

18-Oct-2018

E*TRADE Financial Corp. (ETFC)

Q3 2018 Earnings Call

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Karl A. Roessner

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

Rodger A. Lawson

Executive Chairman, E*TRADE Financial Corp.

Michael A. Pizzi

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

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MANAGEMENT DISCUSSION SECTION

Operator: Good evening, and thank you for joining E*TRADE's Third Quarter 2018 Conference Call. Joining the call today are Chief Executive Officer, Karl Roessner; Executive Chairman of the Board, Rodger Lawson; and Chief Operating 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, financial targets and growth expectations, strategic business initiatives, plans concerning capital deployment and outlook on the broader economic environment, 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 the Form 10-Ks and 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 of 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 October 18, 2018. 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 the call are authorized or may be relied upon.

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

Karl A. Roessner

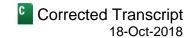
Chief Executive Officer & Director, E*TRADE Financial Corp.

Thanks, Christopher. Good evening, and thank you for joining our third quarter call. In September of 2016, we began a new journey at E*TRADE, a journey defined by a call to accelerate growth and to return to our roots as the undisputed leader for digitally inclined traders and investors. Over the course of the last two years, we've made exceptional progress on this journey, and we've created enormous value for our shareholders along the way. We've truly positioned the company for continued success and for sustainable long-term value creation. On behalf of E*TRADE leadership team, I look forward to expanding on these statements in more detail, but will begin with an overview of tonight's call.

First, our Executive Chairman, Rodger Lawson, will walk you through the board's assessment of our performance and the impact of that assessment on the company's future. Next, I will provide my thoughts on our progress and my team's vision for the future of E*TRADE. Finally, Mike Pizzi will follow with an update on our capital allocation plans and summarize our Q3 results, then we will commence our customary Q&A.

In addition to our earnings press release, we have included supplementary pages in our investor presentation which highlights several of the key elements we will cover on the call this evening. It has been a very exciting and

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fulfilling two years, and it is a pleasure to turn the page on this chapter in such a positive fashion, and I look forward to sharing our vision for the future.

With that, I'll hand the call over to our Executive Chairman, Rodger Lawson.

Rodger A. Lawson

Executive Chairman, E*TRADE Financial Corp.

Thank you, Karl, and good evening, everyone. In the autumn of 2016, having announced the acquisition of OptionsHouse, the board set out a series of business driver-related performance goals to serve as proofs that we could reinvigorate growth, improve operating leverage, and install a deeper sense of urgency in our ranks. As a board, we wanted confirmation that E*TRADE had a bona fide long-term growth trajectory and could keep delivering meaningful value for our shareholders over time. As many of you know, we also expressed that if we couldn't achieve those goals over a reasonable period of time, which we outlined as 18 to 24 months, we would consider other strategic options to protect and enhance shareholder value, including a merger or even a sale of the company.

Two years on, the company has clearly reinvigorated its growth and delivered outstanding returns. While the specific driver goals we set represent only one aspect of the company's strong performance, we are pleased with having outperformed on three of the four benchmarks we laid out. The area where we have fallen short is net new asset growth, which has certainly improved, but has lagged initial targets. We do recognize however that this shortfall is substantially due to our historical lack of an institutional custody capability. Our acquisition and successful integration of TCA is quickly addressing some of that legacy gap, and Karl will talk more about why we are so optimistic about that opportunity.

During the two-year period, the board has evaluated E*TRADE not only against the four 2016 growth goals, which has served as a guidepost for managing top line growth, but also against other important dimensions of performance, including earnings growth, ROE expansion and shareholder value creation, all of which have exceeded our expectations.

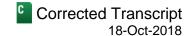
Here are a few of the comments we have noted during this period: The company has meaningfully elevated its offerings for derivative-engaged traders, above and beyond the capabilities we acquired with OptionsHouse. This has attracted more profitable trading activity and created a more resilient user base. We have seen the company's ability to grow its stock plan channel with a record increase in the number of new client wins. This is a critical growth engine for us as we look to our future.

The team successfully integrated two acquisitions, which have significantly expanded our capabilities and reach both for the present, but also for the future. Management has consistently demonstrated an ability to quickly react to a very competitive market landscape, while still expanding our share across our most profitable segments. There has also been great focus on operating discipline as well as revenue growth, both of which are reflected in the expansion of E*TRADE's operating margin.

Overall, therefore, whether looking broadly across E*TRADE or at the specific business driver goals, the board is very pleased with the evolution and progress of the company over the past few years. It's really been terrific. We are also very pleased with the total shareholder returns over that period, during which we have significantly outpaced the performance of the market, the sector, and our direct peers.

We have, however, also been very focused not just on the past, but also growth prospects for the future. We believe this is critical to selecting the best path forward for E*TRADE and its shareholders. In looking at our future

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prospects, we have considered and placed substantial weight on the following areas: First, management's long-term strategic plan. The board's assessment of this multi-year plan is that it is positive and not unreasonably optimistic. It is a sound and credible plan and should generate material value growth for E*TRADE. Second, the board believes, after receiving analysis and advice from our third-party advisors, that with good execution of management's plan, there is material shareholder value upside in E*TRADE's future, which is more compelling than what we believe would be generated from any likely near-term transaction.

Critical elements in the assessment of management's multi-year plan are as follows: First, with approximately 6 million accounts and approaching \$0.5 trillion in assets, the company has built significant scale across our areas of business. Beyond the current value profile of this base of customers and assets, we see meaningful potential to expand our products, and therefore our engagement across this group, which can drive substantial increases in value with just modest improvements. With the pending acquisition of roughly 1 million accounts from Cap One, this potential will only expand.

E*TRADE's position in our core trading segment has improved materially, and as a result, we believe we will continue to participate proportionally in any growth of trading activity in the U.S. We are confident with these growth expectations even considering the potential for future price competition for other industry players. As part of that perspective, as we look out over the five-year time horizon, we do not expect the trading tree to grow to the sky, and we do recognize that markets can go down as well as up.

Additionally, we have significant confidence that we will continue to evolve and grow our presence in the stock plan business. Our capabilities and market share under E*TRADE Corporate Services remain industry-leading, and we have every intention of maintaining that status. Karl and Mike will shed more light in the importance of, and contribution made by, this business in their prepared comments in a moment. Further, we believe the acquisition of TCA provides a sound foundation to influence our growth rates both because of the quality of the custodial platform as well as our ability to expand relative to our existing total asset base.

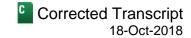
We expect the nature of our business model will evolve over the next few years as we enhance our capabilities in wealth management, both directly and indirectly. When taken with the opportunity to expand the services we offer through transactional banking services, like securities-based lending, savings offerings, and digital payment solutions, we expect the evolved suite of E*TRADE's offerings to be extremely competitive.

We also believe that our progress in the RIA space, robo-advisory and money management will enable us to increase our retention rate on Corporate Services proceeds which has been stable around 15% for some time. We think the historical absence of clear investment choices for plan participants, whether self-directed or advised, has restricted our ability to retain more Corporate Services assets, and the broadening of our capabilities will allow us to engage more deeply with these customers.

Last but by no means least, we are obviously pleased with E*TRADE's ability, both currently and prospectively, to generate excess capital. As a board and a management team, it will be our intention to continue to return that capital to our shareholders. Simply put, if we can't use it, we will not sit on it. We have already demonstrated our commitment to return capital to shareholders by our prior stock buybacks, and today, Karl and Mike will lay out our forthcoming capital management and return plans.

With the confidence we've taken from our assessment of the company's future growth plans, as well as the quality of management's execution, the board's expectations for E*TRADE's future growth are high. During our five-year planning horizon, we expect to see mid-teens growth in earnings per share, aided in part by an expansion of our operating margin, and also a return on equity of 20% or better. With this performance expectation, the board's

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current view therefore is that we do not believe initiating a sale process is the best path for value creation for our shareholders.

I would, however, add the following comments. First, we have no illusions of what our fiduciary responsibilities are when it comes to assessing the performance and prospects of the company we govern and the options that may be available to us over the course of time. The board will not waiver in taking any steps to protect value for our shareholders. As I have said in the past, we want to grow shareholder value, not lose it.

And second, we remain conscious of the fact that, as the smallest player in a highly competitive environment, we have little wiggle room for failure. We don't see that situation changing. We must, for the foreseeable future, continue to deliver an outsized impact through an unyielding focus on efficient execution. Finally, as we look to the future, there are, of course, many material metrics which are relevant to us, and I have little doubt we will be focused on them all. However, over our five-year planning horizon, the board will be most focused on EPS growth, as well as ROE expansion as our major common denominator metrics to assess whether we are succeeding or not.

With that, I will pass the commentary back to Karl.

