STATE STREET CORP
Form 10-Q
August 08, 2014
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UNITED STATES
SECURITIES AND EXCHANGE COMMISSION
Washington, DC 20549
Form 10-Q

(Mark One)

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

For the quarterly period ended June 30, 2014

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 or a smaller reporting company. See the definitions of "large accelerated filer," "accelerated filer" and "smaller reporting company" in Rule 12b-2 of the Exchange Act. (Check one):

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

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

The number of shares of the registrant's common stock outstanding as of July 31, 2014 was 423,519,383.

STATE STREET CORPORATION
QUARTERLY REPORT ON FORM 10-Q FOR THE QUARTERLY PERIOD ENDED
JUNE 30, 2014

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

GENERAL

State Street Corporation, or the parent company, is a financial holding company headquartered in Boston, Massachusetts. Unless otherwise indicated or unless the context requires otherwise, all references in this Management's Discussion and Analysis to “State Street,” “we,” “us,” “our” or similar terms mean State Street Corporation and its subsidiaries on a consolidated basis. Our principal banking subsidiary is State Street Bank and Trust Company, or State Street Bank. As of June 30, 2014, we had consolidated total assets of $282.32 billion, consolidated total deposits of $218.83 billion, consolidated total shareholders' equity of $21.70 billion and 29,420 employees. With $28.40 trillion of assets under custody and administration and $2.48 trillion of assets under management as of June 30, 2014, we are a leading specialist in meeting the needs of institutional investors worldwide.

We have two lines of business:

Investment Servicing provides services for mutual funds, collective investment funds and other investment pools, corporate and public retirement plans, insurance companies, 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; 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 State Street Global Advisors, or SSgA, provides a broad array of investment management, investment research and investment advisory services to corporations, public funds and other sophisticated investors. SSgA offers active and passive asset management strategies across equity, fixed-income and cash asset classes. Products are distributed directly and through intermediaries using a variety of investment vehicles, including exchange-traded funds, or ETFs, such as the SPDR® ETF brand.

For financial and other information about our lines of business, refer to “Line of Business Information” included in this Management's Discussion and Analysis and note 17 to the consolidated financial statements included 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, 2014, and updates the Management's Discussion and Analysis in our Annual Report on Form 10-K for the year ended December 31, 2013, referred to as our 2013 Form 10-K, and in our Quarterly Report on Form 10-Q for the quarter ended March 31, 2014, both of which we 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 those reports. 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 accounting principles generally accepted in the U.S., referred to as GAAP. The preparation of financial statements in conformity with 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 consist of accounting for fair value measurements; other-than-temporary impairment of investment securities; and impairment of goodwill and other intangible assets. 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.

Additional information about these significant accounting policies is included under “Significant Accounting Estimates” in Management's Discussion and Analysis in our 2013 Form 10-K. We did not change these significant accounting policies in the first six months of 2014.

Certain financial information provided in this Management's Discussion and Analysis is prepared on both a GAAP, or reported basis, and a non-GAAP, or operating basis, including certain non-GAAP measures used in the calculation of identified regulatory capital ratios. We measure and compare certain financial information on an operating basis, as we believe that this presentation supports meaningful comparisons from period to period and the analysis of comparable financial trends with respect to State Street's normal ongoing business operations. We believe that operating-basis financial information, which reports non-taxable revenue, such as interest revenue associated with tax-exempt investment securities, on a fully taxable-equivalent basis, facilitates an investor's understanding and analysis of State Street's underlying financial performance and trends in addition to financial information prepared and reported in conformity with GAAP.

We also believe that the use of certain non-GAAP measures in the calculation of identified regulatory capital ratios is useful in understanding State Street's capital position and is of interest to investors. Operating-basis financial information should be considered in addition to, not as a substitute for or superior to, financial information prepared in conformity with GAAP. Any non-GAAP, or operating-basis, financial information presented in this Management's Discussion and Analysis is reconciled to its most directly comparable GAAP-basis measure.

We provide additional disclosures required by applicable bank regulatory standards, including supplemental qualitative and quantitative information with respect to regulatory capital (including market risk associated with our trading activities), and summary results of semi-annual State Street-run stress tests which we conduct under the Dodd-Frank Wall Street Reform and Consumer Protection Act, or Dodd-Frank Act. These additional disclosures are accessible under "Filings and Reports" 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.

FORWARD-LOOKING STATEMENTS

This Form 10-Q, as well as other reports 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, contain statements (including statements in this Management's Discussion and Analysis) 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, market growth, acquisitions, joint ventures and divestitures and new technologies, services and opportunities, as well as regarding 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,"

"anticipate," "estimate," "seek," "may," "will," "trend," "target," "strategy" and "goal," or similar statements or variations of s
are intended to identify 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, 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 net interest revenue, 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 and the performance and volatility of securities, credit, currency and other markets in the U.S. and internationally;
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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, and our ability to deploy deposits in a profitable manner

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consistent with our liquidity requirements and risk profile;

- the manner and timing with which the Federal Reserve and other U.S. and foreign regulators implement the Dodd-Frank Act, changes to the Basel III capital framework and European legislation, such as the Alternative Investment Fund Managers Directive and Undertakings for Collective Investment in Transferable Securities Directives, with respect to the levels of regulatory capital we must maintain, our credit exposure to third parties, margin requirements applicable to derivatives, banking and financial activities and other regulatory initiatives in the U.S. and internationally, including regulatory developments that result in changes to our structure or operating model, or other changes to how we provide services;
- the impact of evolving and increasing regulatory compliance requirements and expectations on our expenses;
- adverse changes in the regulatory capital ratios that we are required or will be required to meet, whether arising under the Dodd-Frank Act or the Basel III capital and liquidity standards, 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;
- increasing requirements to obtain the prior approval of the Federal Reserve or our other regulators for the use, allocation or distribution of our capital or other specific capital actions or programs, including acquisitions, dividends and equity purchases, without which our growth plans, distributions to shareholders, equity purchase programs or other capital 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;

- financial market disruptions or economic recession, whether in the U.S., Europe, Asia or other regions;
- our ability to promote a strong culture of risk management, operating controls, compliance oversight and governance that meet our expectations and those of our clients and our regulators;
- the results of, and costs associated with, governmental or regulatory inquiries and investigations, litigation and similar claims, disputes, or proceedings;
- delays or difficulties in the execution of our previously announced Business Operations and Information Technology Transformation program, which could lead to changes in our estimates of the charges, expenses or savings associated with the planned program and may cause volatility of our earnings;
- 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 depository 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, and 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;
- dependencies on information technology and our ability to control related risks, including cyber-crime and other threats to our information technology infrastructure and systems and their effective operation both independently and with external systems, and complexities and costs of protecting the security of our systems and data;
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our ability to grow revenue, control expenses, attract and retain highly skilled people and raise the capital necessary to achieve our business goals and comply with regulatory requirements;

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- 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;
- changes or potential changes in how and in what amounts clients compensate us for our services, and the mix of services provided by us that clients choose;
- 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 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 emerging 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, including the risk factors discussed in our 2013 Form 10-K. Forward-looking statements in this Form 10-Q should not be relied on as representing our expectations or beliefs as of any date 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 above 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 or financial condition.

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

The following tables present our financial results for the quarters and six months ended June 30, 2014 and 2013:

	Quarters Ended June 30,					
(Dollars in millions, except per share amounts)	2014		2013		% Change	
Total fee revenue	$2,039		$1,971		3	%
Net interest revenue	561		596		(6	)
Gains (losses) related to investment securities, net	(2	)	(7	)		
Total revenue	2,598		2,560		1	
Provision for loan losses	2		—			
Total expenses	1,850		1,798		3	
Income before income tax expense	746		762		(2	)
Income tax expense	124		183			
Net income	$622		$579		7	

Adjustments to net income:					
Dividends on preferred stock	(19	)	(6	)	
Earnings allocated to participating securities	(1	)	(2	)	
Net income available to common shareholders	$602		$571		
Earnings per common share:					
Basic	$1.41		$1.26		
Diluted	1.38		1.24		11
Average common shares outstanding (in thousands):					
Basic	427,824		452,176		
Diluted	435,320		461,040		
Cash dividends declared per common share	$.30		$.26		
Return on average common equity	11.9	%	11.3	%	

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MANAGEMENT’S DISCUSSION AND ANALYSIS OF FINANCIAL CONDITION AND RESULTS OF OPERATIONS (Continued)

	Six Months Ended June 30,		
(Dollars in millions, except per share amounts)	2014	2013	% Change
Total fee revenue	$3,963	$3,828	4 %
Net interest revenue	1,116	1,172	(5)
Gains (losses) related to investment securities, net	4	(5)	
Total revenue	5,083	4,995	2
Provision for loan losses	4	—	
Total expenses	3,878	3,624	7
Income before income tax expense	1,201	1,371	(12)
Income tax expense	216	328	
Net income	$985	$1,043	(6)
Adjustments to net income:			
Dividends on preferred stock	(25)	(13)	
Earnings allocated to participating securities	(2)	(4)	
Net income available to common shareholders	$958	$1,026	
Earnings per common share:			
Basic	$2.23	$2.26	
Diluted	2.19	2.22	(1)
Average common shares outstanding (in thousands):			
Basic	429,215	453,240	
Diluted	436,958	461,630	
Cash dividends declared per common share	$.56	$.52	
Return on average common equity	9.6 %	10.2 %	

The following “Highlights” and “Financial Results” sections provide information related to significant events, as well as highlights of our consolidated financial results for the second quarter of 2014 presented in the preceding table. More detailed information about our consolidated financial results, including comparisons of our financial results for the second quarter of 2014 to those for the second quarter of 2013 and for the six months ended June 30, 2014 to those for the six months ended June 30, 2013, is provided under “Consolidated Results of Operations,” which follows these sections.

Highlights

- We were notified by the Federal Reserve on February 21, 2014 that we completed our Basel III qualification period, or parallel run, and would be required to begin using the advanced approaches framework in the Basel III final rule in the determination of our risk-based capital requirements. Pursuant to this notification, we have begun to use the advanced approaches framework to calculate and disclose our regulatory capital ratios starting with the second quarter of 2014.

Information about our regulatory capital ratios as of June 30, 2014 is provided under "Financial Condition - Capital" in this Management's Discussion and Analysis, and in note 11 to the consolidated financial statements, included in this Form 10-Q.

- In the second quarter of 2014, under a purchase program approved by our Board of Directors in March 2014 which authorizes us to purchase up to $1.70 billion of our common stock through March 31, 2015, we purchased approximately 6.3 million shares of our common stock at an average price of $65.02 per share and an aggregate cost of approximately $410 million.
- In the second quarter of 2014, we declared a quarterly common stock dividend of $0.30 per share, totaling approximately $128 million, which was paid in July 2014.

Additional information about our common stock purchase program and our common stock dividends is provided under “Financial Condition – Capital” in this Management's Discussion and Analysis. Information about our common stock purchase program is also provided in Part II Item 2, "Unregistered Sales of Equity Securities and Use of Proceeds," included in this Form 10-Q.

State Street is registered with the Federal Reserve as a bank holding company pursuant to the Bank Holding Company Act of 1956. The Bank Holding Company Act limits the activities in which we (and non-banking entities that we are deemed to control under that Act) may engage to activities the Federal Reserve considers to be closely related to banking or to managing or controlling banks. Financial holding company status expands the activities permissible for a bank holding company to those that are deemed to be "financial in nature" by the Federal Reserve. State Street elected to become a financial holding company under the Bank Holding Company Act. Financial holding company status requires State Street and its banking subsidiaries to remain well capitalized and well managed and to comply with Community Reinvestment Act obligations. Currently, under the Bank Holding Company Act, we may not be able to engage in new activities or acquire shares or control of other businesses.

In addition, we meet the criteria for a systemically important financial institution under the Dodd-Frank Act and we are one of 29 banking organizations identified as a

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global systemically important bank, or G-SIB, by the Financial Stability Board.

Our compliance obligations have increased significantly due to new regulations in the U.S. and internationally that have been adopted or proposed in response to the financial crisis. As a systemically important financial institution, we are subject to enhanced supervision and prudential standards. In Europe, we anticipate that certain of our European banking subsidiaries may become subject to the European Central Bank's new supervisory authority. 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 programs.

