	(91)	(91)	(148)	(148)
Common equity tier 1 capital	12,007	12,007	11,624	11,624	16,002	16,002	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	(38)	(38)	(103)	(103)	—	—	—	—
Tier 1 capital	15,165	15,165	14,717	14,717	16,002	16,002	15,805	15,805
Qualifying subordinated long-term debt	1,074	1,074	1,172	1,172	1,078	1,078	1,179	1,179
Trust preferred capital securities phased out of tier 1 capital	—	—	—	—	—	—	—	—
ALLL and other	4	75	19	77	—	75	15	77
Other adjustments	—	—	1	1	—	—	—	—
Total capital	$16,243	$16,314	$15,909	$15,967	$17,080	$17,155	$16,999	$17,061
Risk-weighted assets:								
Credit risk	$52,755	$105,785	$50,900	$98,125	$50,010	$102,642	$47,383	$94,413
Operational risk(4)	44,123	NA	44,579	NA	43,552	NA	44,043	NA
Market risk(5)	3,387	1,284	3,822	1,751	3,388	1,284	3,822	1,751
	$100,265	$107,069	$99,301	$99,876	$96,950	$103,926	$95,248	$96,164

Total risk-weighted assets										
Adjusted quarterly average assets			$216,940	$216,940	$226,310	$226,310	$214,022	$214,022	$222,584	$222,584
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]								
Common equity tier 1 capital	6.5 %	5.5 %	12.0 %	11.2 %	11.7 %	11.6 %	16.5 %	15.4 %	16.6 %	16.4 %
Tier 1 capital	8.0	7.0	15.1	14.2	14.8	14.7	16.5	15.4	16.6	16.4
Total capital	10.0	9.0	16.2	15.2	16.0	16.0	17.6	16.5	17.8	17.7
Tier 1 leverage	4.0	4.0	7.0	7.0	6.5	6.5	7.5	7.5	7.1	7.1

[1] Common equity tier 1 capital, tier 1 capital and total capital ratios as of June 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 June 30, 2017 and December 31, 2016 were calculated in conformity with the Basel III final rule.
[2] Common equity tier 1 capital, tier 1 capital and total capital ratios as of June 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 June 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 June 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 June 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

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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 common equity tier 1 capital increased $383 million as of June 30, 2017 compared to December 31, 2016 primarily due to net income of $1.12 billion and an increase in accumulated other comprehensive income of $670 million. The increases in common equity tier 1 capital were partially offset by capital distributions of $1.13 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 $448 million, due to the increase in common equity tier 1 capital. Total capital increased $334 million under advanced approaches and increased $347 million under standardized approach due to the changes to tier 1 capital. State Street Bank's tier 1 capital increased $197 million, and total capital increased $81 million and $94 million under the advanced and standardized approaches, respectively, as of June 30, 2017, compared to December 31, 2016. The increase is a result of higher common equity tier 1.

The table below presents a roll-forward of common equity tier 1 capital, tier 1 capital and total capital for the quarter ended June 30, 2017 and for the year ended December 31, 2016.
TABLE 38: CAPITAL ROLL-FORWARD

	State Street			
(In millions)	Basel III Advanced Approaches June 30, 2017	Basel III Standardized Approach June 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	1,122	1,122	2,143	2,143
Changes in treasury stock, at cost	(685)	(685)	(1,225)	(1,225)
Dividends declared	(377)	(377)	(732)	(732)
Goodwill and other intangible assets, net of associated deferred tax liabilities	(366)	(366)	(421)	(421)
Effect of certain items in accumulated other comprehensive income (loss)	670	670	(514)	(514)
Other adjustments	19	19	(60)	(60)
Changes in common equity tier 1 capital	383	383	(809)	(809)
Common equity tier 1 capital balance, end of period	12,007	12,007	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	383	383	(809)	(809)
Net issuance of preferred stock	—	—	493	493
Trust preferred capital securities phased out of tier 1 capital	—	—	(237)	(237)
Other adjustments	65	65	6	6
Changes in tier 1 capital	448	448	(547)	(547)

