

20-Jul-2017

E*TRADE Financial Corp. (ETFC)

Q2 2017 Earnings Call

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MANAGEMENT DISCUSSION SECTION

Operator: Good evening, and thank you for joining E*TRADE's Second Quarter 2017 Earnings Conference Call. Joining the call today are Chief Executive Officer, Karl Roessner; and Chief Financial Officer, Michael Pizzi.

Today's call may include forward-looking statements, including statements about E*TRADE's future operational and financial performance and synergies related to the OptionsHouse acquisition, which reflect management's current estimates or beliefs, and are subject to risks and uncertainties that may cause actual results to differ materially.

During the call, the company will also discuss non-GAAP financial measures. For a reconciliation of such non-GAAP measures to the comparable GAAP figures and for a discussion of additional risks and uncertainties that may affect the future results of E*TRADE Financial, please refer to the company's earnings release furnished on Form 8-K along with Form 10-Ks, 10-Qs and other documents the company has filed with the SEC. All of these documents are also available at about.etrade.com.

Note that the company has not reconciled its forward-looking non-GAAP measures, including non-GAAP adjusted operating margin to the most directly comparable GAAP measures because material items that impact that measure are out of the company's control and cannot be reasonably predicted. This call will present information as of July 20, 2017. The company disclaims any duty to update forward-looking statements made during the call.

This call is being recorded and a replay will be available via phone and webcast later this evening at about.etrade.com. No other recordings or copies of this call are authorized or may be relied upon.

With that, I will now turn the call over to Mr. Roessner.

Karl A. Roessner

*Chief Executive Officer & Director, E*TRADE Financial Corp.*

Thank you, Ash. Good evening and thank you for joining. It's a pleasure to speak with you again, especially in the wake of such strong results and solid progress on our key initiatives. We have a lot to cover tonight so I'll get right to it with a brief rundown of the Q2 highlights, all of which we will address in more detail.

During the quarter, we marched forward on the integration of OptionsHouse, establishing many of the back and middle office connections, which set the stage for the clearing conversion expected in early August. We rolled out a bold new marketing campaign beginning with our brand relaunch that returns us to our irreverent roots as a challenger brand. We delivered solid business growth with our best Q2 ever for asset growth and year-to-date account growth at the top of our target range. We recorded robust customer activity with record DARTs, a record mix of derivative trades, record customer net buying and end-of-period customer margin balances that matched our previous record.

We generated solid revenue growth in spite of absorbing a full period of reduced commissions. We grew our balance sheet as planned, flexing the expanded earnings power that comes from more fully monetizing our customer deposits. And we meaningfully reduced our allowance for loan losses to reflect the preponderance of positive performance data on loans that have converted to amortizing.

And as if that's not enough, today we announced a reduction in our consolidated Tier 1 leverage threshold of 50 basis points, unlocking significant capital to be deployed to the benefit of our shareholders. Given our financial performance and the 50 basis point move, we are commencing a \$1 billion share repurchase program, which we expect to complete by the end of 2018. Not too shabby for what are typically placid Q2 months.

Now to spend a bit more time on each of these elements, on the integration, the team has exerted a tremendous effort to ensure a seamless conversion for customers, and I need to express my sincere gratitude for all the members of the integration team. Their tireless work into the twilight hours, including during the weekends and summer holidays, sacrificing personal and family time has truly gone above and beyond. With each mock conversion, test and retest, they are delivering on our commitment to our customers and to our shareholders to harness and channel the full power of this acquisition.

Over the next few weeks, all OptionsHouse customers will be brought into the E*TRADE ecosystem. This migration will expand their access to tools and services and simultaneously ensure the advanced derivatives tools and products to which they're accustomed remain just a click or a tap away. From that point forward, we will build and further refine our offering, creating a unified and exceptional experience for all customers, with a complete set of industry-leading tools and features.

And now to highlight our most visible and exciting launch of the past quarter, our new brand campaign, which rolled out in late June. Through it, we are making a conscious return to our challenger-brand roots while speaking to our target customer segment in a far more relevant way. Our current executions are just the beginning and we have some serious firepower and flight as we add new work and optimize our creative mix and media spend.

Our brand strategy taps into the everyday frustration consumers feel when faced with constant depictions of exaggerated wealth and offer a positive way to channel that frustration into action. It's about optimism and the opportunity to own your own destiny, all executed with the tongue in cheek humor and irreverence consumers have come to expect from the E*TRADE brand.

It's early days, but we are certainly pleased with the splash we've made thus far and have heard great feedback from customers and prospects alike. Following the launch of the campaign, we have experienced a pronounced boost in key metrics relative to advertising awareness among our target market, prospect website visits and, most importantly, new account growth. So bottom line, we are getting our swagger back and effectively engaging our audience in a way that we haven't done in quite some time. I look forward to continuing to evolve the message, delving more deeply into our value proposition and ensuring that E*TRADE is impossible to ignore.

Since I took the helm in September, we have benefited from a strong market and elevated consumer confidence, but I certainly don't intend to shirk full responsibility for our successes. The enhancements we are making to the company are real and the impacts are tangible.

Over the past three quarters, we have discussed executing on three core initiatives: the integration; our marketing; and improving the customer experience. While the first two are in their early stages, the third has been a pervasive element of every initiative, investment and organizational structured decision. Our results are beginning to reflect these actions.

First and foremost are the changes we've made to our structure, which have positively resulted in improved productivity with clear accountability and strong cross-functional collaboration. We infuse the organization with experienced, focused and decisive leaders, empowered to do what's right for our customers at every turn, which is foundational to achieving our growth goals.

We've also put real focus into more fundamental elements of the employee experience, like socializing a new mission, vision and values that unifies our culture of innovation, collaboration and ownership, and elevating talent development as a key business priority. Altogether, this has better aligned the employee base to our growth goals and focused everyone on the end customer. A key drive in that regard has been addressing and eliminating our top customer dissatisfiers. These range from the incremental in terms of tweaks to our account opening or fund transfer experience, to larger scale efforts around improving efficiencies in our customer service process. All are based on active customer listening.

Key wins thus far include a better navigation experience on the website, an enhanced online application experience and refinements to a handful of our products and customer experiences. Like the steps we took to simplify our managed offerings this quarter, streamlining the customer risk tolerance questionnaire, reducing the minimum investment for robo, introducing a more competitive fee structure and eliminating a handful of allocations that often proved misunderstood or misused by our customers. This is a small illustration, but we are focused on making continued enhancements across the product suite and all stages of the customer journey, and I look forward to sharing updates as we deliver them.