In addition, we and other large banking organizations are required under the Dodd-Frank Act to periodically submit a resolution plan to the Federal Reserve and the Federal Deposit Insurance Corporation, or FDIC, describing our strategy for rapid and orderly resolution in the event of material financial distress or failure. In August 2014, the Federal Reserve and the FDIC announced the completion of their reviews of resolution plans submitted in 2013 by 11 large, complex banking organizations, including State Street, under the requirements of the Dodd-Frank Act, and informed each of these organizations of specific shortcomings with their respective 2013 resolution plans. If we fail to meet regulatory expectations to the satisfaction of the Federal Reserve and the FDIC in the submission of our 2015 resolution plan, we could be subject to more stringent capital, leverage or liquidity requirements, restrictions on our growth, activities or operations, or be required to divest certain of our assets or operations.

Financial Results

- Total revenue in the second quarter of 2014 increased 1% compared to the second quarter of 2013, as a 7% increase in aggregate servicing fee and management fee revenue and a 12% increase in securities finance revenue were partly offset by declines in trading services revenue and net interest revenue of 14% and 6%,

respectively. Total fee revenue increased 3% compared to the second quarter of 2013.

- Servicing fee revenue in the second quarter of 2014 increased 7% compared to the second quarter of 2013, mainly the result of stronger global equity markets, the positive revenue impact of net new business (revenue added from new servicing business less revenue lost from the removal of assets serviced), and the impact of the weaker U.S. dollar. Servicing fees generated outside the U.S. in the second quarter of 2014 and the second quarter of 2013 were approximately 42% and 41%, respectively, of total servicing fees for those periods.
- Management fee revenue increased 8% in the second quarter of 2014 compared to the second quarter of 2013, primarily the result of stronger global equity markets, partly offset by the negative impact of the excess of revenue lost from liquidations of managed assets over revenue added from newly installed assets to be managed. Management fees generated outside the U.S. in the second quarter of 2014 and the second quarter of 2013 were approximately 36% and 35%, respectively, of total management fees for those periods.
- In the second quarter of 2014, trading services revenue, composed of revenue generated by foreign exchange trading and revenue from brokerage and other trading services, declined 14% compared to the second quarter of 2013. Revenue from foreign exchange trading declined 16%, with estimated indirect foreign exchange revenue down 24% and direct sales and trading foreign exchange revenue down 8%, from the second quarter of 2013. Both declines were mainly the result of lower volatility. Brokerage and other trading services revenue in the second quarter of 2014 declined 13% compared to the second quarter of 2013, mainly reflective of lower client volumes in electronic trading.
- Securities finance revenue increased 12% in the second quarter of 2014 compared to the second quarter of 2013, generally reflective of growth in our enhanced custody business, where we participate in securities finance transactions as a principal.
- Net interest revenue in the second quarter of 2014 declined 6% compared to the second quarter of 2013, generally the result of lower yields on interest-earning assets, as lower global interest rates affected revenue from

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floating-rate assets, partly offset by lower interest expense and higher interest-earning assets.

Net interest margin, calculated on fully taxable-equivalent net interest revenue, declined 25 basis points to 1.17% in the second quarter of 2014 from 1.42% in the second quarter of 2013. Continued elevated levels of client deposits increased our average interest-earning assets, but negatively affected our net interest margin, as we placed a portion of these deposits with U.S. and non-U.S. central banks and earned the relatively low interest rates paid by the central banks on these balances.

Fully taxable-equivalent net interest revenue and net interest margin are discussed in more detail under "Consolidated Results of Operations - Net Interest Revenue" in this Management's Discussion and Analysis.

- Total expenses in the second quarter of 2014 increased 3% compared to the second quarter of 2013. Compensation and employee benefits expenses increased 7%, primarily due to costs for additional staffing related to the installation of new business, higher incentive compensation, the impact of the weaker U.S. dollar, annual merit increases and higher regulatory compliance costs. These aggregate increases were partly offset by savings generated from the implementation of our Business Operations and Information Technology Transformation program.

Other expenses decreased 8% in the second quarter of 2014 compared to the second quarter of 2013, as lower levels of charitable contributions and sales promotion costs were partly offset by higher levels of professional services associated with regulatory compliance requirements.

We anticipate that evolving and increasing regulatory compliance requirements and expectations will continue to affect our expenses. Our employee compensation and benefits, information systems and other expenses could increase, as we further adjust our operations in response to new or proposed requirements and heightened expectations.

- With respect to our Business Operations and Information Technology Transformation program, we expect to achieve additional pre-tax expense savings for full-year 2014 of approximately $130 million. These pre-tax

expense savings relate only to the Business Operations and Information Technology Transformation program and are based on projected improvement from our total 2010 expenses from operations, all else being equal. Our actual total expenses have increased since 2010, and may in the future increase or decrease, due to other factors.

Additional information with respect to our expenses, including our Business Operations and Information Technology Transformation program, is provided under "Consolidated Results of Operations - Expenses" in this Management's Discussion and Analysis.

- In the second quarter of 2014, we secured an estimated $250 billion of new business in assets to be serviced; of the total, $89 billion was installed prior to June 30, 2014, with the remaining $161 billion expected to be installed in the remainder of 2014. In the second quarter of 2014, we also installed approximately $54 billion of new asset servicing business that we were awarded in prior periods. As of June 30, 2014, we had an estimated $243 billion of new business in assets to be serviced, including the $161 billion referenced above, which remained to be installed in future periods. New business in assets to be serviced includes assets from new servicing clients, as well as additional assets to be serviced for existing clients.

The new business not installed by June 30, 2014 was not included in our assets under custody and administration as of that date, and had no impact on our servicing fee revenue in the second quarter of 2014, as the assets are not included until their installation is complete and we begin to service them. Once installed, the assets generate servicing fee revenue in subsequent periods in which the assets are serviced.

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.

- In the second quarter of 2014, SSgA added approximately $15 billion of net new business in assets to be managed, composed primarily of $22 billion of net inflows, substantially into

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institutional products and ETFs, partly offset by net outflows of $7 billion from managed cash.
In addition, approximately $6 billion of new business awarded to SSgA but not installed by June 30, 2014 was not included in our assets under management as of that date, and had no impact on our management fee revenue for the second quarter of 2014, as the assets are not included until their installation is complete and we begin to manage them. Once installed, the assets generate management fee revenue in subsequent periods in which the assets are managed.

CONSOLIDATED RESULTS OF OPERATIONS

This section discusses our consolidated results of operations for the second quarter and first six months of 2014 compared to the same periods in 2013 in more detail, and should be read in conjunction with the consolidated financial statements and accompanying condensed notes included in this Form 10-Q.

Total Revenue

Additional information with respect to the sources of our revenue, the products and activities that generate it, and the factors that influence the levels of revenue generated during any period is provided under "Consolidated Results of Operations – Total Revenue" in Management's Discussion and Analysis included in our 2013 Form 10-K.

The following tables present the components of total revenue for the periods indicated:

	Quarters Ended June 30,		
	2014	2013	% Change
(Dollars in millions)			
Fee revenue:			
Servicing fees	$1,288	$1,201	7 %
Management fees	300	277	8
Trading services:			
Foreign exchange trading	144	171	(16)
Brokerage and other trading services	116	133	(13)
Total trading services	260	304	(14)
Securities finance	147	131	12
Processing fees and other	44	58	(24)
Total fee revenue	2,039	1,971	3
Net interest revenue:			
Interest revenue	650	700	(7)
Interest expense	89	104	(14)
Net interest revenue	561	596	(6)
Gains (losses) related to investment securities, net	(2)	(7)	
Total revenue	$2,598	$2,560	1

	Six Months Ended June 30,		
(Dollars in millions)	2014	2013	% Change
Fee revenue:			
Servicing fees	$2,526	$2,376	6 %
Management fees	592	540	10
Trading services:			
Foreign exchange trading	278	317	(12)
Brokerage and other trading services	235	276	(15)
Total trading services	513	593	(13)
Securities finance	232	209	11
Processing fees and other	100	110	(9)
Total fee revenue	3,963	3,828	4
Net interest revenue:			

Interest revenue	1,305	1,387	(6	)
Interest expense	189	215	(12	)
Net interest revenue	1,116	1,172	(5	)
Gains (losses) related to investment securities, net	4	(5)		
Total revenue	$5,083	$4,995	2	

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Fee Revenue

Servicing and management fees collectively composed approximately 78% and 79% of our total fee revenue in the second quarter and first six months of 2014, respectively, compared to 75% and 76%, respectively, for the corresponding periods in 2013. The level of these fees is influenced by several factors, including the mix and volume of our assets under custody and administration and our assets under management, the value and type of securities positions held (with respect to assets under custody) and 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 assets under custody and administration. 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 and other factors, may have a significant effect on our servicing fee revenue.

Generally, management fees are affected by changes in month-end valuations of assets under management. Management fees for certain components of managed assets, such as ETFs, are affected by daily average valuations of assets under management. Management fee revenue is more sensitive to market valuations than servicing fee revenue, since 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, changes in service level and other factors, may have a significant effect on our management fee revenue. While certain management fees are directly determined by the values of assets under management and the investment strategies employed, management fees may reflect other factors as well, including performance fee arrangements, discussed later in this section, 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 involve performance fee arrangements. Performance fees are generated when the performance of certain managed funds exceeds benchmarks specified in the management agreements. Generally, we experience more volatility with performance fees than with more traditional management fees.

In light of the above, we estimate, using relevant information as of June 30, 2014 and assuming that all other factors remain constant, that: (1) a 10% increase or decrease, over the relevant periods for or on which our servicing and management fees are calculated, in worldwide equity valuations would result in a corresponding change in our total revenue of approximately 2%; and (2) a 10% increase or decrease, over the relevant periods for or on which our servicing and management fees are calculated, in worldwide fixed-income security valuations would result in a corresponding change in our total revenue of approximately 1%.

The following table presents selected equity market 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 and the averages of month-end indices demonstrate worldwide changes in equity markets that affect our servicing and management fee revenue. Quarter-end indices affect the values of assets under custody and administration and assets under management as of those dates. The index names listed in the table are service marks of their respective owners.

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	Daily Averages of Indices Quarters Ended June 30,			Averages of Month-End Indices Quarters Ended June 30,			Quarter-End Indices As of June 30,		
	2014	2013	% Change	2014	2013	% Change	2014	2013	% Change
S&P 500®	1,900	1,609	18 %	1,923	1,612	19 %	1,960	1,606	22 %
NASDAQ®	4,196	3,368	25	4,255	3,396	25	4,408	3,403	30
MSCI EAFE®	1,942	1,707	14	1,955	1,698	15	1,972	1,639	20

	Daily Averages of Indices Six Months Ended June 30,			Averages of Month-End Indices Six Months Ended June 30,		
	2014	2013	% Change	2014	2013	% Change
S&P 500®	1,868	1,563	20 %	1,880	1,569	20 %
NASDAQ®	4,203	3,275	28	4,229	3,293	28
MSCI EAFE®	1,918	1,687	14	1,926	1,687	14

The following tables present the components of fee revenue for the periods indicated:

FEE REVENUE

	Quarters Ended June 30,		
(Dollars in millions)	2014	2013	% Change
Servicing fees	$1,288	$1,201	7 %
Management fees	300	277	8
Trading services:			
Foreign exchange trading	144	171	(16)
Brokerage and other trading services	116	133	(13)
Total trading services	260	304	(14)
Securities finance	147	131	12
Processing fees and other	44	58	(24)
Total fee revenue	$2,039	$1,971	3

	Six Months Ended June 30,		
(Dollars in millions)	2014	2013	% Change
Servicing fees	$2,526	$2,376	6 %
Management fees	592	540	10
Trading services:			
Foreign exchange trading	278	317	(12)
Brokerage and other trading services	235	276	(15)
Total trading services	513	593	(13)
Securities finance	232	209	11
Processing fees and other	100	110	(9)
Total fee revenue	$3,963	$3,828	4

Servicing Fees

Servicing fees in the second quarter and first six months of 2014 increased 7% and 6%, respectively, compared to the second quarter and first six months of 2013, primarily the result of stronger global equity markets, the positive revenue impact of net new business (revenue added from new servicing

business less revenue lost from the removal of assets serviced), and the impact of the weaker U.S. dollar. For both the second quarter and first six months of 2014, servicing fees generated outside the U.S. were approximately 42% of total servicing fees, compared to approximately 41% for both the second quarter and first six months of 2013.