Karl A. Roessner

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

Thank you, Rodger. It's been a long road, and I am incredibly proud of our team. We revitalized our product set. We put our brand back on the map. We reclaimed our mantle as the home for active traders. And we worked tirelessly to make sure that our foundation, from our risk framework to our operations and technology capabilities, is sound.

Over the past 24 months, we have delivered meaningful financial growth including over 20% compounded annual growth in revenues, a 30% CAGR in earnings per share, and a remarkable 40% annualized growth in adjusted pre-tax income. We grew our balance sheet by 32%, expanded our adjusted operating margin by 1,100 basis points, and improved our ROE by 900 basis points, while returning over \$1 billion to shareholders through stock repurchases.

We accomplished this by delivering exceptional business growth and integrating a meaningful acquisition in OptionsHouse, which together allowed us to capitalize on a favorable market environment. We are also setting ourselves up for the future with the closing of TCA in April and the upcoming acquisition of nearly 1 million accounts from Capital One, which is on track to close in the fourth quarter.

To this end, we have improved our trailing 12-month DARTs to more than 260,000, up 73% from the pace of 24 months ago, driven by a greater number of accounts and an increase in activity per account which grew from 12 to 18 trades. We more than doubled our derivatives DARTs from 38,000 in Q3 2016 to 86,000 in this most recent quarter. We improved our organic net new brokerage assets from \$9 billion to more than \$14 billion during the trailing 12-month period. We more than doubled our pace of account growth from 88,000 in the 12 months ended in September 2016 to 215,000 over the past 12 months. And we grew our highest value accounts at more than double the rate of our total account growth.

We have attracted net flows of 51% on our Q3 2016 managed asset balance, scaling from \$3.7 billion to more than \$6 billion. We enjoyed this success off a low base, which gives us confidence in our ability to continue scaling managed assets over time given our improved capabilities to serve long-term investors. We onboarded more than \$26 billion of new Corporate Services stock plan assets from new clients since Q3 of 2016. This is

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more than double the amount we brought in over the preceding 24-month period. We added \$135 billion in gross new assets from existing Corporate Services clients. None of this could have happened without a tremendous team effort.

Over the last two years, we acquired OptionsHouse and successfully integrated it within our platform with earnings synergies this year running approximately \$0.10 per share higher than what we originally communicated. We acquired TCA. We launched Power E*TRADE. We reinvigorated our brand with an irreverent new advertising campaign. We significantly upgraded our website and enhanced our active trading suite with truly differentiated enhancements.

We were rated the #1 Mobile Trading, Options Trading and Web Based Platform in the most recent StockBrokers.com survey. We achieved the #1 Loyalty and Overall Satisfaction rating for our stock plan platform Equity Edge Online for the seventh straight year. We deftly responded to competitive pricing by setting up a tiered offering, thereby retaining our most valuable active customers.

We reinforced our best-in-class risk organization and continued improving the company's overall risk profile, allowing us to reduce our bank and consolidated capital thresholds by 100 basis points and 50 basis points, respectively, freeing up approximately \$700 million in capital. We refinanced over \$1.4 billion of debt and TRUPs, yielding annual savings of approximately \$20 million. We exhibited notable expense discipline, confining expense increases to under half of our revenue growth, and this represents only a partial list of our accomplishments.

As most of you are aware, I never tire of discussing our Corporate Services stock plan channel, which is the real differentiator for our franchise. In addition to being a tremendous feeder channel of accounts and assets, the cash profile of our Corporate Services related customers is significantly better than that of our other customers, and thus delivers an outsized contribution to net interest income and to earnings. Over the last two years, Corporate Services related assets have grown by 30% more than assets in other retail accounts.

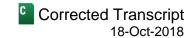
And as of the end of the third quarter, Corporate Services related cash contributed 35% of all customer cash balances. As most of you understand, our Corporate Services channel serves as a funnel to our broader brokerage business, as stock grants turn into vested shares which translate to cash proceeds as well as to engagement with our broader suite of offerings. Due to the extraordinary success of our Corporate Services team, the volume of assets that has entered that funnel has never been greater than it is today.

If we consider the sum of the unvested, unexercised and vested but yet to be transacted stock plan shares, the opportunity set of stock plan assets has increased from approximately \$150 billion in Q3 of 2016 to \$260 billion today. Not only do we expect this to aid future net new asset flows, but it should disproportionately contribute to growth in cash deposits. Finally, with the addition of institutional custody services in concert with our focus on delivering an exceptionally easy to use digital wealth offering, we believe the opportunity to engage more deeply with these stock plan customers will expand significantly.

Needless to say, as we endeavor to retain more proceeds, each percentage point increase on a \$260 billion base contributes meaningfully to net new assets. While we're incredibly proud of our accomplishments, we're not resting on past results, and we're exceedingly focused on adapting our model to position E*TRADE for where the market is headed.

The self-directed trader will always be core to our strategy and we will continue to deliver exceptional product and a truly differentiated service experience for our most discerning and engaged customers. With that said, we must focus our energy on competing more effectively in the digital wealth space. We've also been hard at work building

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out our capabilities to serve a range of investor needs, including meaningfully expanding our list of no-transactionfee mutual funds and ETFs, enhancing our financial consultant powered offerings for those clients who continue to prioritize human touch, and re-launching our best-in-class robo solution, our core portfolios.

These new capabilities have enabled us to surpass our \$6 billion managed assets goal without material advertising focus. We know that this will be the fastest growing segment of the wealth management market and we fully intend to align the power of our brand and our capabilities against this opportunity, as this segment of the market continues to take flight.

By incorporating TCA by E*TRADE, we're expanding our footprint into the RIA segment which will broaden our addressable market and serve as a critical retention tool for brokerage and stock plan accounts in search of higher-touch services. While this addition provides us a foothold in a new market, plugging it into E*TRADE makes the platform considerably stronger. Adding the E*TRADE moniker to the platform is already bearing fruit, adding \$1 billion in custodial assets since April. We see this as an added tool for our financial consultants in meeting our clients' investing needs, while also creating meaningful opportunities for the RIAs that we add to the program.

In that vein, we are thrilled to announce the addition of Edelman Financial Services, an industry stalwart to our platform and aim to connect their advisors to our national referral program launching in the coming weeks. Through this arrangement, client assets from one of the preeminent advisors in the country will be custodied with E*TRADE, while our referral network will provide E*TRADE's financial consultants with a channel to connect clients in need of higher-touch services with RIAs on our platform.

Since we announced the acquisition a year ago, TCA has more than \$12 billion in commitments and we're only just getting started. Just to contextualize that number, at the time we announced the acquisition, TCA had \$17 billion in assets under custody. So, it should go without saying that this growth engine has been ignited in a very real way.

With a solid foundation, we look forward to delivering on concrete financial objectives. First, we are targeting sustainable mid-teens EPS growth for the next five years, amounting to an approximate doubling of our earnings power by 2023. Second, we plan to expand our operating margin from its current 48% level to 50% in 2020 and drive toward a mid-50s level by 2023. Third, we look to expand our ROE from the current level of approximately 16% to beyond 20%. And fourth, we plan to achieve these targets while also returning meaningful capital to shareholders via dividends and buybacks beginning immediately with another \$1 billion repurchase program and our initiation of a \$0.14 quarterly dividend.

Mr. Pizzi will provide additional details on our capital plans. Before I turn the call over to Mike, I want to congratulate him on his recent promotion and the expansion of his role to include the COO title. Mike is an E*TRADE success story progressing during his 15-year tenure from portfolio management to bank Treasurer to Corporate Treasurer to Chief Risk Officer and more recently to Chief Financial Officer. This elevated role is a natural extension of Mike's position and I am confident it will result in great things for this organization and for our shareholders.

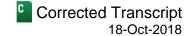
With that, I'd like to turn the call over to our COO and CFO, Mike Pizzi.

Michael A. Pizzi

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



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Thanks, Karl. It's been incredibly fulfilling to build my career at E*TRADE and it is a privilege to help lead this great company into the future. Now, let me begin by discussing our growth objectives in more detail and then I will lay out our capital priorities and then briefly cover Q3 results. First, on our growth objectives, we are advancing from a set of goals that were narrowly defined by business metrics to broader financial targets such as earnings growth, return on equity and capital allocation, which are more directly aligned to delivering value for shareholders. To meet these financial targets, we must flexibly react to the competitive and economic environment and pull on different levers to deliver earnings growth.

With that as a context, I would like to dive into the targets that Rodger and Karl set out. First, we plan to maintain an operating margin above 50% which we expect to reach by 2020. In a stable environment, we expect to expand this to mid-50s level by 2023. Over the last several years, we've grounded our budgeting in an operating margin framework that transparently commits to balance top line growth with expense discipline. This framework ensures that we are judicious on expense growth in favorable market environments and that we are disciplined on spending during more challenging revenue periods. Under this framework, we anticipate growing revenues 350 to 400 basis points faster than expenses, which should lead to the steady and sustainable margin expansion.