Tier 1 capital balance, end of period	15,165	15,165	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	(98)	(98)	(186)	(186)
Trust preferred capital securities phased into tier 2 capital	—	—	(713)	(713)
Changes in ALLL and other	(15)	(2)	7	11
Change in other adjustments	(1)	(1)	(1)	(1)
Changes in tier 2 capital	(114)	(101)	(893)	(889)
Tier 2 capital balance, end of period	1,078	1,149	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	448	448	(547)	(547)
Changes in tier 2 capital	(114)	(101)	(893)	(889)
Total capital balance, end of period	$16,243	$ 16,314	$ 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 June 30, 2017 and for the year ended December 31, 2016.
TABLE 39: ADVANCED APPROACHES RWA ROLL-FORWARD

	State Street	
(In millions)	June 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	1,268	(1,027)
Net increase (decrease) in loans and leases	1,771	575
Net increase (decrease) in securitization exposures	391	(3,246)
Net increase (decrease) in repo-style transaction exposures	468	606
Net increase (decrease) in OTC derivatives exposures	51	1,812
Net increase (decrease) in all other[(1)]	(2,094)	447
Net increase (decrease) in credit risk-weighted assets	1,855	(833)
Net increase (decrease) in credit valuation adjustment	32	512
Net increase (decrease) in market risk-weighted assets	(467)	(627)
Net increase (decrease) in operational risk-weighted assets	(456)	697
Total risk-weighted assets, end of period	$100,265	$99,301

(1) Includes assets not in a definable category, cleared transactions, non-material portfolio, other wholesale, cash and due from, and interest-bearing deposits with banks, equity exposures, and 6% credit risk supervisory charge.
As of June 30, 2017, total advanced approaches risk-weighted assets increased $964 million compared to December 31, 2016, mainly due to an increase in credit risk, partially offset by a decrease in market risk and operational risk. The increase in credit risk was mainly due to an increase in leveraged loans stemming from a new LGD model being introduced, cash and overdrafts. Market risk reduction of $467 million is resulting from a lower stressed VaR. Operational risk decreased approximately $456 million due to an decrease in loss event frequency in the external fraud-investment loss category. The increase in credit valuation adjustment was driven by increased volatility in our FX derivative portfolios, leading to a higher positive market valuation.
As of December 31, 2016, total advanced approaches risk-weighted assets decreased $251 million compared to December 31, 2015, mainly due to a decrease in credit risk and market risk, partially offset by an increase in operational risk and credit valuation adjustment. The decrease in credit risk was mainly due to a decrease in securitization exposures as a result of sell-offs and maturities as well as calls

of agency debt securities within our wholesale investment portfolio, partially offset by an increase in derivatives exposure from marked-to-market FX contracts stemming from a stronger dollar and an increase in securities finance agency lending. The market risk decrease was a result of reduced end of day positions in FX and interest rate risk. Operational risk increased approximately $700 million mainly due to an increase in loss event frequency. The increase in credit valuation adjustment was driven by an increase in the market valuation FX contracts.
The following table presents a roll-forward of the Basel III standardized approach risk-weighted assets for the quarter ended June 30, 2017 and year ended December 31, 2016.
TABLE 40: STANDARDIZED APPROACH RWA ROLL-FORWARD

	State Street	
(In millions)	June 30, 2017	December 31, 2016
Total estimated risk-weighted assets, beginning of period[(1)]	$99,876	$95,893
Changes in credit risk-weighted assets:		

Net increase (decrease) in investment securities-wholesale	1,140	(1,471)
Net increase (decrease) in loans and leases	3,943	998
Net increase (decrease) in securitization exposures	382	(3,144)
Net increase (decrease) in repo-style transaction exposures	3,576	4,994
Net increase (decrease) in OTC derivatives exposures	(1,684)	3,462
Net increase (decrease) in all other[2]	303	(229)
Net increase (decrease) in credit risk-weighted assets	7,660	4,610
Net increase (decrease) in market risk-weighted assets	(467)	(627)
Total risk-weighted assets, end of period	$107,069	$99,876

