STATE STREET CORP
Form 10-Q
May 03, 2013
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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 March 31, 2013

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<br>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 ¨<br>(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 April 30, 2013 was 456,072,479.

STATE STREET CORPORATION
QUARTERLY REPORT ON FORM 10-Q FOR THE QUARTERLY PERIOD ENDED
MARCH 31, 2013

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

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## 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 March 31, 2013, we had consolidated total assets of $218.19 billion, consolidated total deposits of $154.78 billion, consolidated total shareholders' equity of $20.87 billion and 29,500 employees. With $25.42 trillion of assets under custody and administration and $2.18 trillion of assets under management as of March 31, 2013, 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; 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 range of investment management strategies, specialized investment management advisory services and other financial services, such as securities finance, for corporations, public funds, and other sophisticated investors. Management strategies offered by SSgA include passive and active, such as enhanced indexing, using quantitative and fundamental methods for both U.S. and non-U.S. equity and fixed-income securities. SSgA also offers exchange-traded funds, or ETFs.

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 in note 15 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 March 31, 2013, and updates the Management's Discussion and Analysis in our Annual Report on Form 10-K for the year ended December 31, 2012, referred to as our 2012 Form 10-K, 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 estimates and assumptions that are difficult, subjective or complex about matters that are uncertain and may change in subsequent periods are 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. An understanding of the judgments, estimates and assumptions underlying these significant accounting policies is essential in order to understand our reported consolidated results of operations and financial condition.

Additional information about these significant accounting policies is included under “Significant Accounting Estimates” in Management’s Discussion and Analysis in our 2012 Form 10-K. We did not change these significant accounting policies during the first quarter of 2013.

Certain financial information presented in this Management's Discussion and Analysis is prepared on both a GAAP, or reported basis, and a non-GAAP, or operating basis. 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 and excludes the impact of revenue and expenses outside of the normal course of our business, 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. Operating-basis financial information

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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.

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 industry, regulatory, economic and market trends, management's expectations about our financial performance, capital, market growth, acquisitions, joint ventures and divestitures, new technologies, services and opportunities and earnings, management's confidence in our strategies and other matters that do not relate strictly to historical facts. Terminology such as "plan," "expect," "intend," "forecast," "look," "believe," "anticipate," "estimate," "seek," "may," "will," and "goal," or similar statements or variations of such terms, 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 current sovereign-debt risks in Europe and other regions;
- financial market disruptions or economic recession, whether in the U.S., Europe, Asia or other regions;
- increases in the volatility of, or declines in the level of, our net interest revenue, changes in the composition 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;
- 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 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, the Basel II and Basel III capital and liquidity standards, and European legislation 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, increased costs or other changes to how we provide services;
- adverse changes in the regulatory capital ratios that we are required to meet, whether arising under the Dodd-Frank Act, the Basel II or 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 calculating 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

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programs or other capital initiatives may be restricted;

- changes in 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;
- our ability to promote a strong culture of risk management, operating controls, compliance oversight and governance that meet our expectations or those of our clients and our regulators;
- the credit agency ratings of our debt and depository obligations and investor and client perceptions of our financial strength;
- 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 results of, and costs associated with, government investigations, litigation, and similar claims, disputes, or proceedings;
- 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 valuation of assets underlying those pools;
- adverse publicity or other reputational harm;
- dependencies on information technology, complexities and costs of protecting the security of our systems and difficulties with protecting our intellectual property rights;
- 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;
- 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;
- 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;
- the 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 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 disynergies 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;
- our ability to anticipate and manage the level and timing of redemptions and withdrawals from our collateral pools and other collective investment products;
- our ability to control operating risks, data security breach risks, information technology systems 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;
- 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 2012 Form 10-K. Forward-looking statements 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

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

developments that may adversely affect our consolidated results of operations and 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 reports on Forms 10-K, 10-Q and 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 our website at www.statestreet.com.

OVERVIEW OF FINANCIAL RESULTS

| | Quarters Ended March 31, | | |
|---|---|---|---|
| (Dollars in millions, except per share amounts) | 2013 | 2012 | % Change |
| Total fee revenue | $1,857 | $1,785 | 4 % |
| Net interest revenue | 576 | 625 | (8 ) |
| Gains related to investment securities, net | 2 | 11 | |
| Total revenue | 2,435 | 2,421 | 1 |
| Expenses: | | | |
| Expenses from operations | 1,812 | 1,799 | 1 |
| Provisions for litigation exposure | — | 15 | |
| Acquisition and restructuring costs, net | 14 | 21 | |
| Total expenses | 1,826 | 1,835 | — |
| Income before income tax expense | 609 | 586 | 4 |
| Income tax expense | 145 | 159 | |
| Net income | $464 | $427 | 9 |
| Adjustments to net income: | | | |
| Dividends on preferred stock | (7 ) | (7 ) | |
| Earnings allocated to participating securities | (2 ) | (3 ) | |
| Net income available to common shareholders | $455 | $417 | |
| Earnings per common share: | | | |
| Basic | $1.00 | $.86 | |
| Diluted | .98 | .85 | 15 |
| Average common shares outstanding (in thousands): | | | |
| Basic | 454,315 | 484,942 | |
| Diluted | 462,751 | 490,454 | |
| Cash dividends declared per common share | $.26 | $.24 | |
| Return on average common equity | 9.1 % | 8.8 % | |

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

The following "Highlights" and "Financial Results" sections provide information related to significant first-quarter 2013 events, as well as highlights of our consolidated financial results for the first quarter of 2013 presented in the preceding table. More detailed information about our consolidated financial results, including comparisons of our results for the first quarter of 2013 to those for the first quarter of 2012, is provided under "Consolidated Results of Operations," which follows these sections.

## Highlights

In March 2013, we received the results of the Federal Reserve's review of our 2013 capital plan in connection with its comprehensive capital analysis and review, or CCAR, process. The Federal Reserve did not object to the capital actions we proposed, and as we previously announced, in March 2013, our Board of Directors approved a new common stock purchase program authorizing the purchase of up to $2.10 billion of our common stock through March 31, 2014. This new program follows the $1.80 billion program authorized by the Board of Directors in March 2012 and fully executed from April 2012 through February 2013.

We did not purchase any of our common stock under the new program in the first quarter of 2013. We completed the March 2012 program by purchasing approximately 6.5 million shares of our common stock, at an average cost of $54.95 per share and an aggregate cost of approximately $360 million, in the first quarter of 2013. We also declared a quarterly common stock dividend of $0.26 per share, or approximately $118 million in the aggregate, in February 2013, which was paid in April 2013. This dividend compares to a quarterly common stock dividend of $0.24 per share, or approximately $118 million in the aggregate, declared in the first quarter of 2012 and paid in April 2012. 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.