Next, we are targeting mid-teens EPS growth. We're more than doubling of our EPS to a greater than \$7 by 2023. Our target for earnings growth is not based on blind optimism. We anticipate achieving double-digit growth in pretax income with approximately two-thirds coming from revenue growth and one-third from margin expansion. We also plan to continue repurchasing our stock which will contribute to our EPS growth over the five-year period. In terms of the inputs underlying this multi-year plan, we assume a few more Fed rate hikes, including two in 2019 and one the following year. We assume continued strong engagement by our customers, but expect a far more moderate pace of DART and margin growth compared to the rapid expansion we saw this year.

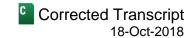
Our model assumes that brokerage cash levels remain relatively in line with the current rate of approximately 13% of brokerage customer assets. Should cash levels moderate back to historical norms higher than 15%, we also expect a commensurate softening of DART activity and customer margin growth. Finally, our model assumes modest contraction within commission portrayed, as competitive trends point to continued pricing pressure by others in the industry. This should be partially offset by a greater share of derivative trading on our platform.

The earnings growth modeled in our plan and the drivers I just covered are presented on slide 34 of the investor presentation. The earnings improvement in our plan comes primarily from consistent sweep deposit growth among our core brokerage and stock plan customers and from the tremendous scale benefits we realize on each new incremental dollar of revenue. We believe it is prudent to exercise conservatism on our modeling, and therefore assign relatively modest growth to some of our emerging platforms. That does not diminish our optimism about the potential in these areas or our excitement about the strong foundations we have in place.

From our digital wealth offerings to our institutional custody services, we have truly differentiated solutions that will deepen engagement, improve retention and expand the wallet share among our existing brokerage and stock plan customers. Through these growth vectors, we also see substantial opportunity to broaden our reach into new households. Success on these fronts could drive meaningful upside to the greater than \$7 EPS target we laid out today.

As for capital plans, our business generates tremendous excess capital that creates capacity to balance reinvestment in the business with distribution to shareholders. Over the last two years, we had the unique opportunity to onboard nearly \$9 billion in off-balance sheet deposits which caused us to retain capital. Despite the growth in our capital base, we recently completed our \$1 billion repurchase authorization more than three months ahead of plan.

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We expect to generate even more excess capital going forward given our earnings run rate is considerably higher than a couple of years ago and that the onboarding of the third party deposits is now complete. With that backdrop and in consideration to the relative cheapness of our shares, we will be opportunistic in the pacing of our new \$1 billion share buyback program with the ability to complete up to half during the fourth quarter of this year. We intend to complete the program by the end of 2019.

With respect to the initiation of a dividend to common shareholders, we are launching a payment of \$0.14 payable on November 15. While we anticipate our capital allocation will remain skewed towards share buybacks given that they have forward tactical flexibility, the initiation of the company's first common dividend program running in parallel provides us with ample avenues to efficiently return capital to shareholders.

Taken together, this should speak to not only the quantum of excess capital generation, but also as a testament to the predictability and stability of our earnings going forward. We hope and expect this would make E*TRADE more appealing to a broader population of investors. This capital plan implies a payout in the 80% to 90% range, which we believe is appropriate considering our targets for double-digit earnings growth. We believe it is sustainable considering our improving capital efficiency and strong operating leverage. And we can always pause share repurchases to the extent that we find compelling in organic growth opportunities.

Putting our earnings growth and capital objectives together, we plan to expand our ROE from its current 16% level on an adjusted basis to beyond 20% by 2023. An emphasis on ROE demands that we remain disciplined in how we allocate and return capital. We will always be focused on growing earnings, but if investments do not enhance shareholder value, then we plan to return that capital to its rightful owners, our shareholders.

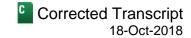
Finally, I would like to briefly cover Q3 results. For the quarter, we reported net income available to common shareholders of \$261 million, or \$1 per diluted share on record net revenues of \$720 million, up \$121 million from the year ago quarter. We had a couple of unique items which benefited pre-tax earnings by \$30 million, including a \$34 million benefit to provision for loan losses and \$5 million in gains related to the sale of our legacy equity investment in the Chicago Stock Exchange. This was partially offset by a \$4 million early extinguishment of debt charge related to the refinancing of our TRUPs and \$4 million in restructuring-related activities.

Our effective tax rate for the quarter included an \$8 million income tax benefit related to the revaluation of our net deferred tax assets. This revaluation typically occurs during Q3 and excluding this benefit, our tax rate was closer to 26%. We expect a full year 2018 tax rate of approximately 26% and a go-forward rate of approximately 27%. As for core results, net interest income increased by \$13 million as our net interest margin expanded by 8 basis points on relatively flat asset balances, driven by the impact of the Fed rate hike, higher average margin balances, and improved securities portfolio performance.

Our average deposit cost, including customer payables, was 18 basis points in Q3, up from 9 basis points last quarter. We expect our blended deposit costs to be 25 basis points in Q4. Following the Fed September rate hike, our average reinvestment rate in the securities portfolio is now in the 300 to 325 basis point range, similar to the prior quarter. For the full year 2018, we are forecasting them to fall within the range of 305 to 310 basis points, assuming customer margin balances remain at current levels.

Commission revenue of \$117 million increased 17% year-over-year, but fell 3% sequentially. DARTs were up modestly, but CPT was down \$0.27, and there were fewer trading days in the quarter. Our CPT of \$7.04 was below our expected range, as heightened equity volumes pressured derivative mix and the average number of contracts per trade and stock plan trades declined. For Q4, we expect commission per trade to fall in the \$7 to

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\$7.05 range. Fees and service charges were mostly flat quarter-over-quarter. The average yield on third party cash was up 5 basis points to 143 basis points in Q3. We anticipate generating roughly 150 basis points on third party cash in Q4.

With respect to expenses, non-interest expense was \$380 million, down \$4 million from the prior quarter. This quarter's adjusted operating margin, which excludes provision benefit and loss on early extinguishment of debt, was 48%, an improvement of 200 basis points from the prior quarter. We expect our full-year 2018 adjusted operating margin to surpass 46%, better than the 45% we commented on last quarter's call, given strong results to date and the benefit of the September rate hike.

One important update to our expense efforts is the run rate savings we recently achieved on the heels of the \$50 billion threshold being lifted with the changes to Dodd-Frank Act. Through some restructuring of our regulatory and enterprise risk managements functions to reflect the current regulatory landscape and the improved risk profile of the company, we have cut \$15 million from our expense base. This savings is embedded in our operating margin assumptions.

A final note on corporate cash, we ended the quarter at \$517 million, down \$426 million sequentially, reflecting the \$413 million redemption of TRUPs, the \$309 million used to repurchase shares, and the \$24 million paid on preferred dividends. This was partly offset by \$322 million of dividends to the parent from the bank and broker. For Q4, we anticipate approximately \$330 million in total dividends to the parent.

And with that, we will open the call for questions.

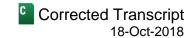
QUESTION AND ANSWER SECTION

Operator: [Operator Instructions] And our first question comes from the line of Steven Chubak with Wolfe Research. Please go ahead.

Steven Chubak Analyst, Wolfe Research LLC	Q
Hey, good evening.	
Karl A. Roessner Chief Executive Officer & Director, E*TRADE Financial Corp.	A
Hi, Steven.	
Steven Chubak Analyst Wolfe Research LLC	Q

So, certainly a lot to unpack here, wanted to ask – just really dig into the five-year earnings target that you guys outlined. And I thought you did a really nice job just speaking to the \$7 earnings walk and most of the assumptions there actually look to be quite reasonable. The two which you're maybe referring to most browsed here are the modest reduction in commission per trade, just given some of the recent developments we've seen on the pricing side, new entrants, price wars, et cetera, as well as the higher cash levels as a percentage of assets. And certainly over the last few years, we've clearly seen that with rising markets and rates that cash levels should continue to grind lower. And just given the long-term earnings walk, I was hoping you could flesh out your

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long-term views on both cash and commission pricing, seeing as those two really appear to be the most contentious.

Karl A. Roessner

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

A

Yeah. So, let me start on the cash side. Looking at sort of the cash levels now, we are down to historic – a level that we haven't seen since going back well over a decade to a pre-crisis environment, roughly at 13% or so of cash per client assets. Looking at that – thinking it'll continue to drop from here, we felt that from a planning perspective, it's best really to hold it flat. Further reductions in cash balances from here will probably mean higher margin balances, higher DART volumes, higher securities lending revenue much similar to the behavior you've seen here today.