The following tables present the components, financial instrument mix and geographic mix of assets under custody and administration, as of the dates indicated:

COMPONENTS OF ASSETS UNDER CUSTODY AND ADMINISTRATION

(In billions)	June 30, 2014	December 31, 2013	June 30, 2013
Mutual funds	$7,122	$6,811	$6,278
Collective funds	6,956	6,428	5,826
Pension products[1]	5,613	5,851	5,447
Insurance and other products	8,709	8,337	8,191
Total	$28,400	$27,427	$25,742

[1] Decline as of June 30, 2014 compared to December 31, 2013 resulted primarily from the loss of assets serviced referenced below in this “Servicing Fees” section.

FINANCIAL INSTRUMENT MIX OF ASSETS UNDER CUSTODY AND ADMINISTRATION

(In billions)	June 30, 2014	December 31, 2013	June 30, 2013
Equities	$15,607	$15,050	$13,407
Fixed-income	9,255	9,072	9,046
Short-term and other investments	3,538	3,305	3,289
Total	$28,400	$27,427	$25,742

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GEOGRAPHIC MIX OF ASSETS UNDER CUSTODY AND ADMINISTRATION[1]

(In billions)	June 30, 2014	December 31, 2013	June 30, 2013
North America	$21,199	$20,764	$19,390
Europe/Middle East/Africa	5,923	5,511	5,245
Asia/Pacific	1,278	1,152	1,107
Total	$28,400	$27,427	$25,742

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

The increase in total assets under custody and administration as of June 30, 2014 compared to both December 31, 2013 and June 30, 2013, resulted primarily from stronger global equity markets and net shareholder subscriptions experienced by our custody clients, partly offset by net losses of assets serviced. Asset levels as of June 30, 2014 did not reflect the estimated $243 billion of new business in assets to be serviced awarded to us in the second quarter of 2014 and prior periods but not installed prior to June 30, 2014. This new business will be reflected in assets under custody and administration in future periods after installation, and will generate servicing fee revenue in subsequent periods.

The value of assets under custody and administration is a broad measure of the relative size of various markets served. Changes in the values of assets under custody and administration from period to period do not necessarily result in proportional changes in our servicing fee revenue.

Management Fees

Management fees increased 8% and 10% during the second quarter and first six months of 2014, respectively, compared to the same periods in 2013, primarily the result of stronger global equity markets, partly offset by the negative impact of the excess of revenue lost from liquidations of managed assets over revenue added from newly installed assets to be managed. For both the second quarter and first six months of 2014, management fees generated outside the U.S. were approximately 36% of total management fees, compared to 35% and 36%, respectively, for the same periods in 2013.

The following tables present assets under management by asset class and investment approach, ETFs by asset class, and the geographic mix of assets under management, as of the dates indicated:

ASSETS UNDER MANAGEMENT BY ASSET CLASS AND INVESTMENT APPROACH[1]

(In billions)	June 30, 2014	December 31, 2013	June 30, 2013
Equity:			
Active	$42	$42	$44
Passive	1,390	1,334	1,152
Total Equity	1,432	1,376	1,196
Fixed-Income:			
Active	16	16	18
Passive	336	311	306
Total Fixed-Income	352	327	324
Cash[2]	413	385	385
Multi-Asset-Class Solutions:			
Active	34	23	22
Passive	116	110	97
Total Multi-Asset-Class Solutions	150	133	119
Alternative Investments[3]:			
Active	18	14	12
Passive	115	110	110
Total Alternative Investments	133	124	122

Total	$2,480	$2,345	$2,146

(1) As of December 31, 2013, the presentation was changed to align with the reporting of core businesses. Amounts reported as of June 30, 2013 have been adjusted for comparative purposes.
(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 Fund, for which State Street is not the investment manager, but acts as distribution agent.

EXCHANGE-TRADED FUNDS BY ASSET CLASS(1)(2)

(In billions)	June 30, 2014	December 31, 2013	June 30, 2013
Alternative Investments	$43	$39	$44
Cash	1	1	2
Equity	331	325	261
Fixed-income	38	34	30
Total Exchange-Traded Funds	$413	$399	$337

(1) Exchange-traded funds are a component of assets under management presented in the preceding table.
(2) Includes SPDR® Gold Fund, for which State Street is not the investment manager, but acts as distribution agent.

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GEOGRAPHIC MIX OF ASSETS UNDER MANAGEMENT[(1)]

(In billions)	June 30, 2014	December 31, 2013	June 30, 2013
North America	$1,533	$1,456	$1,347
Europe/Middle East/Africa	589	560	498
Asia/Pacific	358	329	301
Total	$2,480	$2,345	$2,146

(1) Geographic mix is based on client location or fund management location. Amounts reported as of June 30, 2013 were adjusted for comparative purposes to reflect realignment of reporting.

The increase in total assets under management as of June 30, 2014 compared to December 31, 2013 resulted primarily from net market appreciation during the first half of 2014 in the values of the assets managed, as well as net new business of approximately $18 billion. The net new business of $18 billion in the first six months of 2014 was primarily composed of $27 billion of net inflows into money market funds, partly offset by net outflows of $9 billion from ETFs.

The following table presents activity in assets under management, by product category, for the twelve months ended June 30, 2014:

ASSETS UNDER MANAGEMENT

(In billions)	Equity	Fixed-Income	Cash	Multi-Asset-Class Solutions	Alternative Investments	Total
Balance as of June 30, 2013	$1,196	$324	$385	$ 119	$122	$2,146
Long-term institutional inflows[(1)]	119	31	—	17	8	175
Long-term institutional outflows[(1)]	(151)	(31)	—	(14)	(8)	(204)
Long-term institutional flows, net	(32)	—	—	3	—	(29)
ETF flows, net	26	4	—	—	(6)	24
Cash fund flows, net	—	—	(2)	—	—	(2)
Total flows, net	(6)	4	(2)	3	(6)	(7)
Market appreciation[(2)]	180	—	—	8	7	195
Foreign exchange impact[(2)]	6	(1)	2	3	1	11
Total market/foreign exchange impact	186	(1)	2	11	8	206
Balance as of December 31, 2013	1,376	327	385	133	124	2,345
Long-term institutional inflows[(1)]	138	44	—	26	6	214
Long-term institutional outflows[(1)]	(153)	(37)	—	(18)	(6)	(214)
Long-term institutional flows, net	(15)	7	—	8	—	—
ETF flows, net	(13)	3	—	—	1	(9)
Cash fund flows, net	—	—	27	—	—	27
Total flows, net	(28)	10	27	8	1	18

Market appreciation(2)	78	12	—	8	6	104
Foreign exchange impact(2)	6	3	1	1	2	13
Total market/foreign exchange impact	84	15	1	9	8	117
Balance as of June 30, 2014	$1,432	$352	$413	$ 150	$133	$2,480

(1) Amounts represent long-term portfolios, excluding ETFs.
(2) Amounts represent aggregate impact on each product category for the period.
The net new business of approximately $18 billion in the first six months 2014 presented in the preceding table did not include $6 billion of new asset management business, substantially all of which was awarded to SSgA in the second quarter of 2014 but not installed prior to June 30, 2014. This new business will be reflected in assets under management in future periods after installation, and will generate management fee revenue in subsequent periods.

Total assets under management as of June 30, 2014 included managed assets lost but not yet 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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Trading Services
The following tables summarize the components of trading services revenue for the periods indicated:

	Quarters Ended June 30,		
(Dollars in millions)	2014	2013	% Change
Foreign exchange trading:			
Direct sales and trading	$79	$86	(8)%
Indirect foreign exchange trading	65	85	(24)
Total foreign exchange trading	144	171	(16)
Brokerage and other trading services:			
Electronic foreign exchange trading	43	63	(32)
Other trading, transition management and brokerage	73	70	4
Total brokerage and other trading services	116	133	(13)
Total trading services revenue	$260	$304	(14)

	Six Months Ended June 30,		
(Dollars in millions)	2014	2013	% Change
Foreign exchange trading:			
Direct sales and trading	$150	$167	(10)%
Indirect foreign exchange trading	128	150	(15)
Total foreign exchange trading	278	317	(12)
Brokerage and other trading services:			
Electronic foreign exchange trading	91	124	(27)
Other trading, transition management and brokerage	144	152	(5)
Total brokerage and other trading services	235	276	(15)
Total trading services revenue	$513	$593	(13)

Trading services revenue is composed of revenue generated by foreign exchange, or FX, trading, as well as revenue generated by brokerage and other trading services. We 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 FX," "indirect FX" and "electronic FX trading." With respect to electronic FX trading, 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. In addition, we act as distribution agent for the SPDR® Gold ETF. 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.

FX trading revenue is influenced by three principal factors: the volume and type of client FX transactions and related spreads; currency volatility; and the management of market risk associated with currencies and interest rates. Revenue earned from direct sales and trading FX and indirect FX is recorded in FX trading revenue. Revenue earned from electronic FX trading is recorded in brokerage and other trading services revenue.

The 14% and 13% decrease in total trading services revenue for the second quarter and first six months of 2014, respectively, compared to the second quarter and first six months of 2013, composed of separate changes related to FX trading and brokerage and other trading services, is explained below.

Total FX trading revenue declined 16% and 12% in the second quarter and first six months of 2014, respectively, compared to the same periods in 2013, primarily the result of lower currency volatility and spreads, partly offset by higher client volumes in direct sales and trading foreign exchange.

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 FX.” Alternatively, 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.” We execute indirect FX trades as a principal at rates disclosed to our clients. We calculate revenue for indirect FX using an attribution methodology based on estimated effective mark-ups/downs and observed client volumes. All other FX trading revenue, other than this indirect FX revenue estimate, is considered by us to be direct sales and trading FX revenue. Our clients that utilize indirect FX can, in addition to executing their FX transactions through dealers not affiliated with us, transition from indirect FX to either direct sales and trading FX execution, including our “Street FX” service that enables our clients to define their FX execution strategy and automate the FX trade execution process, in which State Street continues to act as a principal market maker, or to one of our electronic trading platforms.

For the second quarter and first six months of 2014, our estimated indirect FX revenue declined 24% and 15%, respectively, compared to the same periods in 2013. The declines mainly resulted from lower currency volatility and lower client volumes. For the second quarter and first six months of 2014, compared to the same periods in 2013, our direct sales and trading FX revenue declined 8% and 10%, respectively. The declines mainly resulted from lower currency volatility, partly offset by higher client volumes.

We continue to expect that some clients may choose, over time, to reduce their level of indirect FX transactions in favor of other execution methods, including either direct FX transactions or electronic FX trading 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 consistent.

Total brokerage and other trading services revenue declined 13% and 15% in the second quarter and first six months of 2014, respectively, compared to the same periods in 2013. Our clients may choose to execute FX transactions through one of our electronic trading platforms. This service generates revenue through a "click" fee. Revenue from such electronic FX trading declined 32% and 27% in the second quarter of 2014 and first six months of 2014, respectively, compared to the same periods in 2013, mainly due to declines in client volumes.

In the first six months of 2014, other trading, transition management and brokerage revenue declined 5% compared to the same period in 2013. The decrease mainly resulted from a decline in distribution fees associated with the SPDR® Gold ETF, which resulted from outflows as average gold prices declined during the period, partly offset by an increase in currency management revenue. With respect to the SPDR® Gold ETF, fees earned by us as distribution agent are recorded in other trading, transition management and brokerage revenue within brokerage and other trading services revenue, and not in management fee revenue.

Our revenue from transition management and related expenses in the first six months of 2014, as well as in full-years 2013, 2012 and 2011, were adversely affected by compliance issues in our U.K. business, the reputational and regulatory impact of which may continue to adversely affect our transition management revenue in future periods.

Securities Finance

Our agency securities finance business consists of two components: 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, and an agency lending program for third-party investment managers and asset owners, which we refer to as the agency lending funds.

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.