With respect to our Business Operations and Information Technology Transformation program, in 2011 and 2012 combined, we achieved approximately $198 million of cumulative pre-tax expense savings compared to our 2010 expenses from operations, all else being equal. In 2013, we expect to achieve additional pre-tax expense savings of approximately $220 million compared to our above-described 2010 expense base, all else being equal. 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. Our actual total expenses have increased since 2010, and may in the future increase or decrease, due to other factors. Additional information about our Business Operations and Information Technology Transformation program is provided under "Consolidated Results of Operations – Expenses" in this Management's Discussion and Analysis.

## Financial Results

Total revenue in the first quarter of 2013 increased 1% compared to the first quarter of 2012, as a combined 9% increase in aggregate servicing fee and management fee revenue was substantially offset by declines in net interest revenue, processing fees and other revenue and securities finance revenue.

Servicing fee revenue in the first quarter of 2013 increased 9% compared to the first quarter of 2012, mainly the result of stronger global equity markets, net new business installed and revenue from the Goldman Sachs Administration Services, or GSAS, business, acquired in October 2012. In the first quarter of 2013 and the first quarter of 2012, servicing fees generated outside the U.S. were approximately 41% and 42%, respectively, of total servicing fees for those periods. Management fee revenue increased 11% in the same comparison, primarily the result of stronger equity markets and net new business. Management fees generated outside the U.S. in both the first quarter of 2013 and the first quarter of 2012 were approximately 37% of total management fees for those periods.

In the first quarter of 2013, trading services revenue was flat compared to the first quarter of 2012. In the same comparison, foreign exchange trading revenue was down 2%, as declines in currency volatility and spreads were partly offset by higher client volumes. This revenue was also affected by changes in mix between direct sales and trading foreign exchange and indirect foreign exchange. Our estimated indirect foreign exchange revenue declined 13%, mainly the result of lower volatility and spreads, while direct sales and trading foreign exchange revenue increased 9%, mainly the result of higher client volumes, partly offset by lower volatility and spreads. With respect to brokerage and other trading services revenue, our revenue from electronic foreign exchange trading platforms increased 16%, primarily the result of a 34% increase in client volumes. Securities finance revenue in the first quarter of 2013 declined 20% compared to the first quarter of 2012, as a result of lower spreads and lower average lending volumes.

Net interest revenue in the first quarter of 2013 declined 8% compared to the first quarter of 2012, generally the result of lower yields on earning assets related to lower global market rates and repricing on floating-rate investment securities, partly offset by lower funding costs. Yields on the investment portfolio were also affected by the reinvestment of pay-downs and

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other runoff into lower-yielding securities. Net interest revenue in the first quarter of 2013 and the first quarter of 2012 included $31 million and $49 million, respectively, of discount accretion related to investment securities added to our consolidated statement of condition in connection with the 2009 consolidation of our asset-backed commercial paper conduits.

Net interest margin, calculated on fully taxable-equivalent net interest revenue, declined 26 basis points to 1.38% in the first quarter of 2013 from 1.64% in the first quarter of 2012. Higher levels of client deposits, amid continued market uncertainty, increased our average interest-earning assets, but negatively affected our net interest margin, as we generally placed certain of such deposits with central banks and earned the relatively low interest rates paid by the central banks on these balances. Discount accretion, 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 first quarter of 2013 were flat compared to the first quarter of 2012. Compensation and employee benefits expenses declined in the same comparison, partly due to the impact of savings associated with the Business Operations and Information Technology Transformation program. This decline was offset by an increase in information systems and communications expenses, which resulted primarily from the transition of activities to third-party service providers associated with components of our technology infrastructure and application maintenance and support, as we continued to implement the Business Operations and Information Technology Transformation program. Additional information with respect to our expenses is provided under "Consolidated Results of Operations - Expenses" in this Management's Discussion and Analysis.

During the first quarter of 2013, we secured mandates for approximately $223 billion of new business in assets to be serviced; of the total, $180 billion was installed prior to March 31, 2013, with the remaining $43 billion expected to be installed in later periods. The new business not installed by March 31, 2013 was not included in assets under custody and administration as of that date, and had no impact on servicing fee revenue in the first quarter of 2013, as the assets are not included until their installation is complete and we begin to service them. In addition, we installed approximately $479 billion of new business in assets to be serviced in the first quarter that we were awarded prior to January 1, 2013. We will provide one or more various services for these new assets to be serviced, including accounting, fund administration, bank loan services, custody, securities finance, compliance reporting and monitoring, hedge fund servicing, private equity administration, real estate administration, depository banking services, wealth management services, and investment manager and alternative investment manager operations outsourcing.

In the first quarter of 2013, SSgA added approximately $5 billion of net new business in assets to be managed, generally composed of approximately $16 billion of net inflows into managed cash and approximately $3 billion of net inflows into active and enhanced equity funds, partly offset by approximately $8 billion of net outflows from fixed-income funds and approximately $6 billion of net outflows from ETFs.

An additional $34 billion of new business awarded to SSgA but not installed by March 31, 2013 was not included in assets under management as of that date, and had no impact on management fee revenue for the first quarter of 2013, 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 first quarter of 2013 compared to the first quarter of 2012, and should be read in conjunction with the consolidated financial statements and accompanying condensed notes included in this Form 10-Q.

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

## 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 2012 Form 10-K.

| | Quarters Ended March 31, | | | |
|---|---|---|---|---|
| (Dollars in millions) | 2013 | 2012 | % Change | |
| Fee revenue: | | | | |
| Servicing fees | $1,175 | $1,078 | 9 | % |
| Management fees | 263 | 236 | 11 | |
| Trading services: | | | | |
| Foreign exchange trading | 146 | 149 | (2 | ) |
| Brokerage and other trading services | 135 | 131 | 3 | |
| Total trading services | 281 | 280 | — | |
| Securities finance | 78 | 97 | (20 | ) |
| Processing fees and other | 60 | 94 | (36 | ) |
| Total fee revenue | 1,857 | 1,785 | 4 | |
| Net interest revenue: | | | | |
| Interest revenue | 687 | 765 | (10 | ) |
| Interest expense | 111 | 140 | (21 | ) |
| Net interest revenue | 576 | 625 | (8 | ) |
| Gains related to investment securities, net | 2 | 11 | | |
| Total revenue | $2,435 | $2,421 | 1 | |

### Fee Revenue

Servicing and management fees collectively composed approximately 77% of our total fee revenue in the first quarter of 2013, compared to 74% in the first quarter of 2012. The level of these fees is influenced by several factors, including the mix and volume of assets under custody and administration and assets under management, securities positions held and the volume of portfolio transactions, and the types of products and services used by clients, and is generally affected by changes in worldwide equity and fixed-income security valuations.

