Operator

Good day, everyone, and welcome to today's program. At this time all participants are in listen-only mode. Later you will have the opportunity to ask questions during the question-and-answer session. [Operator Instructions] Please note this call is being recorded.

It is now my pleasure to turn the conference over to Mr. Lee McEntire. Please go ahead.

Lee McEntire

Good morning. Thanks to everybody on the phone as well as the webcast for joining us this morning for the second quarter 2016 results. Hopefully everybody's had a chance to review the earnings release documents that were available on our website.

Before I turn the call over to Brian and Paul, let me remind you we may make some forward-looking statements. For further information on those, please refer to either our earnings release documents, our website or our SEC filings.

So before Brian and Paul get into the results, just let me mention one housekeeping item. Please limit your questions to one per caller so that we can get to everyone, and you can circle back.

With that, I'll turn the call over to Brian Moynihan, our Chairman and CEO, for some opening comments; before Paul Donofrio, our CFO, goes through the details. Brian?

Brian Moynihan

Thank you, Lee, and good morning, everyone, and thank you for joining us to review our second quarter results. I'm beginning on slide two of the materials we sent to you.

We reported solid earnings of $4.2 billion after tax, or $0.36 per diluted share, in what was certainly an eventful quarter for the markets from an overall macro perspective. This compares to $5.1 billion or $0.43 per share in the year-ago quarter. This quarter included negative market related NII adjustments that cost $0.05 per share and negative DVA that cost us another penny for a total of $0.06. That compares to a $0.03 benefit for EPS for both those items in the second quarter of 2015.

Earnings neutralizing for the past 91 DVA for both periods improved from $0.40 per share to $0.42 per share on a year-over-year basis. Our results represent another quarter of solid progress in the strategies we have been executing. Those strategies are delivering more of the company's capabilities to each and every client we serve. At BAC, we focus on what we can control, and despite low rates and other macro events, we continue to focus on managing our risk, our costs and our delivery of quality products and customer service.

In Q2, we grew loans $22 billion or approximately 2.5% versus last year, even as we sold a few portfolios during the year. All this growth was organic and consistent with our risk appetite. We also grew deposits more than $66 billion or 6% over that same time period, and we did so while maintaining disciplined deposit pricing.

We also continued to transform our company in a digital way at all things and all businesses. For example, this quarter we crossed over 20 million active mobile users and continued to increase their use of digital channels for both transactions and buying more bank products. Active mobile banking customers logged into their accounts over 900 million times this quarter, depositing more than 25 million checks, with more than 20 million via mobile check deposits. They made over 25 million mobile bill payments, up 30% year-over-year, and made nearly 80 million transfers. Person to person, or P2P, payments continue to ramp up as well. While still a small component of the overall consumer payments this quarter, we had $6.7 billion in P2P payments this quarter. That is more than $13 billion year to date and is up 20% from last year. This channel is a valued channel for all our customers and made possible by the [indiscernible] investment we make.

As we move to slide three, we have talked to you – a lot of you over the last several months including many of you on the phone today. I thought I'd try to address some of the more common questions we get from those conversations by looking at our results – by looking at the income statement and the items therein.

First, one of the core questions is what if rates stay lower for longer? Well, for bank management and for you as investors it would be easier if rates were to rise but that hasn't happened. So the question is can we grow earnings without rates improving? We believe we surely can. We can do that by continued success on things like expense management, by keeping NII stable to growing, stable and growing fees, and continue to manage risk well and hold down our credit costs. As you can see, revenue this quarter was $20.6 billion on an FTE basis. Adjusted for the negative impacts of market-related NII adjustments and DVA, that number is $21.8 billion. Adjusted for the same items in the year-ago quarter, the total was comparable.

Now as we focus in on NII, Paul will take you through some of the changes this quarter later in the presentation. However, in summary, adjusted for market-related changes in both last year's second quarter and this year's second quarter, we grew NII by 400 million or 4% year-over-year. And that took place while the 10-year Treasury yield fell 86 basis points from last year on a spot basis. Going forward in a stable interest rate environment, we believe we can maintain NII around the second quarter 2016 level based on the current loan and deposit growth we see. And if rates rise, we would expect NII to grow.

Another question relates to Global Markets business. That question is often asked how we need to change this business, especially the FICC area as many of our customers have. I want to hit this head on. First of all, fixed income a good business for us here at Bank of America. It is a business which benefits not only by its core activities but by being coupled with our massive global banking franchise that has leadership positions across the globe. Combined together, they generate a pretty steady billion dollars or so of quarterly investment banking fees. It's also an important part of our overall Global Markets platform, the platform which sits on top of the number one global research team for the past five years.

In the second quarter, this business did well. Global Markets generated $3.7 billion in sales and trading revenue excluding DVA. Compared to the same period last year, that is up 12%. This year-over-year improvement is driven by FICC sales and trading, which is up 22%. Now think about that. Sales and trading revenue including DVA for this quarter is the highest second quarter we have experienced in five years and it led to one of the most profitable quarters for Global Markets we have seen in the past five years.

Also the team served clients well during a period of difficult volatility. So clearly it remains a profitable important business for us to serve clients. We're proud of how the team supported their clients through the Brexit both in the periods of volatility related there too.

Another question is getting clarity on how we're transforming the business on the fee lines. Noninterest revenue was $11.2 billion this quarter. Although modestly down from second quarter 2015, it was up nicely from the first quarter. There are a lot of the items that one through the various lines of fees. First with regard to consumer fees, we are largely done with the big card portfolio divestitures and branch divestitures. Both those impacted both card fees and banking service charges and you can see them coming off the bottom as you look at the linked quarters. Fees now will grow with the volume of cards and accounts that are now net growing in our company. Our mortgage business is now sized appropriately for our franchise and the fee line there Paul will talk about later, but will be as that near where it's going to be in the future.

With regard to revenue more closely tied to markets business, the ups and downs in volumes of activity in sales and trading in investment banking and brokerage will move back and forth with the market. But the important thing is we have strong businesses, strong client-facing businesses in these areas and we're getting our share of these revenue streams even while the markets ebbs and flows.

So if we look about move from the fee line to the expense line, many of you give us credit for having managed expenses from $70 billion five years ago to the mid-$50 billion today. But the question is can we do more? And if you look at this quarter we continue to manage expenses well. Noninterest expense this quarter was $13.5 billion, improving more than 3.5% or 3% from 2015 second quarter. This continues a trend of performance that has shown expense declining significantly on a quarterly basis quarter-after-quarter over the past several years. This is the lowest level that we have reported since the fourth quarter of 2008, and that's prior to the Merrill Lynch merger.

If you look at our efficiency ratio and normalize it for the NII adjustment stated above, it would be about 62% this quarter. That's an improvement 200 basis points from last year's second quarter. Cost control and cost effectiveness is a focus for our management team here at Bank of America. So the question is how much more can we do on expenses? So if you think about this, let's start by looking at the costs of the most recent four quarters. In the trailing four quarters the total expense base was $56.3 billion. As we look out from the second – the third quarter of 2016 through the next six quarters into 2018, we believe that with our SIM efforts and the continued work we're doing across the board on expenses, we're targeting an annual expense number of around $53 billion in total expenses for the year 2018.