As for our Q2 metrics, typically the second quarter proves challenging, as tax season pressures net asset growth and the start of summer produces a lull in trading activity. This quarter was clearly distinct, however, as we posted tremendous results across the board. DARTs ticked up from last quarter to 208,000, which is our best quarter on record, adjusting for the exit of our international business in 2009, and our derivative mix improved to 32% of trades, our highest mark ever.

Customer margin balances ended the quarter up 12% at \$8.2 billion, tying our previous record. Net new brokerage assets of \$2.6 billion represent our highest Q2 on record and brought our year-to-date growth rate to a healthy 4.9%, almost 125 basis points higher than the same period last year. Managed assets ended the quarter at \$4.6 billion, an increase of 18% year-to-date, more than double the growth of the equity markets.

We added 41,000 net new brokerage accounts in Q2, bringing us to 99,000 so far this year, which is nearly 60% higher than the same period last year and reflects a year-to-date growth rate of 5.7%, at the top end of our target range.

Attrition decreased slightly to 9% for the quarter, though was still elevated in light of the strong gross new activity last quarter, including the typical flow through of less-permanent as well as Corporate Services accounts. While this is an area of intense focus for the company, it is important to note that our customer attrition across our highest service tier remains exceptionally low. In terms of July activity through yesterday, DARTs for the month were trending at around 200,000, down 7% month-over-month, and customer margin balances had come in slightly to average around \$8 billion.

One element of our business that does not receive as much airtime during these calls, yet certainly garners significant attention internally, is Corporate Services. We've long discussed this channel as a strategically important driver of brokerage accounts and assets as well as a steady source of cash proceeds, which of course are a core component of our earnings power. I've been very happy with the performance of this group and encouraged by the initiatives to bolster our offering. I'm also particularly excited about the renewed focus on growing plan participants, which is no small task.

A few reasons I believe we can win more market share in this reinvigorated pursuit. First, we have the industry-leading platform. Our Equity Edge platform stands head and shoulders above the competition in terms of

functionality, reporting, service and overall experience. And while we do receive external validation that tells us as much, the true proof is in the world-renowned client companies we earn and retain.

Second, our intentions are pure. For many industry players, the prospects of offering private wealth management to a small handful of senior executives is the magnet that attracts them to this business. To those firms, the broader employee base is an undesirable byproduct, which often leads to subpar experiences for the vast majority of plan participants. Our offering, on the other hand, is geared to serve all levels of the organization, and is particularly well-suited for the broader employee population.

Third, many of our competitors have recently chosen to shift to an outsourced software solution to service their clients. This, for participant companies, is tantamount to switching vendors entirely. As with any disruption in service, companies may be compelled to look around for something better. And I very much like our chances in a head-to-head contest with other providers, so we revel in this opportunity. To win in this emerging arena, a company needs the scale and self-directed simplicity that only comes from a digital-first provider, backed by exceptional service. This, of course, is our sweet spot.

And lastly, we have the right folks in the right place leading the charge, several of whom actually joined E*TRADE from participant companies, so our understanding and appreciation of the challenges that face the industry are unparalleled.

In all, E*TRADE Corporate Services shines bright throughout the stock plan space and is an increasingly important component of our path forward. I very much look forward to sharing updates on our progress with this channel in the quarters to come.

Before Mike takes you through our results and capital, I'll add a final note on the growth goals we set last September: We are moving ahead with great purpose and I remain ever more confident that we will nail our objectives on each measure. To quickly recap, those include: improving our growth rates on brokerage account and assets to at least 4.8% and 5.8%, respectively; driving our mix of derivative trades to 35%; and achieving \$6 billion in managed product AUM.

These remain a central focus for the company and serve as the guiding metrics around which we structure our projects, our teams and our efforts. That said, I want to reemphasize exactly what these objectives represent. We announced them to very transparently and publicly illustrate to investors that we can return to meaningful growth in our core business while holding a mirror up to our progress in this pursuit.

By this point, I hope it's becoming positively clear that our growth engine has indeed been reignited. While some editorial coverage of our strategy chooses to prominently feature scenarios where the company does not achieve its goals, the probability of any such outcome is fading further into the ether with each passing day. We have a great team defined by strong alignment and our focus and resolve is unmatched. Our board, which includes me, is very pleased with our progress. And I look forward to driving growth and value for our shareholders for many years to come.

To sum it up, it was a tremendous quarter and first half of the year for E*TRADE. Important inroads were made and we are exactly where we need to be. The energy within our walls is electric. We are sharp. We are focused. We're executing and we will continue to deliver for our customers and for our shareholders.

With that, I will turn it over to our CFO, Mike Pizzi.

Michael A. Pizzi*Chief Financial Officer, E*TRADE Financial Corp.*

Thanks, Karl. For the quarter, we posted net income of \$193 million, or \$0.70 per share, which includes a provision benefit and other noteworthy items totaling \$0.18 per share. The quarter was strengthened by net revenue generation of \$577 million, clearly reflecting growth in the business and the balance sheet, the OH acquisition and the strong operating environment. We also maintained our prudent posture on expense management with an adjusted operating margin of 38%, which includes the unique expenses and excludes the provision benefit.

Now to cover the unique items, which benefited pre-tax income by \$81 million, most prominent was a \$99 million benefit to provision for loan losses. Since we transitioned our loan portfolio to runoff in 2007, we have been discussing the potential risk event of interest-only loans converting to amortizing and the defaults that might arise from borrower payment shocks. The majority of our loans with this feature had a 10-year draw. And with the 2007 vintage widely recognized as the riskiest vintage, our sights were fixed on 2017 to ultimately observe the performance of these loans through the event.

Our reserves assumed a significant worsening of performance post conversion. And while there are many factors contemplated in our loss modeling, the most influential input is the actual performance of the loans themselves. At this point, the population of loans we previously deemed high risk has outperformed our expectations with a significant portion outperforming for more than 12 months post conversion. Accordingly, our loss expectations on the portfolio have improved meaningfully and the allowance has been reduced by almost half. At this point, we expect the allowance will decrease in future periods, in line with charge-offs.

Next is a \$9 million charge in communications expense for customer market data. This primarily relates to the fees charged by the exchanges for real-time market data, for which they assign higher rates for users that meet their definition of professional. We have worked to gather additional customer data that helps define this population. And in Q2, we made significant progress in identifying the appropriate customer set. As a result, we trued up our estimate, recording a \$9 million charge. Excluding this charge, the quarter's communication line should serve as a good run rate.