Generally, servicing fees are affected, in part, 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, in part, by changes in month-end valuations of assets under management. Management fee revenue is relatively 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 values. 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 value of assets under management and the investment strategy employed, management fees reflect other factors as well, including our relationship pricing for clients using multiple services.

Management fees for actively managed products are generally earned at higher rates than those 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, assuming all other factors remain constant, that a 10% increase or decrease in worldwide equity valuations would result in a corresponding change in our total revenue of approximately 2%. If fixed-income security valuations were to increase or decrease by 10%, we would anticipate a corresponding change of approximately 1% in our total revenue.

The following table presents selected average and quarter-end equity market indices. Daily averages and the averages of month-end indices demonstrate worldwide changes in equity markets that affect our servicing and management fee revenue,

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

respectively. Quarter-end indices affect the value 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 March 31, | | | Averages of Month-End Indices Quarters Ended March 31, | | | Quarter-End Indices As of March 31, | | |
|---|---|---|---|---|---|---|---|---|---|
| | 2013 | 2012 | % Change | 2013 | 2012 | % Change | 2013 | 2012 | % Change |
| S&P 500® | 1,514 | 1,349 | 12 % | 1,527 | 1,362 | 12 % | 1,569 | 1,408 | 11 % |
| NASDAQ® | 3,176 | 2,907 | 9 | 3,190 | 2,957 | 8 | 3,268 | 3,092 | 6 |
| MSCI EAFE® | 1,668 | 1,516 | 10 | 1,676 | 1,536 | 9 | 1,674 | 1,553 | 8 |

Servicing Fees

Servicing fees in the first quarter of 2013 increased 9% compared to the first quarter of 2012, primarily as a result of stronger global equity markets, the impact of net new business installed on current-period revenue, and the addition of revenue from the GSAS business, acquired in October 2012. The combined daily averages of equity market indices, individually presented in the foregoing "INDEX" table, increased an average of approximately 10% in the first quarter of 2013 compared to the first quarter of 2012. In the first quarter of 2013 and the first quarter of 2012, servicing fees generated outside the U.S. were approximately 41% and 42%, respectively, of total servicing fees.

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

ASSETS UNDER CUSTODY AND ADMINISTRATION

| (In billions) | March 31, 2013 | December 31, 2012 | March 31, 2012 |
|---|---|---|---|
| Mutual funds | $6,275 | $ 5,852 | $5,681 |
| Collective funds | 5,753 | 5,363 | 4,792 |
| Pension products | 5,331 | 5,339 | 5,116 |
| Insurance and other products | 8,063 | 7,817 | 7,619 |
| Total | $25,422 | $ 24,371 | $23,208 |

FINANCIAL INSTRUMENT MIX OF ASSETS UNDER CUSTODY AND ADMINISTRATION

| (In billions) | March 31, 2013 | December 31, 2012 | March 31, 2012 |
|---|---|---|---|
| Equities | $13,095 | $ 12,276 | $12,004 |
| Fixed-income | 9,069 | 8,885 | 8,384 |
| Short-term and other investments | 3,258 | 3,210 | 2,820 |
| Total | $25,422 | $ 24,371 | $23,208 |

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

| (In billions) | March 31, 2013 | December 31, 2012 | March 31, 2012 |
|---|---|---|---|
| United States | $18,477 | $ 17,711 | $16,757 |
| Other Americas | 757 | 752 | 673 |
| Europe/Middle East/Africa | 5,060 | 4,801 | 4,659 |
| Asia/Pacific | 1,128 | 1,107 | 1,119 |
| Total | $25,422 | $ 24,371 | $23,208 |

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

The increase in total servicing assets from December 31, 2012 to March 31, 2013 primarily resulted from increases in global equity markets and net client subscriptions. The increase in total servicing assets from March 31, 2012 to March 31, 2013 primarily resulted from increases in global equity markets, net client subscriptions and net new servicing business

installations. Servicing asset levels as of March 31, 2013 did not reflect the $43 billion of new business in assets to be serviced awarded to us in first quarter of 2013 but not installed prior to March 31, 2013. 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 in the first quarter of 2013 increased 11% compared to the first quarter of 2012, primarily the result of stronger equity market valuations and the impact of net new business installed on current-period revenue. Combined average month-end equity market indices, individually presented in the foregoing "INDEX" table, increased an average of approximately 9% in the first quarter of 2013 compared to the first quarter of 2012. For both the first quarter of 2013 and the first quarter of 2012, management fees generated outside the U.S. were approximately 37% of total management fees for those periods.

The following tables present the components and geographic mix of assets under management as of the dates indicated:

ASSETS UNDER MANAGEMENT

| (In billions) | March 31, 2013 | December 31, 2012 | March 31, 2012 |
|---|---|---|---|
| Passive: | | | |
| Equities | $813 | $755 | $725 |
| Fixed-income | 289 | 292 | 220 |
| Exchange-traded funds[1] | 354 | 337 | 308 |
| Other[2] | 221 | 211 | 203 |
| Total passive | 1,677 | 1,595 | 1,456 |
| Active: | | | |
| Equities | 53 | 52 | 56 |
| Fixed-income | 17 | 17 | 19 |
| Other | 49 | 55 | 54 |
| Total active | 119 | 124 | 129 |
| Cash | 380 | 367 | 395 |
| Total | $2,176 | $2,086 | $1,980 |

[1] Includes SPDR® Gold Fund, for which State Street is not the investment manager, but acts as distribution agent.
[2] Includes currency, alternatives, assets passed to sub-advisors and multi-asset class solutions.

GEOGRAPHIC MIX OF ASSETS UNDER MANAGEMENT[1]

| (In billions) | March 31, 2013 | December 31, 2012 | March 31, 2012 |
|---|---|---|---|
| United States | $1,477 | $1,394 | $1,367 |
| Other Americas | 41 | 39 | 34 |
| Europe/Middle East/Africa | 357 | 351 | 349 |
| Asia/Pacific | 301 | 302 | 230 |
| Total | $2,176 | $2,086 | $1,980 |

[1] Geographic mix is based on the location at which the assets are managed.