[1] Standardized approach risk-weighted assets as of the periods noted above were calculated using State Street's estimates, based on our then current interpretation of the Basel III final rule.
[2] Includes assets not in a definable category, cleared transactions, other wholesale, cash and due from, and interest-bearing deposits with banks and equity exposures.
As of June 30, 2017, total standardized approach risk-weighted assets increased $7.19 billion compared to December 31, 2016, primarily the result of an increase in credit risk partially offset by a decrease in market risk resulting from a lower stressed VaR. The main drivers of the credit risk change are an increase in equities within the securities finance portfolio of $3.20 billion, an increase in overdrafts of $3.18 billion due to an increase in U.S. short-duration advances to clients and an increase in the investment portfolio offset by a decrease in FX contracts due to a mix shift to counterparties with a lower weighted-average risk-weight.

As of December 31, 2016, total standardized approach risk-weighted assets increased $3.98 billion compared to December 31, 2015, primarily the result of an increase in securities finance agency lending, an increase in market values of FX contracts, partially offset by a decrease in securitization exposures, wholesale investments and market risk. The decrease in securitization was due to sell-offs and maturities while the decrease in wholesale investments was due to calls of agency debt securities. Market risk reduction is resulting from lower stressed VaR.

The regulatory capital ratios as of June 30, 2017, presented in Table 37: Regulatory Capital Structure and Related Regulatory Capital Ratios, are calculated under the standardized approach and advanced approaches in conformity with the Basel III final rule. The advanced approaches-based ratios (actual and estimated pro forma) reflect calculations and determinations with respect to our capital and related matters as of June 30, 2017, based on State Street and external data, quantitative formulae, statistical models, historical correlations and assumptions, collectively referred to as "advanced systems," in effect and used by State Street for those purposes as of the time we first reported such ratios in a quarterly report on Form 10-Q. Significant components of these advanced systems involve the exercise of judgment by us and our regulators, and our advanced systems may not, individually or collectively, precisely represent or calculate the scenarios, circumstances, outputs or other results for which they are designed or intended.

Our advanced systems are subject to update and periodic revalidation in response to changes in our business activities and our historical experiences, forces and events experienced by the market broadly or by individual financial institutions, changes in regulations and regulatory interpretations and other factors, and are also subject to continuing regulatory review and approval. For example, a significant operational loss experienced by another financial institution, even if we do not experience a related loss, could result in a material change in the output of our advanced systems and a corresponding material change in our risk exposures, our total risk-weighted assets and our capital ratios compared to prior periods. An operational loss that we experience could also result in a material change in our capital requirements for operational risk under the advanced approaches, depending on the severity of the loss event, its characterization among the seven Basel-defined UOMs, and the stability of the distributional approach for a particular UOM, and without direct correlation to the effects of the loss event, or the timing of such effects, on our results of operations.

Due to the influence of changes in these advanced systems, whether resulting from changes in data inputs, regulation or regulatory supervision or interpretation, State Street-specific or market activities or experiences or other updates or factors, we expect that our advanced systems and our capital ratios calculated in conformity with the Basel III final rule will change and may be volatile over time, and that those latter changes or volatility could be material as calculated and measured from period to period. Models implemented under the Basel III final rule, particularly those implementing the advanced approaches, remain subject to regulatory review and approval. The full effects of the Basel III final rule on State Street and State Street Bank are therefore subject to further evaluation and also to further regulatory guidance, action or rule-making.

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Estimated Basel III Fully Phased-in Capital Ratios

Table 41: Regulatory Capital Structure and Related Regulatory Capital Ratios - State Street, and Table 42: Regulatory Capital Structure and Related Regulatory Capital Ratios - State Street Bank, present our capital ratios for State Street and State Street Bank as of June 30, 2017, calculated in conformity with the advanced approaches provisions and standardized approach of the Basel III final rule on a pro forma basis under the fully phased-in provisions of the Basel III final rule.