Holding it flat then just really gives you the dynamic that we show you in the investor deck that really just has the business generating cash both from the core account growth as well as the Corporate Services unit which we gave some highlights on as to how that helps us generate cash. When we apply that over the five-year period, we get to the cash type balances and balance sheet type levels that are going to drive that earnings power forward to that \$7 type level.

Michael A. Pizzi

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

A

When you look at it on the commissions side, I think when we look at our business model and how we've structured ourselves focused on our active trader set, there is a pretty large mix of derivatives trades in there, our stock plan administration business and the executions that come through that channel. So, there's not a situation where we see a zero commission level. We have obviously stressed this and included some of the pricing pressure that we foresee over the near term and the longer term in the plan, but we don't take it down to zero just given our business model and given where those fees come from.

Steven Chubak

Analyst, Wolfe Research LLC

Got it. That's really helpful. Appreciate the responses on both of those items. So, just the follow-up for me is going to be on the five-year margin target. Your earnings walk assumes that it approaches somewhere in the mid-50s, 55% over time. In the past, some of your large e-broker competitors have actually talked about a peak margin somewhere closer to 50% simply because competitive pressures make it difficult for profitability to really exceed that threshold and go much beyond that level. Just hoping you could speak to some of the factors you see as differentiated in terms of your business mix that will actually enable you to operate somewhere above 50% and closer to 55% on a sustained basis.

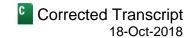
Karl A. Roessner

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

Yeah. I mean, we see it right in kind of the historical performance lifting our sort of operating margin 200 basis points over the past two-year period. We are mainly a digital firm with only 30 branches. It gives us a pretty significant operating leverage base. We focus on using technology smartly to drive that and then sort of the earnings model and how we monetize cash gives us a clear advantage. Without the real estate, with the balance sheet model that we're operating, we think getting to 55% is very realistic.

Operator: And our next question comes from the line of Christian Bolu with Bernstein. Please go ahead.

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Christian Bolu

Analyst, Sanford C. Bernstein & Co. LLC

Good afternoon, Rodger, Karl and Mike. I guess, a quick one for Rodger, maybe bit of a blunt question here. But to the extent there are meaningful cuts in commissions, say, by former Fidelity in the near future, does that change at all the board's calculus around a takeout?

Rodger A. Lawson

Executive Chairman, E*TRADE Financial Corp.

No, I don't think so. I don't think it makes a material difference in the short term even if you believe that. I'm not sure personally I believe that, but I don't think it makes a material difference. I think there are a number of levers which, in fact, Mike has alluded to which we pull in that particular process. Maybe commissions will drop further, but we're getting pretty close to the floor [ph] on all this (00:38:14) commission rates anyway, and the world has changed a great deal. And as I would jokingly say, it's tough to fall off the floor when you get to a certain low position in terms of rates.

So, actually, personally I don't think it would. I think what would – the only thing that would affect our perspective is if there were a series of items that convinced us that we couldn't get to the type of financial performance Mike just described, then I think that would inform the board's decision, we would think about it differently. But at the moment, even changes in prices, and I alluded to that in my prepared comments, we don't anticipate that that's going to make a material difference to our perspective in the foreseeable future.

Christian Bolu

Analyst, Sanford C. Bernstein & Co. LLC

Okay. Thank you. So, Rodger, it feels like you're banking quite a lot here on the Corporate Services business, particularly around the amount of cash that comes out of that business, I think it's fairly meaningful. We have heard a pitch around increase in retention rates for a while, right? And you have had TCA and robos now at least for a couple quarters. Just help us understand, are you actually seeing an increase in retention rates? And can you actually speak to why you think this time is different than we'll see meaningful progress in retention rates over time?

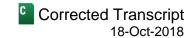
Rodger A. Lawson

Executive Chairman, E*TRADE Financial Corp.

Well, I think I'm the one who's being guilty about talking continuously about upping our retention rates. I seem to remember one of your sell-side colleagues said to me that, hey, Rodger, you've been talking about that since Jesus was a baby. And I think, in fact, to some extent that is the case, but I think the dynamic that — and I think that was introduced in Karl's comments and Mike's comments, is that volume of cash which comes naturally from that Corporate Services business. And even during the last five, six quarters when we all know everyone in the industry has experienced a lot of money moving into the market, cash levels have come down and Mike just talked about that.

The cash levels in the Corporate Services business have either modestly increased or stabilized. So I think Corporate Services, in terms of its value to the institution, has – even with a 15% retention rate at the end of 12 months, is cash value contributor, the company has become more and more significant as we evaluate it. Going forward, if we can move that 15%, I think there are a number of things that we haven't done that we could do. Karl talked about them, Mike talked about them in terms of expanding the kind of products offerings which would encourage people to stay more – to keep more money with E*TRADE.

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I mean, we have a good – in fact, it's hard to believe, but we have a very good investment track record. You'd be hard pressed to find it, you need to be Sherlock Holmes looking through some of the information we have in order to help you do that. But the track record we've generated is very, very good. We just haven't brought it to the fore in a meaningful way. So, I will go back and maybe I'll be accused a year from now in saying, you did that one more year after Jesus was born in terms of when you were talking about it.

But I do think that the cash level contribution rolls in, rolls in every year, and that makes a – and Mike said it, that makes a very significant contribution to what we anticipate will contribute materially to the spread income we see in our five-year growth plan. And spread income is an extremely significant part of it. So, I would say our confidence in the power, particularly with the recent growth of Corporate Services, the cash it's generating, and if that is aided by a further expansion of retention rate, then I think [indiscernible] (00:41:39) growing more strongly.

Karl A. Roessner

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

Yeah. And, Christian, we're really focused on the experience for the end customer here, right, and that's one of the biggest things. There's a focus throughout the organization in our stock plan sort of unit as well as our retail brokerage unit to really focus on the impact we can have on the corporate client coming in and make sure that their service is impeccably delivered. Then the first interaction that that stock plan customer has with us when they go in to accept their award or start their relationship with E*TRADE is as seamless as possible.

And then introducing them to what they can do next and the solutions that we have building out on our digital wealth platform, right, everything from our robo to our pre-built ETF offering that we have now and really concentrating our marketing and our efforts around the dates of those grants, helping these individuals understand, educating them on what's available when they come into new found wealth, that's where the focus comes from and that's where my confidence comes from that we can shift that 15% upwards. On the type of pool that we talked about during the prepared remarks, 1 percentage point move is meaningful. So, that's where we're coming from.

Michael A. Pizzi

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

I would just add, Christian, we grew the pool from \$150 billion to \$260 billion. We have the leading product in the space and are growing quite considerably. Even if the 15% remains, we'll deliver significant value, and that value is what we're reflecting in the plan. We don't make any heroic assumptions about that percentage going up higher to hit the financial targets that we imply.

Karl A. Roessner

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

How's that for a short answer, Christian?

Operator: And our next question comes from the line of Rich Repetto with Sandler O'Neill. Please go ahead.

Richard Henry Repetto

Analyst, Sandler O'Neill & Partners LP

Yeah. Hi. Good evening, Rodger. Good evening, Karl. And good evening, Mike.

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Corrected Transcript
18-Oct-2018

Rodger A. Lawson

Executive Chairman, E*TRADE Financial Corp.

А

Hi, Rich.

Richard Henry Repetto

Analyst, Sandler O'Neill & Partners LP

Q

I guess. How are you doing? I guess, the first question – but thank you, Rodger, for acknowledging, there is the potential for market corrections, recessions, the risk of the zero commissions, you could even see some Fed easing, I guess, over five years. So, I guess, my question is, what discount rate as you're shooting – and I know the opportunities are out there, but what kind of risk or discount rate do you use? If you could help us what would you suggest we use and what's the present value? If you do all this and you measure the risk versus these opportunities, what present value did you all come up with?

Karl A. Roessner

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



Yeah, Rich, I mean, I think that calculating our cost of equity given sort of various measures of beta, the 10-year yield, it should be a pretty straightforward calculation. You're going to land depending on what assumptions you use in sort of a 9% to 10% range, maybe slightly higher, depending on sort of modeled assumptions. I think that that's pretty standard in terms of sort of discounting – in sort of cash flow discounting if you're trying to build some sort of a DCF analysis off what we're modeling.

Rodger A. Lawson

Executive Chairman, E*TRADE Financial Corp.



And, Rich, can I just ask a couple of other comments? I think you and I think Patrick O'Shaughnessy were the two of the individuals that have written relatively comprehensive assessments of what I call revenue yield. And everyone has a different name, but I'll call it revenue because I'm old-fashioned. And I think that it's pretty clear that we...

Richard Henry Repetto

Analyst, Sandler O'Neill & Partners LP



Me too, Rodger.

Rodger A. Lawson

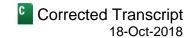
Executive Chairman, E*TRADE Financial Corp.