The increase in total assets under management as of March 31, 2013 compared to December 31, 2012 resulted from net market appreciation during the quarter in the values of the assets managed, as well as net new business of $5 billion. The net new business of $5 billion was generally composed of approximately $16 billion of net inflows into managed cash and approximately $3 billion of net inflows into equity funds, partly offset by approximately $8 billion of net outflows from fixed-income funds and approximately $6 billion of net outflows from ETFs.

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The following table presents activity in assets under management for the twelve months ended March 31, 2013:
ASSETS UNDER MANAGEMENT

| (In billions) | |
|---|---|
| March 31, 2012 | $1,980 |
| Net new business | 71 |
| Market appreciation | 35 |
| December 31, 2012 | 2,086 |
| Net new business | 5 |
| Market appreciation | 85 |
| March 31, 2013 | $2,176 |

The net new business of $5 billion in the first quarter of 2013 presented in the table did not include $34 billion of new business awarded to SSgA in the first quarter of 2013 but not installed prior to March 31, 2013. This new business will be reflected in assets under management in future periods after installation, and will generate management fee revenue in subsequent periods.

Trading Services

The following table summarizes the components of trading services revenue for the periods indicated:

| | Quarters Ended March 31, | | |
|---|---|---|---|
| (Dollars in millions) | 2013 | 2012 | % Change |
| Foreign exchange trading: | | | |
| Direct sales and trading | $81 | $74 | 9 % |
| Indirect foreign exchange trading | 65 | 75 | (13 ) |
| Total foreign exchange trading | 146 | 149 | (2 ) |
| Brokerage and other trading services: | | | |
| Electronic foreign exchange trading | 64 | 55 | 16 |
| Other trading, transition management and brokerage | 71 | 76 | (7 ) |
| Total brokerage and other trading services | 135 | 131 | 3 |
| Total trading services revenue | $281 | $280 | — |

Trading services revenue includes revenue from foreign exchange, or FX, trading, as well as revenue from 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, commission recapture and self-directed brokerage. These products are differentiated by our position as an agent of the institutional investor. Revenue earned from these brokerage and other trading products is recorded in other trading, transition management and brokerage within brokerage and other trading services revenue.

FX trading revenue is influenced by three principal factors: the volume and type of client FX transactions; currency volatility; and the management of currency and rate market risks. 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 change in trading services revenue in the first quarter of 2013 compared to the first quarter of 2012, composed of separate changes related to FX trading and brokerage and other trading services, is explained below.

Total FX trading revenue declined 2% in the first quarter of 2013 compared to the first quarter of 2012, primarily the result of declines in currency volatility and spreads, partly offset by higher client volumes. This revenue was also affected by changes in mix between direct sales and trading FX and indirect FX. We enter into FX transactions with clients and investment

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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.

For the quarters ended March 31, 2013 and 2012, our estimated indirect FX revenue was approximately $65 million and $75 million, respectively. The 13% decline was mainly the result of lower volatility and lower spreads. All other FX revenue, other than this indirect FX revenue estimate, is considered by us to be direct sales and trading FX revenue. For the quarter ended March 31, 2013 compared to the quarter ended March 31, 2012, our direct sales and trading FX revenue increased 9%, mainly the result of higher client volumes, partly offset by lower volatility and lower spreads.

During the first quarter of 2013, some of our clients who relied on our indirect model to execute their FX transactions transitioned to other methods to conduct their FX transactions. Through State Street Global Exchange, a unit of our Investment Servicing line of business, clients can transition 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. The decline in indirect FX revenue in the first quarter of 2013 compared to the first quarter of 2012 was partly attributable to this shift. 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 increased 3% in the first quarter of 2013 compared to the first quarter of 2012. Our clients may choose to execute FX transactions through one of our electronic trading platforms. This service generates revenue through a "click" fee. For the quarter ended March 31, 2013 compared to the quarter ended March 31, 2012, our revenue from electronic FX trading platforms increased 16%, primarily the result of a 34% increase in client volumes.

Securities Finance

Our agency securities finance business consists of two principal components: investment funds with a broad range of investment objectives which are managed by SSgA and engage in agency securities lending, 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.

We also participate in securities lending transactions as a principal. 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, and we have the ability to source securities through our assets under custody and administration.

Securities finance revenue, 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 and the interest-rate spreads and fees earned on the underlying collateral. In the first quarter of 2013, securities finance revenue declined 20% compared to the first quarter of 2012, due to lower spreads and lower average lending volumes. Average spreads declined 16% in the first quarter of 2013 compared to the first quarter of 2012, and securities on loan averaged approximately $313 billion in the first quarter of 2013 compared to approximately $331 billion in the first quarter of 2012, a 5% decline. Market influences may continue to affect 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 declined 36% in the first quarter of 2013 compared to the first quarter of 2012. The decline was mainly due to the positive fair-value adjustments of $24 million recorded in the first quarter of 2012 related to our withdrawal from our fixed-income trading initiative.

NET INTEREST REVENUE

Net interest revenue is defined as total 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-

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equivalent net interest revenue and average total 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 table presents 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 March 31, | | | | | |
|---|---|---|---|---|---|---|
| | 2013 | | | 2012 | | |
| (Dollars in millions; fully taxable-equivalent basis) | Average Balance | Interest Revenue/ Expense | Rate | Average Balance | Interest Revenue/ Expense | Rate |
| Interest-bearing deposits with banks | $30,586 | $31 | .41 % | $25,561 | $42 | .67 % |
| Securities purchased under resale agreements | 5,649 | 13 | .95 | 7,485 | 9 | .52 |
| Trading account assets | 728 | — | — | 719 | — | — |
| Investment securities | 119,601 | 618 | 2.07 | 109,740 | 689 | 2.51 |
| Loans and leases | 12,737 | 56 | 1.77 | 10,762 | 55 | 2.08 |
| Other interest-earning assets | 9,023 | 1 | .06 | 6,937 | 1 | .05 |
| Average total interest-earning assets | $178,324 | $719 | 1.63 | $161,204 | $796 | 1.99 |
| Interest-bearing deposits: | | | | | | |
| U.S. | $13,398 | $6 | .19 % | $2,455 | $3 | .40 % |
| Non-U.S. | 99,720 | 28 | .11 | 87,029 | 50 | .23 |
| Securities sold under repurchase agreements | 7,839 | — | — | 7,439 | — | — |
| Federal funds purchased | 363 | — | — | 808 | — | — |
| Other short-term borrowings | 4,640 | 16 | 1.42 | 4,673 | 18 | 1.54 |
| Long-term debt | 7,400 | 56 | 3.03 | 8,141 | 66 | 3.23 |
| Other interest-bearing liabilities | 6,496 | 5 | .31 | 6,855 | 3 | .20 |
| Average total interest-bearing liabilities | $139,856 | $111 | .32 | $117,400 | $140 | .48 |
| Interest-rate spread | | | 1.31 % | | | 1.51 % |
| Net interest revenue—fully taxable-equivalent basis | | $608 | | | $656 | |
| Net interest margin—fully taxable-equivalent basis | | | 1.38 % | | | 1.64 % |
| Tax-equivalent adjustment | | (32) | | | (31) | |
| Net interest revenue—GAAP basis | | $576 | | | $625 | |