We also participate in securities lending transactions as a principal, which we refer to as our enhanced custody business. As principal, we borrow securities from the lending client and then lend such securities to the subsequent borrower, either a State Street client or a broker/dealer. Our involvement as principal is utilized when the lending client is unable to, or elects not to, transact directly with the market and requires us to execute the transaction and furnish the securities. In our role as principal, we provide support to the transaction through our credit rating. While a significant proportion of the securities furnished by us in our role as principal is sourced 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 in the second quarter and first six months of 2014 increased 12% and 11%, respectively, compared to the same periods in 2013, generally reflective of growth 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, proposed or anticipated regulatory changes 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 decreased 24% and 9% in the second quarter and first six months of 2014, respectively, compared to the same periods in 2013. The decrease was mainly due to higher amortization of tax-advantaged investments, partly offset by higher revenue from our investment in bank-owned life insurance.

Net Interest Revenue

Net interest revenue is defined as interest revenue 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 net interest revenue and average total

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interest-earning assets for the period. 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.

The following tables present the components of average interest-earning assets and average interest-bearing liabilities, related interest revenue and interest expense, and rates earned and paid, for the periods indicated:

	Quarters Ended June 30,					
	2014			2013		
(Dollars in millions; fully taxable-equivalent basis)	Average Balance	Interest Revenue/ Expense	Rate	Average Balance	Interest Revenue/ Expense	Rate
Interest-bearing deposits with banks	$53,564	$51	.38 %	$28,244	$31	.44 %
Securities purchased under resale agreements	4,307	10	.94	5,852	12	.79
Trading account assets	953	—	—	638	—	—
Investment securities	117,593	568	1.94	118,522	609	2.06
Loans and leases	15,061	61	1.62	14,003	79	2.29
Other interest-earning assets	14,845	2	.06	11,016	2	.04
Average total interest-earning assets	$206,323	$692	1.34	$178,275	$733	1.64
Interest-bearing deposits:						
U.S.	$20,698	$4	0.09 %	$7,969	$3	.13 %
Non-U.S.	109,290	14	0.05	102,127	24	.09
Securities sold under repurchase agreements	8,747	—	—	8,469	—	—
Federal funds purchased	19	—	—	300	—	—
Other short-term borrowings	4,000	(12)	(1.20)	3,641	15	1.63
Long-term debt	9,340	64	2.73	8,200	54	2.65
Other interest-bearing liabilities	7,559	19	0.99	6,273	8	.52
Average total interest-bearing liabilities	$159,653	$89	0.22	$136,979	$104	.30
Interest-rate spread			1.12 %			1.34 %
Net interest revenue—fully taxable-equivalent basis		$603			$629	
Net interest margin—fully taxable-equivalent basis			1.17 %			1.42 %
Tax-equivalent adjustment		(42)			(33)	
Net interest revenue—GAAP basis		$561			$596	

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	Six Months Ended June 30,					
	2014			2013		
(Dollars in millions; fully taxable-equivalent basis)	Average Balance	Interest Revenue/ Expense	Rate	Average Balance	Interest Revenue/ Expense	Rate
Interest-bearing deposits with banks	$43,543	$85	.40 %	$29,408	$62	.42 %
Securities purchased under resale agreements	5,463	19	.69	5,751	25	.87
Trading account assets	927	—	—	682	—	—
Investment securities	117,713	1,165	1.98	119,059	1,227	2.06
Loans and leases	14,833	119	1.61	13,374	135	2.04
Other interest-earning assets	14,190	3	.04	10,025	3	.05
Average total interest-earning assets	$196,669	$1,391	1.42	$178,299	$1,452	1.64
Interest-bearing deposits:						
U.S.	$16,409	$5	.07 %	$10,669	$9	.17 %
Non-U.S.	105,308	28	.05	100,930	52	.10
Securities sold under repurchase agreements	8,586	—	—	8,156	—	—
Federal funds purchased	20	—	—	331	—	—
Other short-term borrowings	3,955	3	.16	4,138	31	1.51
Long-term debt	9,503	127	2.66	7,802	110	2.83
Other interest-bearing liabilities	7,161	26	.73	6,384	13	.41
Average total interest-bearing liabilities	$150,942	$189	.25	$138,410	$215	.31
Interest-rate spread			1.17 %			1.33 %
Net interest revenue—fully taxable-equivalent basis		$1,202			$1,237	
Net interest margin—fully taxable-equivalent basis			1.23 %			1.40 %
Tax-equivalent adjustment		(86)			(65)	
Net interest revenue—GAAP basis		$1,116			$1,172	

Average total interest-earning assets for the first six months of 2014 were higher compared to the first six months of 2013, the result of the investment of elevated levels of client deposits in interest-bearing deposits with banks, as well as higher levels of cash collateral (included in other interest-earning assets in the preceding tables) provided in connection with our enhanced custody business, and higher average loans and leases.

Our average other interest-earning assets, largely associated with enhanced custody, composed approximately 7% of our total average interest-earning assets for both the second quarter and first six months of 2014, compared to approximately 6% for both the second quarter and first six months of 2013, as this business continued to grow. While these securities finance activities support our overall profitability by generating securities finance revenue, they put downward pressure on our net interest margin, as interest on the collateral provided is earned at a lower rate than on our investment securities portfolio.

The higher level of investment in interest-bearing deposits with banks resulted from continued higher levels of client deposits, discussed further below, while the increase in average loans and leases

resulted from growth in mutual fund lending and senior secured bank loans.

During the past year, our clients have continued to place elevated levels of deposits with us, as low global interest rates have made deposits attractive relative to other investment options. The portion of these client deposits characterized as transient in nature has been generally placed with various central banks globally, while deposits characterized as more stable have been invested in our investment securities portfolio and used to support growth in other client-related activities.

Net interest revenue decreased 6% in the second quarter of 2014, and on a fully taxable-equivalent basis declined 4%, compared to the second quarter of 2013. In the first six months of 2014, net interest revenue decreased 5%, and on a fully taxable-equivalent basis declined 3%, compared to the first six months of 2013. The decreases were generally the result of lower yields on interest-earning assets, as lower global interest rates affected our revenue from floating-rate assets, partly offset by the benefit of those rates on interest expense and a higher level of interest-earning assets. Subsequent to the commercial paper conduit consolidation in 2009, we have recorded aggregate discount accretion in interest revenue of $1.96 billion

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($621 million in 2009, $712 million in 2010, $220 million in 2011, $215 million in 2012, $137 million in 2013 and $55 million in the first six months of 2014). The timing and ultimate recognition of any applicable discount accretion depends, in part, on factors that are outside of our control, including anticipated prepayment speeds and credit quality. The impact of these factors is uncertain and can be significantly influenced by general economic and financial market conditions. The timing and recognition of any applicable discount accretion can also be influenced by our ongoing management of the risks and other characteristics associated with our investment securities portfolio, including sales of securities which would otherwise generate interest revenue through accretion.

Depending on the factors discussed above, among others, we anticipate that, until the former conduit securities remaining in our investment portfolio mature or are sold, discount accretion will continue to contribute, though generally in declining amounts, to our net interest revenue. Assuming that we hold the remaining former conduit securities to maturity, all else being equal, we expect the remaining former conduit securities carried in our investment portfolio as of June 30, 2014 to generate aggregate discount accretion in future periods of approximately $522 million over their remaining terms, with approximately half of this aggregate discount accretion to be recorded over the next four years.

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

Interest-bearing deposits with banks averaged $53.56 billion for the quarter ended June 30, 2014, compared to $28.24 billion for the quarter ended June 30, 2013. For the first six months of 2014, such deposits averaged $43.54 billion, compared to $29.41 billion for the first six months of 2013. While these deposits reflect our maintenance of cash balances at the Federal Reserve, the European Central Bank, or ECB, and other non-U.S. central banks to satisfy regulatory reserve requirements, the above-described amounts also reflect the additional impact of continued elevated levels of client deposits and our investment of the excess deposits with these banks.

Certain client deposits were characterized as transient in nature and were placed with various central banks globally. If client deposits remain at or close to current elevated levels, we expect to continue to invest them in either money market assets, including central bank deposits, or in

investment securities, depending on our assessment of the underlying characteristics of the deposits.

Average investment securities decreased slightly to $117.59 billion for the quarter ended June 30, 2014 from $118.52 billion for the quarter ended June 30, 2013, and in the year-to-date comparison decreased to $117.71 billion from $119.06 billion. The decreases were generally the result of an asset allocation shift from our investment portfolio to loans and leases. Detail with respect to our investment portfolio as of June 30, 2014 and December 31, 2013 is provided in note 3 to the consolidated financial statements included in this Form 10-Q.

Loans and leases averaged $15.06 billion for the second quarter of 2014, compared to $14.00 billion for the second quarter of 2013, and $14.83 billion for the first six months of 2014, up from $13.37 billion for the same period in 2013. The increases were mainly related to mutual fund lending and our increased investment in senior secured bank loans, which in the aggregate averaged $10.13 billion for the quarter ended June 30, 2014 compared to $8.64 billion, the latter of which was all mutual fund lending, for the quarter ended June 30, 2013.

Average loans and leases also include short-duration advances. The proportion of the daily average of short-duration advances to average loans and leases declined to approximately 26% for the second quarter of 2014 from approximately 30% for the second quarter of 2013, and declined to approximately 25% for the first six months of 2014 from approximately 29% for the first six months of 2013. Short-duration advances provide liquidity to clients in support of their investment activities.

The following table presents average U.S. and non-U.S. short-duration advances for the periods indicated:

	Quarters Ended June 30,	
(In millions)	2014	2013
Average U.S. short-duration advances	$2,338	$2,652

Average non-U.S. short-duration advances	1,511	1,587
Average total short-duration advances	$3,849	$4,239

	Six Months Ended June 30,	
(In millions)	2014	2013
Average U.S. short-duration advances	$2,209	$2,372
Average non-U.S. short-duration advances	1,461	1,494
Average total short-duration advances	$3,670	$3,866

The decreases in average short-duration advances for the second quarter and first six months of 2014 compared to the second quarter and first six months of 2013 were mainly the result of clients continuing to hold higher levels of liquidity.

Average other interest-earning assets increased to $14.85 billion for the second quarter of 2014 from $11.02 billion for the second quarter of 2013, and increased to $14.19 billion from $10.03 billion in the year-to-date comparison. The increased levels were primarily the result of higher levels of cash collateral provided in connection with our enhanced custody business.

Aggregate average interest-bearing deposits increased to $129.99 billion for the second quarter of 2014 from $110.10 billion for second quarter of 2013, and increased to $121.72 billion from $111.60 billion in the year-to-date comparison. Higher levels of interest-bearing deposits were primarily the result of increases in both U.S. and non-U.S. transaction accounts. Future transaction account levels will be influenced by the underlying asset servicing business, as well as market conditions, including the general levels of U.S. and non-U.S. interest rates.

Average other short-term borrowings increased slightly to $4.00 billion for the second quarter of 2014 from $3.64 billion for the second quarter of 2013. In the year-to-date comparison, average other short-term borrowings declined to $3.96 billion from $4.14 billion, as higher levels of client deposits provided additional liquidity. The negative rate paid in the second quarter, and the significant decline in the rate paid in the first six months of 2014 compared to the first six months of 2013, resulted from a reclassification of certain derivative contracts that hedge our interest-rate risk on certain assets and liabilities, which reduced interest revenue and interest expense.

Average long-term debt increased to $9.34 billion for the second quarter of 2014 from $8.20 billion for the second quarter of 2013, and increased to $9.50 billion from $7.80 billion in the year-to-date comparison. The increase primarily reflected the issuance of $1.5 billion of senior and subordinated debt in May 2013 and the issuance of $1.0 billion of senior debt in November 2013, partly offset by the maturity of $500 million of senior debt in May 2014 and $250 million of senior debt in March 2014.

Average other interest-bearing liabilities increased to $7.56 billion for the second quarter of 2014 from $6.27 billion for the second quarter of 2013 and increased to $7.16 billion from $6.38 billion in the year-to-date comparison, primarily the result of higher levels of cash collateral received from clients in connection with our enhanced custody business.

Several factors could affect future levels of our net interest revenue and margin, including the 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; and the yields earned on securities purchased compared to the yields earned on securities sold or matured.