And lastly, we realized \$9 million of expense in the quarter, primarily related to the OptionsHouse integration and the work surrounding crossing \$50 billion in assets. Recall that we initially outlined \$22 million in one-time integration expense and \$10 million in 2017 to build out for balance sheet growth. Year-to-date, we have incurred \$12 million across both categories and we expect the initial \$20 million will be realized over the remainder of the year evenly across Q3 and Q4.

Now on to our core results. Net revenue of \$577 million was up \$24 million from the prior quarter, reflecting balance sheet growth and improved interest rates, offset by the full quarter impact of our updated commission pricing. Year-over-year, revenues were up \$103 million on the same dynamics coupled with the addition of OptionsHouse.

Net interest income increased 12% to \$356 million during the quarter as we grew average interest-earning assets by \$3.2 billion. Our net interest margin increased 11 basis points to 274 basis points. The increase was driven by the full quarter impact of the March Fed hike, higher customer margin balances and strong securities lending activity attributable to a popular March IPO.

Commission revenue of \$105 million decreased 17% sequentially, driven by the full quarter impact of our pricing reductions. Commission per trade for the quarter was \$8.02, which we believe should continue to be a good run rate. Fees and service charges increased \$12 million quarter-over-quarter to \$98 million. This was driven by higher order flow revenue related to a higher mix of options trades and higher asset-based fees on larger mutual fund balances as well as the increased rate on off-balance sheet deposits. I'll cover more on this in a moment.

As a reminder, at the clearing conversion, we will capture all of the revenue synergies and the vast majority of remaining expense synergies associated with the OH acquisition. When we announced the acquisition nearly a year ago, we highlighted \$16 million of annual revenue synergies, predominantly derived from onboarding customer cash and margin balances. With the subsequent increases in short-term rates coupled with the growth in the balance sheet, we now believe we'll capture closer to \$20 million of annual revenue synergies.

Noninterest expense for the quarter was \$359 million, up \$17 million sequentially, inclusive of \$18 million in unique costs. Our 38% adjusted operating margin was up slightly from the prior quarter and above our expectations as a result of strong customer activity during the quarter. With respect to the full year adjusted operating margin, we previously noted that a June hike could add up to 100 basis points to our target of 38%. We are still of that belief and accordingly are increasing our 2017 operating margin target to 39%.

You should expect the third quarter to be line with Q2 before increasing in Q4 on balance sheet growth and a full quarter of realized synergies from OptionsHouse. Note that this assumes our current plans for investment spending as well as all unique charges. Our effective tax rate for the quarter was 39%, which is in line with our expectations for the next two quarters.

As for net interest margin sensitivity rates, in Q2, we benefited from the full quarter impact of the Fed's March rate hike, and modestly from the June hike. And while the long end of the curve didn't show resiliency until quarter-end, we did maintain an average reinvestment rate on the securities in the 230 basis point to 250 basis point range. This, aided by an improved rate on customer margin with strong growth in that product, raises our expectations for full year 2017 NIM for the low 270s. This expectation assumes no changes in the rate environment and that margin balances are held constant.

During the quarter, the yield on third-party customer cash averaged 92 basis points, up from 58 basis points in Q1, incorporating the benefit of the June Fed hike. Our expectation for the remainder of the year, barring any further rate hikes, is for those deposits to yield approximately 120 basis points, noting the volume should continue to reduce as we onboard deposits to grow the balance sheet. Third-party cash will reprice roughly in line with short-term market rates with around a three month lag to receive the full benefit of the move.

On the capital front, we have several forces acting in our favor this period. Strong earnings, the significant reduction in our allowance, and the lowering of our consolidated Tier 1 leverage threshold together drive an outsized formation of capital. This has enabled us to launch a larger buyback program while maintaining balance sheet growth at our planned pace.

We believe the move to 6.5% reflects a more appropriate leverage threshold in consideration of our overall strategy, asset composition and risk profile. It recognizes our continued strong financial performance as well as ongoing dialogue with our regulators. Following the change, we now have approximately \$520 million of excess parent capital pro forma for Q2 levels. That, in conjunction with our strong financial performance, has enabled us to institute a meaningful share repurchase program with plans to complete \$1 billion in buybacks by the end of 2018. We will proceed at a measured pace over the course of the program.

As for balance sheet growth, we are on track to end the year with \$63 billion in total assets, even in the wake of Q2's record customer net buying. I will note, however, that the factors making onboarding deposits the most compelling use of capital can shift with interest rates and the shape of the curve. The rate on off-balance sheet sweep toggles more closely with Fed funds while our incremental yield on securities is more closely tied to the belly of the curve. If the economics flip, we will change course, but at this point we plan to get our balance sheet growth targets.

One last point on capital and parent liquidity. During Q2, we distributed \$50 million of capital to the parent from the broker-dealer. In Q3, we anticipate distributing \$100 million.

Also worth noting, earlier this week, our corporate debt rating was upgraded to BBB by Standard & Poor's, citing our continued reduction in legacy risks and our growth of stable revenues. I believe we have additional upside potential on our ratings over the medium term, driven by all we are doing to improve the business, our earnings and our continued efforts in risk management.

In closing, it was an awesome quarter. We completed significant work on the OptionsHouse integration, we generated strong business growth and we grew revenue in solid fashion. Shrugging off the impact of the commission reductions, we progressed well on our balance sheet growth and we crystallized the next leg of capital deployment, bolstered by a reduction of our leverage threshold. All are positively value-generative for shareholders and all tie back to Karl's points about renewed energy within our walls.

And with that, we'll open the call for questions.

QUESTION AND ANSWER SECTION

Operator: Thank you. [Operator Instructions] And our first question comes from the line of Rich Repetto with Sandler O'Neill. Your line is now open. Please proceed with your question.

Richard Henry Repetto
Analyst, Sandler O'Neill & Partners LP

Q

Yeah. Good evening, Karl. Good evening, Mike. I guess, the first question is the substantial buyback and I see the \$520 million, or freed up capital. I guess, if you could walk through how you came up with the \$1 billion and – well, how you came up with that number, I guess, starting with the \$520 million because of the lower leverage ratio?

Michael A. Pizzi
*Chief Financial Officer, E*TRADE Financial Corp.*

A

Well, the \$520 million of excess is pro forma for where we ended this quarter at 7.5% down to the level of 6.5%. Inclusive in that is the \$100 million of reserve release. So, that gives you sort of the starting formation of capital. The remainder of that amount is really, as we look at our capital plan over the next sort of horizon cycle in terms of looking at the out-years, specifically the next budget year, through the year-end 2018, we look at the capital generation and corporate cash and corporate liquidity available to fund the buyback program. And that gave us a rough idea in terms of how we wanted to size it overall. Looking at that, we feel \$1 billion is a good number that we can complete at a measured pace over that time period.