TABLE 41: REGULATORY CAPITAL STRUCTURE AND RELATED REGULATORY CAPITAL RATIOS - STATE STREET

June 30, 2017 (In millions)	Basel III Advanced Approaches	Phase-In Provisions	Basel III Advanced Approaches Fully Phased-In Pro-Forma Estimate	Basel III Standardized Approach	Phase-In Provisions	Basel III Standardized Approach Fully Phased-In Pro-Forma Estimate
Total common shareholders' equity	$18,876	$(3)	$18,873	$18,876	$(3)	$18,873
Regulatory capital adjustments:						
Goodwill and other intangible assets, net of associated deferred tax liabilities	(6,714)	(273)	(6,987)	(6,714)	(273)	(6,987)
Other adjustments	(155)	(39)	(194)	(155)	(39)	(194)
Common equity tier 1 capital	12,007	(315)	11,692	12,007	(315)	11,692
Additional tier 1 capital:						
Preferred stock	3,196	—	3,196	3,196	—	3,196
Trust preferred capital securities	—	—	—	—	—	—
Other adjustments	(38)	38	—	(38)	38	—
Additional tier 1 capital	3,158	38	3,196	3,158	38	3,196
Tier 1 capital	15,165	(277)	14,888	15,165	(277)	14,888
Tier 2 capital:						
Qualifying subordinated long-term debt	1,074	—	1,074	1,074	—	1,074
Trust preferred capital securities	—	—	—	—	—	—
ALLL and other	4	—	4	75	—	75
Tier 2 capital	1,078	—	1,078	1,149	—	1,149
Total capital	$16,243	$(277)	$15,966	$16,314	$(277)	$16,037
Risk weighted assets	$100,265	$66	$100,331	$107,069	$62	$107,131
Adjusted average assets	216,940	(205)	216,735	216,940	(205)	216,735
Total assets for SLR	243,910	(205)	243,705	243,910	(205)	243,705

Capital ratios[1]:	Minimum Requirement	Minimum Requirement Including Capital Conservation Buffer	Minimum Requirement Including Capital Conservation Buffer

		and G-SIB Surcharge 2017	and G-SIB Surcharge 2019				
Common equity tier 1 capital[2]	4.5 %	6.5 %	8.5 %	12.0 %	11.7 %	11.2 %	10.9 %
Tier 1 capital	6.0	8.0	10.0	15.1	14.8	14.2	13.9
Total capital	8.0	10.0	12.0	16.2	15.9	15.2	15.0
Tier 1 leverage	4.0	NA	NA	7.0	6.9	7.0	6.9
Supplementary leverage	5.0	NA	NA	6.2	6.1	6.2	6.1

(1) Common equity tier 1 ratio is calculated by dividing common equity tier 1 capital (numerator) by risk-weighted assets (denominator); tier 1 capital ratio is calculated by dividing tier 1 capital (numerator) by risk-weighted assets (denominator); total capital ratio is calculated by dividing total capital (numerator) by risk-weighted assets (denominator); tier 1 leverage ratio is calculated by dividing tier 1 capital (numerator) by adjusted average assets (denominator); and supplementary leverage ratio, or SLR, is calculated by dividing tier 1 capital (numerator) by total assets for SLR (denominator).
(2) Common equity tier 1 ratios were calculated in conformity with the provisions of the Basel III final rule; refer to Table 37: Regulatory Capital Structure and Related Regulatory Capital Ratios.
NA Not applicable

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TABLE 42: REGULATORY CAPITAL STRUCTURE AND RELATED REGULATORY CAPITAL RATIOS - STATE STREET BANK