In the first quarter of 2013 compared to the first quarter of 2012, average total interest-earning assets increased, mainly the result of the investment of higher levels of client deposits into interest-bearing deposits with banks, as well as purchases of investment securities. During the past year, our clients continued to place additional deposits with us amid market and public concerns related to various economic events. Those deposits determined to be transient in nature are placed with various central banks globally, whereas deposits determined to be more stable are invested in our securities portfolio or elsewhere to support growth in other client-related activities to monetize their value.

The increase in average U.S. interest-bearing deposits resulted primarily from the issuance of additional certificates of deposit in connection with our management of liquidity (refer to our discussion of liquidity management under “Financial Condition - Liquidity” in this Management's Discussion and Analysis). Although the placement of client deposits and proceeds from the issuance of certificates of deposit with various central banks increases our average interest-earning assets, it negatively affects our net interest margin, as placements generate only marginal, and in some cases zero percent, returns.

Average loans and leases were higher due to growth in lending to mutual fund clients.  Higher levels of cash collateral provided in connection with our role as principal in certain securities finance activities drove other interest-earning assets higher. While these activities support our overall profitability, they put downward pressure on our net interest margin.

Net interest revenue decreased 8% in the first quarter of 2013 compared to the first quarter of 2012. The decrease was primarily driven by the impacts of lower global market rates, which negatively affected the rates paid on funds held with non-U.S. central banks, and repricing on floating-rate investment securities. Yields on investment securities were also affected by higher levels of pay-downs and subsequent reinvestment in lower-yielding securities. The decrease in net interest revenue was partly offset by the impacts of growth in the investment portfolio, lower funding costs, and higher levels of client deposits invested with the Federal Reserve, the European Central Bank, or ECB, and other non-U.S. central banks. Subsequent to the previously disclosed 2009 commercial paper conduit consolidation, we have recorded aggregate discount accretion in interest revenue of $1.80 billion ($621 million in 2009, $712 million in 2010, $220 million in 2011, $215 million in 2012 and $31 million in the first quarter of 2013). 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 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 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 March 31, 2013 to generate aggregate discount accretion in future periods of approximately $684 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 12 to the consolidated financial statements included in this Form 10-Q.

Interest-bearing deposits with banks, which include cash balances maintained at the Federal Reserve, the ECB and other non-U.S. central banks to satisfy reserve requirements, averaged $30.59 billion for the quarter ended March 31, 2013, compared to $25.56 billion for the quarter ended March 31, 2012, reflecting the impact of the placement of higher levels of client deposits. Given the expiration of the Federal Deposit Insurance Corporation's, or FDIC's, Transaction Account Guarantee, or TAG, and the likelihood that the low-rate environment will persist, we expect to continue to invest client deposits in either money market assets, including central bank deposits, or in investment securities, depending on our assessment of the characteristics of the deposits.

Our average investment securities portfolio increased to $119.60 billion for the quarter ended March 31, 2013 from $109.74 billion for the quarter ended March 31, 2012. The increase was generally the result of ongoing purchases of securities, partly offset by maturities, sales and prepayments. Period-end portfolio balances are more significantly influenced by the timing of purchases, sales and runoff; as a result, average portfolio balances are a more effective indication of trends in portfolio activity. As of March 31, 2013, securities rated "AAA" and "AA" represented approximately 88% of our portfolio, consistent with such composition as of March 31, 2012.

Loans and leases averaged $12.74 billion for the quarter ended March 31, 2013 compared to $10.76 billion for the quarter ended March 31, 2012. This increase was mainly related to mutual fund lending, which grew to an average of $8.11 billion for the quarter ended March 31, 2013 from an average of $6.47 billion for the quarter ended March 31, 2012. Client demand for short-duration liquidity increased as well, but declined as a percentage of our average loan-and-lease portfolio to approximately 27% in the quarter ended March 31, 2013 from 29% in the quarter ended March 31, 2012. Short-duration advances provide liquidity to clients in support of their investment activities related to securities settlement.

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

| | Quarters Ended March 31, | |
|---|---|---|
| (In millions) | 2013 | 2012 |
| Average U.S. short-duration advances | $2,089 | $1,802 |
| Average non-U.S. short-duration advances | 1,401 | 1,267 |
| Average total short-duration advances | $3,490 | $3,069 |

In the first quarter of 2013 compared to the first quarter of 2012, average total short-duration advances increased but remained low relative to historical levels, mainly the result of clients continuing to hold higher levels of liquidity.

Average other interest-earning assets increased to $9.02 billion in the first quarter of 2013 from $6.94 billion in the first quarter of 2012, primarily the result of higher levels of cash collateral provided in connection with our role as principal in certain securities finance activities.

Aggregate average interest-bearing deposits increased to $113.12 billion in the first quarter of 2013 from $89.48 billion in the first quarter of 2012. This increase mainly reflected higher levels of certificates of deposit issued in connection with our management of liquidity (refer to our discussion of liquidity management under "Financial Condition - Liquidity" in this

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Management's Discussion and Analysis). In addition, non-U.S. transaction accounts associated with new and existing business in assets under custody and administration continued to grow, although there has been a modest decline in non-interest bearing deposits as a result of the expiration of the FDIC's TAG. Future deposit levels will be influenced by anticipated growth in the underlying asset servicing business, as well as market conditions, including the general levels of U.S. and non-U.S. interest rates.

Average long-term debt decreased to $7.40 billion in the first quarter of 2013 from $8.14 billion in the first quarter of 2012. The decrease primarily reflected the maturities of $250 million of senior notes and $1.5 billion of senior notes in April 2012, the latter of which was previously issued by State Street Bank under the FDIC's Temporary Liquidity Guarantee Program. This decrease was partly offset by the issuance of $1 billion of extendible notes by State Street Bank in December 2012.

Average other interest-bearing liabilities decreased to $6.50 billion in the first quarter of 2013 from $6.86 billion in the first quarter of 2012, primarily the result of lower levels of client cash collateral received in connection with our role as principal in certain securities finance activities.