Richard Henry Repetto

Analyst, Sandler O'Neill & Partners LP

Q

Got it. Okay. And then I'll just do one follow-up and that'd be on the, I guess, Karl, on the revenue synergies from OptionsHouse. You upped the revenue synergies. And I'm just trying to understand, with the price reductions, how would you up the revenue synergies. I guess, is it all from Fed rate hikes and on the net interest side? Or how you come are going from \$16 million and higher, I guess?

Michael A. Pizzi

*Chief Financial Officer, E*TRADE Financial Corp.*

A

Yeah. The largest revenue synergy from the OH deal, as we talked about, is really related to the cash balance that comes from the OH customers being fully deployed within our model. That amount is now better simply because we are in a better rate environment overall and can earn a higher rate of return on that cash. That's the primary driver in the increase in the revenue synergies.

Operator: Our next question comes from the line of Conor Fitzgerald with Goldman Sachs. Your line is now open. Please proceed with your question.

Conor Fitzgerald

Analyst, Goldman Sachs & Co. LLC

Q

Good evening. And thanks for the feedback you're seeing on the new advertising campaign. I was just wondering if there's a way for you to quantify how much of an impact do you think the new campaign could have on your account growth. And then just a question on your targeted demographics with the new campaign. It seemed like you were targeting customers who want to invest on their own ideas versus some of your previous campaigns, which were more geared toward customer retirements. Is that a fair read? I'm just curious what demographics you're going after.

Karl A. Roessner

*Chief Executive Officer & Director, E*TRADE Financial Corp.*

A

Sure. So, Conor, on the first point, it's really looking at – rolling out the ad campaign is sort of early days, right? It was end of June when we took it out. And what we've seen so far is a good reception, a nice increase in share of voice, share of awareness, and then it's a new account build and also just driving more eyes to our website on the prospect side and more interest overall in E*TRADE.

So, the first part of that rollout was really about branding. And it starts to get to the second part of your question, this is going to be a staged rollout. First one is getting us back on the map by sharing the irreverent voice that we have, letting customers know that not only we're still in the game, but that we're here to help them with their finances at every stage along their life. So, it's not a targeted demographic we're looking at; you'll see more of the campaign rollout over time as it starts to shift. So, it's definitely not a shift from a starting investor versus retirement versus some of the other tools or products and services that we offer. You'll see more around our functionality and more around the products and services and our value prop in particular out into the fall and thereafter. So this is just the very beginning of the campaign and it's really just on brand, Conor.

Conor Fitzgerald

Analyst, Goldman Sachs & Co. LLC

Q

That's helpful. Thank you. And then just on expenses, I think excluding the one-time communications expense and the integration charges, your pre-tax margin was 41% this quarter. Just given some of the revenue tailwinds

you have from the larger balance sheet and the June hike, should we think about your core pre-tax margin as growing from that 41%, ex any integration charges?

Michael A. Pizzi

*Chief Financial Officer, E*TRADE Financial Corp.*

A

Well, as we outlined, we gave the guidance at 39%, including the \$20 million of remaining charges, which we expect to occur pretty much evenly over Q3 and Q4. Keep in mind there's some variability in timing on some of the \$50 billion work. We're moving at pace and making great progress. But sometimes things take a little bit longer, but we are doing well and moving through it.

Yes, the environment is good. You can see that really within the margin balances, within the net interest margin and other factors. And so we'll have more to say about what the 2018 operating margin guidance will be at a later call.

Operator: Our next question comes from the line of Devin Ryan with JMP Securities. Your line is now open. Please proceed with your question.

Devin P. Ryan

Analyst, JMP Securities LLC

Q

Hey, thanks. Good afternoon, guys. Maybe first one here just on the record level of net investor buying in the quarter. How does that make you think about the client cash management and your duration profile? Obviously, the firm still has flexibility with off-balance sheet sweep. But as that diminishes here as you just move more to on-balance sheet, do you think about maybe [ph] holding (30:10) more floating rate? Or does that just naturally shorten the duration of the overall balance sheet because you want to kind of keep more liquid?

Michael A. Pizzi

*Chief Financial Officer, E*TRADE Financial Corp.*

A

Well, we look at our deposit flows quantitatively. We break down a volatile balance away from core balances. That volatile balance is invested in floating rate type securities or very short duration securities overall. So we factor that in, in terms of the overall volatility in the product and the estimation of the product duration. From a liquidity standpoint, I would say that the very high level of liquidity in the balance sheet really holding the preponderance of government and agency obligations that we do I don't think will be changing really our mix or approach to it at this point.

Devin P. Ryan

Analyst, JMP Securities LLC

Q

Got it. Okay. And then a follow-up here, just the retail brokerage industry has been seeing some pretty good asset flows over the past several quarters I think as a whole. When you look at your net new assets and kind of break them down, can you give us any sense of how much is new customers that are kind of new to the market? Or how much is transfers of accounts and within the TOAs? Is that coming from kind of direct competitors and discount brokerage space or is it from wire-houses or just where are you seeing the flows from?

Karl A. Roessner

*Chief Executive Officer & Director, E*TRADE Financial Corp.*

A

So, it's interesting, right? When I look at what the commission cuts did and the price cuts did a couple months ago and then coming into this. It really tangibly show that there're a lot of money in motion. It got people to really think

about their finances again and sort of check in and look at what they have and where they are. So there's a lot of money in motion. I think we've gotten our fair share across the board. So I wouldn't say it's from any particular source. We're seeing both new money come in, we're seeing money from wire-houses, we're seeing money from competitors. It does remain extremely competitive out in the marketplace, but I do think this caused a reengagement along the retail brokerage side, and that coupled with what's gone on in the marketplace and just how strong the markets have been. We're absolutely seeing a lot of money in motion. But there's nothing I can put my finger on to say 60%, 70%, 80% from this one source. It's really across the board.

Operator: Our next question comes from the line of Steven Chubak with Nomura Instinet. Your line is now open. Please proceed with your question.

Steven Chubak

Analyst, Nomura Instinet

Hi. Good evening.

Q

Karl A. Roessner

*Chief Executive Officer & Director, E*TRADE Financial Corp.*

Hi.