June 30, 2017 (In millions)	Basel III Advanced Approaches	Phase-In Provisions	Basel III Advanced Approaches Fully Phased-In Pro-Forma Estimate	Basel III Standardized Approach	Phase-In Provisions	Basel III Standardized Approach Fully Phased-In Pro-Forma Estimate
Total common shareholders' equity	$22,510	$—	$22,510	$22,510	$—	$22,510
Regulatory capital adjustments:						
Goodwill and other intangible assets, net of associated deferred tax liabilities	(6,417)	(264)	(6,681)	(6,417)	(264)	(6,681)
Other adjustments	(91)	—	(91)	(91)	—	(91)
Common equity tier 1 capital	16,002	(264)	15,738	16,002	(264)	15,738
Additional tier 1 capital:						
Preferred stock	—	—	—	—	—	—
Other adjustments	—	—	—	—	—	—
Additional tier 1 capital	—	—	—	—	—	—
Tier 1 capital	16,002	(264)	15,738	16,002	(264)	15,738
Tier 2 capital:						
Qualifying subordinated long-term debt	1,078	—	1,078	1,078	—	1,078
ALLL and other	—	—	—	75	—	75
Tier 2 capital	1,078	—	1,078	1,153	—	1,153
Total capital	$17,080	$(264)	$16,816	$17,155	$(264)	$16,891
Risk weighted assets	$96,950	$(245)	$96,705	$103,926	$(232)	$103,694
Adjusted average assets	214,022	(197)	213,825	214,022	(197)	213,825
Total assets for SLR	240,919	(197)	240,722	240,919	(197)	240,722

Capital ratios[1]:	Minimum Requirement	Minimum Requirement Including Capital Conservation Buffer and G-SIB Surcharge 2017	Minimum Requirement Including Capital Conservation Buffer and G-SIB Surcharge 2019				
Common equity tier 1 capital[2]	4.5 %	6.5 %	8.5 %	16.5 %	16.3 %	15.4 %	15.2 %
Tier 1 capital	6.0	8.0	10.0	16.5	16.3	15.4	15.2
Total capital	8.0	10.0	12.0	17.6	17.4	16.5	16.3
Tier 1 leverage	4.0	NA	NA	7.5	7.4	7.5	7.4
Supplementary leverage	6.0	NA	NA	6.6	6.5	6.6	6.5

(1) Common equity tier 1 capital ratio is calculated by dividing common equity tier 1 capital (numerator) by risk-weighted assets (denominator); tier 1 capital ratio is calculated by dividing tier 1 capital (numerator) by risk-weighted assets (denominator); total capital ratio is calculated by dividing total capital (numerator) by risk-weighted assets (denominator); tier 1 leverage ratio is calculated by dividing tier 1 capital (numerator) by adjusted average assets (denominator); and supplementary leverage ratio is calculated by dividing tier 1 capital (numerator) by total assets for SLR (denominator).
(2) Common equity tier 1 ratios were calculated in conformity with the provisions of the Basel III final rule; refer to Table 37: Regulatory Capital Structure and Related Regulatory Capital Ratios.
NA Not applicable
Fully phased-in pro-forma estimates of common shareholders' equity include 100% of accumulated other comprehensive income, including accumulated other comprehensive income attributable to available-for-sale securities, cash flow hedges and defined benefit pension plans. Fully phased-in pro-forma estimates of common equity tier 1 capital reflect 100% of applicable deductions, including but not limited to, intangible assets net of deferred tax liabilities. Fully phased-in tier 1 capital reflects the transition of trust preferred capital securities from tier 1 capital to tier 2 capital. For both Basel III advanced and standardized approaches, fully phased-in pro-forma estimates of risk-weighted assets reflect the exclusion of intangible assets, offset by additions related to non-significant equity exposures and deferred tax assets related to temporary differences.

The Volcker rule, including the required capital deduction for investments in a covered fund, became effective on July 21, 2015, for investments in and relationships with a covered fund made after December 31, 2013. For legacy covered funds, the Volcker rule capital deduction became effective on July 21, 2017. For additional information on the Volcker rule, refer to pages 9 to 10 under “Regulatory Capital Adequacy and Liquidity Standards” in "Supervision and Regulation" included under Item 1, Business, in our 2016 Form 10-K.