So over six quarters we continue to absorb investment, merit increases, rising healthcare costs, and bring the expenses down a nominal amount. Our continued work in driving down costs to service delinquent loans will help with this, but the other reductions are generally coming from the core work and simplified improved. The work we continue to do to simplify those work processes but also the core work we do to allow us to self-fund our growth initiatives, are continuing investments in technology and salespeople.

While I'm on the topic of expenses, I want to point out another important milestone for our company in quarter. This quarter we changed our reporting to eliminate the legacy assets in the servicing segment. This completes transformation. This segment was last place for product orientation was reported, not customer orientation. And more importantly, it also reflects the last of legacy is really behind us from an operational basis. We added a couple slides in the appendix today to go along with our 8-K we filed a few days ago. They explain the methodology of the realignment of LAS and the highlights that impacts the segment with those loans and associated P&L are reported now.

But what I want to get to across to you is LAS as an operational segment successfully did what it was tasked to do: to clean up one of the largest mortgage servicing businesses in the U.S. Consider that progress. From 1.4 million delinquent mortgage loans we're down to 80,000 a day. At one point we had 58,000 teammates and 20,000 contractors working on this task, and now we're down to 10,000 teammates. From one peak a quarter of $3 billion plus in expenses, we're down to $600 million this quarter. That phase of the work is complete and we need to move that operating business in with the rest of the company to do the further consolidation and further work to improve our servicing cost. We are pleased with the accomplishments of this group but there is still more to be done.

And that brings us to our provision. Simply put, the question we often get is, is credit deteriorating? As you can see, we remain very pleased with both consumer and commercial credit performance. Not only have net charge-offs not gotten worse, but they have improved in the most recent quarter moving back below $1 billion. Provision expense is and will remain roughly equivalent to net charge-offs. Even our energy portfolio we have seen lower exposures improve losses.

And that brings us to our returns. In this operating environment, can we get our returns above our cost of capital? Well as you can see, we've made solid progress on our returns this quarter. Our return on tangible common equity adjusted for the market related and DVA impacts was 10.9%. On a similarly adjusted basis, ROA has moved to 90 basis point. We still have work to do, but you can see the improvement coming through.

As we move to slide four, you can see our business segment results. You see strong year-over-year results in every business driven by the generation of operating leverage. Consumer banking continue its momentum around client activity and operating leverage. Consumer satisfaction continues to improve as does adoption and use of digital capabilities and functionality. And our wealth management business, they grew earnings as costs declined more than revenue while we continue to invest in this business. Revenue is impacted by AUM valuations from market variability.

Our global banking team drove results with continued solid loan growth, operating leverage of 9% and strong credit results. Global markets executed well for its clients, as I stated earlier, in a very difficult period, and used operating leverage to grow its earnings year over year as well. So on a combined basis, those four business segments improved 16% from last year's second quarter earning about $5 billion this quarter. Partially offsetting this was the loss at all other, and that primarily reflects the market related NII adjustments I spoke about earlier. You can see the returns and efficiency ratios for each of these segments, and note that each segment is earning well above our cost of capital.

With that, I'll turn it over to Paul to take you through the numbers.

Paul Donofrio

Thanks, Brian. Good morning, everyone. Since Brian covered the income statement, I will start with the balance sheet on page five. As you know, when general deposit flows drive the size of our balance sheet, and they on a lending basis were relatively flat this quarter as inflows were partially offset by outflows to fund seasonal tax payments. So total assets were stable compared to Q1 with loans increasing modestly, security balances rising and cash down a corresponding amount.

Liquidity also saw a small decline. However, we remain well compliant with LCR requirements. Tangible common equity of $170 billion improved by $3.6 billion from Q1, driven by earnings and OCI. This was partially offset by 1.1 billion in share repurchases and roughly 500 million in common dividends. As a reminder, following the CCAR results we announced an increase in both our share repurchase authorization as well as a planned increase of 50% in our quarterly dividend. On a per share basis, tangible book value per share increased to $16.68, up 11% from Q2 2015.

Turning to regulatory metrics, as a reminder, we report capital under the advanced approaches. Our CET 1 transition ratio under Basel III ended the quarter at 10.6%. On a fully phased-in basis, CET 1 capital improved $4.3 billion to $161.8 billion. Under the advanced approaches compared to Q1 2016, the CET 1 ratio increased seven basis points to 10.5% and is above our current 2019 requirement. RWA declined roughly 13 billion, driven by reductions related to retail exposures primarily from credit improvement.

We also provide our capital metrics under the standardized approach. Here our CET 1 ratio improved to 11.4%. Supplementary leverage ratio for both parent and bank continue to exceed U.S. regulatory minimums that take effect in 2018.

Turning to slide six and on an average basis, total loans were up 7 billion from Q1 and 23 billion or 3% from Q2 2015. On an ending period basis, loan growth this quarter was impacted by pay-downs near the end of the quarter and the non-U.S. corporate loan facilities and about 1.6 billion in FX translations across international loans, including the K Card [ph]. Note on the slide, there is a breakdown of the loans in our business segments and all other. Again, on an average basis year-over-year, loans and all other were driven by 42 billion driven by continued runoff of first and second main mortgages while loans in our Business segments were up 65 billion or 9%.

In Consumer Banking we continued to see strong growth in consumer real estate and vehicle lending, offset somewhat by runoff in home equity outpacing originations. In Wealth management, we saw growth in consumer real estate and structured lending. Global banking loans were up 35 billion or 12% year over year and up 7% annualized from Q1. Deposits were stable with Q1 at 1.2 trillion, but grew 67 billion or 6% from Q2 2015. Broad-based growth was led by consumer, increasing more than 44 billion or 8% year over year, while wealth management deposits grew 6% and deposits with corporate clients and global banking improved nearly 4%.

Turning to asset quality on slide seven, we saw improvement from Q1. Total net charge-offs improved 83 million from Q1 to less than 1 billion in Q2. Consumer losses declined modestly across a number of products, and while slight commercial losses also declined from Q1 as a result of lower energy losses, provision of 976 million in Q2 was down $21 million from Q1. Finally, we had a small overall net reserve release in the quarter as consumer releases were modestly offset by builds in commercial.

On slide eight, we provide credit quality data on our consumer portfolio. Net charge-offs declined $68 million from Q1. While driven by lower real estate losses, the improvement, as I mentioned, was broad-based. Over half of the losses in this book are U.S. credit card, where the loss rate improved five basis points from Q1 to 2.66%. Delinquency levels and NPLs improved and reserve coverage remains strong.

Moving to the commercial credits on slide nine, net charge-offs improved $15 million from Q1 as energy losses declined. Energy charge-offs decreased $23 million from Q1 to $79 million this quarter.

There isn’t a lot of new news on the commercial asset quality front other than the modest improvement in our energy-related exposure. As you all know, the price of oil and gas was more stable in Q2. Within this backdrop, we experienced some improvement in both energy losses and exposure. A few clients refinanced with equity issuances and other financing solutions, which also helped improve exposures.