A

Steven Chubak

Analyst, Nomura Instinet

So, Karl, I really appreciate the helpful commentary you provided on the corporate stock plan business and some of the competitive dynamics in the space. Recently one of your large wire-house competitors, which predominantly serves the high net worth clientele within the corporate stock plan business, actually outlined a new initiative in an effort to take market share and really cast a wider net by moving down market. And just seeing that this is an area where you continue to have a leading presence, I was hoping you could speak about the competitive dynamics in the space today and maybe how you are positioning the firm to build a little bit of a moat to ensure you protect your market share against any new entrants.

Q

Karl A. Roessner

*Chief Executive Officer & Director, E*TRADE Financial Corp.*

Yes. So, it's a great question, and thank you, and [ph] the timing is (33:34) absolutely appropriate. So, one thing is, I don't look at it as building a moat around what we have. I'm actually quite proud of the product that we have and Equity Edge is the leading platform out there.

A

So when you look at stock plan and you look at the way that it's been run, historically, I'm quite proud of what we did when we came in and sort of realigned the leadership and ownership of that business to make sure that the stock plan business itself was focused on just that. Right? Getting out there and serving and winning new big ticket customers in the client base, new big ticket corporations and companies, whether they be public companies or those about to go public, right, with their stock plans, and make sure we're serving that client base with our number one sort of leading platform. So, that's the first piece.

In that space, I'm extremely confident in our ability to compete. And when you talk about sort of going – folks out in the marketplace saying they're going to go down market, I question sort of just what that is. In the prepared remarks, I talked a little bit about serving the entire broad-based employee population. I think our product does that very well. So, competing head-to-head, I'm very happy with our chances there.

When you look at what they talk about in terms of – some of our competitors are going to this outsourced technology solution, it's a great product, but that's a change for the client. Right? It's a change for the corporation. So, many of those are going to be put out to bid and in that situation, I like our chances very much. So, yes, it's very competitive, but we are one of the leaders in the space. We continue to invest in the platform and it's a broad-based platform, so we don't need to go down market. We serve the whole market. Right? We're happy to take all comers to our platform.

The second side of that is really in the realignment was making sure as when you talk about the plan participants, right, we have about 1.5 million plan participants on us who are potential E*TRADE customers. Making sure that those are focused on by our E*TRADE Securities reps and make sure that we are in there, they know what services we can provide. They understand that we can offer them help in their financial well-being. It's just another part of what we're focused on. So I like the competitive environment in this space. I like our leadership position in this space. And I promise you I'm not building a moat around it.

Steven Chubak

Analyst, Nomura Instinet

Q

Okay. Thanks for the helpful color on that, Karl. And switching gears to the capital management side, Mike, you gave some helpful detail in response to an earlier question around what prompted you to decide on the \$1 billion as the appropriate size for the buyback. I'm just thinking about all the capital management priorities that you've outlined in the past. Why not take the – since it's \$500 million of excess you have today, why not initiate a dividend in lieu of a buyback? And maybe thinking about other potential alternatives, how should we interpret this recent announcement in the context of the strategic M&A priorities that you've outlined in the past?

Michael A. Pizzi

*Chief Financial Officer, E*TRADE Financial Corp.*

A

Sure. I'll just answer the question on a possible dividend first and Karl can cover where we are on M&A priorities. In the release of capital or the reduction in capital requirement is a one-time item. It's not really a core basis to form a dividend around. And you see also the release coming out of the allowance as well also really being one-time. We think a dividend needs to really be built around sort of the core earnings and growth over time from that earnings stream. Now we're combining both of those when we do this. So, I guess, you could've introduced a small dividend. But our decision really in looking at it from a capital generation standpoint, since a good portion of this is related to actions that we're taking within the capital plan, we felt that the right pathing here was to do this by a buyback and really look at that over the next year, so beginning now through the end of 2018.

Karl A. Roessner

*Chief Executive Officer & Director, E*TRADE Financial Corp.*

A

And on the acquisition front, we have talked about the areas that we would think about going into and starting again with the overlay. That we're just not interested in the market for a transformative transaction right now. So, we'd be looking for additional products or additional services that we might be able to bolt on, right, what other functionality or technology we might be able to bolt on to our offering to either leapfrog, catch up, or get into a new space in that respect.

But it's an interesting market right now in terms of valuations and what else is available out there. And we've been very good stewards of our capital. We don't intend to change that decision. Right now, this is far and away the best use of our capital is to return it to shareholders and continue to grow our balance sheet.

In terms of the areas that we would look at and if there was something compelling, we would still consider and that's really in the stock plan space. Right? Is there a way to get additional scale to bolt-on additional corporates and grow that area? Right? Is there something out there? But right now, there's not a lot on the horizon, and this is the best use of capital and we'll continue to look at things that way.

Operator: Our next question comes from the line of Chris Harris with Wells Fargo. Your line is now open. Please proceed with your question.

Chris M. Harris

Analyst, Wells Fargo Securities LLC

Q

So, credit quality continues to surpass your expectations. I would think that your prospects of potentially getting capital release at the bank have now improved. Can you guys talk a little bit about how we should be thinking about that opportunity?

Michael A. Pizzi

*Chief Financial Officer, E*TRADE Financial Corp.*

A

Right now, the minimum at the bank is 7.5%, the minimum at the parent is 6.5%. That's our operating mandate for the time being and really the binding constraint really go forward on the buyback program really becomes the overall level of corporate liquidity.

In the past, we've talked about two-times debt service. We should think of that as really a minimum in the overall level. Really with what we need from an operations standpoint and what we feel good from a risk management standpoint in running the company is probably about twice that level and naturally what's going to form our expectation of pacing going forward.

From a movement of the bank capital level, the bank capital level is at 7.5% today and we're holding it there in our planning process. But I will say that the balance sheet is improving continually. As the portfolio runs down, there is less risk and the reinvestment is defined into agency securities only at this point. So we're optimistic of [ph] the possible (40:28) opportunity, but for right now, the level is 7.5%.

Chris M. Harris

Analyst, Wells Fargo Securities LLC

Q

All right. Sounds good. And a quick one on expenses. Is there much in the way of expenses that are still tied to the loan book at this point? And if so, can you guys quantify that for us?

Michael A. Pizzi

*Chief Financial Officer, E*TRADE Financial Corp.*

A

The expenses with the loan book are what you can imagine. It's the number of head count that we need across the areas in terms of the administration and operations of the book. So, essentially, servicer oversight, workouts, loan modification review, compliance around the operation of the loan portfolio as well as the modeling of the allowance process and stress testing. We haven't really broken those expenses out in a direct way.