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Supplementary Leverage Ratio

In 2014, U.S. banking regulators issued final rules implementing an SLR, for certain bank holding companies, like State Street, and their insured depository institution subsidiaries, like State Street Bank, which we refer to as the SLR final rule. Upon implementation, the SLR final rule requires that, as of January 1, 2018, (i) State Street Bank maintain an SLR of at least 6% to be well capitalized under the U.S. banking regulators' PCA framework and (ii) State Street maintain an SLR of at least 5% to avoid

limitations on capital distributions and discretionary bonus payments. In addition to the SLR, State Street is subject to a minimum tier 1 leverage ratio of 4%, which differs from the SLR primarily in that the denominator of the tier 1 leverage ratio is only a quarterly average of on-balance sheet assets and does not include any off-balance sheet exposures. Beginning with reporting for March 31, 2015, State Street was required to include SLR disclosures, calculated on a transitional basis, with its other Basel disclosures.

TABLE 43: SUPPLEMENTARY LEVERAGE RATIO

June 30, 2017 (Dollars in millions)	Transitional SLR	Phase-In Provisions	Fully Phased-in Pro-Forma SLR Estimate
State Street:			
Tier 1 capital	$15,165	$(277)	$14,888
On-and off-balance sheet leverage exposure	250,543	—	250,543
Less: regulatory deductions	(6,633)	(205)	(6,838)
Total assets for SLR	$243,910	$(205)	$243,705
Supplementary leverage ratio	6.2%	(0.1)%	6.1%
State Street Bank:			
Tier 1 capital	$16,002	$(264)	$15,738
On-and off-balance sheet leverage exposure	247,156	—	247,156
Less: regulatory deductions	(6,237)	(197)	(6,434)
Total assets for SLR	$240,919	$(197)	$240,722
Supplementary leverage ratio	6.6%	(0.1)%	6.5%

Capital Actions

Preferred Stock

The following table summarizes selected terms of each of the series of the preferred stock issued and outstanding as of June 30, 2017:

TABLE 44: PREFERRED STOCK ISSUED AND OUTSTANDING

	Issuance Date	Depositary Shares Issued	Ownership Interest Per Depositary Share	Liquidation Preference Per Share	Liquidation Preference Per Depositary Share	Net Proceeds of Offering (In millions)	Redemption Date[1]
Preferred Stock[2]:							
Series C	August 2012	20,000,000	1/4,000th	$100,000	$ 25	$ 488	September 15, 2017

Series D	February 2014	30,000,000	1/4,000th	100,000	25	742	March 15, 2024
Series E	November 2014	30,000,000	1/4,000th	100,000	25	728	December 15, 2019
Series F	May 2015	750,000	1/100th	100,000	1,000	742	September 15, 2020
Series G	April 2016	20,000,000	1/4,000th	100,000	25	493	March 15, 2026

(1) On the redemption date, or any dividend declaration date thereafter, the preferred stock and corresponding depositary shares may be redeemed by us, in whole or in part, at the liquidation price per share and liquidation price per depositary share plus any declared and unpaid dividends, without accumulation of any undeclared dividends.
(2) The preferred stock and corresponding depositary shares may be redeemed at our option in whole, but not in part, prior to the redemption date upon the occurrence of a regulatory capital treatment event, as defined in the certificate of designation, at a redemption price equal to the liquidation price per share and liquidation price per depositary share plus any declared and unpaid dividends, without accumulation of any undeclared dividends.

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The following tables present the dividends declared for each of the series of preferred stock issued and outstanding for the periods indicated:

TABLE 45: PREFERRED STOCK DIVIDENDS QUARTERS TO DATE

	Quarters Ended June 30,					
	2017			2016		
	Dividends Declared per Share	Dividends Declared per Depositary Share	Total (In millions)[1]	Dividends Declared per Share	Dividends Declared per Depositary Share	Total (In millions)
Preferred Stock:						
Series C	$1,313	$ 0.33	$ 7	$1,313	$ 0.33	$ 6
Series D	1,475	0.37	11	1,475	0.37	11
Series E	1,500	0.38	11	1,500	0.38	11
Series F	—	—	—	—	—	—
Series G	1,338	0.33	7	951	0.24	5
Total			$ 36			$ 33

TABLE 46: PREFERRED STOCK DIVIDENDS

	Six Months Ended June 30,					
	2017			2016		
	Dividends Declared per Share	Dividends Declared per Depositary Share	Total (In millions)	Dividends Declared per Share	Dividends Declared per Depositary Share	Total (In millions)
Preferred Stock:						
Series C	$2,626	$ 0.66	$ 13	$2,626	$ 0.66	$ 13
Series D	2,950	0.74	22	2,950	0.74	22
Series E	3,000	0.76	22	3,000	0.76	22
Series F	2,625	26.25	20	2,625	26.25	20
Series G	2,676	0.66	14	951	0.24	5
Total			$ 91			$ 82

[1] Dividends were paid in June 2017.