[ph] I know (00:45:08) who's getting younger, Rich. I think, in fact, what this – I think the revenue yield analysis, this is an important one because the model we have, I think, does deliver higher revenue yield. Now, the point you made, I think, in your last note was, ah, yeah, guys, but can you sustain that with growth? And, of course, it's the right question. We all agree with that's the right question.

I think when the board went through the multi-year plan, I mean – you know many of the member of the board members and I think the reality is, this is not an easy group, it's a demanding group. We went through the plan, we went through it in consummate detail. Actually, I think, as we traversed our five-year plan without – I'll use Mike's comment, without any heroic assumptions around growth in some of the key driver metrics, we still are sustaining a very, very attractive high revenue yield, it clearly contributes to the margins that people were questioning about.

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So, I think as we look forward, yeah, there could be a big market correction. I mean, we'll all suffer with that, although I'm not sure does today count as a big market correction? I guess, you just saw it comes down from \$66 to \$50, if you own the stock, you feel that's a pretty big market correction. So, I think [indiscernible] (00:46:17) we've had a pretty significant market correction in the last few months. But I think it could continue to happen. And if it does, it does. But the essence of our model, I think even if we do see that, I won't say there are natural hedges in everything that we do, but trading comes down, potentially margin comes down, cash goes up, there are many interesting trade-offs.

And as we talked about this with the board, I think we've got ourselves reasonably comfortable, I mean the sky can fall, who knows. But we've got ourselves reasonably comfortable in the fact that this – the kind of numbers that Mike talked about over the five-year horizon are very achievable in most environments. We all lived through 2008, no one knew what most was in 2008, it's a totally different world. But I think we believe even in negative scenarios that our revenue yield will hold up and our ability to deliver the kind of returns we're talking about will hold up. Time will tell, Rich.

Richard Henry Repetto

Analyst, Sandler O'Neill & Partners LP

Q

Yeah. Yeah. And I appreciate the insight. It's great to communicate with you on this. So, I guess the follow-up question would be, I have done the discounting in the time that we had and present value off of a multiple of earnings, but I guess the question is when we compare that, did you all seek out what the market would put on E*TRADE today? Did you actually seek out – I mean get bids or have any interaction like that? And as long as we're on that subject as well and you've been guiding the process, Rodger, just trying to see what your future – I think your employment contract ends at the end of the year, and just want to see whether you'll still be guiding the ship here to the five year and \$7 of earnings.

Rodger A. Lawson

Executive Chairman, E*TRADE Financial Corp.



Rich, let me start with the last one. When we had the – I think – I've come – we went to the Barclay (sic) [Barclays] conference after we had the management changes in 2016 because we figured it was best to get out there and explain what the hell we were doing. At that time, I think I talked about the fact that as we've made the changes, well, I rationalized why we had confidence in Karl, why we had confidence in Mike. I also explained the fact the board had asked me if for two years I would be Executive Chairman, so I moved from being Non-Executive Chairman and the life of luxury to becoming Executive Chairman which is what I did. So, now we're into day-to-day life.

I think frankly since then, we've had our ups and downs, a lot of things have been happening. But I think we feel comfortable, I thought I know if you're comfortable that things are moving in the right direction. I think the need for an Executive Chairman certainly at this period of time has been removed. So, we will be sticking to the original plan we discussed. I will step down at the end of this year, into the end of December, and I will revert back to being Non-Executive Chairman, so I'll no longer be part of management, Rich. I will revert back to being a member of the board. But bearing in mind, I'll be back to the stage as I was just before we made the changes we made the last time. And Karl?

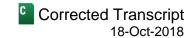
Karl A. Roessner

 ${\it Chief Executive Officer \& Director, E*TRADE Financial Corp.}$



And, Rich, on the question about whether or not we did a market check, we went out to third parties, that wasn't something that the board pursued in its evaluation. But please keep in mind that we had a large investment bank

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come in and do the assessment for us and that assessment obviously included all of the current market information, ability, capacity to pay, I mean, you name it and go through it. The board looked at it. It's a very fully informed board. They had the right legal counsel, they had the right banks here and they did what they needed to do to get themselves comfortable with the value creation that this management team believes that it can deliver over a period of time versus what could hypothetically be out there in the marketplace.

Rodger A. Lawson

Executive Chairman, E*TRADE Financial Corp.

A

And to just confirm what Karl is saying and what Mike said earlier, we are well informed. We didn't come in one day and toss the coin. This was a lot of work which was done to get into this position. And so there were no hockey sticks in this plan. There were no ridiculous aspirational goals which can never be fulfilled. So, it was a very, very serious consideration. And I mean the bottom line of it is, the comments which we made in the prepared statements, we clearly felt that this was where we are at the moment is a better path forward than the alternative which I know a lot of other people speculated about.

Operator: And our next question comes from the line of Chris Harris with Wells Fargo. Please go ahead.

Christopher Harris

Analyst, Wells Fargo Securities LLC

Thanks. Hey, guys.

Rodger A. Lawson

Executive Chairman, E*TRADE Financial Corp.

A

Chris.

Christopher Harris



Analyst, Wells Fargo Securities LLC

So, deposit growth and balance sheet growth is a clear challenge for everyone in the industry right now. I know the puts and takes in your operating model here. And I just wanted to ask you guys directly if we assume that the balance sheet kind of stays flat, do you still think you can hit your mid-teens EPS growth target under that scenario?

Karl A. Roessner

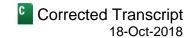


Chief Executive Officer & Director, E*TRADE Financial Corp.

Chris, let me answer the question this way. If you look at sort of the puts and takes of the sort of the current balance sheet, we are in another record year of customer net buying. So, it'll be two subsequent years of very high levels of customer net buy. That should, in theory, drive your cash balances down. We're holding relatively flat. That flatness is caused by the dynamics of our business in terms of growth in terms of Corporate Services.

So, if you're saying the environment is to see a continual market environment where we see this level of engagement and this level of interest, then what we're going to see is sort of higher DART volumes, higher margin balances as really offsets to lower cash growth, and that's exactly what you've seen in the current year. We have to look at that scenario, but I would feel really good about the value that that scenario would deliver over the same five years.

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Christopher Harris

Analyst, Wells Fargo Securities LLC

Okay. Thank you.

Operator: And our next question comes from the line of Kyle Voigt with KBW. Please go ahead.

Kyle Voigt

Analyst, Keefe, Bruyette & Woods, Inc.

Hi. Good evening. Just another question on the 50% operating margin target by 2020, just wondering in a scenario where pricing may come under more pressure than you anticipate, do you still believe that you have the expense flexibility to hit that 50% target? And maybe you could talk about what levers you have on the expense side? Thanks.

Karl A. Roessner

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

Well, we grew our operating margin rate through the last cut and the environment had a lot to do with that. But we grew through that period. So, in looking at it, yeah, obviously in the period of what you have to make a pricing adjustment, you'll suffer a deterioration in operating margin, but if you pick up on the growth trend right thereafter, you'll get right back on and driving it forward. As far as expense levers, there are numerous expense levers that — we've been very disciplined and that would cause us to be even more disciplined about how we allocate sort of the dollars and money that we spend to achieve the 50% target.

Operator: And our next question comes from the line of Brian Bedell with Deutsche Bank. Please go ahead.

Brian Bedell

Analyst, Deutsche Bank Securities, Inc.

Great. Good evening, folks. I mean just going back to the valuation analysis for independent E*TRADE versus a sales scenario. Rodger, in that analysis, do you guys run that or have you run that on a scenario basis? In other words, is your sort of DCF based purely on the outlook for slide 34 or do you also consider a percentage chance versus a scenario of obviously an adverse environment over that period where the margins would be much lower or the condition for trade cut would be much lower than where the Fed will be cutting? Is that part of what gets put into the valuation analysis?

Rodger A. Lawson

Executive Chairman, E*TRADE Financial Corp.

We certainly look to multiple scenarios with the outside advisors in terms of how we reach the range of valuation that we saw over the course of the next five years. Whether we tested every single upside/downside scenario, I think, is questionable, but I would say 90% of the scenarios we could envisage, we tested. And I think in the context of that, looking at the markets at this moment in time and there's little doubt that the decision to remain independent in terms of the intrinsic value it would probably create for our shareholders was I would characterize as a no-brainer. It was so very, very straightforward. That may change. I mean, I think there's little doubt — Kyle (sic) [Brian], that may change over time, but it certainly, I think, is crystal clear at the moment based on all the analytics we did.

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Corrected Transcript
18-Oct-2018

Brian Bedell

Analyst, Deutsche Bank Securities, Inc.

So, even in running an adverse scenario, you wouldn't come up with a valuation that was potentially lower than what someone would be willing to pay for E*TRADE?