From an overall expense base, they're not going to be incredibly meaningful. But from a cost-basis around the size of the loan portfolio in terms of the revenue to loan portfolios putting off, they're actually quite meaningful in the overall sort of if you were to create a segmented loan P&L. And so that's how we think about it. They don't scale very well with the portfolio, although they do scale to some degree. But we do think at this point holding the portfolio for the foreseeable future is still in the best interest of our shareholders.

Operator: Our next question comes from the line of Michael Carrier with Bank of America Merrill Lynch. Your line is now open. Please proceed with your question.

Michael Carrier

Analyst, Bank of America Merrill Lynch

Q

Thanks, guys. Just a question on the balance sheet. On the off-balance sheet cash, are there any limits in terms of what you can bring on? And then, Mike, you just mentioned in terms of the rate backdrop, different scenarios can shift the priority on what you want to do with the capital. So just any color on that? And then it sounds like from the initiatives that you guys have in place, the focus on growing the balance sheet after the transfers is on the core brokerage business. And if clients have 10% to 20% in cash, then that will continue to grow. Just anything that's more focused direct on cash balances from a growth initiative?

Michael A. Pizzi

*Chief Financial Officer, E*TRADE Financial Corp.*

A

Yeah. From what we can bring on the balance sheet, we are targeting \$63 billion for year-end. We've got enough to get to \$63 billion in terms of what's off-balance sheet, so we don't really need to see organic growth to get to that level. In addition, we're probably left with around \$1 billion of additional deposits we can onboard into next year beyond the \$63 billion target for this year, and that would use up what really could realistically be brought on. The rest would need to remain off-balance sheet for FDIC insurance purposes. So that's essentially larger cash balances in the remaining portion of the balance.

And the best way to think about cash growth from that point going forward is it's going to scale overall with account growth, the average balance of cash per account in that sort of 15% to 20% range depending on sort of customer risk appetite. It's going to scale really, as accounts grow, with some additional cash really coming from the Corporate Services business as Corporate Service executions work through over time, and you typically will see that during Q1.

Michael Carrier

Analyst, Bank of America Merrill Lynch

Q

Okay. Thanks a lot.

Operator: Our next question comes from the line of Dan Fannon with Jefferies. Your line is open. Please proceed with your question.

Daniel Thomas Fannon

Analyst, Jefferies LLC

Q

Thanks. I guess, I want to talk about activity levels and how you're thinking about that once you fully integrate the platforms. I mean, you're getting the full suite of products and technologies across the OptionsHouse and the E*TRADE customers. And then also I think in your previous comments, that's not included in potential revenue synergies. That was the \$20 million or so that you highlighted.

Michael A. Pizzi

*Chief Financial Officer, E*TRADE Financial Corp.*

A

Yeah. The revenue synergies we gave, the vast majority of them are coming from the OH's cash. The second pool is really just coming from taking the clearing in-house and monetizing the full value of the margin that is essentially being split with a third-party pre-integration.

Karl A. Roessner

*Chief Executive Officer & Director, E*TRADE Financial Corp.*

A

Yeah. And in terms of activity and what we expect post-integration, it's one of the reasons that when I talk about this and I talk about sort of the excitement that we have around here is we haven't fully integrated yet. We haven't gotten the fantastic tools and technology that OptionsHouse brought to the table out to our E*TRADE customer base. So we absolutely look at that as a very big part of us going forward, which is why I'm so pleased with where we are today on growth goals.

Daniel Thomas Fannon

Analyst, Jefferies LLC

Q

Great. And then just to follow up on the fees and service charges. Mike, you mentioned some moving parts in terms of the increase this quarter. And then just thinking about going into next quarter and thereafter with the higher rates and from the June hike, should we see, all else equal, that number continue to rise based on the money market yields of the off-balance sheet cash that's coming through there?

Michael A. Pizzi

*Chief Financial Officer, E*TRADE Financial Corp.*

A

Well, yeah, to the extent, we – we outlined the rate for you in the prepared remarks. So we expect about 120 basis points or so on the off-balance sheet. So it's going to go up from the 90 basis points that we are at this quarter, but the balance is coming down as we onboard cash.

So when we look at the total fees and service charges line for this quarter, the increase is across a couple different categories. One is the increase in rate on a declining balance. The rate effect in the quarter is bigger than the balance effect and so we get a benefit this period because of the two rate hikes that occurred.

The other elements driving it are really within the order flow line. Our increase in options in the quarter led us to have better overall payment for order flow from options because we get more on an option order than we do on an equity order. Those two combined with some of the asset-based fees that we're earning, which were also up, contributed to the improvement in fees and service charges on the quarter.

Daniel Thomas Fannon

Analyst, Jefferies LLC

Q

All right. Thanks.

Operator: Our next question comes from the line of Brian Bedell with Deutsche Bank. Your line is now open. Please proceed with your question.

Brian Bedell

Analyst, Deutsche Bank Securities, Inc.

Q

All right. Thanks very much. So just maybe back on the buyback, maybe if you can just talk about whether you plan to be more opportunistic or more sort of regular through the quarters. And if your stock price goes up significantly, would you pair that back and look at other alternative uses of capital, such as [ph] a VC as you want

to be (47:15) opportunistic on small-sized M&A? And when can you actually get back in the market after [ph] earnings here (47:22)?

Michael A. Pizzi

*Chief Financial Officer, E*TRADE Financial Corp.*

A

Yeah. So, look, I think we've shown in the last program that we can be a little bit tactical. To the extent we have corporate liquidity and excess capital to work with, we can be tactical around the execution. That said, we don't authorize large buyback programs with a view of just leaving them out there. We intend to return capital. And so I would expect us to get started. But within those confines, we can be tactical, as we have been in the past around possible share price movements.

In terms of upside, I think it would depend on the conditions at the time under what should happen in terms of where that price is. We don't really have a target at which we would stop at this point. But, I mean, I think we would consider in the environment we're in and the [ph] relative (48:10) alternative capital opportunities that we would have.

Brian Bedell

Analyst, Deutsche Bank Securities, Inc.

Q

Okay, great. And then maybe a question for Karl. Obviously, you are proceeding well towards the growth goals. It's still early days, of course. Assuming that you do hit them and can sustain them, if you can improve the P/E, I guess, in terms of what investors are willing to pay for, for the earnings growth, how do you think about or, I guess, how do you and the board think about staying independent versus other strategic alternatives, such as a sale?