In July 2017, we declared dividends on our Series C, D, E, F and G preferred stock of approximately $1,313, $1,475, $1,500, $2,625 and $1,338, respectively, per share, or approximately $0.33, $0.37, $0.38, $26.25 and $0.33, respectively, per depositary share. These dividends total approximately $6 million, $11 million, $11 million, $20 million and $7 million on our Series C, D, E, F and G preferred stock, respectively, which will be paid in September 2017.

Common Stock

In June 2017, our Board approved a common stock purchase program authorizing the purchase of up to $1.4 billion of our common stock through June 30, 2018 (the 2017 Program). No shares were purchased by us under this program in the quarter ended June 30, 2017.

In June 2016, our Board approved a common stock purchase program authorizing the purchase of up to $1.4 billion of our common stock through June 30, 2017 (the 2016 Program). The table below presents the activity under the 2016 Program during the periods indicated:

TABLE 47: SHARES REPURCHASED

	Quarter Ended June 30, 2017			Six Months Ended June 30, 2017		
	Shares Acquired (In millions)	Average Cost per Share	Total Acquired (In millions)	Shares Acquired (In millions)	Average Cost per Share	Total Acquired (In millions)
2016 Program[1]	2.7	$ 83.84	$ 227	9.4	$ 79.93	$ 750

[1] Includes $158 million relating to shares acquired in exchange for BFDS stock during the first quarter of 2017. Additional information about the exchange is provided in Note 1 to the consolidated financial statements included in this Form 10-Q.

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The table below presents the dividends declared on common stock for the periods indicated:

TABLE 48: COMMON STOCK DIVIDENDS

	Quarters Ended June 30,				Six Months Ended June 30,			
	2017		2016		2017		2016	
	Dividends Declared per Share	Total (In millions)	Dividends Declared per Share	Total (In millions)	Dividends Declared per Share	Total (In millions)	Dividends Declared per Share	Total (In millions)
Common Stock	$0.38	$ 142	$0.34	$ 133	$0.76	$ 286	$0.68	$ 268

Federal and state banking regulations place certain restrictions on dividends paid by subsidiary banks to the parent holding company. In addition, banking regulators have the authority to prohibit bank holding companies from paying dividends. For information concerning limitations on dividends from our subsidiary banks, refer to pages 49 to 50 in "Related Stockholder Matters" included under Item 5, Market for Registrant's Common Equity, Related Stockholder Matters and Issuer Purchases of Equity Securities, and to Note 15 on pages 176 to 178 to the consolidated financial statements included under Item 8, Financial Statements and Supplementary Data, in our 2016 Form 10-K. Our common stock and preferred stock dividends, including the declaration, timing and amount thereof, are subject to consideration and approval by the Board at the relevant times.

Stock purchases may be made using various types of mechanisms, including open market purchases, accelerated share repurchases or transactions off market, and may be made under Rule 10b5-1 trading programs. The timing of stock purchases, types of transactions and number of shares purchased will depend on several factors, including, market conditions and State Street's capital positions, its financial performance and investment opportunities. The common stock purchase program does not have specific price targets and may be suspended at any time.