Several factors could affect future levels of our net interest revenue and margin, including the mix of client liabilities; actions of the various central banks; changes in U.S. and non-U.S. interest rates; the various yield curves around the world; 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 re-invest the proceeds from pay-downs and maturities of securities in highly-rated investment securities, such as U.S. Treasuries and Agencies, federal agency mortgage-backed securities and U.S. and non-U.S. mortgage- and asset-backed securities. The pace at which we continue to re-invest and the types of securities purchased will depend on the impact of market conditions and other factors over time. We expect these factors and the levels of interest rates worldwide to dictate what effect our re-investment program will have on future levels of our net interest revenue and net interest margin.

Gains (Losses) Related to Investment Securities, Net

The following table presents net realized gains from sales of securities and the components of net impairment losses, included in net gains and losses related to investment securities, for the periods indicated:

| | Quarters Ended March 31, | |
|---|---|---|
| (In millions) | 2013 | 2012 |
| Net realized gains from sales of available-for-sale securities | $5 | $19 |
| Losses from other-than-temporary impairment | — | (25) |
| Losses reclassified (from) to other comprehensive income | (3) | 17 |
| Net impairment losses recognized in consolidated statement of income | (3) | (8) |
| Gains (losses) related to investment securities, net | $2 | $11 |
| Impairment associated with expected credit losses | $— | $(4) |
| Impairment associated with adverse changes in timing of expected future cash flows | (3) | (4) |
| Net impairment losses recognized in consolidated statement of income | $(3) | $(8) |

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 quarter of 2013, we sold approximately $2.75 billion of such investment securities, compared to approximately $1.09 billion in the first quarter of 2012, and recorded net realized gains of $5 million and $19 million, respectively.

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 and losses 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.

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EXPENSES

The following table presents the components of expenses for the periods indicated:

| | Quarters Ended March 31, | | |
|---|---|---|---|
| (Dollars in millions) | 2013 | 2012 | % Change |
| Compensation and employee benefits | $1,035 | $1,064 | (3)% |
| Information systems and communications | 237 | 191 | 24 |
| Transaction processing services | 180 | 181 | (1) |
| Occupancy | 116 | 119 | (3) |
| Acquisition costs | 15 | 13 | |
| Restructuring charges, net | (1) | 8 | |
| Other: | | | |
| Professional services | 79 | 81 | (2) |
| Amortization of other intangible assets | 53 | 51 | 4 |
| Securities processing costs (recoveries) | 5 | (1) | |
| Regulator fees and assessments | 15 | 15 | |
| Other | 92 | 113 | (19) |
| Total other | 244 | 259 | (6) |
| Total expenses | $1,826 | $1,835 | — |
| Number of employees at period-end | 29,500 | 29,800 | |

Expenses from Operations

Total expenses in the first quarter of 2013 were flat compared to the first quarter of 2012. Compensation and employee benefits expenses declined 3% in the same comparison, primarily as a result of lower employee levels and the related impact of savings associated with the Business Operations and Information Technology Transformation program. Compensation and employee benefits expenses in the first quarter of 2013 included approximately $23 million of costs related to our continuing implementation of the Business Operations and Information Technology Transformation program, compared to approximately $19 million of such costs in the first quarter of 2012. These costs are not expected to recur subsequent to full implementation of the program.

The increase in information systems and communications expenses in the first quarter of 2013 compared to the first quarter of 2012 was primarily the result of the transition of activities to third-party service providers associated with components of our technology infrastructure and application maintenance and support, as we continued to implement the Business Operations and Information Technology Transformation program.

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

Acquisition Costs

In the first quarter of 2013 and the first quarter of 2012, we incurred acquisition costs of $15 million and $13 million, respectively, related to previously disclosed acquisitions.

Restructuring Charges

In the first quarter of 2013, we recorded a net restructuring credit of $1 million, composed of $8 million of restructuring charges related to the continuing implementation of our Business Operations and Information Technology Transformation program, offset by credits of $9 million related to expense control measures initiated by us in the fourth quarter of 2012. In the first quarter of 2012, we recorded $8 million of restructuring charges, composed of $15 million related to the Business Operations and Information Technology Transformation program, partially offset by a $7 million credit related to expense control measures we initiated in December 2011, specifically our withdrawal from our fixed-income trading initiative.

Information with respect to these initiatives (the Business Operations and Information Technology Transformation program and the 2011 and 2012 expense control measures), including charges, employee reductions and aggregate activity in the related accruals, is provided in the following sections.

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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 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 service providers associated with components of our information technology infrastructure and application maintenance and support. We expect the transfer of core software applications to a private cloud to occur primarily in 2013 and 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 $364 million in our consolidated statement of income, composed of $156 million in 2010, $133 million in 2011, $67 million in 2012 and $8 million in the first quarter of 2013. The following table presents the charges 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 |
| First quarter of 2013 | 9 | — | (1) | 8 |
| Total | $ 226 | $ 78 | $ 60 | $ 364 |

The employee-related costs included severance, benefits and outplacement services. Real estate consolidation costs resulted from actions taken to reduce our occupancy costs through consolidation of leases and properties. Information technology costs included transition fees related to the above-described expansion of our use of 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 was substantially complete at the end of 2011. In addition, in 2011, in connection with the expansion of our use of service providers associated with our information technology infrastructure and application maintenance and support, we identified 530 employees to be involuntarily terminated as their roles were eliminated. In 2012 and in the first quarter of 2013, an additional 164 and 148 positions, respectively, were identified for elimination. As of March 31, 2013, in connection with the planned aggregate staff reduction of 2,242 employees described above, 2,065 of such identified employees had been involuntarily terminated, composed of 550 employees in 2010, 782 employees in 2011, 697 employees in 2012 and 36 employees in the first quarter of 2013.

In connection with the continuing implementation of the program, we achieved approximately $86 million of pre-tax expense savings in 2011, and additional pre-tax expense savings of approximately $112 million in 2012, compared to our 2010 total expenses from operations. As of December 31, 2012, we have achieved total pre-tax expense savings of approximately $198 million since the program's inception in 2010. Additional pre-tax expense savings in 2013 are forecasted to be approximately $220 million.

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 realized in 2015. We expect the business operations transformation component of the program to result in approximately $450 million of these savings, with the majority of these savings expected to be achieved by the end of 2013. In addition, we expect the information technology transformation component of the program to result in approximately $150 million of these savings.

These pre-tax 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. 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 will affect compensation and employee benefits expenses. These savings will be modestly offset by increases in information systems and communications expenses as we implement the program.