Karl A. Roessner

*Chief Executive Officer & Director, E*TRADE Financial Corp.*

A

Yeah. So, look, it's a good question. It's one I face quite often. So what I would say is, as a management team here, right, I've said this before. As a management team here, we are focused on continuing to drive value in the business every day, right? You guys see the changes that we're making. You see some of the impacts they're having. Yes, we have some tailwinds behind us. But I think we've done quite a nice job in terms of bringing this place along and really reigniting the growth engine that we have.

As a board, we know what our duties are and we will continue to evaluate those. Right? This is a very well-informed board. We go through an exercise once a year where we look at the intrinsic value. We have third parties come in and talk to the board and educate them to make sure that the board understands what the starting point is for any discussion, should those even happen. Right?

As the CEO, I can tell you, I fully expect to hit the growth goals and I fully expect to be independent and come out of this with flying colors. Those growth goals are not the end game of this organization. They are not a targeted state. They're merely to show that we can continue to grow the franchise and drive growth in it. So, that's really the process I go through with those three hats on. And I'm quite proud of what the organization has done so far.

Operator: Our next question comes from the line of Brennan Hawken with UBS. Your line is open. Please proceed with your question.

Brennan Hawken

Analyst, UBS Securities LLC

Q

Good afternoon. Thanks for taking the question, guys. First one from me on the deposit beta. Nice to see that sustaining at a remarkably low level. How should we think about the competitive environment and any potential upward pressure on that rate on a go-forward basis?

Karl A. Roessner

*Chief Executive Officer & Director, E*TRADE Financial Corp.*

A

Well, look, we absolutely continue to keep an eye on the competitive environment and sort of what's out there. You may see some pressure at the higher end of the book for customers who have extremely large cash balances who look at us in that respect. Right now, we're quite pleased with where we are and we'll continue to evaluate that as the market evolves.

Brennan Hawken

Analyst, UBS Securities LLC

Q

Okay. But just circling back to one of the points you made earlier, I think you made a reference to the idea that certain balances above FDIC thresholds remain – a portion remains off-balance sheet. Does that help maybe insulate some of that upward pressure on the high balance accounts?

Michael A. Pizzi

*Chief Financial Officer, E*TRADE Financial Corp.*

A

Yeah. I mean, within our two bank charters, we can hold the first \$500,000, essentially, of a customer's balance. After that, it's going to get pushed out to third-party banks for FDIC insurance purposes. We have multiple different pricing tiers and so we can apply different betas. When we talk about deposit beta, it's not one number. We can apply it across different pricing tiers so that essentially the larger cash balance customers, we can pay a higher rate through, if they're going to hold that cash for a longer period of time.

Frequently what you see with the large cash balances customers is that they sort of ebb and flow, as they go in and out of the market. And so, from an overall sensitivity, they're more sensitive, though, than small cash balance customers, but not meaningfully so in a way that they're trading in and out of the market. I will say, at this point, we have outperformed our estimates, and frankly would have gone back before any Fed moves, we would have had moves by now in terms of overall beta. But we are watching very closely to the competitive environment, looking at what our customers are expecting, what they're sensitive to, and we'll move accordingly when we feel that the time is necessary.

Operator: Our next question comes from the line of Kyle Voigt with KBW. Your line is now open. Please proceed with your question.

Kyle Voigt

Analyst, Keefe, Bruyette & Woods, Inc.

Q

Hi. Good evening. Just one question just on the futures offering. I think you said in that past that futures trades are about 2% of total DARTs and you also noted that you're planning on rolling out an integrated futures problem after the OptionsHouse integration. Just that we're getting – now that we're getting closer to that in August, I'm just wondering if you can give some more color on the offering, if you have plans for the rollout already, and then maybe what you think the opportunity is in terms of where futures can get to as a percentage of total DARTs. Thanks.

Karl A. Roessner

*Chief Executive Officer & Director, E*TRADE Financial Corp.*

A

Sure. And thank you for that because it sort of helps clarify a little bit of what we've talked about with the integration. So, in early August, we intend to complete the move of the OptionsHouse customers into the E*TRADE ecosystem, which basically means plugging them in, their functionality and their customers into our back and middle office on that offering.

So at that point in time, we will have them in our ecosystem. We will have our tools available to them. We'll have some other functionality available. But going forward, it will really be a platform that we will be very thoughtful about rolling out. Right? We have many different platforms right now. We have customers who like those, who have ways that they like to trade, ways that they're set up on their own E*TRADE accounts and the way that they've traded for years. So you don't want to just sort of unplug them and plug them into a new environment and offer them something that they really aren't interested in. So we're being very careful and thoughtful about rolling out the best for all of our customers.

As part of that will be a fully integrated futures offering. Right now, you're right, we're at about 2% of DARTs on futures. I see the opportunity there when you look at what some of our competitor set does. I mean, just to be quite frank and blunt, our futures offering, I love the fact that we have 2% coming through it because it's not that easy to use, right, the way that it's set up now. So when you fully integrate it, I think that our opportunity is more. We'd like to grow it to 10% of our overall DARTs. I think that's where we should be on a normalized basis when we have a fully integrated, seamless offering that our customers find easy to use, and that's sort of where we're headed. But that's a little bit longer term. It's probably a couple months down the road in terms of thinking about the platform, rolling it out and getting that done the right way for our customers.

Kyle Voigt

Analyst, Keefe, Bruyette & Woods, Inc.

Q

Great. Thank you.

Karl A. Roessner

*Chief Executive Officer & Director, E*TRADE Financial Corp.*

A

Yeah.

Operator: Our next question comes from the line of Chris Allen with Rosenblatt Securities. Your line is now open. Please proceed with your question.

Christopher Allen

Analyst, Rosenblatt Securities

Q

Evening, guys. Just a quick one, and I apologize if I missed this. Where do the OptionsHouse expense synergies currently stand? Is it still roughly 50% of the \$49 million? And is the remainder going to be triggered with the conversion, which I think it is?

Michael A. Pizzi

*Chief Financial Officer, E*TRADE Financial Corp.*

A

Yeah. I mean, in the prepared remarks, we talked a little bit about it. Post-conversion, we will have reached virtually all of the expense synergies. There are some small ones that'll go on over the remaining quarter or so.

But we will get all of the revenue synergies and most all of the expense synergies really by the time we're wrapping up Q3.

Christopher Allen

Analyst, Rosenblatt Securities

Q

And the expense synergies are currently about halfway?

Michael A. Pizzi

*Chief Financial Officer, E*TRADE Financial Corp.*

A

The \$49 million is the right total and we haven't updated exactly where we are, but most of the remaining ones are tied to integration.

Christopher Allen

Analyst, Rosenblatt Securities

Q

Great. Thanks, guys.