Based on market conditions and other factors, 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, 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 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 net interest revenue and net interest margin.

Gains (Losses) Related to Investment Securities, Net

The following tables present net realized gains from sales of available-for-sale securities and the components of net impairment losses, included in net gains and losses related to investment securities, for the periods indicated:

	Quarters Ended June 30,			
(In millions)	2014		2013	
Net realized gains from sales of available-for-sale securities	$—		$—	
Net impairment losses:				
Gross losses from other-than-temporary impairment	—		(6	)
Losses reclassified (from) to other comprehensive income	(2	)	(1	)

Net impairment losses[1]	(2)	(7)
Gains (losses) related to investment securities, net	$(2)	$(7)

[1] Net impairment losses, recognized in our consolidated statement of income, were composed of the following:

Impairment associated with expected credit losses	$(1)	$—
Impairment associated with management's intent to sell impaired securities prior to recovery in value	—	(6)
Impairment associated with adverse changes in timing of expected future cash flows	(1)	(1)
Net impairment losses	$(2)	$(7)

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MANAGEMENT'S DISCUSSION AND ANALYSIS OF FINANCIAL CONDITION AND RESULTS OF OPERATIONS (Continued)

	Six Months Ended June 30,	
(In millions)	2014	2013
Net realized gains from sales of available-for-sale securities	$15	$5
Net impairment losses:		
Gross losses from other-than-temporary impairment	(1)	(6)
Losses reclassified (from) to other comprehensive income	(10)	(4)
Net impairment losses[1]	(11)	(10)
Gains (losses) related to investment securities, net	$4	$(5)
[1] Net impairment losses, recognized in our consolidated statement of income, were composed of the following:		
Impairment associated with expected credit losses	$(10)	$—
Impairment associated with management's intent to sell impaired securities prior to recovery in value	—	(6)
Impairment associated with adverse changes in timing of expected future cash flows	(1)	(4)
Net impairment losses	$(11)	$(10)

From time to time, in connection with our ongoing management of our investment securities portfolio, we sell available-for-sale securities to manage risk, to take advantage of favorable market conditions, or for other reasons. In the first six months of 2014, we sold approximately $2.84 billion of such investment securities, compared to approximately $4.82 billion in the first six months of 2013, and recorded net realized gains of $15 million and $5 million, respectively, as presented in the preceding table.

We regularly review our investment securities portfolio to identify other-than-temporary impairment of individual securities. Additional information about investment securities, the gross gains and losses that compose the net gains from sales of securities and other-than-temporary impairment is provided in note 3 to the consolidated financial statements included in this Form 10-Q.

Expenses

The following tables present the components of expenses for the periods indicated:

	Quarters Ended June 30,		
(Dollars in millions)	2014	2013	% Change
Compensation and employee benefits	$978	$917	7 %
Information systems and communications	244	235	4
Transaction processing services	193	186	4
Occupancy	115	114	1
Acquisition costs	15	19	
Restructuring charges, net	13	11	
Other:			
Professional services	116	103	13
Amortization of other intangible assets	54	54	—
Securities processing costs	8	5	
Regulatory fees and assessments	19	17	
Other	95	137	(31)
Total other	292	316	(8)
Total expenses	$1,850	$1,798	3
Number of employees as of quarter-end	29,420	29,225	

	Six Months Ended June 30,		
(Dollars in millions)	2014	2013	% Change

Compensation and employee benefits	$2,135	$1,952	9	%
Information systems and communications	488	472	3	
Transaction processing services	384	366	5	
Occupancy	229	230	—	
Acquisition costs	36	34		
Restructuring charges, net	25	10		
Other:				
Professional services	221	182	21	
Amortization of other intangible assets	108	107	1	
Securities processing costs	31	10		
Regulatory fees and assessments	38	32		
Other	183	229	(20	)
Total other	581	560	4	
Total expenses	$3,878	$3,624	7	

Total expenses in the second quarter and first six months of 2014 increased 3% and 7%, respectively, compared to the second quarter and first six months of 2013.

Compensation and employee benefits expenses in the second quarter and first six months of 2014 increased 7% and 9%, respectively, compared to the second quarter and first six months of 2013. The increases were primarily the result of costs for additional staffing associated with the installation of new business, higher incentive compensation, the impact of the weaker U.S. dollar, annual merit increases, and higher regulatory compliance costs. These increases were partly offset by savings generated from the implementation of our Business Operations and Information Technology Transformation program. The six-month increase in compensation and employee benefits expenses also included $76 million of severance costs associated with staff reductions recorded in the first six months of 2014.

Compensation and employee benefits expenses in the second quarter and first six months of 2014 included approximately $15 million and $27 million, respectively, of costs related to the implementation of our Business Operations and Information Technology Transformation program, compared to approximately $19 million and $42 million, respectively, in the second quarter and first six months of 2013. These costs are not expected to recur subsequent to full implementation of the program, planned for the end of 2014.

The increases in information systems and communications expenses in the second quarter and first six months of 2014 of 4% and 3%, respectively, compared to the same periods in 2013 were mainly associated with higher infrastructure costs related to the implementation of our Business Operations and Information Technology Transformation program and the support of new business.

Additional information with respect to the impact of the Business Operations and Information Technology Transformation program on future compensation and employee benefits and information systems and communications expenses is provided in the following "Restructuring Charges" section.

Transaction processing services expenses increased 4% and 5% in the second quarter and first six months of 2014, respectively, compared to the second quarter and first six months of 2013. The increase primarily reflected higher equity market values and higher transaction volumes in the investment servicing business.

The 8% decrease in other expenses in the second quarter of 2014 compared to the second quarter of 2013 was primarily due to lower levels of charitable contributions and sales promotion costs, partly offset by higher levels of professional services associated with regulatory compliance requirements. The 4% increase in the first six months of 2014 compared to the first six months of 2013 was primarily the result of higher levels of professional services associated with regulatory compliance requirements, as well as securities processing costs associated with our transition management business, partly offset by a lower level of charitable contributions.

Our compliance obligations have increased significantly due to new regulations in the U.S. and internationally that have been adopted or proposed in response to the financial crisis. 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 programs. We anticipate that these evolving and increasing regulatory compliance requirements and expectations will continue to affect our expenses. Our employee compensation and benefits, information systems and other expenses could increase, as we further adjust our operations in response to new or proposed requirements and heightened expectations.

Acquisition Costs

In the second quarter and first six months of 2014, we recorded acquisition costs of $15 million and $36 million, respectively, compared to $19 million and $34 million, respectively, for the same periods in 2013. These amounts related to previously disclosed acquisitions, mainly our October 2012 acquisition of Goldman Sachs Administration Services.

Restructuring Charges

Information with respect to our Business Operations and Information Technology Transformation program and our 2012 expense control measures, including charges, employee reductions and aggregate activity in the related accruals, is provided in the following sections.

Business Operations and Information Technology Transformation Program

In November 2010, we announced a global multi-year Business Operations and Information Technology Transformation program. The program includes operational, information technology and targeted cost initiatives, including plans related to reductions in both staff and occupancy costs.

With respect to our business operations, we are standardizing certain core business processes, primarily through our execution of the State Street Lean methodology, and driving automation of these

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business processes. We are currently creating a new technology platform, including transferring certain core software applications to a private cloud, and have expanded our use of third-party service providers associated with components of our information technology infrastructure and application maintenance and support. We transferred the majority of our core software applications to a private cloud in 2013, and we expect to transfer the remaining core software applications in 2014.

To implement this program, we expect to incur aggregate pre-tax restructuring charges of approximately $400 million to $450 million over the four-year period ending December 31, 2014. To date, we have recorded aggregate restructuring charges of $400 million in our consolidated statement of income, as presented in the following table by type of cost:

(In millions)	Employee-Related Costs	Real Estate Consolidation	Information Technology Costs	Total
2010	$ 105	$ 51	$ —	$ 156
2011	85	7	41	133
2012	27	20	20	67
2013	13	13	(1)	25
First six months of 2014	16	3	—	19
Total	$ 246	$ 94	$ 60	$ 400

Employee-related costs included severance, benefits and outplacement services. Real estate consolidation costs resulted from actions taken to reduce our occupancy costs through the consolidation of leases and properties. Information technology costs included transition fees related to the above-described expansion of our use of third-party service providers.

In 2010, in connection with the program, we initiated the involuntary termination of 1,400 employees, or approximately 5% of our global workforce, which we completed by the end of 2011. In addition, in connection with our announcement in 2011 of the expansion of our use of third-party service providers associated with our information technology infrastructure and application maintenance and support, as well as the continued implementation of the business operations transformation component of the program, we identified 1,554 additional involuntary terminations. As of June 30, 2014, we eliminated 1,437 of these positions.

In connection with the continuing implementation of the program, we achieved incremental pre-tax expense savings of approximately $220 million in 2013, $112 million in 2012 and $86 million in 2011, in each case compared to our 2010 expenses from operations, all else being equal. We expect to achieve additional pre-tax expense savings in 2014 of approximately $130 million.

These pre-tax expense savings relate only to the Business Operations and Information Technology

Transformation program and are based on projected improvement from our total 2010 expenses from operations, all else being equal. Our actual total expenses have increased since 2010, and may in the future increase or decrease, due to other factors. The majority of the annual savings have affected compensation and employee benefits expenses. These savings have been modestly offset by increases in information systems and communications expenses. Excluding the expected aggregate restructuring charges of $400 million to $450 million described earlier, we expect the program to reduce our pre-tax expenses from operations, on an annualized basis, by approximately $575 million to $625 million by the end of 2014 compared to 2010, all else being equal, with the full effect to be realized in 2015. We expect the business operations transformation component of the program to result in approximately $450 million of these savings and the information technology transformation component of the program to result in approximately $150 million of these savings.

2012 Expense Control Measures

In the fourth quarter of 2012, in connection with expense control measures designed to better align our expenses to our business strategy and related outlook for 2013, we identified additional targeted staff reductions. As a result of these actions, we have recorded aggregate pre-tax restructuring charges of $142 million in our consolidated statement of income, as presented in the following table by type of cost:

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MANAGEMENT'S DISCUSSION AND ANALYSIS OF FINANCIAL CONDITION
AND RESULTS OF OPERATIONS (Continued)

(In millions)	Employee-Related Costs	Asset and Other Write-Offs	Total
2012	$ 129	$4	$133
2013	(4)	7	3
First six months of 2014	—	6	6
Total	$ 125	$17	$142

Employee-related costs included severance, benefits and outplacement services. Costs for asset and other write-offs were primarily related to contract terminations. We originally identified involuntary terminations of 960 employees (630 positions after replacements). As of March 31, 2014, we substantially completed these reductions.

Aggregate Restructuring-Related Accrual Activity

The following table presents aggregate activity associated with accruals that resulted from the charges associated with the Business Operations and Information Technology Transformation program and expense control measures:

(In millions)	Employee-Related Costs	Real Estate Consolidation	Information Technology Costs	Fixed-Income Trading Portfolio	Asset and Other Write-Offs	Total
Initial accrual	$105	$ 51	$—	$—	$—	$156
Payments	(15)	(4)	—	—	—	(19)
Balance as of December 31, 2010	90	47	—	—	—	137
Additional accruals for Business Operations and Information Technology Transformation program	85	7	41	—	—	133
Accruals for 2011 expense control measures	62	—	—	38	20	120
Payments and adjustments	(75)	(15)	(8)	—	(5)	(103)
Balance as of December 31, 2011	162	39	33	38	15	287
Additional accruals for Business Operations and Information Technology Transformation program	27	20	20	—	—	67
Additional accruals for 2011 expense control measures	3	—	—	(9)	5	(1)
Accruals for 2012 expense control measures	129	—	—	—	4	133
Payments and adjustments	(126)	(10)	(48)	(29)	(11)	(224)
Balance as of December 31, 2012	195	49	5	—	13	262
Additional accruals for Business Operations and Information Technology Transformation program	13	13	(1)	—	—	25
Additional accruals for 2012 expense control measures	(4)	—	—	—	7	3
Payments and adjustments	(154)	(13)	(4)	—	(13)	(184)
Balance as of December 31, 2013	50	49	—	—	7	106
Additional accruals for Business Operations and Information Technology Transformation program	16	3	—	—	—	19

Additional accruals for 2012 expense control measures	—	—	—	—	6	6
Payments and adjustments	(26)	(29)	—	—	(4)	(59)
Balance as of June 30, 2014	$40	$ 23	$—	$—	$9	$72

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MANAGEMENT'S DISCUSSION AND ANALYSIS OF FINANCIAL CONDITION
AND RESULTS OF OPERATIONS (Continued)

Income Tax Expense
Income tax expense was $124 million in the second quarter of 2014 compared to $183 million in the second quarter of 2013. In the first six months of 2014 and 2013, income tax expense was $216 million and $328 million, respectively. Our effective tax rate for the first six months of 2014 was 18.0% compared to 23.9% for the same period in 2013, with the decline primarily associated with an increase in tax-advantaged investments, primarily renewable energy.
LINE OF BUSINESS INFORMATION
We have two lines of business: Investment Servicing and Investment Management. Given our services and management organization, 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. Information about our two lines of business, as well as the revenues, expenses and capital allocation methodologies associated with them, is provided in note 25 to the consolidated financial statements included in our 2013 Form 10-K.