2011 Expense Control Measures

In the fourth quarter of 2011, in connection with expense control measures designed to calibrate our expenses to our outlook for our capital markets-facing businesses in 2012, we took two actions. First, we withdrew from our fixed-income trading initiative, in which we traded in fixed-income securities and derivatives as principal with our custody clients and other third-parties that trade in these securities and derivatives. Second, we undertook other targeted staff reductions. As a result of these actions, we recorded aggregate pre-tax restructuring charges of $120 million in 2011 and a net pre-tax credit of $1 million in 2012, in our consolidated statement of income. We did not record any restructuring charges in the first quarter of 2013 related to these expense control measures. The following table presents the charges related to the 2011 expense control measures by type of cost:

| (In millions) | Employee-Related Costs | Fixed-Income Trading Portfolio | Asset and Other Write-Offs | Total |
|---|---|---|---|---|
| 2011 | $ 62 | $ 38 | $ 20 | $ 120 |
| 2012 | 3 | (9) | 5 | (1) |
| First quarter of 2013 | — | — | — | — |
| Total | $ 65 | $ 29 | $ 25 | $ 119 |

The employee-related costs included severance, benefits and outplacement services with respect to both aspects of the expense control measures. In connection with these measures, we identified 442 employees to be involuntarily terminated as their roles were eliminated. As of March 31, 2013, 384 employees had been involuntarily terminated, composed of 15 employees in 2011, 363 employees in 2012 and 6 employees in the first quarter of 2013.

The costs related to the fixed-income trading portfolio resulted primarily from fair-value adjustments to the initiative's trading portfolio related to our decision to withdraw from the initiative. In connection with our withdrawal, in 2012, we wound down that initiative's remaining trading portfolio. Costs for asset and other write-offs were related to asset write-downs and contract terminations.

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 recorded aggregate pre-tax restructuring charges of $133 million in 2012 and a net pre-tax credit of $9 million in the first quarter of 2013, in our consolidated statement of income. The following table presents the charges related to the 2012 expense control measures by type of cost:

| (In millions) | Employee-Related Costs | Asset and Other Write-Offs | Total |
|---|---|---|---|
| 2012 | $ 129 | $ 4 | $ 133 |
| First quarter of 2013 | (9) | — | (9) |
| Total | $ 120 | $ 4 | $ 124 |

The employee-related costs included severance, benefits and outplacement services. In connection with these expense control measures, we identified 630 employees to be involuntarily terminated as their roles are eliminated. As of March 31, 2013, 453 employees had been involuntarily terminated, composed of 40 employees in 2012 and 413 employees in the first quarter of 2013. Costs for asset and other write-offs were related to contract terminations. The credit recorded in the first quarter of 2013 was related to adjustments to severance and benefits-related charges recorded in 2012.

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

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 the 2011 and 2012 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 |
| Net 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 | 9 | — | (1) | — | — | 8 |
| Adjustments of accruals for 2012 expense control measures | (9) | — | — | — | — | (9) |
| Payments and adjustments | (44) | (6) | (4) | — | (3) | (57) |
| Balance as of March 31, 2013 | $151 | $43 | $— | $— | $10 | $204 |

INCOME TAX EXPENSE

Income tax expense was $145 million in the first quarter of 2013 compared to $159 million in the first quarter of 2012. Our effective tax rate in the first quarter of 2013 was 23.8% compared to 27.2% in the same period in 2012, with the decline primarily associated with an increase in renewable energy investments in 2013.

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 15 to the consolidated financial statements included in this Form 10-Q.

The following is a summary of our line of business results for the periods indicated. The “Other” columns for 2013 and 2012 included net acquisition and restructuring costs. The “Other” column for 2012 also included provisions for litigation exposure. The amounts in the “Other” columns were not allocated to State Street's business lines. Results for 2012 reflect reclassifications, for comparative purposes, related to management changes in methodology associated with funds transfer pricing and expense allocation reflected in results for 2013.

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

| | Quarters Ended March 31, | | | | | | | |
|---|---|---|---|---|---|---|---|---|
| | Investment Servicing | | Investment Management | | Other | | Total | |
| (Dollars in millions, except where otherwise noted) | 2013 | 2012 | 2013 | 2012 | 2013 | 2012 | 2013 | 2012 |
| Fee revenue: | | | | | | | | |
| Servicing fees | $1,175 | $1,078 | $— | $— | $— | $— | $1,175 | $1,078 |
| Management fees | — | — | 263 | 236 | — | — | 263 | 236 |
| Trading services | 281 | 280 | — | — | — | — | 281 | 280 |
| Securities finance | 69 | 88 | 9 | 9 | — | — | 78 | 97 |
| Processing fees and other | 31 | 60 | 29 | 34 | — | — | 60 | 94 |
| Total fee revenue | 1,556 | 1,506 | 301 | 279 | — | — | 1,857 | 1,785 |
| Net interest revenue | 557 | 605 | 19 | 20 | — | — | 576 | 625 |
| Gains related to investment securities, net | 2 | 11 | — | — | — | — | 2 | 11 |
| Total revenue | 2,115 | 2,122 | 320 | 299 | — | — | 2,435 | 2,421 |
| Expenses from operations | 1,586 | 1,566 | 226 | 233 | — | — | 1,812 | 1,799 |
| Acquisition and restructuring costs, net | — | — | — | — | 14 | 21 | 14 | 21 |
| Provisions for litigation exposure | — | — | — | — | — | 15 | — | 15 |
| Total expenses | 1,586 | 1,566 | 226 | 233 | 14 | 36 | 1,826 | 1,835 |
| Income before income tax expense | $529 | $556 | $94 | $66 | $(14) | $(36) | $609 | $586 |
| Pre-tax margin | 25% | 26% | 29% | 22% | | | 25% | 24% |
| Average assets (in billions) | $204.4 | $184.3 | $3.9 | $3.9 | | | $208.3 | $188.2 |

Investment Servicing

Total revenue in the first quarter of 2013 was flat compared to the first quarter of 2012, while total fee revenue increased 3% in the same comparison. The increase in total fee revenue generally resulted from increases in servicing fees, partly offset by decreases in processing fees and other revenue and securities finance revenue.

Servicing fees in the first quarter of 2013 increased 9% compared to the first quarter of 2012. The increase primarily resulted from the impact of stronger global equity markets and the impact of net new business installed on current-period revenue, as well as the addition of revenue from the October 2012 GSAS acquisition.