Operator: Our next question comes from the line of Doug Mewhirter with SunTrust. Your line is now open. Please proceed with your question.

Doug R. Mewhirter

Analyst, SunTrust RobinsonHumphrey, Inc.

Q

Hi. Good evening. First question on your loan portfolio. You talked about the 2007 vintage and how it's performing a lot better than expected post-conversion from interest only. What's the tail on that portfolio? So I imagine that part of that outperformance could be sort of economically related. How much time do you have before you – you actually don't even have to worry about the economy because most of those loans are going to be paid off anyway. Are you sort of holding your breath for 3 more years, 5 more years, 10 more years on [indiscernible] (56:53)?

Michael A. Pizzi

*Chief Financial Officer, E*TRADE Financial Corp.*

A

Well, I mean, contractually there is different amortization periods that they move into. But the bulk I believe are at 20-year amortizations, but that's not really necessarily the most relevant. The most relevant is the prepayment rate. They're prepaying and it's sort of almost 20% type range. That's going to give you on a 20-year amortizing loan really a – probably a weighted-average life I would guess right around three to four years or so, in that range. So I think the important aspect is even if they're economically sensitive, the amortization really begins to build collateral value – not collateral value, but begins to pay down the collateral value in the loan improving the overall LPD. So, at this point, as the portfolio seasons, it will naturally improve in credit quality.

Doug R. Mewhirter

Analyst, SunTrust RobinsonHumphrey, Inc.

Q

Okay. Thanks. And just one last very quick question. On your operating margin guidance, you had mentioned 100 basis points a little higher than you thought. That was for 2017. Is that correct?

Michael A. Pizzi

*Chief Financial Officer, E*TRADE Financial Corp.*

A

That's correct. Yes.

Doug R. Mewhirter

Analyst, SunTrust RobinsonHumphrey, Inc.

Q

Okay. Thanks. Those are all my questions.

Karl A. Roessner

*Chief Executive Officer & Director, E*TRADE Financial Corp.*

A

Thank you.

Operator: Our next question comes from the line of Mike Cyprys with Morgan Stanley. Your line is now open. Please proceed with your question.

Michael J. Cyprys

Analyst, Morgan Stanley & Co. LLC

Q

Hi. Good evening. Thanks for taking the question. Just curious on the Adaptive Portfolio, the robo-advisor that you have, if you could update us on the progress there. What's sort of been the feedback from customers, latest thoughts on the marketing campaign? You were planning to relaunch the marketing campaign for that at some point. And just how much in assets you have? And how you're thinking about the opportunities out there?

Karl A. Roessner

*Chief Executive Officer & Director, E*TRADE Financial Corp.*

A

Yeah. I mean, look, so robo, I talked about this – talked about it quite often in terms of the robo that we went out with on Adaptive Portfolio. It's a very nice tool. I think it works quite well. It has about \$400-plus million in it right now. I think to be in this space and to provide the right set of tools to your customers is extremely important. So I think when we look at the robo, we also need to think about just a more simplified robo offering that's easy to use for our customers. And I think you'll see a more integrated sort of easy-to-use offering rolling out over the next few months.

So, Adaptive has its place, but it'd also be a nice thing to have that sort of simplified offering that [ph] we'll roll with (59:16) for our customers. So I would look for a marketing campaign more around the tools and functionality as we go forward, as we get sort of more into the value proposition from the entry level., a new customer all the way through to the seasoned sort of derivatives trader.

Michael J. Cyprys

Analyst, Morgan Stanley & Co. LLC

Q

Okay, thanks. And then just following up on the dividend, you mentioned that you view a dividend is needing to have to be built around core earnings and growth over time. So just curious how you're thinking about E*TRADE's core earnings today and your ability to grow that over time and why not pay out a dividend from that core earnings stream today?

Michael A. Pizzi

*Chief Financial Officer, E*TRADE Financial Corp.*

A

Yeah. I mean, we looked at the capital plan in terms of the generation of capital up to the parent that we can move from subsidiaries over the course of the year and then really this one-time – the one-time benefit of the move in ratios plus the reserve release that occurred in the quarter. We felt that we are still relatively tactical around the capital planning process and we want to be flexible in our capital priorities, much like you saw in the OH acquisition, we were in mid of a program that was authorized to the \$800 million level and completed roughly

\$500 million when we switched and deployed some of that cash in the acquisition of OH. I think that that's a good example of tactical flexibility in the program. That's not to say we wouldn't look to dividends in the future. I just think at this phase in our evolution, the buyback program is what makes the most sense.

Operator: And our next question comes from the line of Patrick O'Shaughnessy with Raymond James. Your line is open. Please proceed with your question.

Patrick J. O'Shaughnessy

Analyst, Raymond James & Associates, Inc.

Q

Hey. So net new asset growth is arguably your most ambitious goal. What's your confidence level in achieving 5.8% to 6.8% net new asset growth, which by my math implies from going from about \$10 billion of net new assets in 2016 to probably closer to \$18 billion or so in 2018.

Karl A. Roessner

*Chief Executive Officer & Director, E*TRADE Financial Corp.*

A

Yeah. Look, Patrick, it's something that I am still extremely confident in. Right? We laid them out as realistic goals and that growth will come from the complete integration of the OptionsHouse platform, growing our customer base. It will come from our Corporate Services channel and the asset and account growth that we get through that channel. So I am still extremely confident in the numbers that we put out there.

Patrick J. O'Shaughnessy

Analyst, Raymond James & Associates, Inc.

Q

Great. And then maybe a follow-up for Mike. Can you quantify how much order flow revenue increased quarter-over-quarter? And probably more importantly, how much upside is there to that revenue line when you kind of achieve your long-term derivatives as a percentage of trading goal?

Michael A. Pizzi

*Chief Financial Officer, E*TRADE Financial Corp.*

A

Order flow revenue was up about \$4 million overall versus the \$11 million gain in fees and service charges. In terms of what the long run is, we ended at about 32% overall for Options DARTs. Our goal in the intermediate term is 35%. That's really what's driving that. So you can scale up the increase in payment if we are successful there in terms of the overall proportion of DARTs in driving that additional value from the fees and service charges line.

Operator: There are no further questions at this time. I will now turn the call over to our presenters.

Karl A. Roessner

*Chief Executive Officer & Director, E*TRADE Financial Corp.*

Well, thank you all for joining, and have a great evening.

Operator: Ladies and gentlemen, that does conclude the call for today. We thank you for your participation and ask that you please disconnect your lines.

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