The following is a summary of our line-of-business results for the periods indicated. The "Other" column for the second quarter and first six months of 2014 included severance costs associated with staff reductions of $4 million and $76 million, respectively, as well as net acquisition and restructuring costs of $28 million and $61 million, respectively. In addition, the first six months of 2014 included net provisions for litigation exposure and other costs of $6 million. The "Other" column for the second quarter and first six months of 2013 included net acquisition and restructuring costs of $30 million and $44 million, respectively, as well as net provisions for litigation exposure and other costs of $15 million for both periods. The amounts in the "Other" columns were not allocated to State Street's business lines. Results for the 2013 periods reflect reclassifications, for comparative purposes, related to management changes in methodologies associated with allocations of revenue and expenses reflected in line-of-business results for 2014.

	Quarters Ended June 30,									
	Investment Servicing			Investment Management			Other		Total	
(Dollars in millions, except where otherwise noted)	2014	2013	% Change Q2 2014 vs. Q2 2013	2014	2013	% Change Q2 2014 vs. Q2 2013	2014	2013	2014	2013
Fee revenue:										
Servicing fees	$1,288	$1,201	7 %	$—	$—		$—	$—	$1,288	$1,201
Management fees	—	—		300	277	8 %	—	—	300	277
Trading services	249	287	(13)	11	17	(35)	—	—	260	304
Securities finance	147	131	12	—	—		—	—	147	131
Processing fees and other	42	58	(28)	2	—		—	—	44	58
Total fee revenue	1,726	1,677	3	313	294	6	—	—	2,039	1,971
Net interest revenue	545	571	(5)	16	25	(36)	—	—	561	596
Gains (losses) related to investment securities, net	(2)	(7)		—	—		—	—	(2)	(7)

Total revenue	2,269	2,241	1	329	319	3	—	—	2,598	2,560
Provision for loan losses	2	—		—	—		—	—	2	—
Total expenses	1,593	1,549	3	225	204	10	32	45	1,850	1,798
Income before income tax expense	$674	$692	(3)	$104	$115	(10)	$(32)	$(45)	$746	$762
Pre-tax margin	30%	31%		32%	36%				29%	30%
Average assets (in billions)	$231.3	$203.6		$3.4	$4.1				$234.7	$207.7

	Six Months Ended June 30, Investment Servicing			Investment Management			Other		Total	
(Dollars in millions, except where otherwise noted)	2014	2013	% Change 6 mos. 2014 vs. 6 mos. 2013	2014	2013	% Change 6 mos. 2014 vs. 6 mos. 2013	2014	2013	2014	2013
Fee revenue:										
Servicing fees	$2,526	$2,376	6%	$—	$—		$—	$—	$2,526	$2,376
Management fees	—	—		592	540	10%	—	—	592	540
Trading services	490	552	(11)	23	41	(44)	—	—	513	593
Securities finance	232	209	11	—	—		—	—	232	209
Processing fees and other	97	105	(8)	3	5		—	—	100	110
Total fee revenue	3,345	3,242	3	618	586	5	—	—	3,963	3,828
Net interest revenue	1,083	1,128	(4)	33	44	(25)	—	—	1,116	1,172
Gains (losses) related to investment securities, net	4	(5)		—	—		—	—	4	(5)
Total revenue	4,432	4,365	2	651	630	3	—	—	5,083	4,995
Provision for loan losses	4	—		—	—		—	—	4	—
Total expenses	3,266	3,139	4	469	426	10	143	59	3,878	3,624
Income before income tax expense	$1,162	$1,226	(5)	$182	$204	(11)	$(143)	$(59)	$1,201	$1,371
Pre-tax margin	26%	28%		28%	32%				24%	27%
Average assets (in billions)	$221.8	$204.0		$3.4	$4.0				$225.2	$208.0

Investment Servicing

Total revenue in the second quarter and first six months of 2014 for our Investment Servicing line of business, as presented in the preceding tables, increased 1% and 2%, respectively, compared to the same periods in 2013. Total fee revenue increased 3% in both comparisons, generally the result of increases in servicing fees and securities finance revenue, partly offset by a decline in trading services revenue.

Servicing fees in the second quarter and first six months of 2014 increased 7% and 6%, respectively, compared to the same periods in 2013. The increases for both comparisons primarily reflected stronger global equity markets, the positive revenue impact of net new business (revenue added from new servicing business less revenue lost from the removal of assets serviced), and the impact of the weaker U.S. dollar.

Trading services revenue in the second quarter and first six months of 2014 declined 13% and 11%, respectively, compared to the same periods in 2013. The decreases in both comparisons were mainly the result of lower volatility

(partly offset by higher client volumes in direct sales and trading foreign exchange) and lower client volumes in electronic trading.
Securities finance revenue in the second quarter and first six months of 2014 increased 12% and 11%, respectively, compared to the same periods in 2013. The increase was generally reflective of growth in our enhanced custody business.
Processing fees and other revenue in the second quarter and first six months of 2014

decreased 28% and 8%, respectively, compared to the same periods in 2013, mainly due to higher amortization of tax-advantaged investments, partly offset by higher revenue from our investment in bank-owned life insurance.
Servicing fees, securities finance revenue and net gains (losses) related to investment securities for our Investment Servicing business line are identical to the respective consolidated results. Refer to “Servicing Fees,” "Securities Finance" and “Gains (Losses) Related to Investment Securities, Net” under “Total Revenue” in this Management’s Discussion and Analysis for a more in-depth discussion. A discussion of trading services revenue and processing fees and other revenue is provided under “Trading Services” and “Processing Fees and Other” in “Total Revenue.”
Net interest revenue in the second quarter and the first six months of 2014 decreased 5% and 4%, respectively, compared to the same periods in 2013. The decreases were generally the result of lower yields on interest-earning assets, as lower global interest rates affected revenue from floating-rate assets, partly offset by lower interest expense and higher interest-earning assets. A discussion of net interest revenue is provided under “Net Interest Revenue” in “Total Revenue.”
Total expenses in the second quarter and first six months of 2014 increased 3% and 4%, respectively, compared to the same periods in 2013. Both comparisons reflected increases in compensation and employee benefits expenses, driven primarily by costs associated with the installation of new business, higher incentive compensation, the impact of the weaker U.S. dollar, annual merit increases, and higher regulatory

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compliance costs. The increase was partly offset by savings generated from the continued implementation of our Business Operations and Information Technology Transformation program. A more detailed discussion of expenses is provided under “Expenses” in “Consolidated Results of Operations.”

Investment Management

Total revenue in the second quarter and first six months of 2014 for our Investment Management line of business, as presented in the preceding tables, increased 3% compared to the same periods in 2013. Total fee revenue increased 6% and 5%, respectively compared to the same periods in 2013, primarily the result of increases in management fees, partly offset by decreases in trading services revenue.

Management fees in the second quarter and first six months of 2014 increased 8% and 10%, respectively, compared to the same periods in 2013. The increases in both comparisons primarily resulted from stronger global equity markets, partly offset by the negative impact of the excess of revenue lost from liquidations of managed assets over revenue added from newly installed assets to be managed. Trading services revenue in the second quarter and first six months of 2014 declined 35% and 44%, respectively, compared to the same periods in 2013, mainly due to lower distribution fees associated with the SPDR® Gold ETF, which resulted from outflows as average gold prices declined during the periods.

Management fees for the Investment Management business line are identical to the

respective consolidated results. Refer to “Management Fees” in “Total Revenue” in this Management's Discussion and Analysis for a more in-depth discussion. A discussion of trading services revenue is provided under “Trading Services” in “Total Revenue.”

Total expenses in the second quarter and first six months of 2014 both increased 10% compared to the same periods in 2013. The increases in both comparisons generally resulted from credits related to gains and recoveries associated with Lehman Brothers-related assets recorded in the second quarter of 2013. In addition, the year-to-date comparison reflected higher incentive compensation, higher sales promotion expenses, and increased costs associated with information technology contract staff.

FINANCIAL CONDITION

The following table presents the components of our average total interest-earning and noninterest-earning assets, average total interest-bearing and noninterest-bearing liabilities, and average preferred and common shareholders' equity for the six months ended June 30, 2014 and 2013. Additional information about our average statement of condition, primarily our interest-earning assets and interest-bearing liabilities, is included under “Consolidated Results of Operations - Total Revenue - Net Interest Revenue” in this Management's Discussion and Analysis.

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MANAGEMENT'S DISCUSSION AND ANALYSIS OF FINANCIAL CONDITION
AND RESULTS OF OPERATIONS (Continued)

Six Months Ended June 30,	2014	2013
(In millions)	Average Balance	Average Balance
Assets:		
Interest-bearing deposits with banks	$43,543	$29,408
Securities purchased under resale agreements	5,463	5,751
Trading account assets	927	682
Investment securities	117,713	119,059
Loans and leases	14,833	13,374
Other interest-earning assets	14,190	10,025
Average total interest-earning assets	196,669	178,299
Cash and due from banks	4,963	3,897
Other noninterest-earning assets	23,538	25,782
Average total assets	$225,170	$207,978
Liabilities and shareholders' equity:		
Interest-bearing deposits:		
U.S.	$16,409	$10,669
Non-U.S.	105,308	100,930
Total interest-bearing deposits	121,717	111,599
Securities sold under repurchase agreements	8,586	8,156
Federal funds purchased	20	331
Other short-term borrowings	3,955	4,138
Long-term debt	9,503	7,802
Other interest-bearing liabilities	7,161	6,384
Average total interest-bearing liabilities	150,942	138,410
Noninterest-bearing deposits	41,312	34,421
Other noninterest-bearing liabilities	11,786	14,281
Preferred shareholders' equity	979	489
Common shareholders' equity	20,151	20,377
Average total liabilities and shareholders' equity	$225,170	$207,978

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MANAGEMENT'S DISCUSSION AND ANALYSIS OF FINANCIAL CONDITION AND RESULTS OF OPERATIONS (Continued)

Investment Securities

The following tables present the carrying values of investment securities by type as of the dates indicated:

(In millions)	June 30, 2014	December 31, 2013
Available for sale:		
U.S. Treasury and federal agencies:		
Direct obligations	$3,435	$709
Mortgage-backed securities	22,139	23,563
Asset-backed securities:		
Student loans(1)	13,962	14,542
Credit cards	6,566	8,210
Sub-prime	1,101	1,203
Other	4,635	5,064
Total asset-backed securities	26,264	29,019
Non-U.S. debt securities:		
Mortgage-backed securities	11,435	11,029
Asset-backed securities	4,200	5,390
Government securities	3,823	3,761
Other	5,757	4,727
Total non-U.S. debt securities	25,215	24,907
State and political subdivisions	10,617	10,263
Collateralized mortgage obligations	5,374	5,269
Other U.S. debt securities	4,842	4,980
U.S. equity securities	37	34
Non-U.S. equity securities	1	1
U.S. money-market mutual funds	615	422
Non-U.S. money-market mutual funds	7	7
Total	$98,546	$99,174

(In millions)	June 30, 2014	December 31, 2013
Held to Maturity:		
U.S. Treasury and federal agencies:		
Direct obligations	$5,119	$5,041
Mortgage-backed securities	74	91
Asset-backed securities:		
Student loans(1)	1,900	1,627
Credit cards	897	762
Other	692	782
Total asset-backed securities	3,489	3,171
Non-U.S. debt securities:		
Mortgage-backed securities	4,274	4,211
Asset-backed securities	2,898	2,202
Government securities	2	2
Other	245	192
Total non-U.S. debt securities	7,419	6,607
State and political subdivisions	15	24
Collateralized mortgage obligations	2,641	2,806

Total	$18,757	$17,740

(1) Substantially composed of securities guaranteed by the federal government with respect to at least 97% of defaulted principal and accrued interest on the underlying loans.