The decline in processing fees and other revenue compared to the first quarter of 2012 was mainly due to the positive fair-value adjustments of $24 million recorded in the first quarter of 2012 related to our withdrawal from our fixed-income trading initiative. Securities finance revenue decreased 22% as a result of lower spreads and lower lending volumes.

Servicing fees, trading services revenue and gains related to investment securities, net, for our Investment Servicing business line are identical to the respective consolidated results. Refer to “Servicing Fees,” “Trading Services” 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 securities finance revenue and processing fees and other revenue is provided under “Securities Finance” and “Processing Fees and Other” in “Total Revenue.”

Net interest revenue in the first quarter of 2013 declined 8% compared to the first quarter of 2012, generally the result of lower yields on earning assets related to lower global market rates and repricing on floating-rate investment securities, partly offset by lower funding costs. Yields on the investment portfolio were also affected by the reinvestment of pay-downs and other runoff into lower-yielding securities. The decrease was partially offset by the impacts of growth in the investment portfolio, lower funding costs, and higher levels of client deposits invested with the Federal Reserve, the ECB and other non-U.S. central banks.

Total expenses from operations increased 1% in the first quarter of 2013 compared to the first quarter of 2012. Information systems and communications expenses increased, primarily the result of the transition of activities to third-party service providers associated with components of our technology infrastructure and application maintenance and support. Also contributing to the increase in information systems and communications expenses were costs incurred to support business growth and the addition of expenses from the acquired GSAS business. These increases were partly offset by the effect of declines in staffing levels on employee compensation and benefits expenses.

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Investment Management
Total revenue in the first quarter of 2013 increased 7% compared to the first quarter of 2012, mainly the result of an increase in management fees, partly offset by a decline in processing fees and other revenue.
Management fees increased 11% in the first quarter of 2013 compared to the first quarter of 2012, primarily the result of stronger equity market valuations and the impact of net new business installed on current-period revenue. 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.

## FINANCIAL CONDITION
The structure of our consolidated statement of condition is primarily driven by the liabilities generated by our Investment Servicing and Investment Management lines of business. Our clients' needs and our operating objectives determine balance sheet volume, mix and currency denomination. As our clients execute their worldwide cash management and investment activities, they utilize short-term investments and deposits that constitute the majority of our liabilities. These liabilities are generally in the form of non-interest-bearing demand deposits; interest-bearing transaction account deposits, which are denominated in a variety of currencies; and repurchase agreements, which generally serve as short-term investment alternatives for our clients.
Deposits and other liabilities generated by client activities are invested in assets that generally match the liquidity and interest-rate characteristics of the liabilities, although the weighted-average maturities of our assets are significantly longer than the contractual maturities of our liabilities. Our assets consist primarily of securities held in our available-for-sale or held-to-maturity portfolios and short-duration financial instruments, such as interest-bearing deposits and securities purchased under resale agreements. The actual mix of assets is determined by the characteristics of the client liabilities and our desire to maintain a well-diversified portfolio of high-quality assets.
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 quarters ended March 31, 2013 and 2012. 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)

| Quarters Ended March 31, (In millions) | 2013 Average Balance | 2012 Average Balance |
|---|---|---|
| Assets: | | |
| Interest-bearing deposits with banks | $30,586 | $25,561 |
| Securities purchased under resale agreements | 5,649 | 7,485 |
| Trading account assets | 728 | 719 |
| Investment securities | 119,601 | 109,740 |
| Loans and leases | 12,737 | 10,762 |
| Other interest-earning assets | 9,023 | 6,937 |
| Total interest-earning assets | 178,324 | 161,204 |
| Cash and due from banks | 3,984 | 2,245 |
| Other noninterest-earning assets | 25,957 | 24,729 |
| Total assets | $208,265 | $188,178 |
| Liabilities and shareholders' equity: | | |
| Interest-bearing deposits: | | |
| U.S. | $13,398 | $2,455 |
| Non-U.S. | 99,720 | 87,029 |
| Total interest-bearing deposits | 113,118 | 89,484 |
| Securities sold under repurchase agreements | 7,839 | 7,439 |
| Federal funds purchased | 363 | 808 |
| Other short-term borrowings | 4,640 | 4,673 |
| Long-term debt | 7,400 | 8,141 |
| Other interest-bearing liabilities | 6,496 | 6,855 |
| Total interest-bearing liabilities | 139,856 | 117,400 |
| Noninterest-bearing deposits | 34,061 | 37,005 |
| Other noninterest-bearing liabilities | 13,509 | 13,991 |
| Preferred shareholders' equity | 489 | 500 |
| Common shareholders' equity | 20,350 | 19,282 |
| Total liabilities and shareholders' equity | $208,265 | $188,178 |

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

Investment Securities

The following table presents the carrying values of investment securities by type as of the dates indicated:

| (In millions) | March 31, 2013 | December 31, 2012 |
|---|---|---|
| Available for sale: | | |
| U.S. Treasury and federal agencies: | | |
| Direct obligations | $804 | $841 |
| Mortgage-backed securities | 28,745 | 32,212 |
| Asset-backed securities: | | |
| Student loans(1) | 15,666 | 16,421 |
| Credit cards | 9,668 | 9,986 |
| Sub-prime | 1,385 | 1,399 |
| Other | 4,460 | 4,677 |
| Total asset-backed securities | 31,179 | 32,483 |
| Non-U.S. debt securities: | | |
| Mortgage-backed securities | 10,895 | 11,405 |
| Asset-backed securities | 5,748 | 6,218 |
| Government securities | 2,961 | 3,199 |
| Other | 4,371 | 4,306 |
| Total non-U.S. debt securities | 23,975 | 25,128 |
| State and political subdivisions | 7,600 | 7,551 |
| Collateralized mortgage obligations | 4,828 | 4,954 |
| Other U.S. debt securities | 5,307 | 5,298 |
| U.S. equity securities | 138 | 112 |
| Non-U.S. equity securities | 2 | 1 |
| Money-market mutual funds | 1,258 | 1,102 |
| Total | $103,836 | $109,682 |
| Held to Maturity: | | |
| U.S. Treasury and federal agencies: | | |
| Direct obligations | $5,000 | $5,000 |
| Mortgage-backed securities | 131 | 153 |
| Asset-backed securities: | | |
| Student loans(1) | 511 | — |
| Credit cards | 25 | — |
| Other | 722 | 16 |
| Total asset-backed securities | 1,258 | 16 |
| Non-U.S. debt securities: | | |
| Mortgage-backed securities | 3,617 | 3,122 |
| Asset-backed securities | 822 | 434 |
| Government securities | 15 | |