OFF-BALANCE SHEET ARRANGEMENTS

On behalf of clients enrolled in our securities lending program, we lend securities to banks, broker/dealers and other institutions. In most circumstances, we indemnify our clients for the fair market value of those securities against a failure of the borrower to return such securities. Though these transactions are collateralized, the substantial volume of these activities necessitates detailed credit-based underwriting and monitoring processes. The aggregate amount of indemnified securities on loan totaled $370.47 billion as of June 30, 2017, compared to $360.45 billion as of December 31, 2016. We require the borrower to provide collateral in an amount in excess of 100% of the fair market value of the securities borrowed. We hold the collateral received in connection with these securities lending services as agent, and the collateral is not recorded in our consolidated statement of condition. We revalue the securities on loan and the collateral daily to determine if additional collateral is necessary or if excess collateral is required to be returned to the borrower. We held, as agent, cash and securities totaling $387.75 billion and $377.92 billion as collateral for indemnified securities on loan as of June 30, 2017 and December 31, 2016, respectively.

The cash collateral held by us as agent is invested on behalf of our clients. In certain cases, the cash collateral is invested in third-party repurchase agreements, for which we indemnify the client against loss of the principal invested. We require the counterparty to the indemnified repurchase agreement to provide collateral in an amount in excess of 100% of the amount of the repurchase agreement. In our role as agent, the indemnified repurchase agreements and the related collateral held by us are not recorded in our consolidated statement of condition. Of the collateral of $387.75 billion and $377.92 billion, referenced above, $64.82 billion and $60.00 billion was invested in indemnified repurchase agreements as of June 30, 2017 and December 31, 2016, respectively. We or our agents held $69.10 billion and $63.96 billion as collateral for indemnified investments in repurchase agreements as of June 30, 2017 and December 31, 2016, respectively.

Additional information about our securities finance activities and other off-balance sheet arrangements is provided in Notes 7 and 9 to the consolidated financial statements included in this Form 10-Q.

RECENT ACCOUNTING DEVELOPMENTS

Information with respect to recent accounting developments is provided in Note 1 to the consolidated financial statements included in this Form 10-Q.

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QUANTITATIVE AND QUALITATIVE DISCLOSURES ABOUT MARKET RISK

The information provided under “Financial Condition - Market Risk Management” in Management’s Discussion and Analysis, included in this Form 10-Q, is incorporated by reference herein. For more information on our market risk refer to pages 98 to 105 included under Item 7, Management's Discussion and Analysis of Financial Condition and Results of Operations, in our 2016 Form 10-K.

CONTROLS AND PROCEDURES

State Street has established and maintains disclosure controls and procedures that are designed to ensure that information related to State Street and its subsidiaries on a consolidated basis required to be disclosed in its reports filed or submitted under the Securities Exchange Act of 1934 is recorded, processed, summarized, and reported within the time periods specified in the SEC's rules and forms, and that such information is accumulated and communicated to State Street's management, including its Chief Executive Officer and Chief Financial Officer, as appropriate, to allow timely decisions regarding required disclosure. For the quarter ended June 30, 2017, State Street's management carried out an evaluation, with the participation of the Chief Executive Officer and Chief Financial Officer, of the effectiveness of the design and operation of State Street's disclosure controls and procedures. Based on the evaluation of these disclosure controls and procedures, the Chief Executive Officer and Chief Financial Officer concluded that State Street's disclosure controls and procedures were effective as of June 30, 2017.

State Street has also established and maintains internal control over financial reporting as a process designed to provide reasonable assurance regarding the reliability of financial reporting and the preparation of consolidated financial statements for external purposes in conformity with GAAP. In the ordinary course of business, State Street routinely enhances its internal controls and procedures for financial reporting by either upgrading its current systems or implementing new systems. Changes have been made and may be made to State Street's internal controls and procedures for financial reporting as a result of these efforts. During the quarter ended June 30, 2017, no change occurred in State Street's internal control over financial reporting that has materially affected, or is reasonably likely to materially affect, State Street's internal control over financial reporting.

STATE STREET CORPORATION
CONSOLIDATED STATEMENT OF INCOME
(UNAUDITED)

	Three Months Ended June 30,		Six Months Ended June 30,	
(Dollars in millions, except per share amounts)	2017	2016	2017	2016
Fee revenue:				
Servicing fees	$1,339	$1,239	$2,635	$2,481
Management fees	397	293	779	563
Trading services	289	267	564	539
Securities finance	179	156	312	290
Processing fees and other	31	98	143	150
Total fee revenue	2,235			