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 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.

Our portfolio is concentrated in securities with high credit quality, with approximately 89% of the carrying value of the portfolio rated "AAA" or "AA" as of both June 30, 2014 and December 31, 2013.

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MANAGEMENT'S DISCUSSION AND ANALYSIS OF FINANCIAL CONDITION
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The following table presents the composition of the carrying value of the portfolio, by external credit rating, as of the dates indicated:

	June 30, 2014		December 31, 2013	
AAA[1]	70	%	70	%
AA	19		19	
A	6		6	
BBB	3		3	
Below BBB	2		2	
	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, 2014, the investment portfolio of 9,720 securities was diversified with respect to asset class. As of June 30, 2014 and December 31, 2013, approximately 71% and 74%, respectively, of the aggregate carrying value of the portfolio as of that date was composed of mortgage-backed and asset-backed securities. The asset-backed portfolio, of which approximately 97% of the carrying value as of both dates 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.

In December 2013, U.S. regulators issued final regulations to implement the so-called "Volcker rule," one of many provisions of the Dodd-Frank Act. The Volcker rule will, among other things, require banking organizations covered by the rule to either restructure or divest certain investments in and relationships with "covered funds," as defined in the final Volcker rule regulations. The classification of certain types of investment securities or structures, such as collateralized loan obligations, or CLOs, as "covered funds" remains subject to market, and ultimately regulatory, interpretation, based on the specific terms and other characteristics relevant to such investment securities and structures.

As of June 30, 2014, we held an aggregate of approximately $5.10 billion of investments in CLOs. As of the same date, these investments had an aggregate pre-tax net unrealized gain of approximately $120 million, composed of gross unrealized gains of $132 million and gross unrealized losses of $12 million. In the event that we or our banking regulators conclude that such investments in CLOs, or other investments, are "covered funds," we will be required to divest such investments if we are

unable to "cure" those investments before the conformance period ends on July 21, 2017. If other banking entities reach similar conclusions with respect to similar investments held by them, the prices of such investments could decline significantly, and we may be required to divest such investments at a significant discount compared to the investments' book value. This could result in a material adverse effect on our consolidated results of operations in the period in which such a divestment occurs or on our consolidated financial condition.

Based on our assessment to date of the remaining conformance period, we believe that it is not likely that we will be required to sell those investments before they recover in value.

Non-U.S. Debt Securities

Approximately 28% and 27% of the aggregate carrying value of our investment securities portfolio as of June 30, 2014 and December 31, 2013, respectively, was composed of non-U.S. debt securities.

The following table presents the carrying values of our non-U.S. debt securities available for sale and held to maturity, included in the preceding table of investment securities carrying values, by significant country of issuer or location of collateral, as of the dates indicated:

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(In millions)	June 30, 2014	December 31, 2013
Available for Sale:		
United Kingdom	$8,768	$9,357
Australia	4,168	3,551
Netherlands	3,479	3,471
Canada	2,568	2,549
France	1,541	1,581
Germany	1,155	1,410
Japan	1,008	971
South Korea	620	744
Finland	452	397
Norway	447	369
Italy	434	—
Sweden	141	142
Belgium	136	—
Austria	82	83
Other	216	282
Total	$25,215	$24,907
Held to Maturity:		
Australia	$2,348	$2,216
Germany	1,729	1,263
United Kingdom	1,615	1,474
Netherlands	1,002	934
Italy	260	270
Spain	197	206
Ireland	81	86
Other	187	158
Total	$7,419	$6,607

Approximately 90% and 89% of the aggregate carrying value of these non-U.S. debt securities was rated "AAA" or "AA" as of June 30, 2014 and December 31, 2013, respectively. The majority of these securities comprise 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, 2014 and December 31, 2013, approximately 73% and 72%, respectively, of the aggregate carrying value of these non-U.S. debt securities was floating-rate, and accordingly, the securities are considered to have minimal interest-rate risk. As of June 30, 2014, these non-U.S. debt securities had an average market-to-book ratio of 101.5%, and an aggregate pre-tax net unrealized gain of approximately $482 million, composed of gross unrealized gains of $515 million and gross unrealized losses of $33 million. These unrealized amounts included a pre-tax net unrealized gain of $286 million, composed of gross unrealized gains of $297 million and gross unrealized losses of $11 million, associated with non-U.S. debt securities available for sale.

As of June 30, 2014, the underlying collateral for these mortgage- and asset-backed securities primarily included U.K. prime mortgages, Australian and Dutch mortgages and German automobile loans. The securities listed under "Canada" were composed of Canadian government securities and corporate debt. The securities listed under "France" were composed of automobile loans and corporate debt. The securities listed under "Japan" were substantially composed of Japanese government securities. The securities listed under "South Korea" were composed of South Korean government securities. The "other" category of available-for-sale securities as of June 30, 2014 and December 31, 2013 included approximately $76 million and $133 million, respectively, related to Portugal, Ireland and Spain, all of which were mortgage-backed securities. The "other" category of held-to-maturity securities as of

June 30, 2014 and December 31, 2013 included approximately $42 million and $44 million, respectively, of securities related to Portugal, all of which were mortgage-backed securities.

Our aggregate exposure to Spain, Italy, Ireland and Portugal as of June 30, 2014 did not include any direct sovereign debt exposure to any of these countries. Our indirect exposure to these countries as of June 30, 2014 totaled approximately $1.09 billion, including approximately $926 million of mortgage- and asset-backed securities, composed of $197 million in Spain, $530 million in Italy, $119 million in Ireland and $80 million in Portugal. These mortgage- and asset-backed securities had an aggregate pre-tax net unrealized gain of approximately $120 million as of June 30, 2014, composed of gross unrealized gains of $122 million and gross unrealized losses of $2 million. We recorded no other-than-temporary impairment on these mortgage- and asset-backed securities in our consolidated statement of income in the first six months of 2014. We recorded other-than-temporary impairment of $6 million on one of these securities in our consolidated statement of income in the first six months of 2013, all in the second quarter of 2013, associated with management's intent to sell an impaired security prior to its recovery in value.

Throughout the sovereign debt crisis, the major independent credit rating agencies have downgraded, and may in the future do so again, 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. As a result, we may be exposed to increased counterparty risk, leading to negative ratings volatility.

Municipal Securities

We carried an aggregate of approximately $10.63 billion and $10.29 billion of municipal securities, classified as state and political subdivisions in the preceding table of investment securities carrying values, in our investment securities portfolio as of June 30, 2014 and December 31, 2013, respectively. Substantially all of these securities were classified as available for sale, with the remainder classified as held to maturity. As of the same dates, we also provided approximately $7.50 billion and $8.16 billion, respectively, of credit and liquidity facilities to municipal issuers as a form of credit enhancement.

The following tables present our combined credit exposure to state and municipal obligors that represented 5% or more of our aggregate municipal credit exposure of approximately $18.13 billion as of June 30, 2014 and $18.45 billion as of December 31, 2013 across our businesses, grouped by state to display geographic dispersion:

June 30, 2014	Total Municipal Securities	Credit and Liquidity Facilities	Total	% of Total Municipal Exposure	
(Dollars in millions)					
State of Issuer:					
Texas	$ 1,265	$ 1,566	$2,831	16	%
New York	919	996	1,915	11	
California	409	1,479	1,888	10	
Massachusetts	993	756	1,749	10	
Maryland	422	504	926	5	
Total	$ 4,008	$ 5,301	$9,309		

December 31, 2013	Total Municipal Securities	Credit and Liquidity Facilities	Total	% of Total Municipal Exposure	
(Dollars in millions)					
State of Issuer:					
Texas	$ 1,233	$ 1,628	$2,861	16	%
New York	919	1,000	1,919	10	
Massachusetts	967	759	1,726	9	
California	373	1,266	1,639	9	
Maryland	327	643	970	5	
Total	$ 3,819	$ 5,296	$9,115		

Our aggregate municipal securities exposure presented in the foregoing table was concentrated primarily with highly-rated counterparties, with approximately 90% of the obligors rated "AAA" or "AA" as of June 30, 2014, compared to approximately 84% rated "AAA" or "AA" as of December 31, 2013. As of June 30, 2014, approximately 68% and 31% of our aggregate exposure was associated with general obligation and revenue bonds, respectively, compared to 64% and 34%, respectively, as of December 31, 2013. In addition, we had no exposures associated with healthcare, 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.

Additional information with respect to our assessment of other-than-temporary impairment of our municipal securities is provided in note 3 to the consolidated financial statements included in this Form 10-Q.

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 debt securities available for sale and held to maturity, 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 following table presents the amortized cost and fair value, and associated net unrealized gains and losses, of investment securities available for sale and held to maturity as of the dates indicated:

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MANAGEMENT’S DISCUSSION AND ANALYSIS OF FINANCIAL CONDITION AND RESULTS OF OPERATIONS (Continued)

(In millions)	June 30, 2014[1] Amortized Cost	Net Unrealized Gains(Losses)	Fair Value	December 31, 2013[1] Amortized Cost	Net Unrealized Gains(Losses)	Fair Value
Available for sale[2]	$97,739	$ 807	$98,546	$99,159	$ 15	$99,174
Held to maturity[2]	18,757	107	18,864	17,740	(180)	17,560
Total investment securities	$116,496	$ 914	$117,410	$116,899	$ (165)	$116,734
Net after-tax unrealized gain (loss)		$ 548			$ (96)	

(1) Amounts excluded the remaining net unrealized losses primarily related to reclassifications of securities available for sale to securities held to maturity in 2008, recorded in accumulated other comprehensive income, or AOCI, within shareholders' equity in our consolidated statement of condition. Additional information is provided in note 10 to the consolidated financial statements included in this Form 10-Q.
(2) Securities available for sale are carried at fair value, with after-tax net unrealized gains and losses recorded in AOCI. Securities held to maturity are carried at cost, and unrealized gains and losses are not recorded in our consolidated financial statements.

The aggregate improvement to a net unrealized gain as of June 30, 2014 from a net unrealized loss as of December 31, 2013 presented above was primarily attributable to narrowing spreads and declining interest rates in the first six months of 2014.

We conduct periodic reviews of individual securities to assess whether other-than-temporary impairment exists. Our assessment of other-than-temporary impairment 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, other-than-temporary impairment could increase, in particular the credit-related component that would be recorded in our consolidated statement of income.

In the aggregate, we recorded net losses from other-than-temporary impairment of $2 million and $11 million in the second quarter and first six months of 2014, respectively, compared to $7 million and $10 million in the second quarter and first six months of 2013, respectively. Additional information with respect to this other-than-temporary impairment and net impairment losses, as well as information about our assessment of impairment, is provided in note 3 to the consolidated financial statements included in this Form 10-Q.

Given the exposure of our investment securities portfolio, particularly mortgage- and asset-backed securities, to residential mortgage and other consumer credit risks, the performance of the U.S. housing market is a factor in the portfolio's credit performance. As such, our assessment of other-than-temporary impairment relies, in part, on our estimates of trends in national housing prices in addition to

trends in unemployment rates, interest rates and the timing of defaults. Generally, indices that measure trends in national housing prices are published in arrears. As of March 31, 2014, national housing prices, according to the Case-Shiller National Home Price Index, had declined by approximately 21% peak-to-current. Overall, our evaluation of other-than-temporary impairment as of June 30, 2014 continued to include an expectation of a U.S. housing recovery characterized by relatively modest growth in national housing prices over the next few years. In connection with our assessment of other-than-temporary impairment with respect to relevant securities in our investment portfolio in future periods, we will consider trends in national housing prices that we observe at those times, including the Case-Shiller National Home Price Index, in addition to trends in unemployment rates, interest rates and the timing of defaults.