Rodger A. Lawson

Executive Chairman, E*TRADE Financial Corp.

Lower than – well, I'm not sure I understand your question. Say It again, Kyle (sic) [Brian].

Brian Bedell

Analyst, Deutsche Bank Securities, Inc.

Yeah. If you've got a scenario where things are moving adversely such as of that cutting environment and/or commission per trade being more challenged than the modest reduction that you have in the scenario, just the valuation that you would come up with for your company under those adverse scenarios, did that also exceed what a third party valuation would be?

Rodger A. Lawson

Executive Chairman, E*TRADE Financial Corp.

Well, of course, it depends who the buyer is and what they're offering. If someone comes along and offers us \$100 a share, Kyle, (sic) [Brian] I'm sure we will think seriously about it. But I think the reality is – the answer to your question is, yes, it did. I think we felt very, very comfortable with the value that was being generated in relation to any probable realistic scenario that we could see in terms of a sale environment.

Operator: And our next question comes from the line of Dan Fannon with Jefferies. Please go ahead.

Daniel Thomas Fannon

Analyst, Jefferies LLC

Thanks. I guess just another question on the process and you highlighted EPS growth and ROE expansion are the primary metrics that you're going to be focused on. Five years is a long time period. So, how should we think about the pace of that in terms of the reevaluation the board will take. Are we going to hear from you once a year in terms of coming in and updating us? Or just want to get a sense of what the – if there is limited growth here to start or expansion for the first year or two, is that something that a short enough time period to reevaluate?

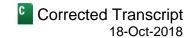
Karl A. Roessner

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

So, Dan, I think the easiest way to explain this one is this is, as I've said, a very engaged board. So, Rodger in his role as Executive Chairman is obviously part of the management team, has been engaged and involved with us. As he sort of steps down and goes into his Chairman role again, I would fully imagine that he will continue to be engaged with us. He won't be on the earnings calls going forward, unless he has something obviously to say to you all about something.

But the process the board goes through, they do their scrutiny of where we are in the valuation of this company and they evaluate what we can produce for our shareholders on a regular basis, right? This is a board that takes their fiduciary duties very seriously. So, I don't want to pin the board to a timeframe or event driven or other items. But I can just tell you rest assured this is a board that will look at all scenarios and if there is something that can impact the value that we can deliver to our shareholders, they'll absolutely act on it.

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Rodger A. Lawson

Executive Chairman, E*TRADE Financial Corp.



And, Dan, let me add a couple of other items. As I go to – go back to Rich Repetto's question, is I go back to be Non-Executive Chairman and it is going to be part of the process of being an Executive Chairman, the company is run by the CEO and by his management team. And we're very conscious of making certain there is the appropriate relationship between board and management.

I'm kind of a hybrid or sort of a mongrel in the middle at the moment. But before we move to this structure and again just be perfectly blunt, we move to this structure, we had – the board believed in Karl, we supported Karl. Karl was my recommendation to take over as CEO. The board supported that totally, Karl was General Counsel. It's not normal to promote General Counsel. He came in and he did a terrific job and part of my process was to be here as a – or shall I say a transitional figure. I've always struggled to keep my mouth shut anyway, but the point is I was there as a transitional figure. But before we had the change, the board was very active. I'm just echoing Karl's comments, and I would imagine that is not going to change. We're not going to disappear into the ether as a result of this.

So, you should expect the board will continue to be very involved. With regard to the other part of your question, which I think is a good question, I've certainly thought about it, look, I don't want to get into, oh my God, you missed your net new asset growth by a 0.25%, you should jump out of the window. We don't want to go through that process all over again. But we are conscious as a board about the fact that how do we evaluate this over time in terms of how we're performing and are we performing. And I'm not being evasive, that will be an ongoing process.

There are some metrics. I remember occasions at Fidelity when I tried to preach to the media about the value of a Fidelity managed dollar versus the value of a Vanguard managed dollars went into their index funds, I totally was preaching to the unconverted, I made zero progress. So, as we look to the future, there may well be issues of asset flows, that's why I made the comment about the revenue yield in terms of Rich's observations. But there will be periods when we see numbers which make us a little uncomfortable, but we will continuously come back to the issue of what are the financial returns that we're generating because those financial returns will obviously generate shareholder value.

And I don't think there is any fixed period when we're going to make any decisions, we're not going to come in every other Thursday and decide, but I think you could – you can – I was about to say I think you assume – I can definitely tell you, with this board, you can assume we're constantly reviewing – are these metrics in line, are we delivering – on the earlier questions from Kyle about will we be able – are we truly attaining the potential values, the shareholder values that we anticipated. So it's going to continue to be an active process. It will still be a pain in the neck. I'm sure that that's the way it's going to be.

Operator: And our next question comes from the line of Michael Cyprys with Morgan Stanley. Please go ahead.

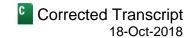
Michael J. Cyprys

Analyst, Morgan Stanley & Co. LLC



Hi, good afternoon. Thanks for taking the question. Just on revenue streams, how satisfied would you say that you are with the diversity of revenue today at E*TRADE, it's about two-thirds interest income? How are you thinking about diversifying it, and which revenue line do you see the biggest room for growth looking out?

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Rodger A. Lawson

Executive Chairman, E*TRADE Financial Corp.

Let's all have a whack at that. It's a very, very good question. I think that the – clearly a large part of our revenue stream is from spread income, say, oh my God, you're a regional bank when you look at things like that. But in reality, the genesis of a lot of those revenue streams is not regional bank like, I mean, Mike talked about Corporate Services. We see what's happening in our retail brokerage space. So as we look at those, those are clearly going to be important revenue streams and important margin streams for the company.

Mike and Karl talked and come to it more articulately better than I can. As we look, though, to the future, RIA, managed money, banking services, I really do think and the board believes that they will become quite more important elements of our earnings. But even by 2023, they will more than pay for lunch, but they're not going to be the dominant – as dominant as a spread income is in the company.

I would however add, let's just take the issues of managed money, as I said earlier, I think our competence is much greater than the Street realizes. It will be really in terms of revenue quite a small proportion of our revenue. But as a retention elements – and one of the board members said yesterday, as a defensive element, it really does keep a lot of clients in-house, so it also adds therefore to that issue of spread income, because these clients frequently leave cash to us. So even out to the 2023 period, I would say, less than the third of our total revenue is going to be coming out of those what you might characterize as newer spaces or spaces that we've been developing over the last 18 months or so but we only have a toe holding.

Karl A. Roessner

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

Yeah. And again to look at it holistically in that same vein, but we will always be focused on our active trader, so the core customer or the population. So when you talk about some of these other items that we have and that we've gone into in the RIA channel with TCA on – expanding what we're doing on the Corporate Services side and making sure that we're driving that funnel, looking at our digital wealth solutions, right, even the simple core portfolios, the robo, the pre-built ETFs, the managed solutions that we have, those are all about forming – and our bank products, we talk about bank products a lot – those are about forming a deeper and broader relationship with our customer set to drive more share of wallet to E*TRADE to make them a more holistic E*TRADE customer.

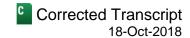
When you look at the bank products, for example, if you can help someone become a banking customer with E*TRADE on the data that we have, they have three times more assets with us. They are two times higher in wallet share. They've three times higher revenue with us. They do twice as many trades and they trade about half the time or half as much as our normal customer set does. So that's relationship building, that's driving at our core which is going to continue we believe to keep those cash balances that Mike talked about at the right levels or growing while we engage and drive additional revenue streams. So it's all part of sort of the holistic message. So, I think Rodger has got it spot on in terms of the way that it'll split out over time. I don't believe you'll see an enormous diversification of revenue streams. What you will see is a broader and deeper client relationship where we have more of their funds with us.

Michael A. Pizzi

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

I think the only thing I would add to that is that the key drivers on the net interest side, you have the margin book, you have securities lending, those are core to our business. It's been a record quarter on margin again at \$11.2

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billion for the quarter-end. There's a lot of things that go through net interest, and a good bit of it is related to the core of our business and the growth of that business.

Michael J. Cyprys

Analyst, Morgan Stanley & Co. LLC

Okay, great. Just a follow-up on the operating margin, mid-50s, can you just talk about what's embedded in there in terms of investments back into the business for growth, and how do you know you're investing enough for growth just given increased competition and disruptors in the space?

Michael A. Pizzi

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

We look actively in terms of project list, in terms of resourcing, in terms of where to draw the line in terms of things to fund and investments to make in the overall business. We understand the power of technology, how to improve in terms of operational efficiency and driving that investment. That's a lot of work that we're doing right now really within the company.

Looking forward, we've evaluated the environment, we're looking at the amount we're spending, we're looking at what reasonably can be put to work, and we think we're making the right investments. Obviously, if disruption changes the industry or we need to spend more, we're going to talk to you about that, and we're going to do what we need to do to maintain competitiveness and position within the industry.

Rodger A. Lawson

Executive Chairman, E*TRADE Financial Corp.

Mike, can I just add another thing as a plug for Karl and Mike, our Mike? And that is — and I think part of the rationale for moving to a COO officer role, I mean, we have some very, very strong people within the company. But whilst ensure that we didn't lose anything in terms of operating efficiency, and Mike made the comments in his prepared remarks about continuing to grow our operating leverage, and Karl and I chatted about this a few days ago. We understand the challenges in the marketplace. I'm sure there are things we don't see that will come along. But I mean I do think we view money as fungible. And I think we will make whatever harsh decisions we have to make in terms of the allocation of resources to ensure that, even in our scale, I'm not outmaneuvered by some people who have larger budgets.

But I think actually [indiscernible] (01:07:25) for these guys, I don't think the management team gets enough credit for the discipline in terms of the execution around efficiencies and driving operating margin, and all of those I think will contribute to – to answering your question, I think your question is a good question, by the way. I think it's a very relevant question.

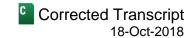
Operator: And our next question comes from the line of Patrick O'Shaughnessy with Raymond James. Please go ahead.

Patrick J. O'Shaughnessy

Analyst, Raymond James & Associates, Inc.

Hey, good afternoon. Maybe just one from me, and you guys might disagree with this characterization, but at least to my perception, E*TRADE's external communications about the criteria to remain independent does seem to have morphed between September 2016 and today, but initially a much greater emphasis on those tangible growth factors and things like net new asset growth, things that you discussed at the Barclays Conference and

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your third quarter 2016 earnings call, can you talk about why the evaluation criteria appears to have expanded over time?

Rodger A. Lawson

Executive Chairman, E*TRADE Financial Corp.

A

Well, I don't know that they extended that much over time, Patrick. Well, by the way, good evening, Patrick, it's a long time since I've heard your voice. I don't think they've morphed that much over time. But, I mean, I think one of the intriguing things, and I kind of touched on it earlier, all those drivers, all those things are very, very important. So, we hit \$6.2 billion in terms of that managed money. That was one of our targets, well done. The reality is it will – it doesn't make a material difference in terms I think of our bottom line or EPS at this stage of the game.

But as we've gone through that period, and we've been focused on those operational drivers, three of which I would argue, other than the one which I know you've focused on we have hit, I would say that it has changed very positively the discipline of the company in terms of how we approach, how we manage. And I think that – I would say, in all seriousness, Patrick, the financial results that has been delivered by the company speak for themselves in terms of the progress that's been made over those two years. I think also it's given us a realistic appreciation of net new asset flow.

I mean, earlier when Rich was asking the question – I read your book, Patrick, and I think in fact when you were talking about revenue yield, I can't remember [ph] what you would call, is it ROCA? (01:09:40) I can't even remember, but what I call revenue yield, but we look to that. And I think as we've gone through this period, I think we recognize there are other drivers – we all live and learn – there are other drivers of our revenue yield and therefore our contribution to our gross margins that we haven't seen. So, yes, we may – we've missed on the [ph] ROCA (01:09:59) target, we've hit the other ones.

But I think the most important thing that's come out of it, I'm going to say is the new E*TRADE, that sounds too theatrical, but I do think those – all the things that we've made – the comments we've made in our prepared remarks, it has changed the attitude towards the company. And that is also, by the way, why I talked to the end about EPS growth rate and ROE, there are a gazillion things we look at, and I'm sure you guys will look at more than I will because you actually have more detail and knowledge. But what is nice about the ROE and EPS, it fundamentally drives valuation if you believe it over a period of time. And I think it is a nice straightforward common denominator metrics.

So it's a long way to answer your question, but I'd say we have been focused on them, but they have enabled the company's performance to morph much more aggressively by focusing on them, Patrick, than we originally thought would happen.

Patrick J. O'Shaughnessy

Analyst, Raymond James & Associates, Inc.

All right. That's helpful. Thank you, Rodger.

Rodger A. Lawson

Executive Chairman, E*TRADE Financial Corp.

А

You're welcome.

Operator: And our next question comes from the line of Craig Siegenthaler with Credit Suisse. Please go ahead.

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Corrected Transcript
18-Oct-2018

Craig Siegenthaler

Analyst, Credit Suisse Securities (USA) LLC

Thanks. I just wanted to come back to the net new asset organic growth rate in some of your earlier comments on the RIA custody channel, do you think there is an opportunity to improve the gap versus Schwab and Ameritrade? And also, have you thought about also reporting an adjusted metric that also include inflows from your Corporate Services business?

Michael A. Pizzi

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

Yeah. Obviously, I think we can improve our growth rate with what we're doing in E*TRADE Advisory Services. The \$12 billion of pipeline that we announced today is a pretty amazing number. We have \$12 billion of commitments to move on to the platform. We bought the business – it was about \$17 billion to \$18 billion, and we've onboarded \$1 billion since April. When you look at sort of our quarterly flows what is an amount of assets worth coming from that channel, well, you can see quite clearly that it's going to pick up the percentage growth rate in assets.

Now, in Corporate Services, yeah, we don't – we have customers who do not take an action. They sort of just allow their stock to vest. We don't report that in net new assets. We wait for that customer to take an action and sell that stock. We've given you that breakout really for the first time in the investor deck. That's a very conservative way of looking at net new assets. We've historically, that's the way we've done it, we thought that that's the right way, but if you actually took that vesting and put it through net new and moved it from the unvested portion in, you would get a much higher rate of net new asset growth.

Craig Siegenthaler

Analyst, Credit Suisse Securities (USA) LLC

Got it. Thank you.

Operator: And our next question comes from the line of Devin Ryan with JMP Securities. Please go ahead.

Devin Ryan

Analyst, JMP Securities LLC

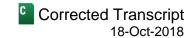
Hey, great. Thanks. Good evening. So you guys highlighted M&A a couple of times in the prepared remarks. And I think the view was that any M&A during the past two year assessment period would be modest, which makes sense. But now that we're through that, do you expand what you're thinking about or open to? And then I guess is there anything larger that maybe it could make sense to enter with a scale deal and then just more broadly, any other update on the types of things you might be looking at?

Karl A. Roessner

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

Yeah, I think, look, for the most part, our focus remains the same, like what can we do to deliver better for our customers, are there product set, or are there additional capabilities that our customers are looking for, whether that be through the RIA custody channel, through our retail brokerage channel, or on the Corporate Services side. And obviously, if there's any kind of a scale play in Corporate Services or something we can do to accelerate the growth of the RIA channel, we'll look at that.

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The one thing that I would say is, we were pretty restrictive in terms of discussing transformative or larger scale M&A during the last two years. What I would say is we will remain disciplined, we will continue to run anything that we look at through the same capital lens that we've used in the past to make sure that that will either generate or drive significant value for our shareholders or we're not going to do it. But I'm not going to say anything about not looking at larger transactions or larger deals that may be able to drive shareholder value over time.

Devin Ryan

Analyst, JMP Securities LLC

Q

Okay, great. Thank you. And then just a quick follow-up here, and they are kind of related to TCA, internal referrals have been huge for your custodian peers and so I appreciate some of that color. Do you have any stats internally of either whether it'd be in the corporate stock plan or the self-directed brokerage side, how many assets you're actually losing to RIA relationships or any thoughts on that?

And then just on the economics, can you just help us with what those will look like if you keep those assets inhouse and some others around 25 basis points?

Michael A. Pizzi

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



So, I think this might be actually the shortest answer of the evening, and I apologize for that. We don't disclose the stats. We do know where they transfer to and when they go. We do have some pretty good data on the conversations that – or had with our FC channel when folks come to E*TRADE and ask whether or not we have an RIA channel or they have somebody that can provide them with the advice. So there is a reason that we went out after the RIA platform that we did in terms of the custody platform with TCA.

And the other part of that is, our referral network and some of the pieces that are going into place will really start to fall in line over the next few weeks, so more to come on that channel including what we believe it drives and what value we're deriving from it. But we look at it as just a phenomenal tool to help us with both maintaining our stock plan customers and also driving additional value from both existing retail and future retail that come to us.

Operator: And our next question comes from the line of Michael Carrier with Bank of America Merrill Lynch. Please go ahead.

Michael Carrier

Analyst, Bank of America Merrill Lynch

C

Hi. Thanks, guys. Rodger, just a question for you. The growth has been healthy and management's plan seems reasonable. I guess just curious given where we are in the cycle for rates and retail engagement [indiscernible] (01:16:09) competition heating up, net new asset targets bit tougher to hit, why not look at maybe a dual track, the management plan and then also seeing with bids are out there just given the known synergies [indiscernible] (01:16:25) consolidation?

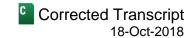
Rodger A. Lawson

Executive Chairman, E*TRADE Financial Corp.



Well, actually, I'm glad you asked that question, Mike, because I was going to make a comment at the end, because two or three good questions have been asked about that. The board really effectively assesses valuation every year on this company. I think I mentioned it at the first time at the Barclays Conference a couple years ago, but it is a process that's going on for a reasonably lengthy period of time. We're not casual about it. We recognize

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where E*TRADE's come from, and Lazarus rising from the dead effectively, but getting into such a strong position now.

But each year as we've gone through that process, we've done valuation. I will say that we have looked at times at – I recall one period when I think the stock was \$11 a share – I joined in 2012 myself and Becky Saeger both joined at the same time, the stock was \$8, so I think it probably dropped, that was great my ego. But then when it was around \$11, we did a very, very thorough assessment of valuation. We did something similar and then there were – we had comments from people who we respected and people [ph] we understood that (01:17:34) said we should do that. So at \$11, we did it I think in the low \$20s as well, it was extremely thorough evaluation, we didn't talk to third parties on the outside. We did it pretty much on the same basis we've just done it. And obviously, we made the decisions [ph] that are appropriate at that time we should stay where we would going (01:17:54) forward.

And I would argue in spite of the fact the market's been lousy in the course of the last six or eight weeks that the board made – and it's a very similar board, we've had very modest changes – we made very wise decisions in terms of the shareholder value. So what I would say rather than [indiscernible] (01:18:10) running parallel experiences which I think can be disruptive of value, I think we do trust our judgment in terms of using the kind of processes we've used as to where value sits. I'd also say and it is the reality we know – I used the words – we know our fiduciary responsibilities, actually we do.

And we're open-minded, when someone comes along and wants to talk to us that may well be an interesting opportunity, all I know is, Michael, we would look at it very seriously and we'll do what we did. When we looked at those two prior examples I gave you, they were not formal offers, but they were certainly formal discussions. So, I think the process we have, we don't want to destroy value. We don't want to start hares running. We want as much stability. People do work here with their tails off to bring this company back to – I think as you look at our margins, a highly competitive state and so I think a process which we should do as a board in terms of evaluating our value. The way we approach it, I think, is a more sanguine and a more responsible way of handling it.

Operator: And our next question comes from the line of Brennan Hawken with UBS. Please go ahead.

Brennan Hawken

Analyst, UBS Securities LLC

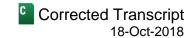
Good evening. Thanks for taking the question and thanks for the patience, it's been a long call. So, my question is for Rodger. You laid out these targets two years ago. What's often held up as the most important metric for the group is net new assets. It's the target that you missed and you missed the range by a pretty wide margin. So, I know that you laid out that you don't have the RIA business and that might be the reason, but you knew you didn't have the RIA business when you laid the targets out. So, there are a lot of investors that have got involved in your stock based upon targets, hitting the targets or pursuing a sale and now you're telling us that you didn't even get any bids. So, can you just explain that with a little bit more of a justification as to why you wouldn't pursue that process a bit more thoroughly?

Rodger A. Lawson

Executive Chairman, E*TRADE Financial Corp.

All right. So, I'll go back to the beginning on the conference – on the Barclays conference in September. Actually immediately after that conference when we met with various investors, I can remember meeting with T. Rowe, they made it very clear that they thought that we were diluting ourselves because of the absence of that channel. I

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think we probably expected more in terms of where that would – we could grow it. We probably underestimated – heaven forbid, we underestimated what we anticipated might be the growth rate from our business.

In terms of going forward, another comment which I've kind of alluded to when I talked to them about Rich and Patrick's observations about revenue yield, the model we have is not exactly shabby. It does generate a very, very high level of revenue yield. We're very, very pleased with that. Even though our growth rate in net new assets is not as great as others in the marketplace, and forgive me, I think it was Dan Fannon asked the question about did we expect effectively to grow at the same rate or similar to competition. I think the answer is no. I mean, I don't think we expect to grow at the pace of someone like Schwab. Probably it's a machine in terms of [ph] that (01:21:27) raises assets, and I think that even TD, I think, has been very effective in raising assets through its RIA channel.

We don't expect to grow at that rate. But we look at it and I would say truthfully, Brennan, I think the – we put our money where our mouth is in terms of how we developed the financial performance of the company. I don't think – I can't remember precisely, I know I should, but I can't. At the time we had that conference, our stock was \$26 or \$27, I mean, okay, we're all crying out there at the moment because it's become a setback in the market for whatever reason, but it's affecting us all pretty much.

We probably even marginally more because I'm sure some of our [indiscernible] (01:22:04) figured we weren't going to sell and therefore get the hell out of it. But in practical terms, we have delivered a lot of value; I mean material value. So, in a sense, I don't think it's anything we need to be ashamed of and, as I said earlier, we're certainly not going to jump out of the window because we didn't hit our net new asset flows. Scale is very, very valuable. We agree scale matters, size matters and I would rather see us have more flows than not.

But we're not going to chase after them or overpay for them. We'll build them in a considerate and realistic way. So, we feel extremely comfortable of what we've done. And the key to your question – your question is a fair question, I'm not offended by it, your question is a fair question. I think, as we go forward, we really believe we could deliver these values. I mean, shareholders of E*TRADE got turned upside down in 2007 and 2008, we're not going to give away value now if we really see it there and the board sees that value.

Brennan Hawken

Analyst, UBS Securities LLC

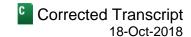
That's fair, that's fair. But I guess, another way of looking at it would be that there's been tremendous earnings growth which is totally true and totally valid. But here we're standing towards the tail end of what's been a great cycle. Interest rates have been a huge tailwind. The management team has done a great job of not watching it which previous E*TRADE management teams may be a different story. But isn't this a time to look around, you've got this wonderful setup given you laid out the two-year target. You guys are small, and it's a scale business increasingly. And so there are many who argue that this could be an opportune time to actually go through and assess some bids. And so, I guess that's the difficulty that I'm struggling with here.

Rodger A. Lawson

Executive Chairman, E*TRADE Financial Corp.

So, Brennan, let me come back and try to give you more color. In a sense that – we look around all the time, [indiscernible] (01:24:00). There's nothing happening around this in the world. We look around all the time. So, to whatever premium we could prognosticate from where we are today, the plans we look out, we believe whatever valuation and methodology you use, we believe the plans we have will deliver considerably more value than taking our understanding of what's going on forward into a more serious engagement with someone. So, we made as a broader realistic decision, there is more value remaining independent and growing through the plan than

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what we see in terms of what's out there in the marketplace. If someone wants to come along and offer us \$100 a share, we know our responsibilities.

Brennan Hawken

Analyst, UBS Securities LLC

All right. Thanks for entertaining my pressing questions. Appreciate it.

Rodger A. Lawson

Executive Chairman, E*TRADE Financial Corp.

You're welcome, Brennan.

Operator: And our last question comes from the line...

Karl A. Roessner

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

Sorry. Go ahead, Christopher.

Operator: Our last question comes from the line of Chris Allen with Compass Point. Please go ahead.

Chris Allen

Analyst, Compass Point Research & Trading, LLC

Good evening, guys. Just wanted to ask two quick questions. One, on TCA, the \$12 billion in the pipeline is impressive. Maybe if you could give us some color just in terms of how many TCA clients use them for the sole provider. I'm just trying to think about who's coming onboard to tap into the E*TRADE referral program versus using them as a sole provider and think about organic growth on a longer term there.

And then secondarily, any update on October DART to margin balance, because we're getting a number of client inquiries on that one.

Michael A. Pizzi

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

Yeah, sure. So, the TCA channel is pretty widespread in terms of the uptake we've seen. We are right now sizing and scoping the referral programs both for the national and then we'll have obviously regional and local programs. Many of TCAs, we have – or lots of TCAs existing, RIAs are interested in getting involved with that. And we announced that in the prepared remarks that Edelman Financial has joined us as well which we're quite excited about. So, that's sort of where we are. I think that business is a very nice business for us. In terms of the custody platform, it gives us lot of optionality and a lot of opportunities to engage a little differently with our retail clients and our stock plan administration plans as they come through the pipeline.

On the DARTs number, to date we're up about 8% from the end of September and our margin balance is sitting at about \$11.5 billion as of yesterday.

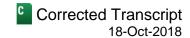
Chris Allen

Analyst, Compass Point Research & Trading, LLC

Thanks, guys.



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Karl A. Roessner

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

Yeah.

A

Karl A. Roessner

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

Okay. So, that's it for this call. I appreciate everybody joining and I look forward to speaking with you next quarter. Thanks a lot.

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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