Overall, our committed energy exposure declined $3 billion from Q1, with utilized exposure declining more modestly and exposure to exploration and production as well as oilfield services, which we believe are the two higher-risk subsectors, declined 1% from Q1.

Outside of energy, commercial asset quality continues to perform well. Let me share with you a few metrics that exhibit the quality of this book and its performance.

The reservable criticized exposure ratio is 3.8%, and excluding energy, metals and mining, exposure is 2.4%, which is near pre-recession levels. The commercial net charge-off ratio excluding small business has been below 15 basis points for 14 consecutive quarters, even with the elevated levels of energy charge-offs we experienced over the past three quarters. The NPL ratio which today is at 37 basis points has been below 40 basis points for 11 consecutive quarters.

Turning to slide 10, net interest income on a reported non-FTE basis was $9.2 billion. Included in NII this quarter was a negative $974 million market-related adjustment to true-up bond premium amortization. This follows Q1's more negative adjustment of $1.2 billion, and it's important to note that the adjustment in Q2 2015 was a benefit of $669 million.

NII on an FTE basis excluding market-related adjustments was $10.4 billion. This was lower than Q1 primarily due to lower long end rates and Q1's seasonal impacts. Compared to Q2 2015, results were up nearly $400 million, or 4%, as higher short end rates combined with loan growth funded by deposits offset the negative impact of lower long end rates.

Looking forward to Q3, we will benefit from an extra day which will be offset by the impact of declines in long end rates over the past two quarters and put pressure on our MBS bond yields and reinvestment yields more generally. As we get into Q4 and the next year, we get more optimistic about NII, assuming both the current forward curve and the current pace of loan and deposit growth.

With respect to asset sensitivity, as of 6/30, an instantaneous 100 basis point parallel increase in rates is estimated to increase NII by $7.5 billion over the subsequent 12 months driven by the increase in long end rates.

Now we think it's also important to understand what we expect to happen to NII if rates don't rise. Referring to the bottom left of the slide, the adjusted NII has been fairly stable, averaging between $10.3 billion and $10.4 billion over the past five quarters. If we have stability in long end rates, we would expect to maintain that level in the near-term, again, assuming modest loan and deposit growth. Rates moving up or down from here would obviously impact that perspective slightly in the near-term, but building as we extend that scenario into future quarters and years.

Turning to slide 11, noninterest expense was $13.5 billion in the quarter. That is a half a billion dollars or 3% lower than Q2 2015 driven by good expense discipline across the company. As you can see, we are presenting expenses a little bit differently now that we have eliminated the LAS segment. Having said that, we made steady progress on reducing legacy loan servicing costs this quarter and we still expect to achieve our original goal of lowering the former LAS segment costs ex-litigation to $500 million in Q4. Q2 litigation expense was $270 million which was higher by $95 million than Q1 2015, so year-over-year expense improvement ex-litigation was actually $600 million.

Nearly every category of cost was lower year-over-year. It was led by personnel including the expiration of the fully amortized advisor awards and the revenue related incentives mostly in wealth management. While the rest of the improvement I would characterize as just good, hard work, grinding expenses lower through SIM and other initiatives. While the rate of decline has been slowing, our employee base is down 3% from Q2 2015. As the employee base continues to go lower, we think it’s important to point out that the reductions on a percentage basis now include more highly paid managerial associates.

So while the rate of FTE reduction has slowed, the relationship to expense reductions is not linear. Also, we continue to increase the number of client-facing associates to drive growth while at the same time through SIM and other efforts simplify and streamline activities and thereby reduce non-client-facing positions. Lastly, as I said last quarter, we expect our quarterly FDIC expense to increase approximately $100 million for a number of quarters starting in Q3 2016.

Turning to the business segments and starting with consumer banking on slide 12, consumer earned $1.7 billion, continuing its trend of solid improvement and reporting a robust 20% return on allocated capital. Revenue and earnings were driven by deposit and loan growth coupled with continued expense improvement driving operating leverage. As a result of this operating leverage, the efficient ratio improved roughly 360 basis points year-over-year. Note that the lack of reserve releases this quarter versus a meaningful release last year mitigated some of the improvement in the operating leverage. So while earnings were up 3% year-over-year, pre-tax pre-provision earnings rose 11%.

On slide 13, we focus on additional key consumer banking trends. First on the upper left, the stats are a reminder of our strong competitive position.

Revenue increased by 107 million and NII growth more than offset lower noninterest income. Net interest income continued to improve as we drove deposits and loans higher. Noninterest income was down due mostly to lower mortgage banking income. This decline is in part a result of selling fewer loans and instead holding more on our balance sheet, thereby shifting mortgage banking income to NII. Expense declined 5% from Q2 2015. The positive expense trend is a result of a number of initiatives.

As an example, I would note that our growth to mobile banking continues to play an important role in helping us optimize our delivery network while improving customer satisfaction. Our cost of deposits as a percentage of average deposits also continued to improve and now stands at 162 basis points. Focusing on client balances on the bottom of the page, Merrill Lynch broker assets at $132 billion or up 8% versus Q2 2015 on strong account flows partially offset by lower market valuations. We increased the number of Merrill Lynch customers by 10% from Q2 2015. We now have more than 1.6 million households using our platform for self-directed trading.

Moving across on the bottom right of the page, note that loans are up 5% from Q2 2015 on strong mortgage and vehicle lending growth. Average vehicle loans are up 20% from Q2 2015 with average booked FICO scores remaining well above the 770 level and net losses remaining below 30 basis points and improving on a linked quarter basis. Mortgage loan growth was aided by solid mortgage production of $16 billion, up modestly from Q2 2015, as customers took advantage of historically low interest rates. On consumer card – or I should say on U.S. Consumer Card, we issued more than 1.3 million cards in the quarter, which is the highest level since 2008. Average balances were modestly down; however, adjusting for divestitures, average card balances grew $1.4 billion compared to Q2 2015.

Spending on credit cards adjusted for divestitures was up 7.5% compared to Q2 2015. As we viewed in previous quarters, we continue to focus on originating high FICO loans which generally produce low loss rates and strong risk adjusted margins.

Last quarter, we highlighted the quality of our underwriting in the consumer business. This quarter, we’re highlighting our leading position in digital banking. This technology continues to reshape how our customers bank. Importantly, as adoption rises, particularly around transaction processing and self-service, we see improved efficiency and customer satisfaction. We added more than 2.5 million new mobile customers in the past 12 months. With more than 20 million active users, deposits from devices now represents 17% of deposit transactions. Mobile customers on average process 280,000 deposits per day, an increase of 28% year-over-year and the equivalent to volume of 800 financial centers.

Mobile sales are up nearly 50% from last year. We're promoting mobile sales and electronic adoption by deploying digital ambassadors in our financial centers. We now have more than 3,500 digital ambassadors in our branches engaging with customers who come into the branch to transact. They educate these customers on alternatives to branch banking, which are not only more convenient for them but also more efficient for us. Digital sales, appointments and satisfaction all continue to achieve new highs.

Also as you know, we are a leader in person-to-person and person-to-business money movement through digital transfers and bill payment capabilities. The adoption and popularity of these capabilities continues to drive growth with record volume of $246 billion this quarter, up nearly 5% year-over-year.

Turning to slide 15. Global Wealth and Investment Management produced earnings of $722 million, up 8% from Q2 2015. Year-over-year, revenue was down modestly but expenses were down even more, improving pre-tax margin to 26%, up meaningfully from Q2 2015. This quarter included a modest gain from the previously announced sale of Bank of America Global Capital Management. This reduced AUM comprised of short-term liquid assets by approximately $80 billion. Overall, revenue declined 2% from Q2 2015, as strong NII growth and the gain were more than offset by lower market-sensitive revenue.

Asset management revenues declined from Q2 2015 on lower market values while improving modestly on a linked-quarter basis. Transactional revenue was down and continues to be impacted by market uncertainty as well as the migration of activity from brokerage to managed relationships. NII benefited from solid deposit and loan growth. Non-interest expense declined nearly $200 million or 6% from Q2 2015, with half of that benefit derived from the expiration of the amortization of advisor retention awards that were put in place at the time of the Merrill Lynch merger. The rest of the improvement was a result of lower revenue-related incentives and other support costs.

Moving to slide 16. Despite volatile markets, we continued to see overall solid client engagement. Client balances at $2.4 trillion were down from Q1; but excluding the sale I mentioned earlier were up from Q1, as higher market valuation levels, $10 billion of long-term AUM flows and loan growth more than offset tax-related deposit outflows.

Driven by the expected seasonality, average deposits were down from Q1 as clients paid income taxes. Importantly, average deposits are up 6% from Q2 2015, driven by growth in the second half of 2015. Average loans also grew this quarter. Growth was concentrated in consumer real estate and structured lending as well.

Turning to slide 17. Global Banking earned $1.5 billion, producing solid improvement over both Q1 and year-over-year. Returns on allocated capital was 16%, a 200 basis point improvement from Q2 2015, despite adding $2 billion in allocated capital. Double-digit percent revenue growth year-over-year offset a low single digit expense growth creating strong operating leverage that improved the efficiency ratio to 45%. Global banking continues to drive solid loan growth within its risk and client frameworks producing solid year-over-year improvement in NII. Revenue benefited this quarter from mark-to-market gains on our FBO loan portfolio due to recovery in certain energy and mining exposures. Higher Treasury fees and leasing gains also aided the improvement from Q2 2015.

While total investment banking fees for the firm were down from Q2 2015, global banking gained a little share supported by M&A fees which were up on an absolute basis. A modest increase in noninterest expense compared to Q2 2015 reflects the cost of adding sales professionals over the past 12 months and a modest increase in incentive related due to do the higher revenue.

Looking at trends on page 18, and comparing Q2 last year, clients were comforted – excuse me, clients were confronted with increased volatility once again this quarter, with concerns around both global growth as well as the outcome of the U.K. referendum. However, despite concerns, companies still need to finance as well as store and move their money, and this is when the strength and diversity of our franchise is most appreciated by our clients. Average loans on a year-over-year basis grew $35 billion or 12%. Growth was broad-based across large corporates as well as middle market borrowers and spread across most products. Having said that, we slowed our construction-led commercial real estate lending a few quarters ago. Average deposits increased from Q2 2015, up 11 billion or 4% from both new and existing clients.

Switching to global markets on slide 19, the past couple of quarters are great examples of the importance of this segment to not only its clients around the world but also to our customers and clients in all our business segments. Customers and clients were able to live their financial lives better in Q2 because global markets delivered for them under challenging market conditions, helping them raise capital, buy and sell securities, as well as manage risk. We believe we increased our relevance with clients during Q2 and more specifically during the market volatility after the U.K. referendum. We did this by showing them that we will be there for them when they need us most. That we are there for them with consistent set of products and services at terms that make sense for our clients and our shareholders.

And therefore, then, with thoughtful advice as well as the capabilities, strength, and confidence to make markets and execute, all of this resulted in global markets reporting earnings of $1.1 billion and a return on capital of 12%, 13% excluding net DVA impact. Revenue was up appreciably year-over-year as well as linked quarter. Total revenue excluding DVA was up 8% year-over-year on solid sales and trading results and up 18% over a Q1 that saw challenging market conditions. Strong expense management drove expenses 6% lower year-over-year even while revenue was higher.

Moving to trends on the next slide, and focusing on the components of our sales and trading performance, sales and trading revenue of $3.7 billion excluding net DVA was up 12% from Q2 2015 driven by FICC. In terms of revenue, this was the best second quarter we have had in the past five years. Excluding DVA and versus Q2 2015, FICC sales and trading of $2.6 billion increased 22% as the improvement which began in late Q1 continued through Q2 as global concerns abated and central banks took further monetary policy actions. Improvement was across both macro and credit products driven by stronger rates and currency, client activity as well as improved credit market conditions.

Tighter spreads benefited mortgage, trading and municipal bonds outperformed treasuries with strong retail demand. Equity sales and trading was $1.1 billion, declining 8% versus Q2 2015 which saw significant client activity in Asia driven by stock market rallies in the region.

On slide 21, we show all other which reported a loss of $815 billion. This loss was driven by the current quarter's $974 million market related NII adjustment. The loss is lower than Q1 due to both a lower market related NII adjustment as well as the absence of retirement-eligible incentive costs.

Compared to Q2 2015, the difference is driven by a number of factors. First, the negative NII market-related adjustment in this quarter versus a large positive adjustment in Q2 2015. Second, we had reps and warranty recoveries in Q2 2015 related to a court ruling and gains on the sale of consumer real estate loans. Third, provision expense declined from Q2 2015 driven by continued portfolio improvement.

The effective tax rate for the quarter was about 29%, which is in-line with what we expect for the remainder of the year, absent any unusual items. And as a reminder, we still expect to record a tax charge of about $350 million, most likely in 3Q that reduces the carrying value of our U.K. DTAs as a result of the U.K. tax reform announced last year. The vast majority of this charge will not impact regulatory capital.

Okay. So let me offer a few takeaways as I finish. Q2 was another quarter of solid progress in a challenging global environment. While growth concerns persist in many countries, the U.S. economy continues to steadily improve, albeit at a less than optimum pace. The diversity and strength of our franchise makes us more relevant to clients and customers during times such as these, and you can see that in our results.

Clearly, interest rates affected our financial performance this quarter. Still, while we cannot control interest rates, we are not waiting for them to rise. We grew in this environment by focusing on the things that we can control and drive. We grew deposits, we grew loans, we managed risk well, reflected in reduced charge-offs. We delivered for customer clients in another challenging quarter, especially around the U.K. referendum. We invested in our future by adding sales professionals and continuing to deploy technology that improves customer satisfaction. We returned capital to shareholders and we announced plans to return increasing amounts. And we did all of this while we lowered expenses and drove operating leverage

Thank you. And with that, let's open it up for questions.

Question-and-Answer Session

Operator

[Operator Instructions]. We'll take our first question from Matt O'Connor with Deutsche Bank. Please go ahead.

Matt O'Connor

Good morning.

Brian Moynihan

Good morning.

Matt O'Connor

I had a few follow ups on the expense commentary. I guess first, though, just maybe what drove the timing of giving a three-year expense outlook? Is it acknowledging kind of lower for longer rates? Is it finding more opportunities, or what was kind of the motivation to give expense outlook for 2018 at this point?

Brian Moynihan

Well, Matt, as we looked at it, this is our current plan, so there's no new news for us in terms of how we operate the company. But what we saw is that people were not sort of getting the expenses right in the out years thinking that we could not continue the rate of investment and continue to bring down expenses.

Secondly, to make sure people understood it in terms of blending in LAS and putting it into the base. It's now become less of the contribution and now it's more the general expense base we're working on. So I think it was consistent with the way we're running the company but we want to make sure that people had clarity over the next six quarters and going into 2018 of where we think the expense base goes versus what we saw in some of your guys' estimates and stuff.

Matt O'Connor

Okay. And then I guess specifically, the $53 billion that you pointed to, does that include the first quarter stock expense of around a billion and some I assume nominal amount for legal?

Brian Moynihan

Yeah, it includes an estimate based on current views of both. That's all-in expenses for the year. Now they come in different quarters, as you just pointed out. We have it front-loaded of that, but – so this quarter did not include that I think it was about a quarter of a billion dollars plus a quarter when you think about the $13.5 billion this quarter. But overall, it includes the estimate for that out there plus the litigation estimate.

Matt O'Connor

Okay. And then just separately, if I can ask, we've had a couple other banks talk about loosening standards a bit on the consumer side. I feel like you've held your standards quite high, especially in credit card. But just any thoughts on appetite for loosening standards a little bit here, given the challenging rate environment and the economy still hanging in there?

Paul Donofrio

We've worked I think extraordinarily hard to transform the company, its balance sheet, its ability to produce earnings. We've got a customer and risk framework on the consumer side that is focused on prime and super prime. That strategy, I think, works for our shareholders and our customers and we're sticking to it.

Brian Moynihan

And just to give you a simple view of that, Matt, this quarter we did the highest number of new credit card originations we've done for a long time. And all of them are consistent with that risk appetite. So there's plenty of market share to gain there by just concentrating on current customers and deepening. And while people always ask the question you ask, the answer is there's still about seven out of 10 mortgage customers at Bank of America get their mortgage somewhere else that fit within our credit customers. There's plenty of cardholder that fit our credit parameters that are out there that don't have our card or aren't using our card as their primary card. And so just giving those couple of examples, there's plenty of market share to get there. So we don't need to change the standards to grow and you're seeing that come through.

Matt O'Connor

Okay. Thank you very much.

Operator

And we'll take the next question from Jim Mitchell with Buckingham Research. Please go ahead.

Jim Mitchell

Hey. Good morning.

Brian Moynihan

Good morning.

Jim Mitchell

Maybe I could follow up a little bit on the NII discussion. Maybe if you could help us think through – you talked about near-term kind of flattish, but as we think a little bit longer term, if the forward curve is realized and/or maybe give some color. You've had good deposit growth, core loan growth of 9% but net loan growth's only been about 2.5%. Do we start to see that inflect more? And does that start to help the out years as well? So just any color on NII beyond the next quarter or two would be helpful.

Brian Moynihan

Sure. Look, as I said in my comments, if rate follow the current path of the forward curve, we would expect with the extra day and the client long-term rates to be at around a $10.4 billion range in the next quarter. So...

Jim Mitchell

Right.

Brian Moynihan

But as you get out to 4Q and next year, I think we get more optimistic about being able to grow, given just our current pace of deposit and loan growth. We've obviously experiencing good deposit growth. We've got, as we talked about, a strong risk in client framework, so we'd like to put all of that deposit growth into loan growth. But we're going to only do so if it meets our criteria. Whatever deposit growth doesn't get absorbed by good loans with our clients obviously goes into the investment portfolio and we get a return there. So I think, look, it's just a question of the further you get out, the more that wave of deposits and asset growth kind of overwhelms the change in interest rates and we see growth.

Paul Donofrio

Also if you look at page six, you can see that – a point you made is that the inflection point was hit a few quarters ago where the sort of the non-core loans and leases were running down and not being made up by growth. We've passed that. And so as we think about it going forward, in the upper right-hand part of page six, you can see that other loan and leases balances coming down. They'll continue to come down but there's just less of them. And then if you look at the lower left, you see the core loans are growing at a good rate, have been growing a good rate now can come through. So I think your point about what give us encouragement because you saw it last year second quarter, this year second quarter about how even in a lower for longer rate environment we can grow NII is that you're actually are growing the net loan book pretty consistently now each quarter.

Jim Mitchell

So I guess you don't want to put too many numbers around it. But should we think that maybe starting in 4Q or 1Q, we might start to see some incremental NII growth; and maybe that accelerates – as you point out, the loan growth overwhelms the rate picture?

Paul Donofrio

I think we'd say that you got to be careful about your rate scenario, even on a spot basis because it can move around and move that around. But think about it as second quarter next year, you'd start to see this breakthrough again, based on absolutely no change in rates from the low point they were.

Jim Mitchell

Right. Okay. Great. Thanks.

Operator

And we'll take the next question from Ken Usdin with Jefferies. Please go ahead.

Ken Usdin

Hey. Good morning, guys. Just one. On the fee side, you mentioned all the great metrics in terms of the growth of activity and account growth and whatnot. But we're continuing to see declines year-over-year in card income, service charges and the brokerage business. So I was wondering, you can walk us through when do you anticipate some of the, kind of the building blocks turning into revenue? Or are there still some of the – kind of the spending or kind of competitive pressures building in underneath? So just kind of the outlook for some of those kind of core consumer and brokerage-related fee areas would be great. Thanks.

Paul Donofrio

Okay. Well, let's start with card. I think card actually is up on a linked-quarter basis, down year-over-year. But you have to remember, again, we had portfolio divestitures. So I think we're at the point now, we're not going to be seeing those sorts of divestitures in the future. And we start feeling better about more consistent growth around card.

If you look at brokerage income, we have been in a multi-quarter, trend of people shifting from brokerage to more managed accounts. That trend has obviously put pressure on the revenue line because at the same time that was going on, we had had a lot of volatility in the marketplace, lower overall capital markets, lower overall activity. But I think over time as – if capital markets continue to rise, we will get – we will offset that decline in transactional revenue.

Operator

Thank you. We'll take our next question from Glenn Schorr with Evercore ISI.

Glenn Schorr

[Audio gap] in terms of FA attrition? And then the second part is in Wealth Management, what specific products or behavioral changes are you putting in place ahead of the DOL rules kicking in in April?

Brian Moynihan

So on the first quarter, we haven't seen any change in attrition after retention. And most of the retention – most of the attrition experienced financial advisors have been more due to our change in our way we do the international business, which has been going on for about a year. But in terms of aggregate numbers, it's been relatively stable. In terms of the attrition we see is actually in the lower production levels, mainly due to people not being able to kind of build a book of business. And we're trying to fix that through the integrated business system with our consumer and preferred teams.

In terms of DOJ and the fiduciary standard, we're visibly implementing this. It's consistent with where we're going with the business. It's consistent with the move from an old view of what financial advisory was versus a managed money fee-based, loaded with a financial planning driven business. Admittedly it's a little tricky, because the actual rules only apply to the $200-odd billion of 401(NYSE:K) and retirement assets we have, but it's consistent with where we're taking the business and the team drawing we don't see meaningful revenue or changes due to that. We'll see meaningful changes to implemented, but not meaningful revenue changes.

Glenn Schorr

Okay. I appreciate that. And just a follow-up on the 2018 expense target, which everyone appreciates, it might be a silly question, but should – is it safe to assume that 2017 will be somewhere between 2016 and actual in 2018's target?

Brian Moynihan

Well, we've got – yes, it's a safe assumption. It's not a silly question. But we've got six quarters between now and then, and you can see what we're running at now to get it down to that level. It will take work every quarter.

Glenn Schorr

Okay. Thanks, Brian.

Operator

We'll take the next question from Steven Chubak with Nomura. Please go ahead.

Steven Chubak

Hi. Good morning.

Brian Moynihan

Morning.

Steven Chubak

So I hate to beat a dead horse on the expense question, but, Brian or Paul, I was hoping you could provide some more detail as to what specific expense levers you can pull to really drive that figure to 53 billion? It is a pretty meaningful delta versus the 56 billion run rate over the last four quarters. I'm just trying to gauge how those expense initiatives might impact revenues? And whether we should expect any revenue attrition as those additional initiatives take hold?

Brian Moynihan

Sure. So let me just back up a little bit. I will definitely answer your question, but I want to emphasize again, we're talking about LTM 56 billion going to 53 billion, absorbing in that merit, healthcare, inflation and other investment. And the first thing I would point out as you sort of think about the credibility of that, look at what we accomplished over the last five years. From Q2 2011 to Q2 2016 we have reduced quarterly expenses by $4.8 billion. That's a $19 billion annualized run rate. And we did this by not only reducing legacy mortgage related expenses, which were only make up $2 billion of that $4.8 billion, but just through good expense management in every major category across the company.

So from here it's about a number of things. A lot of those things have been identified through our simplify and improve initiative. We're investing in technology and capabilities to improve efficiency. The most obvious example of that you can see is in the increasing adoption of customers for digital channels. But I do want to emphasize that it is, you know – it is about making progress across the entire company from our leaders and our teams. So if you look in consumer, they're an example of the digital adoption. We've got mobile users of 15% over 2015.

When they make a deposit, that's one-tenth the cost. We've got digital sales up 12% year-over-year. We've got more customers using digital statements, a lot more work to do there with transition from paper to electronic. We are optimizing the coverage model in both consumer and GWIM, and they all have goals. We all have goals and initiatives around controllable expenses including travel, supply, support costs. If you look at global banking and global markets, we're simplifying our legal entity structure and business model. We're integrating wholesale credit origination and processing across the lines of business. We're centralizing data platforms. We're expanding electronic capabilities and we're optimizing the coverage model. So, you know, there’s a lot going on and we’re going to need all of it to get to our goals

Steven Chubak

Okay. So, Paul, from based on your comment, it sounds like it’s really going to be driven by technology and other efficiency initiatives. So there shouldn’t be any expectation that we could see any meaningful revenue drop-off or attrition in light of those actions that you’re taking?

Brian Moynihan

I think Paul gave you a lot of different places it comes from, but I think you have to back up and say it comes from reducing the expense base and by people. And you can see that even in markets, year-over-year we’re down 7% and people revenue went up. So it’s electronification of fixed income platform and the equity’s platform continue down that road. So every single area is moving here and then if you also have to think about the stability of the platform, this company has now been operating with a consistent strategy and a consistent ability to execute for many years. And what’s gone with the legacy and stuff that just allows us to keep operating on ourselves. And we always have performed best in history when we had that period of time no acquisitions, no divestitures, no legacy asset servicing.

So we’re very confident that it will happen. On revenue, I’d say look at it year-over-year, look at it linked quarter so last three or four quarters you’re seeing revenue is stable and well bounces around with market activity in a given quarter. The core revenue continues to go forward and the expenses keep coming down on a core basis. So we’re comfortable that there’s nothing – we won’t allow our people and our responsible growth to give us cost saves and not grow the business. So it has to be sustainable. It has to be actually taking out real work and yet still investing in more client-facing teammates, more salespeople and more technology capability for customers.

Steven Chubak

Thanks very much.

Operator

We’ll take the next question from Eric Wasserstrom with Guggenheim Securities. Please go head.

Eric Wasserstrom

Thanks. Just a couple of questions on auto and then one clarification on the OpEx guidance. I'm sorry to come back to that but on the OpEx, is it the 2018 figure where you expect to begin 2018 or end 2018?

Paul Donofrio

That's for the full year.

Eric Wasserstrom

For the full year. On auto, you underscored the origination quality and the high end of the FICO range, but one of the things that we're hearing from dealers is, is about the compression and pricing that's occurring in the high end ranges, some other lenders move up out of the mid-FICO range. And I wanted to see if that's something that you think you're experiencing or if you're in fact seeing some stabilization in the competitive area around high FICO auto lending.

Paul Donofrio

I would say we haven't experienced that. We can check and get back to you. I would – I would just make a couple more comments about auto. We are – we're maintaining our share, but we are very focused on the prime and super prime. And as we pointed out last quarter, we're booking these loans at FICO scores of around 70, 74. We've got debt-to-income at all-time lows, and importantly, we are not from a structuring standpoint extending kind of way we see in the marketplace.

Eric Wasserstrom

Thanks very much.

Operator

We'll take the next question from Mike Mayo with CLSA. Please go ahead.

Mike Mayo

Hi. Still more on expenses. This might be good news bad news. I guess the good news is your expenses over the last year, branches are down 2%, FTE down 3%, almost every expense line is lower. So that's good. And your efficiency ratio is down to 62%. But the bad news the way I look at it is over the last five years, your expenses are down a lot, but your core revenues are down even more. So what might resolve at least the issue in my mind? Do you have a specific efficiency target for 2018?

Paul Donofrio

Well, Mike, the – if you look at the risk adjusted revenue, you would come to a different conclusion. So, yes, we had a lot of revenue in 2011 or 2012, but the charge-offs were running tens of billions of dollars more a year than we have now. So a lot of that revenue was just going off the back end. So if you look at it from a risk adjusted basis, I think we grew from a low 60s to the low 80s over the last five or six years. So that is actually the work that gets done. So we could – going back a point, we focus on very high credit quality so we keep that credit cost moving in the right direction or stable when the world has gone a different way. We don’t have a target efficiency ratio.

You can calculate on of that out in 2018 because as we talked about earlier, the NII differences will be driven by where rates go to some degree. But the idea is we are going to take expenses from $56 billion in the last four quarters to $53 billion and we think that’s where we’ll get them to. And if rates stay stable or go up a little bit, you’ll see a lower efficiency ratio. Right now, we’re running about 62% this quarter fairly stated and we think we can push it down from here.

Mike Mayo

And I don’t want to take away – I think we collectively appreciate having a 2018 expense target, but if you just take the second quarter annualized, you’re at $54 billion, and then if you reduce your LAS expenses, you kind of get down to a $53 billion number. So if...

Paul Donofrio

Mike, you’re missing the FAS 123 and social security, which is $1.2 billion in the first quarter that doesn’t occur this quarter but you’ve got to add that back too.

Mike Mayo

Okay. That’s helpful. And you said a lot is anything on, and I think some other analysts tried to restate what you’re saying. But what are the three biggest drivers then of that reduction of what you might term a core expense base?

Paul Donofrio

It’s then people. We’re down 2,600 people quarter over quarter. It’s a constant reduction in personnel through hard work and automation while we’re continuing to increase the investment in salespeople. And so that helps on the revenue side and the revenue equation versus expense. It’s the things like our data center configuration. We’ve been in a program to take about a billion, billion and a half out of the data work, all the data centers and configuration that we're part way through. And in part it's just like Paul said, every line item is just grinding that. As we continue to bring down people, we have less occupancy, less telecommunications and everything else. So it really comes across the board.

Mike Mayo

And then lastly, should we expect a restructuring charge? Or do you pay as you go?

Paul Donofrio

We have consistently paid as we've gone, as you well know, and even in every quarter we have between $50 million and $100 million of severance expense that we don't even talk bout.

Mike Mayo

All right. Thank you.

Operator

The next question comes from Vivek Juneja with JPMorgan

Vivek Juneja

Hi. I won't beat the dead horse on expenses. Just a quick question on the card business. If I look at purchase volumes year on year, it slowed further from last quarter. Any color on what's going on there?

Paul Donofrio

Yeah, I think purchase volumes are up 7% if you normalize for the divestitures.

Vivek Juneja

Okay. But the divestiture happened in 4Q. It slowed from where it was. It was up 2% year on year in the first quarter, and it slowed to 1% year on year in the second quarter. So it seems to me a little bit of a weakening trend.

Paul Donofrio

I think we've had divestitures in 2Q last year and in the fourth quarter.

Vivek Juneja

I know. I am [indiscernible]. Those were both reflected in 1Q 2016 year on year growth rates. And I'm comparing growth rates...

Paul Donofrio

Let me just make it simple for you. The year-to-date through July is up – taking out divestitures, up 4% on debit and credit both and up 7% on credit card purchases normalized for divestitures year to year the first six months plus this part of July. So it's growing fine.

Vivek Juneja

Okay. Got it. Thanks.

Operator

We'll go next to Paul Miller with FBR and Company. Please go ahead.

PaulMiller

Yeah, thank you very much. On the LAS, so you now consolidate the LAS segment into pretty much the consumer segment. You still – the last on the appendix you said you had about 11,000 workers in that area where I guess continue to work through about 88,000 loans. Is that number – should that number continue to move down? Will we continue to see that move down? Or what's the thoughts behind that?

Brian Moynihan

Be careful because those 10,000 people work on the 88,000 loans plus the 3 million good loans. They service both good and not good loans, to make it simple. And so that's one of the reasons why we're separating. In all other going forward is the loans that we are actually only loans we'd never do again and that we're running off 600,000, 700,000 units. Moved into the segments whether it's consumer, U.S. trust, or Merrill Lynch are the loans that relate to their businesses in terms of servicing costs, too. So that was one of the confusions.

As this thing got down, you got the point where the good servicing costs are becoming a more meaningful part of the total. It'll continue on, because that portfolio, whether it's direct servicing costs for third parties or even the stuff on the balance sheet, will continue.

But to give you a sense, from first quarter, second quarter, we're down the total head-count of about 2,600. About 900 and change came from LAS from the servicing side. So it still contributes, but its contribution is going down each quarter, because the amount left to service the good stuff and just generally service our portfolio will be a higher percentage of what's left.

Paul Miller

Okay. And then you gave some guidance on where you think LAS expenses will be by the fourth quarter. And I'm not sure I wrote it down correctly, and I might have misinterpreted it, but was it close to 500 million you said? Or am I off somewhere?

Brian Moynihan

Yeah, so this quarter we ran about 600 and we said we'd get – a long time ago we said we'd get to 500 by the fourth quarter this year. So we're almost there, and the idea is that will be completed.

Paul Miller

So is 500 the run rate to service the good loans? I'm confused. Or is that still servicing the bad loans?

Brian Moynihan

Both.

Paul Miller

Both. Okay. Thank you very much, guys.

Operator

The next question comes from Brennan Hawken with UBS. Please go ahead.

Brennan Hawken

Good morning. Sorry to come back here, but I just hate horses. So I'm anything to take another whack at this thing. On expenses, what should we think about as far as your assumptions for legal and then some of your market-related businesses, market-sensitive businesses GOM and markets? Just because the expense line items in those businesses do have a pretty big impact from market conditions.

Paul Donofrio

So I'll start with legal. From a legal perspective, if you look over the last four, five, six, seven quarters, we've been running around 300 million per quarter. We did 270 this quarter. You know, that I feel like is a reasonable range if you're building a model for the near term.

And in terms of the Capital Markets businesses, I'm not quite sure I get your question. Obviously they are – that line is tied to the performance of the business. The total performance of the business, returns, earnings and revenue, and we have – we have programs in place that we think are competitive with what's on Wall Street so that we can attract the best of talent and retain the best of talent. We're constantly benchmarking against those programs, and we feel like we're where we should be for the quality and the market presence we have in those areas.

Q – Brennan Hawken

Overall, you should think about the environment we're talking about is an environment consistent where we are now from growth of 1.5%, 2% of U.S. GDP and stuff. So it doesn't contemplate any change in the current environment from just a general operating principle.

Paul Donofrio

Again, remember what I think Brian said and what I emphasized again, that 53 billion is absorbing increases in merit, absorbing increases in healthcare, investment that are just inflation that are just natural in the business.

Brennan Hawken

Right. I guess I was just – so you're saying that first of all on legal, the 53 billion includes roughly 300 million per quarter rate, and that your operating assumption for the GWIM and other market business would assume a revenue inflation and corresponding payout inflation from those businesses from here?

Paul Donofrio

Yeah, based upon our current plan.

Brennan Hawken

Got it. Got it. Got it.

Paul Donofrio

Within our current plan. And in terms of legal, I hope it's going to be less than 300 million when we get out there. I'm not telling you to stick that in your model, but that's a good range to be thinking about.

Brennan Hawken

Okay. That’s really helpful. Thank you. And one quick follow up on GWIM, you guys highlight a gain on sale, but could you talk about how much that impacted the margins in that business? And then whether or not there was any EPS tailwind there?

Paul Donofrio

Yeah, it’s – it was 80 billion of AUM again. That was all short-term. It had minimal impact on margins. Minimal.

Brennan Hawken

Okay. Thanks.

Operator

We’ll go next to Matthew Burnell with Wells Fargo Securities.

MatthewBurnell

Good morning. Thanks for taking my question. Paul, I wanted to follow up on the mortgage banking side of things. That was one of the areas you highlighted in terms of potential growth. Year over year the mortgage banking revenue was down fairly substantially. It seems like a lot of that was hedging gains and losses and things like that. But you also mentioned that you’re planning on keeping more mortgages that you originate on the balance sheet. Could you give us a little bit more color in terms of how you’re thinking about that going forward, both in terms of the mortgage originations being kept in the balance sheet and sort of how you’re thinking about mortgage banking fees?

Brian Moynihan

Sure. Let me – you’re right. MBI line was down year-over-year. That was planned for. We knew that was coming. I just want to walk – so for everybody else, I just want to walk through kind of why it’s down and then we can talk a little bit about going forward. So kind of four items. First, we sold an appraisal business last year, so there was revenue in last year’s second quarter that isn’t in this quarter. Second, we had some servicing sales in the second quarter of last year for a gain that we didn’t have this quarter. Third and probably most significant from a revenue perspective is that we have the ace decision in the second quarter last year, so we released last year some reps and warranties. That was a significant amount of benefit last year.

And then fourth and probably strategically most important in the point you're getting to is we are selling less mortgages choosing instead to hold them on our balance sheet, and obviously this decreases MBI but increases NII over time. So and plus you have to note that as we just talked about, servicing bad servicing is going to continue to run off. So if servicing is running off and not being replaced as fast, if we're holding more mortgages on the balance sheet as we transition from MBI to NII you could see that line continues sort of trend lower. In terms of the mortgages, you know, I think in the short-term, it's going to be fairly stable and that trend is going to this is a good base.

This quarter is a good base to sort of start from. I think that trend lower is going to be, you know, in some quarters very slow because as you point out other items – other line items are a little bit messy and bounce around there depending on what happens with interest rates.

Matthew Burnell

Right.

Brian Moynihan

But that's the trend. In terms of what we're trying to accomplish, all of the loans we originate that are nonconforming we would like to keep on our balance sheet. And even the conforming loans that have a certain characteristic we're going to be holding on our balance sheet. So right now that's around 75-ish percent of the loans we're originating are going on our balance sheet. Is that helpful?

Q – Matthew Burnell

Yes. Thanks. Thanks very much.

Operator

And we'll go next to Richard Bove with Rafferty Capital. Please go ahead.

Richard Bove

Hi. I apologize for going back to the net interest income issue, but obviously the reason why central banks keep interest rates down is because they expect it to increase lending. And I'm wondering if you have any elasticity studies which show what happens to loans when interest rates go down or up. And as part of that, there are multiple examples of what happens to earnings if interest rates go up 100 basis points or down. And I'm wondering if you have done anything to show if interest rates remain flat and loans go up 2%, 5%, 6%, 8% what the impact on earnings would be.

Brian Moynihan

Yeah, absolutely. On that last part of your question is precisely what I think we've been talking about today in the Q&A and in the remarks. We've got interest rates – we talked about interest rates following the forward curve. We talked about interest rates being flat. And despite both of those circumstances, we think in the out years we can grow NII or in the out quarters we can grow NII because we're growing deposits, and we're putting them to work where we can within our risk and client frameworks to grow well priced loans. Any amount of deposits that doesn't go to our clients and customers we're sticking in the securities portfolio and getting as much yield as we can get there within the constraints of liquidity and capital risk and interest rate risk.

So we think we can grow in even a flat interest rate environment, grow the NII line not necessarily in the next quarter but as we again move out into the future. Brian has already pointed out all the work we're doing around expenses, so when you combine what we think we can do from a fee base, from an NII perspective and lowering expenses, we think we can grow earnings of a company even if interest rates are flat.

Richard Bove

What I'm asking is a lot more specific in the sense that you do this with interest rate changes, right? In other words, there's these bubble charts which show what will happen to net interest income if interest rates go up 100 basis points. There's nothing which says what happens to earnings if you see a 5% increase in loans. In other words, what is more important? I mean, in the old days, people would show these charts if you hold interest rates flat and volume goes up, what happens to earnings if you get a 5% increase in lending as a result of interest rates staying so low?

Paul Donofrio

Yeah, I get it, Dick. You're right. I mean, we tend to talk in our disclosures about interest rates moving 100 basis points, 50 basis points, and holding all else kind of equal what's in our plans.

We could just as easily do the opposite. We could hold interest rates flat and then you could see the effect of deposit and loan growth. We certainly have that analysis. That's how we arrive at our perspective on the future. And I think if that's something that interests you, maybe after the call, we can kind of share with you some of that work. It's just math.

Richard Bove

Yeah, no, the reason why I'm interested is because the whole discussion that we now have is that interest rates are staying flat, and therefore, bank earnings cannot go up because the other side of the equation which is what happens to volume when interest rates go down is just not discussed at all. So I'd love to talk to you more about it.

Paul Donofrio

Yeah, okay. That'd be great.

Operator

Okay. Next we'll go to Jim Mitchell with Buckingham Research.

Jim Mitchell

Oh, thanks. Just a quick follow up on the capital ratios. Paul, we saw a pretty big improvement across you and your peers in PP&R on seemingly lower op risk hits, particularly legal. Do we start to see that factor into the advanced approach calculation? You guys get punished pretty hard on op risk in the advanced approach. Do you start to see some, I guess some light at the end of the tunnel of being able to reduce that, given all the reductions in legacy risk assets that you've seen?

Paul Donofrio

Thanks for noticing. So let me start by saying that we are very pleased with our results in CCAR this year. And we believe they really do reflect all the hard work we've been putting into that process and improving capital planning.

Operational risk, we have a third of our advanced RWA roughly is operational risk. And we would characterize most of that, Brian might say all of it, as for businesses we're no longer in, products that we no longer sell, and risk that I don't think we ever took as a basic Bank of America. So there's a lot of RWA sitting there, and we have to work overtime to show the regulators that we can get that down.

Jim Mitchell

But this – you're not – there's nothing to read into the results in CCAR yet anyway?

Paul Donofrio

No, I don’t think so. I mean, obviously CCAR is on a standardized basis, so it doesn’t incorporate operational risk.

Jim Mitchell

No, no. But in the PP&R, they obviously made that point that...

Paul Donofrio

Yeah, you’re right.

Jim Mitchell

Okay.

Paul Donofrio

You’re right. I think they improved their models. I mean, I don’t know, but I think we’re all kind of looking at what they’ve done and trying to understand it, and I think they probably improved their models a little bit around op risk and there was a little bit less across all the banks. I think the banks that had the most maybe benefited because it was more of an average type of thing.

Jim Mitchell

Right.

Paul Donofrio

So maybe we got a little extra benefit in that. But I don’t know, to tell you the truth. We don’t know what’s in their models.

Jim Mitchell

Right. So it’s just a little too early to see any kind of spillover benefits yet?

Paul Donofrio

Yes.

Jim Mitchell

Okay. Thanks.