Good morning. This is Sharon Yeshaya, Head of Investor Relations. During today's presentation, we will refer to our earnings release and financial supplement, copies of which are available at morganstanley.com.

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I will now turn the call over to Chairman and Chief Executive Officer, James Gorman.

James Gorman

Hi, good morning, everyone. Thank you for joining us. In the second quarter, we achieved 9% ROE reflecting the stability of many of our businesses, which offset a relatively difficult trading environment. In many ways, this quarter provided a robust test of our business strategy. Whilst many trading businesses are affected by benign markets, characterized by low volatility and the absence of meaningful macro events, other business lines demonstrative resilience.

Investment banking showed continued strength, reflecting diversity of our global M&A and capital markets franchises. Investment management, saw asset inflows and solid performance across alternatives. As a result, this business saw improved revenues and returns.

Wealth management performed at the high end of our 2017 target, achieving 25% pre-tax margin and a record profit before tax of over $1 billion. It is worth noting that in the first year after the acquisition of Smith Barney, wealth management generated approximately $1 billion to pre-tax profit annually.

Compensation expenses are in line with our stated targets and higher accruals year-to-date reflect higher revenues. Non-compensation expenses, include one notable item, which Jon will take you through in a moment.

Given the obvious headwind this quarter, we're pleased to have generated respectable return to shareholders, albeit at the bottom-end of our target range. Of course with the firm now on solid footing, [performance] (Ph) could still materially improve in the years ahead assuming constructive markets.

In addition, there are three tailwinds worth calling out, each of which has the potential to impact our long-term performance in a material and positive way, capital, tax reform and interest rates.

On capital, this year through CCAR, we asked for and received approval to buyback up to $5 million of stock and increase our dividend to an aggregate of $1 per share annually. While we intend to invest in our business as opportunities present themselves, we're determined to use any excess capital to continue to reduce our share count.

Much has been told through adjustments as some of the Doug Frank rules that were put in place over the past eight years. It is fair to say that now is the time to make some practical changes for the multitude of regulations. These changes would allow U.S. banks to be greater engines of economic growth.

Second, U.S. corporate taxes are too high. If the administration in Congress can achieve a sensible realignment of tax rates with other major developed economies, then that would be a clear positive for our business and corporate America in general.

Finally, as the major U.S. depository we have endured historically low interest rates for a very long time. Each move when hiring rates assuming a measured path should benefit our business. In summary, in the second quarter we showed resilient in a challenging market. In a more favorable environment, we should see better results.

More interesting to us though, of a long-term impact as some of the changes just described. We've built meaningful operating leverage in our business, while we remain cautious in the near-term, we launch our business mix and remain bullish on the long-term outlook for the firm.

I will now turn the call over to John to discuss the quarter in greater detail. Thank you.

Jonathan Pruzan

Thank you and good morning. The optimism that characterized the first quarter was replaced with a more subdued tone amongst clients for the majority of the second quarter. Activity was more sporadic in market sensitive businesses particularly within fixed income were impacted. That said, we supported our clients when market opportunities presented themselves.

Equity sales and trading and investment banking produced strong results. Wealth management and investment management both witnessed continued growth and stabilized our headline performance. Firm revenues were $9.5 billion, down 2% compared to a strong Q1. PBT was $2.6 billion, EPS was $0.87 and ROE was 9.1.

Non-compensation expenses were up approximately $138 million or 65 quarter-over-quarter. Well over half of the increase was due to a provision that we recorded as a result of a self identified item relating to that on inter-company services provided to our UK operation.

We also saw some seasonal increase in professional services, marketing and business development and higher volume driven expenses. We continue to exercise compensation expense discipline, which led to a 1% sequential decline in total non-interest expense.

On project streamline, virtually all identified projects are in flight and we are on-track to complete the target outlined at the start of last year. Compared to the same period in 2016, our 2017 year-to-date revenues have increased by over $2.5 billion. In the same period, our non-compensation expenses have increased by about $300 million and total expenses by approximately $1.3 million in the same comparison.

As a result, our year-to-date efficiency ratio of 72% is approximately 300 basis points lower than the same period last year and remains well inside the 74% target for the full-year. That said, we recognize that expenses in any one quarter maybe impacted by business mix, geographical mix, seasonal patterns and other factors.

During the remainder of 2017, our focus will be on completing all remaining initiatives and making sure that the culture of costs discipline represented by project streamline remains best practice. This will help ensure that the savings achieved to-date remain permanently out of the expense based.

Now to the businesses. Net revenues across institutional securities businesses of $4.8 billion were down 8% sequentially. The trading environment slowed from the first quarter, market moving events were episodic, volatility in many asset classes hit multi-year lows and activity was sporadic. Despite the quarter-over-quarter decline revenues across ISG were strong.

Non-competition expenses were $1.7 billion for the quarter, up 6% sequentially driven by the UK VAT expense, as well as higher execution related costs due to a shift in business and geographic mix of client activity.

Compensation expenses were $1.7 billion with the compensation to net revenue ratio of approximately 35%. In investment banking, both advisory and underwriting performed well revenues of $1.4 billion were unchanged versus the first quarter. This result contributed to an exceptionally strong first half of the year.

Advisory revenues for the quarter were $504 million, up 2% sequentially. Broadly M&A volumes remain healthy. The fundamental drivers of activity including challenging organic growth remained in place encouraging client engagement.

However, we have seen a decrease in larger transformational deals on a year-to-date basis compared to 2016 as the current market environment is impacting management's decision to act. Additionally uncertainty over taxes, regulatory reform and the broader political landscape will likely weigh on activity. As such, we remain cautious as we look towards the rest of the year.

Turning to underwriting, our continuation of stable capital markets with low volatility and range down credit spreads contributed to another strong quarter for underwriting. Overall, equity volumes continue to recover from the weak level seen last year particularly in Europe. The market was receptive to both IPOs and follow-on. We generated equity revenues of $405 million, up 4%. We expect activity levels to remain healthy although near-term issuance windows maybe impacted by macroeconomic uncertainties and a typical summer slowdown.

Fixed income underwriting revenues decreased 5% sequentially to $504 million, a market wide decline in volumes relative to strong first quarter was partially offset by market share gains across both investment grade bond and high yield financing.

Our sales and trading performance was solid, the post election excitement that began to slow towards the end of the first quarter did not reassert itself for most of the second quarter predominantly impacting our fixed income franchise.

However, activities saw a notable uptick towards the end of the period as rates felled off. This contributed to our overall performance and underscores the strength and resilience of our franchise.

In equities, we retained our leadership position and expect to be number one globally with revenues of $2.2 billion, up 7% sequentially. Strong prime brokerage revenues aided by seasonal factors contributed to the sequential increase.

We continue to witness growth in client balances positioning us well in this business. Derivative revenues remain solid. These gains were partially offset by lower cash revenues driven by lower volatility. Once again, our diversified strategy and global footprint benefited from pocket to regional strength. In the quarter we saw a very strong European activity as well as increases up in Asia.

Fixed income revenues in the second quarter were $1.2 billion down 28% versus a very strong first quarter and 4% versus a year ago. Historically, low volatility, a rally in interest rates over most of the quarter and fewer market events contributed to a slowdown in overall performance, while the revenue showed a sequential decline given the market backdrop, we're pleased with the results.

In our credit businesses revenues were down quarter-over-quarter driven by lower levels of activity. Our securitized products business also witnessed a decrease in revenues compared to last quarter, as the frequency of larger transaction slowed.

Within macro, our rates businesses were negatively impacted by low levels of volatility. This was partially offset by foreign exchange in emerging markets where discreet geopolitical events and pockets of volatility lead to stronger revenues. Commodities saw a sequential decline as there were fewer structured deals in the quarter.

While the environment did weigh on the results, this quarter revenues underscores the progress the business has made over the last 18 months. Since we restructured our business in 2015, we have experienced various market backdrops. Clearly, some have been more favorable than others.

We are encouraged by the consistency of recent results and are critically and credibly sized to service our clients as the backdrop evolves. Average trading VaR for the period was $51 million up versus $44 million last quarter. We deployed capacities to support accretive client opportunities.

Now turning to wealth management, which reported another record quarterly revenue and pre-tax profit result. The revenue and margin achievements underscores the businesses ability to benefit from the scale of the platform. These results were achieved despite a normalization in activity following a strong first quarter as retail sentiment reflected the same uncertainties faced by our institutional clients.

Second quarter revenues were $4.2 billion a 2% sequential increase. The PBT margin 25% slightly above our full-year 2017 target range reflected growth in fee based revenues and operating leverage. Client assets grew 2% to $2.2 trillion, fee based assets increased 4% to $962 billion were 43% of total client assets.

While the department of labor fiduciary rule has contributed to these fee base close, the majority of the movements have been from non-retirement accounts, reflecting client's choosing the enhanced service levels provided by this offering. We saw strong fee based asset flows of $20 billion.

Higher asset levels and positive flows contributed to asset management revenues of $2.3 billion representing 5% growth relative to the first quarter. Net interest income of $1 billion was up 2% over last quarter, that benefit a higher rates and lending balances was partially offset by lower deposit levels. This reduction in deposits reflects both typical seasonal client tax payments and deployment of cash into the markets.

NII was further negatively impacted by higher prepayment amortization. Wealth management lending in the U.S. banks grew by about $3.5 billion in the quarter or 6%, as clients drew on their SPL lines to manage liquidity needs, a trend we often witnessed in the second quarter.

Year-to-date our NII of $2 billion is up approximately $340 million or 21% compared to the same period last year. While market expectations for additional rate hikes have lessened. We remain comfortable with the full-year NII guidance provided in Q1. In particular, we expect to continue to benefit from further lending risk.

Transactional revenues of $766 million were down 7% from Q1. While clients deployed cash into the market, the frequency of trading captured in brokerage accounts decreased from the previous quarter. Again, mimicking the pattern witnessed in the institutional space. Lower mark-to-market gains on our deferred compensation plans were also a driver of the sequential decrease.

Total non-interest expenses were essentially unchanged versus Q1 highlighting the operating leverage in this scale business. Lower compensation expenses were offset by seasonally higher marketing and business development and professional services expenses. The compensation ratio was below our full-year target of 56%.

Looking forward, we remain optimistic about the outlook for this business and the value of its contribution to the firm's business mix. Annuitized revenue continue to grow with fee based assets and increased loan balances. Additionally, our investments into improving our digital capabilities will enhance future productivity and provide more operating leverage to the franchise over time.

Investment management witnessed a solid quarter with strength across both asset management fees and investment results. Total net revenues were $665 million up 9% quarter-over-quarter. overall, AUM grew 3% to $435 billion driven by investment performance with particular strength across our active equity strategies. We also saw positive flows across our equities, fixed income and alternative businesses with strong capital raising internationally.

On the back of higher AUM, we saw a commensurate 4% growth in asset management fees to $539 million. Investment revenues were up 28% to a $125 million driven by gains in our infrastructure and real estate funds. Despite the 9% revenue increase, overall expenses were up only 3% quarter-over-quarter.

Turning to the balance sheet, on a sequential basis total spot assets of $841 billion were up $9 billion and average assets were up $12 billion reflecting continued support of client activities within the sales and trading businesses. Our pro forma fully phased in advance RWAs are expected to be up approximately $22 billion versus the first quarter to $381 billion driven by higher market RWAs consistent with the increase in VaR metrics over the quarter.

As a result, our pro forma fully phased in Basel III advanced common equity Tier-1 ratio decreased approximately 70 basis points sequentially to 15.9% which remains in line with our pro forma fully phased in Basel III standardized common equity Tier-1 ratio. We continue to expect the two ratios to remain relatively close in the near-term. Our pro forma fully phased in supplementary leverage ratio for the quarter remained at 6.4%.

During the second quarter, we repurchased approximately $500 million of common stock or approximately 12 million shares. Our tax rate in the second quarter was 32%, we continue to expect our tax rate for the remainder of the year to be in the 32% to 33% range.

This quarter's results reaffirm that our strategy is working. As James said at the outset, this quarter represented an important test of our model. Notwithstanding a challenging trading environment we achieved a 9% ROE on account of our balanced business mix and the resiliency of the franchise.

However, investors slightly remains fragile. The same questions that lingered around timing and achievability of the administration's policy initiatives at the end of the first quarter remain unresolved as we enter the third quarter. In addition, the market continues to grapple with mixed economic data and questions around the timing and pace to monitory policy tightening. This dynamic may continue to weigh on activity and sentiment in addition to typical seasonality in the summer.

At the same time, we should not lose focus on the broader macroeconomic issues that could have a materially positive impact to our business. After years of headwinds for the industry, we are finally starting to see some tailwinds that can be promising for our business in the long-term including the potential for tax reform, sensible regulatory change and a rising interest rate environment. We are confident that we will achieve our stated goals.

With that, we will open the line for questions.

Question-and-Answer Session

Operator

[Operator Instructions]. And our first question comes from the line of Glenn Schorr with Evercore ISI. Your line is now open.

Glenn Schorr

First question on wealth management, I noticed the deposits down 7% I think, sometimes its seasonality and then sometimes it's cash deployment. I'm just curious, how you attribute some of that and also if this is late competition and what we expect on deposit data, if there are more rates hikes?

James Gorman

Sure Glenn. I think as I mentioned in the script, it was a combination of both. Clearly, we normally see in the second quarter PBT deposits going down, because of tax season. We also saw continued deployment into the markets. I don't think, we have seen a lot of deployment into other cash product. So again from a competitive dynamic, I don't think it's a rate story, I just think it's an opportunity story.

We've started a couple of quarters ago initiating some other strategies around the deposits including premier cash management product and some CD products and we've got a couple of billion dollars in those products. So we feel good about the overall deposit franchise and the overall ability to fund that business as we continue to see growth in the asset side.

Glenn Schorr

So maybe bluntly, if we get a couple more rate hikes do you capture the majority of it - even without as us said a rate story. Do you have to hike along the way or are the clients looking to participate in that move-up?

James Gorman

I think the best indication of how we feel about that is really looking at the NII line, which is as you know has been a very good story for us. All right, back in 2012, we had a $1.6 billion of NII in wealth business, last year was

$3.5 billion grew more than $500 million. In February, we talked about what we thought we would see and we thought we would continue to see good growth in the NII line, albeit at a slightly slower pace. Year-to-date were at $2 billion, which is up over $340 million over last year.

So again, we feel very confident about that story, it is reliant on the lending growth, which we saw a good growth across all the product this quarter. So we feel good about that, I think the composition is a little different, your comments about betas, generally the betas have lagged what we've modeled. So that's been a positive, we've also, if you go back to the first quarter, remember what the curve looked like, I think we've gotten rate hikes faster than we thought back then.

On the other side of the ledger, you just mentioned the deposits are down. So, we brought down the liquidity pool in the banks as well as started to use other savings and deposit products as well as some wholesale funding to support that business. And then lastly, we clearly, we didn't model any pre-payment acceleration that we saw in the second quarter as rates went down. So on balance, we are very confident with where we are on NII and it's been a good story, but the composition has been a little different.

Operator

Thank you. And our next question comes from the line of Brennan Hawken with UBS. Your line is now open.

Brennan Hawken

Good morning. Thanks for taking the questions. So, first on [Indiscernible] really again encouraging to see the sustained stability, say that a few times - now that clearly you demonstrated some stability here after the repositioning. Has there been a shift in mix. Can you give us a sense for the different business lines now that the business has been adjusted and can you also - I know you mentioned Jon that commodities were down sequentially, but was this quarter extraordinary from your perspective we've heard some mixed things from some of the competitors some additional color there will be great. Thanks.

Jonathan Pruzan

Sure I'll try. You know I think the way I would look at it is the results clearly just reflect the environment that we were operating in. if you look over year-over-year the results are pretty flat. So, when we look at the individual product mix, as I did mention our rates business given the low volatility is down, yet our FX did a little bit stronger particularly in the emerging market areas.

Credits were hung in there, less movement in credit spreads this quarter, but again comparable type of results in light of effected the year-over-year results were essentially flat. So we feel good about the business, commodities are also down a little bit, less activity and a tighter trading band there, but the results reflect the moves and the changes that we made and the results reflect that the business is really starting to come together and jelling and I think we feel pretty good about the results in light of the environment.

Brennan Hawken

Right. So I guess from your perspective paraphrasing you said that commodities were tough, but not necessarily extraordinarily difficult or remarkable in that way?

Jonathan Pruzan

Yes, listen the commodity business that we have has been totally reshaped and resized, more traditional sales and trading supporting our client base. It's a smaller contributor for us. So the movements are not that dramatic.

Operator

Thank you. And our next question comes from the line of Steven Chubak with Nomura. Your line is now open.

Steven Chubak

Good morning. So, wanted to started up with the question on wealth management and pre-tax margin, certainly encouraging to see that you guys eclipse the 25% target for the quarter. I'm just wondering as we look ahead to the second half, given a number of favorable trends for the business that Jon you had cited whether it's strong fee based conversions, healthy loan growth and NII expansion. I'm wondering barring any market exogenous market shocks whether you can sustain margins above that 25% target for the remainder of the year.

Jonathan Pruzan

Listen, I think you highlighted what we think is driving that margin. Right now, with the rates and higher markets those are good trends that will drive our asset base fees as well as our NII, our lending growth has been solid, I think the one area of potential volatility or softening is around transactional. We are heading into the summer months, but again, I think the tailwinds for this business are very good. We saw really nice operating leverage here, we saw really nice growth across all products in the lending book and we feel very good about the results, I mean the PBT at $1 billion plus is obviously a record and it's a really important contributor to the overall franchise.

Steven Chubak

Thanks and just one follow-up on capital. You guys had outlined a couple of the potential benefits to your business in terms of capital release that were outlined in the treasury white paper. One of the areas that's getting quite a bit of focus is this notion that the prospects for cash and liquid assets to be exquisite from the SLR denominator. And I'm wondering given the Tier-1 leverage constraint in CCAR of 4% appears to be a binding constraint for the moment. It's not clear weather that carve out is going to apply to that measure. I didn't know if you had had any feedback from regulators as to whether they were considering that possibility and what that might mean for you guys in terms of capital release?

Jonathan Pruzan

On the first part of the question I think clearly the reform around SLR would be helpful for a variety of reasons whether or not it's our binding constraint this quarter or next quarter is certainly not a foregone conclusion. So there could be some benefit from that but we also think there is just general benefit with that calculation in terms of what it means for their overall sales and trading businesses. But I do think there are several changes have been discussed or that are being discussed that would clearly help our position including around the balance sheet and how you think about capital actions going forward.

So I think it's a little early on 2018 CCAR to sort of have a prediction, but clearly we were pleased with the results, if you look back at year ago where we were versus what came out of the report a couple of weeks ago with a 100%ish payout and a 33% increase in capital return and a clean report we're very pleased.

James Gorman

I would just add on the leverage ratio, specifically, we have argued for a number of years and present to regulators for a number of years that the fact that a balance sheet growth during the time of financial stress is hard to understand how that happens. As such depreciate assets run off, new businesses not gathered, it would be hard to imagine in fact during the crisis in the years following of our own balance sheet obviously shrink dramatically both through our actions and through market activity.

So the leverage ratio constraint is made more acute by the fact that the denominator is growing at I think it's about 4.5% a year for the nine quarters. There being quite a lot of sympathy to that view that if we should look not at some blanket growth rate, but what actually experience was during the crisis and during other periods of financial stress. And I think that experience would largely hold up the balance sheet shrink.

So if you just held our balance sheet flat for that time period, that would have a material impact on our leverage ratio. So I think there is certainly a good dialogue going on through the treasury white paper and with the regulators on that topic alone.

Operator

Thank you. [Operator Instructions]. And our next question comes from the line of Guy Moszkowski with Autonomous Research. Your line is now open.

Guy Moszkowski

Good morning. Just looking at the VaR and the [indiscernible] metrics, which you talked about and floated up on average basis, I guess it's about an 8%, depending on which one you look at. So could you give us a sense for given that those are average daily I guess metrics. What we look like at on a spot basis towards the end of the quarter, should we be expecting that these things will close down again?

Jonathan Pruzan

Sure. A couple of things. So on the VaR metric, obviously the 51 million was the average for the quarter. If you have queue, it was actually 57 at period end at March 31. So that actually came down overtime and it has actually continue to come down and the spot period end will be lower than the 51 that we said.

On the RWA comments, actually some of the calculations are daily average volumes, some of them 12-week averages. And the VaR metrics are important in those calculations. So I think the same trend that we've seen in the VaR would be consistent in terms of how we finished out quarter end in that metrics. With the ratio that we have at CET1 even at the 16 or 59 level, we're still obviously very, very strong in terms of our capital positions.

Guy Moszkowski

Great that's helpful. And then just my follow-up question is more targeted on SIC. Specifically given the success that you have had in generating revenue even in a period like the one that we just had which was certainly weaker characterize by low vol, et cetera on the things that you have said.

Would you consider raising your quarterly average expectation from that $1 billion number that you've been talking about for quite a while now?

James Gorman

Guy, I'm surprise, it took somebody this many questions to get to let's trace the targets discussion. We just went on the pre-tax margin a few questions ago. I think the short answer you know and it's no. We've been pretty consistent, we took these targets for proof of business model for this year. We're going to stay with them. We think, listen, we were - recall certain fourth quarter 2015, we were doing 500 million and 600 million in SIC first quarter of 2016, I think if memory serves its about 800 million.

A billion dollar number on a study run rate basis is a good number with 25% less people much smaller organization, much more focused organization. If we consistently do better than that and that's terrific. But I don't think, the point of setting the target to establish, what we needed to prove to ourselves on an average run rate for the business to justify the expenses in capital balance sheet that we put behind it at that level. Everything we do better than that with the same expenses capital and balance sheet is obviously a gift.

Operator

Thank you. And our next question comes from the line of Jim Mitchell with Buckingham Research. Your line is now open.

Jim Mitchell

Good morning. Maybe a follow-up in the SLR and the treasury report. If we assume that both the Tier-1 leverage ratio and the SLR treated similarly by exempting cash and maybe short-term treasuries. How do you think that impacts the business, I guess, I think a lot of people are asking the question of? Is this a revenue opportunity to kind of re-expand the business whether it would be REPO or other businesses or is it really more of an excess capital story. Just trying to get a sense of, if you think business has been held back by the SLR?

James Gorman

Let me tell start with and Jon might want to add to it. First and foremost this is a capital question. We believe, we are over capitalized. There were good reasons for that several years ago as we were coming out of those financial crisis, we had a dividend of $0.05 a quarter, we've raised that four years in a row to $0.25. Our initial buyback program was zero then went to $500 and it's now all the way up to $5 billion over five year period. And our payout ratio is closing in on 100%. So we clearly believe that we are over capitalized and for good reasons we were coming off the crisis and we needed to shore up our defenses.

There is plenty of opportunity for business expansion with the amount of capital we have today. The more fundamental issue is what is the right level of capital this firm should hold. Are we holding too much capital, because the way the leverage ratio is being constructed, what is the right denominator for the SLR, in fact what is the right ratio. In Europe it's 3% of the balance sheet and that the growth of balance sheet. In the U.S. they took the [indiscernible] balance sheet ratio of 5% and attached it to this SLR balance sheet from Europe. So we sort of ended up with a fairly [draconian] (Ph) answer.

I think let's start with number one, if the trades in other type securities can be taken out of the SLR that obviously make sense. Number two, to not gross up the balance sheet under the core leverage ratio make sense. And I think we have capacity at that point both for further capital distributions and for sensible business growth. You saw the RWAs bounce a little bit this quarter, that was consistent with sensible business growth, there was opportunity clearly Tier-1 capital ratio is another constraint or no way near it. So that's the RWA constraint is not there for this firm at the moment.

Jim Mitchell

Okay. That's helpful. And maybe as a follow-up on just the treasury report generally. Is there any other aspects of the proposals that you would be particularly helpful for your business?

James Gorman

I'm trying to remember all the aspects of the report, but I actually can't do off the top of my head. I think clearly, I think there is a general recognition from the regulators all the way through the treasury that the Volcker Rule as it play out overtime straight a fair bit distance from Paul Walker initially envisaged, which was a simple restriction on the amount of capital put into proprietary invest and proprietary trading and but then frankly constrained on the ability of institutions to make markets and effective market liquidity. So I think the treasury reports spoke about that.

There was reference to the fact that the banks are required to continue their payouts, not withstanding there in the period of financial stress for nine quarters, no bank board would authorize continuing on buyback program during a financial crisis, that clearly wouldn't happen. You could holding the dividends static, but certainly the buyback shouldn't be and that would have material effect on the institutions.

So our approach has been and we've talked about this somewhat publicly recently, let's focus on a few things that don't require major legislative change, let's see the basic architecture of Dodd-Frank in place. Let's focus on some sensible changes, because we've now had eight years of experience and digest and see what worked and what didn't. And the cumulative effect of a lot of these regulations in some cases end up if you will with a double counting. And I think the spirit of the treasury report reflected that. I think they are focused on sensible pragmatic change, they are not focused on trying to redo the whole legislative agenda. And I think that's the right approach.

Operator

Thank you. And our next question comes from the line of Devin Ryan with JMP Securities. Your line is now open.

Devin Ryan

Hey, thanks. Good morning. Maybe first here just in wealth management, you've recently outlined the digitalization strategy, which was very helpful and with respect to the [robo] (Ph) offering, it sounds like you're not going to be able to focus on the children of the existing clients and some lower balance accounts which does seem to mark us with this generation of wealth transfer coming here and where the money is going to be over the next several decades. So as we think about that process, how do you protect against maybe some cannibalization of existing business as clients look at the lower price point. You know I guess the question is a revenue opportunity here just much more of an offset or do you just not think this as something that would appeal to some of your existing higher net worth clients for a portion of their accounts, it's a just a different bucket.

Jonathan Pruzan

Yes, I think that your description of what we're doing on the digitalization and the robo strategies is pretty accurate. Listen, we have a business that is built to cater to clients with wealth. Those wealth clients want advice, they want personal advice, we're seeing it as we see the brokerage fee base flows coming out of brokerage into the fee based accounts. Obviously digital is going to be an important part of that strategy, but the digital only client is not someone right now that would generally be interested in the types of products and services that we have.

We think the digital strategy is going to be important for both revenue opportunities longer term but also optimization and efficiency around what happens in a branch and how we free up people's time to spend more time with their clients. So overall it's a strategy that's going to be built for the longer term but the thesis of our business is around providing people with personnel advice around their wealth and their planning.

James Gorman

I would just like to add to that because it's an important question. We actually saw this maybe once before in 1999 when the direct players came out and the big fear was cannibalization. That would only have held true if people actually didn't value the financial advisors and advice that we're getting from those advisors. And it didn't play out that way. The reality is the marketplace has different segments based on consumer preference and I think the digital strategy makes all the sense in the world. That's clearly a segment whether they change their behavior as they become wealthy remains to be seen. But there is clearly a segment that wants to deal digitally just as so the segment that wanted to deal through direct brokerage trading and so on.

But on the price sensitivity, it's interesting, I think I'm right in this. If you look at the average basis points paid from the various robo platforms, they range in general like things from something like 20 to 40 basis points. If you look at the average basis points for a full service advisory like us, just divide our revenue into our assets including everything, you get somewhere in the 70s, low 70 basis points. So the value added of the financial buys and the institutions behind it and the research, the product offering, the new issued calendar you could argue is being putout there for 30 to 40 basis points.

It's not clear to me that, that is such an expensive gap that that's going to lead to the cannibalization issues. I think it's more that we just need a very compelling digital platform to deal with clients who want to deal with Morgan Stanley, but want to deal with us digitally and don't want to deal through a traditional wealth management advisory relationship. That's an exciting opportunity for us, frankly given our brand and add technology capabilities.

Devin Ryan

Okay, great. That's great color, looking forward to seeing it. Maybe an equity is trading here, we're six months away or within six months of method to in Europe I'm sure there is lot of corporation at the firm right now. So just curious with respect to expectations there, is this something that you feel like it will weigh on the research fee pool, but you'll pick it up in trading market share or just Morgan Stanley is going to take market share of the overall equities pool. I'm just curious kind of how you would frame your expectations right now, this is we're getting pretty close to be implementation?

Jonathan Pruzan

Yes. Well, I think, as you know, we've been preparing for a while both in terms of dialogues with clients, but also systems and technology related investments that we needed to make. But I would tell you, it's going to be very hard to estimate what the impact of this is. Any time you have a change of this magnitude where you just sort of flip a switch. We would expect the potential for disruption to be pretty high, how would affects longer term structural markets, it's still up in the air, we've global clients to already doing this.

We have global clients, so we're going to probably adopt it in all the markets. Even though, we don't expected to be adopted in the U.S., we have some clients [indiscernible] off that European operation. So how it all plays out is certainly unclear. But given the fact that we are number one in the world in this business and we have a full service platform and intellectual capital and product. There is consolidation in a number of counter parties. We would expect to participate in that, but I think it's a little early to make a call here and trying to estimate the impact is also probably a little early to make a call.

Operator

Thank you. And our next question comes from the line of Chris Kotowski with Oppenheimer & Company. Your line is now open.

Chris Kotowski

Yes. I mean recognizing the excellent outcome that you had in the CCAR capital return process. I have to say, I was surprised a week before, when the DFAS results came out that, that still shows Morgan Stanley has been severely impacted by the severely adverse scenario. That said, the booklet shows you losing 8.4 percentage points of capital and against the median of 2.8. And given all you've done and de-risking your balance sheet. I would have thought that we would have seen more progress in that and can you tell us what it is in the fed methodology that seems to cut against you, so disproportionally?

Jonathan Pruzan

Again, we were very pleased with the results. We had the same issue last year around DFAS and people sort of concerned with our outcome and about 100% payout ratio continue to increased capital return, part of our core strategy. We clearly have de-risked the balance sheet or RWA density is lower and basically every other firm out there, which is why you see some of that disparaging percentages. If you look at the leverage base ratio, as you get a slighter different picture. We clearly had de-risk, we've got and you've seen that through the dollar amount of losses that we've seen over the last several years have come down.

We have met our strategic objective of increasing capital return. We still think we're capital sufficient. When we came out in January of 2016 with that statement. We said, we were capital sufficient, we did not want to grow our equity base, we have grown our equity base a couple of billion dollars, but we've also supported our businesses and grown our balance sheet by $50 billion. So we've increased capital return and we've increased the size of the balance sheet and we feel very comfortable with our capital position.

James Gorman

Chris, we don't have complete excess to the fed models as I think you know. The construction of operating risk capital, the various stress falls that are in there, counter party risks, how the trading book is managed, how you derive your PP&I, there is a hell of lot of stuff that goes into this. Our own submission was 45,000 pages. And frankly looking back at this point, I don't think that's going to be very valuable. The regulators and treasury are all focused on how to make both the models more transparent, the process more transparent and to make some sensible adjustments for it.

So honestly I may not to be equipped about it, but I sort of don't care what the past was. What I do care is that our distribution this year approved to is about $6.8 billion and five years ago it was $400 million. So let's start with that one and number two, let's see what changes comes through, we may all be pleasantly surprised, we may be in the same place we're in, but we're operating now currently with about 100% pass. So I would let this one play out a little bit and see what comes out of the treasury efforts.

Chris Kotowski

Okay. And I mean I guess the thing is right, just again if you look at the old way of doing it right, if you need at five, after the stress then you were losing eight or nine and you need one for a margin of safety that would suggest you need to see T1 ratio on a 14%, 15% on an operating basis, I mean is there an outlook for like operating at less than that?

James Gorman

I think you are torturing yourself by looking it backwards. Honestly, I wouldn't do it. Focus on the big picture here. The big picture is, we distributed $400 million five years ago, we're distributing $6.8 billion now and there's the full review of the whole capital process being undertaken right now.

Operator

Thank you. And our next question comes from the line of Andrew Lim with Societe Generale. Your line is now open.

Andrew Lim

Hi there. Can I foresee a bit more new claim of excess capital? As things currently spanned [Indiscernible] scenario and that's 3.2% slightly up to 3% minimum. So you're maxing out your capital return here. You came with excess capital as contingent on changes kind of true form the treasury or as you say the fed being more lenient on how do you guys leverage [Indiscernible] stress scenario. And so I mean can you give a bit more color on that?

James Gorman

I'm really not sure what else I can say. We have consistently increased that capital payouts while the tests become consistently more severe, we're now at a 100% payouts, by definition, any excess capital we have and gating constraint was the leverage ratio this year and we were above the gating constraint after we did our distribution, so by definition we are carrying excess capital.

And our view is that, the way we calculate our capital needs to run our business, we continue to have excess above that, but we're waiting for the outcome of the white paper and the various efforts from the regulators to see what changes take place, there are clearly going to be changes. How favorable they are and to what extent they fit Morgan Stanley remains to be seen is not going to be productive to try and guess that.

Andrew Lim

Right. Understood. And just a follow up question. [Indiscernible] background we haven't heard anything like that for a long time now. But [indiscernible] when you might get some disclosure of the impact on capital ratios or the timing?

Jonathan Pruzan

Yes, I don't think we have much more visibility than anyone else in this area. I think the thing that sometimes people fail to recognize is we obviously have this white paper and if you think about it, we are actually going to enter a period of refinement and adjustment to regulations versus where we were a year ago, where our expectation was incremental regulation for periods of periods of periods of time to come, we're clearly going to be in a better place. Now how that plays out and what timeframe and what the actual changes are, it's very hard to predict, but we are clearly entering a different period going forward that we have been in the last eight years.

Operator

Thank you. And the next question comes from the line of Gerrard Cassidy with RBC Capital Markets. Your line is now open.

Gerrard Cassidy

Thank you, good morning. Can you guys share with us once we get into a more normalized return on capital environment that we see in the future. What kind of dividend payout ratio are you guys comfortable with as we look further out?

James Gorman

You know I don't think it probably serves us well to get a head of that discussion with the regulators and others. I think the current regulatory environment anticipates for the G-Sifi banks at payout ratios of something like 30% and for some of the smaller institutions I think they've gone higher than that maybe up to 40%. Whether that changes, you know post all the work being done, I don't know we're not at the 30% of this point. I think we're close to it.

So one way to think about our business which is I thought about it for a while the wealth management business is almost like a yield stock. So you can imagine the dividend coming out of wealth management earnings and obviously the institutional businesses are more volatile overtime. So they are more capital distribution businesses or capital investment businesses. But I don't know Gerrard that we want to change what the targets that are currently being given to us by regulators.

Gerrard Cassidy

Okay, great. And then second in the supplement package, on page five you give us the total loans of the organization. And could you share with us some color on - I may have missed this I apologize if I did. Why the corporate loans were down 37% or so year-over-year and a little color behind that really good growth you're seeing around the wealth management side where those loans are up 20%.

Jonathan Pruzan

I'm just flipping to page five, give me a second here. Okay, I think the changes in the corporate book are really around the size of the event book in sort of the event activity as well as some just overall management of the relationship book. The real story for us is as you mentioned has been in the wealth business as we continue to increase the penetration of our client base with lending products. The growth has been very good across all of our three core products the SPL, the mortgage and tailored lending.

And we feel like we've got good momentum in the growth last quarter at $3.5 billion was pretty balanced across the business a little bit more skewed towards SPL and tailored versus mortgage given what happened in rates, but again that lending story we feel very good about, our levels of penetration of how many of our clients have lending products is still probably a bit below peer level. So we expect or feel good about the ability to continue to grow that and that's been a real key driver to our wealth business.

Operator

Thank you and our next question comes from the line of Christopher Wheeler with Atlantic Equities. Your line is open.

Christopher Wheeler

Yes, good morning. A couple of questions on wealth management. I think during the quarter we've had the news that I think yourself and couple of your big competitors are now stepping back from filing away experience financial advisors and obviously in doing obviously reducing the cost of amortizing the [indiscernible] senior producers. I would like to perhaps understand how that perhaps progressing, how you're getting on with that because obviously it's a big change. And then perhaps to sort of link it up with the end of the Smith Barney payouts and talk about what you think this might do to your pre-tax margin, because I think at one said you say it might add, once a Smith Barney payouts retention packages run out, I mean, next year. You might be adding 1.5% percentage points deal your pre-tax margin. So a bit of color there would be helpful. Thank you.

Jonathan Pruzan

I'll go first on the second part of your question, which is the retention payments conclude in first quarter of 2019. Obviously, it's a function of numerator and denominator, but 1.5% increase is a reasonable approximation and obviously that will drop directly to the bottom-line. In terms of the attrition in the recruiting that we've seen is clearly slowdown and that is obviously helpful both in terms of just ins and outs. The expense associated would bring in new FAs, but also when a FA leads generally they're book goes with them or a good chunk of their book goes with them. So just lower levels of recruiting and lower levels of attrition has been overall helpful to the business.

Christopher Wheeler

And when you just want to decide whether do you think your competitor is holding the line, but it does seem like the beneficial move, but there are one or two players out there, of course, still sort of quite came take away some of your senior people?

James Gorman

Listen, these are big organizations. Our major competitors each have, I don't know 10,000 to 15,000, 16,000 advisors. if you have 1% attrition that's three-people a week. So it's not like going to have movement, you'll always have moment Chris. I think what's changed structurally with the industry is frankly, there are fewer competitors, if you think Morgan Stanley, Morgan Stanley is now a composites that includes Dean Witter Reynolds & Company, Robinson, Humphrey, Legg Mason, Smith Barney, Shearson, Hutton. And probably some that I'm missing, all of which use to compete against each of it, recruit against each of it.

So it's a consolidated industry, the big and small films continue to recruit, there are fewer numbers, all that I think the deal structures have become shall I say more sensible, there was a bit of a crazy period there. So, yes, but there will always be some recruiting and that make sense to many people ever right to getting work whether want to work.

Operator

Thank you. And our next question comes from the line of Brian Kleinhanzl with KBW. Your line is now open.

Brian Kleinhanzl

Okay thanks. Maybe just a first question on equity sales and trading. I think this is probably third or fourth quarter now, you called out strength and time broker. As a driver of those revenues, can you maybe give us a little bit more color as to what's driving that strength? Is it by region, is it existing clients more active, is it client growth?

Jonathan Pruzan

The simple answer is yes to all of those. Very strong quarter, the growth was across all of the regions, particularly stand out being EMEA, given some of seasonality there. Balances are up, we continue to invest in the balance sheet. And so, again it's been a very good story for quite some time, it's the full service platform and our clients have been very responsive to that.

Brian Kleinhanzl

And then second question, can you give us an update on kind of where the banking pipeline stand especially for M&A, it seems like there is been pick-up and activity thus far early in the third quarter, I mean how does the pipeline stand at the end of the second quarter versus first quarter?

Jonathan Pruzan

I would say that, first of all its very early in the third quarter, point number one. I would say that's a IBD pipeline, it's clearly healthy into the third quarter. I think if we look specifically advisory, it's probably down slightly. But overall, the equity and, debt underwriting remains healthy. IPOs backlog is healthy and broad and activities picked up really nicely here. So again a healthy environment. We are going into the summer months, so we'll have to see how that impacts us as well as all of the sort of policy uncertainty, uncertainty that we talked about in the past. But right now, pretty healthy.