The other-than-temporary impairment of our investment securities portfolio continues to be sensitive to our estimates of future cumulative losses. However, given our positive outlook for U.S. national housing prices, our sensitivity analysis indicated, as of June 30, 2014, that our investment securities portfolio was less exposed to the overall housing price outlook relative to other factors, including unemployment rates and interest rates.

The residential mortgage servicing environment continues to be challenging. The time line to liquidate distressed loans continues to extend, but to a lesser degree as a result of strengthening in the national housing market. The rate at which distressed residential mortgages are liquidated may affect, among other things, our investment securities portfolio. Such effects could include the timing of cash flows or the credit quality associated with the mortgages collateralizing certain of our residential

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MANAGEMENT'S DISCUSSION AND ANALYSIS OF FINANCIAL CONDITION
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mortgage-backed securities, which, accordingly, could result in the recognition of additional other-than-temporary impairment in future periods.

Our evaluation of potential other-than-temporary impairment of mortgage-backed securities with collateral located in Spain, Italy, Ireland and Portugal takes into account government intervention in the corresponding mortgage markets and assumes a conservative baseline macroeconomic environment for this region, factoring in slow economic growth and government austerity measures. Our baseline view assumes a recessionary period characterized by high unemployment and by additional declines in housing prices of between 2% and 15% across these four countries. Our evaluation of other-than-temporary impairment in our base case does not assume a disorderly sovereign debt restructuring or a break-up of the Eurozone.

In addition, we perform stress testing and sensitivity analysis in order to assess the impact of more severe assumptions on potential other-than-temporary impairment. For example, we estimate, using relevant information as of June 30, 2014 and assuming that all other factors remain constant, that in more stressful scenarios in which unemployment, gross domestic product and housing prices in these four countries deteriorate over the relevant periods more than we expected as of June 30, 2014, other-than-temporary impairment could increase by a range of $2 million to $39 million. This sensitivity estimate is based on a number of factors, including, but not limited to, the level of housing prices and the timing of defaults. To the extent that such factors differ significantly from management's current expectations, resulting loss estimates may differ materially from those stated.

Excluding other-than-temporary impairment recorded in the first six months of 2014, management considers the aggregate decline in fair value of the remaining investment securities and the resulting gross unrealized losses as of June 30, 2014 to be temporary and not the result of any material changes in the credit characteristics of the securities. Additional information about these gross unrealized losses is provided in note 3 to the consolidated financial statements included in this Form 10-Q.

Loans and Leases

The following table presents our U.S. and non-U.S. loans and leases, by segment, as of the dates indicated:

(In millions)	June 30, 2014	December 31, 2013
Institutional:		
U.S.	$12,765	$10,623
Non-U.S.	3,771	2,654
Commercial real estate:		
U.S.	263	209
Total loans and leases	16,799	13,486
Allowance for loan losses	(32)	(28)
Loans and leases, net of allowance for loan losses	$16,767	$13,458

The increase in loans in the institutional segment presented in the preceding table was mainly related to an increase in mutual fund lending, higher levels of short-duration advances, and our continued investment in the non-investment-grade lending market through participations in loan syndications, specifically senior secured bank loans, that we began in 2013. Aggregate short-duration advances to our clients included in the institutional segment were $5.41 billion and $2.45 billion as of June 30, 2014 and December 31, 2013, respectively. Senior secured bank loans are more fully described below.

Additional information about all of our loan-and-lease segments, as well as underlying classes, is provided in note 4 to the consolidated financial statements included in this Form 10-Q, and in note 5 to the consolidated financial statements included in our 2013 Form 10-K.

As of June 30, 2014 and December 31, 2013, our investment in senior secured bank loans totaled approximately $1.32 billion and $724 million, respectively. In addition, we had binding unfunded commitments as of June 30, 2014 totaling $236 million to participate in such syndications. We expect to increase our level of participation in these loan syndications in future periods.

These loans, which we have rated “speculative” under our internal risk-rating framework (refer to note 4 to the consolidated financial statements included in this Form 10-Q), are externally rated “BBB,” “BB” or “B,” with approximately 95% of the loans rated “BB” or “B” as of June 30, 2014, compared to 94% as of as of December 31, 2013. We limit our investment to larger, more liquid credits underwritten by major global financial institutions, we apply our internal credit analysis process to each potential investment, and we diversify our exposure by counterparty and industry segment. However, these loans have significant exposure to credit losses relative to higher-rated loans. As of June 30, 2014, our allowance for loan losses included approximately $20 million related to these commercial and financial loans.

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MANAGEMENT’S DISCUSSION AND ANALYSIS OF FINANCIAL CONDITION AND RESULTS OF OPERATIONS (Continued)

As of June 30, 2014 and December 31, 2013, unearned income deducted from our investment in leveraged lease financing was $117 million and $121 million, respectively, for U.S. leases and $274 million and $298 million, respectively, for non-U.S. leases.

As of both June 30, 2014 and December 31, 2013, we held an aggregate of approximately $130 million of commercial real estate loans which were modified in troubled debt restructurings. No impairment loss was recognized upon restructuring of the loans, as the discounted cash flows of the modified loans exceeded the carrying amount of the original loans as of the modification date. No loans were modified in troubled debt restructurings in the first six months of 2014 or in all of 2013.

The following table presents activity in the allowance for loan losses for the periods indicated:

	Six Months Ended June 30,	
(In millions)	2014	2013
Allowance for loan losses:		
Beginning balance	$28	$22
Provision for loan losses:		
Institutional	4	—
Ending balance	$32	$22

The provision of $4 million recorded in the six months ended June 30, 2014 was composed of a provision of $14 million associated with an increase in our estimates of credit losses on our portfolio of senior secured bank loans, as the portfolio continues to grow and become more seasoned, net of a negative provision of $10 million associated with the pay-down of an unrelated commercial and financial loan with speculative-rated credit quality.

As of June 30, 2014, approximately $20 million of our allowance for loan losses was related to senior secured bank loans included in the institutional segment; the remaining $12 million was related to other commercial and financial loans in the institutional segment. The senior secured bank loans were purchased in connection with our participation in loan syndications in the non-investment-grade lending market beginning in 2013.

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.

Additional information with respect to the nature of our cross-border outstandings is provided under “Financial Condition - Cross-Border Outstandings” in Management's Discussion and Analysis included in our 2013 Form 10-K.

The following table presents our cross-border outstandings in countries in which we do business, and which amounted to at least 1% of our consolidated total assets as of the dates indicated. The aggregate of the total cross-border outstandings presented in the table represented approximately 17% and 19% of our consolidated total assets as of June 30, 2014 and December 31, 2013, respectively.

(In millions)	Investment Securities and Other Assets	Derivatives and Securities on Loan	Total Cross-Border Outstandings
June 30, 2014			
United Kingdom	$16,793	$862	$17,655
Japan	11,321	90	11,411
Australia	7,767	133	7,900
Netherlands	4,559	132	4,691

Germany	3,643	356	3,999
Canada	3,235	395	3,630
December 31, 2013			
United Kingdom	$15,422	$1,697	$17,119
Australia	7,309	672	7,981
Netherlands	4,542	277	4,819
Canada	3,675	620	4,295
Germany	4,062	147	4,209
France	2,887	735	3,622
Japan	2,445	605	3,050

Aggregate cross-border outstandings in countries which amounted to between 0.75% and 1% of our consolidated total assets totaled approximately $2.10 billion to France as of June 30, 2014, and

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approximately $1.85 billion to China as of December 31, 2013.
The following table presents our cross-border outstandings in Italy, Ireland, Spain and Portugal as of the dates indicated:

(In millions)	Investment Securities and Other Assets	Derivatives and Securities on Loan	Total Cross-Border Outstandings
June 30, 2014			
Italy	$1,060	$2	$1,062
Ireland	509	386	895
Spain	197	42	239
Portugal	80	—	80
December 31, 2013			
Italy	$763	$2	$765
Ireland	369	304	673
Spain	271	11	282
Portugal	78	—	78

As of June 30, 2014, none of the exposures in these countries was individually greater than 0.75% of our consolidated total assets. The aggregate exposures consisted primarily of interest-bearing deposits, investment securities, loans, including short-duration advances, and foreign exchange contracts. We had not recorded any provisions for loan losses with respect to any of our exposure in these countries as of June 30, 2014.

Risk Management

General

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;
- market risk associated with our trading activities;
- market risk associated with our non-trading, or asset-and-liability management, activities, which consists primarily of interest-rate risk; and
- business risk, including reputational 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 under Item 1A, "Risk Factors," included in our 2013 Form 10-K.

The scope of our business requires that we balance these risks with a comprehensive and well-integrated risk management function. The

identification, assessment, monitoring, mitigation and reporting of risks are essential to our financial performance and successful management of our businesses. These risks, if not effectively managed, can result in losses to State Street as well as erosion of our capital and damage to our reputation. Our systematic approach allows for an assessment of risks within a framework for evaluating opportunities for the prudent use of capital that appropriately balances risk and return.

Our objective is to optimize our return and to operate at a prudent level of risk. In support of this objective, we have instituted a risk appetite framework that aligns our business strategy and financial objectives with the level of risk that we are willing to incur.

Our risk management is based on the following major goals:

- A culture of risk awareness that extends across all of our business activities;
- The identification, classification and quantification of State Street's material risks;
- The establishment of our risk appetite and associated limits and policies, and our compliance with these limits;
- The establishment of a risk management structure at the “top of the house” that enables the control and coordination of risk-taking across the business lines;
- The implementation of stress testing practices and a dynamic risk-assessment capability; and
- The overall flexibility to adapt to the ever-changing business and market conditions.

Our risk appetite framework outlines the quantitative limits and qualitative goals that define our risk appetite, as well as the responsibilities for measuring and monitoring risk against limits, and for reporting, escalating, approving and addressing exceptions. Our risk appetite framework is established by management with the guidance of Enterprise Risk Management, or ERM, a corporate risk oversight group, in conjunction with our Board of Directors. The Board formally reviews and approves our risk appetite statement annually.

The risk appetite framework describes the level and types of risk that we are willing to accommodate in executing our business strategy, and also serves as a guide in setting risk limits across our business units. In addition to our risk appetite statement, we use stress testing as another important tool in our risk management practice. Additional information with respect to our stress testing process and practices is provided under “Capital” in Management's Discussion and Analysis of Financial Condition and Results of

Operations, or Management's Discussion, included under Item 7 of our 2013 Form 10-K.
The following table provides a reference to the disclosures about our management of significant risks provided herein.

Governance and Structure

We have a disciplined approach to risk management that involves all levels of management, from the Board and the Board’s Risk and Capital Committee, or RCC, its Examining & Audit, or E&A, Committee and its Technology Committee, to each business unit and each employee. We allocate responsibility for risk oversight so that risk/return decisions are made at an appropriate level, and are subject to robust and effective review and challenge. Risk management is the responsibility of each employee, and is implemented through three lines of defense: the business units, which own and manage the risks inherent in their business, are considered the first line of defense; ERM and other support

functions, such as Legal, Compliance, Finance and Vendor Management, provide the second line of defense; and Corporate Audit, which performs an independent assessment of the effectiveness of the first two lines of defense.

The responsibilities for effective review and challenge reside with senior managers, management oversight committees, Corporate Audit and, ultimately, the Board and its committees. While we believe that our risk management program is effective in managing the risks in our businesses, internal and external factors may create risks that are not identified or anticipated.

Corporate-level risk committees provide focused oversight, and establish corporate standards and policies for specific risks, including credit, sovereign exposure, market, liquidity, operational information technology as well as new business products, regulatory compliance and ethics, vendor risk and model risks. These committees have been delegated the responsibility to develop recommendations and remediation strategies to address issues that affect or have the potential to affect State Street.

We maintain a risk governance committee structure which serves as the formal governance mechanism through which we seek to undertake the consistent identification, management and mitigation of various risks facing State Street in connection with its business activities. This governance structure is enhanced and integrated through multi-disciplinary involvement, particularly through ERM. The following chart presents this structure.

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Risk Governance Committee Structure

Executive Management Committees: