Good morning. This is Kathleen McCabe, Head of Investor Relations. Welcome to our first quarter earnings call. Today's presentation may include forward-looking statements which reflect management's current estimates or beliefs and are subject to risks and uncertainties that may cause actual results to differ materially.

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

James Gorman

Thank you, Kathleen, good morning everyone and thank you for joining us on what is the last earnings call from our favorite CFO, Ruth Porat. I will now give you some highlights for the first quarter results and mark to market our execution against the strategic plan that we provided an update of in January.

We begin this year on a solid footing with all businesses contributing to our performance. Excluding DVA, this was the strongest quarter in firm revenue and PBT in many years. In fact, it was the second best quarter in revenue, ex-DVA, in the firm's 80 year history.

Key highlights include the following. Equity showed continued leadership. We delivered strong performance across products and regions both quarter over quarter and year over year. Fixed income delivered a stronger quarter consistent with our strategy.

Investment Banking performed solidly and the pipeline remains healthy. Wealth Management achieved record revenue, record revenue per financial advisor and delivered a pretax margin of 22%. Investment Management results were steady but there's more to be done as this business remains an important part of our growth opportunity.

Most significantly we took a meaningful step toward achieving our state of return on equity target, delivering in this quarter an ROE of 10.1%. This ROE excludes the affect of the net discrete tax benefit and DVA. On a reported basis, as you'll have seen, the ROE for the quarter was actually 14.2%. This performance reflects our strategic plan and demonstrates the business' flexibility to respond to increased client activity and market movements.

While the firm has clearly made progress, there remains work to be done in achieving the six-point plan we laid out in January. An update of which I'll briefly provide today. First, we continue to improve our wealth management margin, which reached 22% for the quarter. The business is also benefiting from additional factors described during our last call.

Secondly, we'll continue to execute on our bank strategy through deploying our deposits and again delivering prudent loan growth across Wealth Management and institutional securities.

Third, fixed income and commodities saw its strongest revenue quarter in three years, as volumes returned to the market with increased volatility. This quarter was important evidence of the execution of our strategy to significantly reduce the capital required to support the fixed income business, while maintaining the appropriately sized global footprint to meet our client’s needs. Needless to say, we must see this play out for more than one quarter.

Fourth, we're just beginning to realize the benefit of lower funding costs as we refinance the debt post crisis. This provides us with a tailwind across the businesses. We maintained our focus on expense management discipline and showed strong progress in the first quarter, delivering an overall expense ratio of 72%, excluding DVA. This level reflects an Institutional Securities compensation ratio of 38% and that ratio is consistent with our stated target of being at or below 39%.

Finally, with respect to steadily increasing capital returns to shareholders, we were pleased to receive a non-objection from the Federal Reserve on our 2015 capital plan to increase our dividend to $0.15 per quarter and a repurchase up to $3.1 billion of common stock for the five quarters beginning in the second quarter of this year.

We hope to maintain this trend of increasing dividends and share repurchases in future cycles, subject of course to regulatory approval. In aggregate, we continue to execute against the benchmarks previously established and will remain focused on them for the duration of 2015.

Before closing I would like to note several organization changes we recently made. These changes, where we moved executives across the firm, reflect our strong desire to build a very deep bench of senior management for the years ahead. And finally, I would like to thank our CFO Ruth Porat for her partnership, friendship and commitment to Morgan Stanley and to me personally.

She has been an extraordinarily highly valued part of my team for the five years and a tremendous asset to this firm since her arrival. We indeed have been lucky to have her. We are delighted to appoint as CFO, Jon Pruzan, a 20 year veteran of our investment banking division at the end of this month, and I wish John luck in this new role.

I will now turn the call over to Ruth to discuss the quarter in detail.

Ruth Porat

Thank you, James, and good morning. I will provide both GAAP results and results excluding the effect of DVA. We have provided reconciliations in the footnotes to the earnings release to reconcile these non-GAAP measures.

Results for the first-quarter include a net discrete tax benefit of $564 million, or $0.29 per diluted share, primarily associated with the repatriation of non-US earnings at a lower cost than originally estimated. In addition, the impact of DVA in the quarter was a positive $125 million, with $100 million in fixed income sales and trading and $25 million in equity sales and trading. Excluding the impact of DVA, firm-wide revenues were $9.8 billion, up 30% versus the fourth quarter.

Earnings from continuing operations applicable to Morgan Stanley common shareholders, excluding DVA, were $2.2 billion. Earnings from continuing operations per diluted share, excluding DVA, were $1.14 after preferred dividends.

On a GAAP basis, including the impact of DVA, firm-wide revenues for the quarter were $9.9 billion. Earnings from continuing operations applicable to Morgan Stanley common shareholders were $2.3 billion.

Reported earnings from continuing operations per diluted share were $1.18 after preferred dividends. Reported return on equity from continuing operations was 14.2% in the first quarter, excluding both DVA and the net discrete tax benefit, our ROE for the quarter was 10.1%. Book value at the end of the quarter was $33.80 per share and tangible book value was $28.91 per share.

Turning to the balance sheet. Total assets were $829 billion at March 31, up from $802 billion at the end of the fourth quarter. Deposits as of quarter end were $136 billion, up $2 billion versus Q4. Our liquidity reserve at the end of the quarter was $195 billion, compared with $193 billion at the end of the fourth quarter.

Turning to capital. Although our calculations are not final, our common equity tier 1 transitional ratio will be approximately 13.1% and our tier 1 capital ratio under this regime will be approximately 14.7%.

Basel III transitional risk weighted assets are expected to be approximately $440 billion at March 31. Reflecting our best estimate of the final Federal Reserve rules, our pro forma common equity tier 1 ratio using the Basel III, fully phased-in advanced approach was 11.6% at March 31, up from 10.7% in the fourth quarter.

Our pro forma standardized ratio was 11.6%, up from 10.9% in the fourth quarter. Pro forma, fully phased-in Basel III advanced RWAs are expected to be approximately $449 billion. Pro forma, fully phased-in Basel III standardized RWAs are expected to be approximately $446 billion.

We estimate our pro forma supplementary leverage ratio under the US final rule to be approximately 5.1% at March 31, up from 4.7% at the end of 4Q. All of these estimates are preliminary and are subject to revision.

Turning to expenses. Our total expenses this quarter were $7.1 billion, down 34% versus the fourth quarter. Compensation expense was $4.5 billion in the quarter, down 11%, driven primarily by the change in compensation structure discussed in the fourth quarter, partly offset by increased compensation related to higher revenue.

Non-compensation expense was $2.5 billion for the quarter, down 55% quarter over quarter driven by decreased legal expense as well as continued expense discipline.

Let me now discuss our businesses in detail. In Institutional Securities, revenues excluding DVA were $5.3 billion, up 45% sequentially after excluding the implementation charge for FDA in 4Q. Non-interest expense was $3.6 billion, down 49% versus the fourth quarter due to legal expenses and the compensation expense adjustment occurred in the prior quarter.

Compensation expense was $2 billion for the first quarter, down 17% versus the fourth quarter reflecting the impact of the change in compensation structure I just noted.

Excluding DVA, the compensation ratio was 38%, down quarter over quarter and down approximately 300 basis points year-over-year, reflecting the impact of the change in compensation structure and operating leverage in the business.

Non-compensation expense was $1.6 billion, down 65% versus the fourth quarter, driven by significantly lower legal expense in the quarter. Including the impact of DVA, revenues were $5.5 billion.

In investment banking, revenues of $1.2 billion were down - last quarter. According to Thomson-Reuters, Morgan Stanley ranked at number one in global IPOs and number three in global equity and global announced M&A at the end of the first quarter. Notable transactions included, in advisory Morgan Stanley acted as sole financial advisor to AbbVie in its acquisition of Pharmacyclics for an aggregate value of $20 billion. AbbVie obtained financing for Morgan Stanley and MUFG.

In equity underwriting, Morgan Stanley as joint global coordinator, lead left book runner and stabilization agents, priced a $3.7 billion follow-on offering for Citizens Financial Group. This was the largest financial institutions follow-on offering since 2012. In debt underwriting, Morgan Stanley acted as active book runner for Coca-Cola in its EUR8.5 billion senior unsecured notes, offering the largest euro transaction for a US issuer on record and the second largest euro transaction of all time.

Advisory revenues of $471 million decreased 3% versus our fourth-quarter results, driven by lower revenues in EMEA and Asia. Underwriting revenues of $702 million decreased 13% versus our fourth quarter results, driven by equity underwriting revenues of $307 million, down 11% versus 4Q reflecting fewer IPOs and lower revenues from EMEA and Asia.

Fixed income underwriting revenues of $395 million, down 15% versus the fourth quarter, primarily due to decreases in non-investment grade loans and high-yield bonds that more than offset increases in investment grade activity.

Equity sales and trading revenues, excluding DVA, were $2.3 billion, up 40% compared to last quarter. Results reflected broad-based gains across products and regions. Cash equities saw increased volume and share gain. Derivatives revenues were higher across regions. Prime brokerage revenues increased, driven by an uptick in balances and client activity.

Fixed income and commodities sales and trading revenues, excluding DVA, were $1.9 billion, up significantly versus the fourth quarter. Commodities results were up meaningfully versus the fourth quarter, benefiting from structured transactions, improved client flow and extreme weather.

Fixed Income revenues increased quarter over quarter driven by increased contribution across regions, with particular strength in macro products and EMEA. Average trading VaR for the first quarter was $47 million, flat to the fourth quarter.

Turning to wealth management. Revenues were $3.8 billion in the first quarter, up 1% sequentially. Asset management revenues of $2.1 billion were relatively flat with the last quarter.

Transaction revenues were down 3% compared to last quarter consisting primarily of commissions of $526 million, down 8% to the prior quarter driven in part by fewer trading days as well as activity levels.

Investment banking related fees of $192 million, up 11% versus last quarter primarily reflecting a revenue-sharing arrangement with Institutional Securities related to municipal securities. And trading revenues of $232 million, a slight uptick versus the fourth quarter. Net interest revenue increased 10% to $689 million, driven primarily by investment portfolio returns as well as continued growth in lending products.

Non-interest expense was $3 billion, down 3% versus last quarter. Non-compensation expense was $754 million, down 3% from last quarter. Compensation expense was $2.2 billion, down 3% versus the fourth quarter, in part due to the change in compensation structure last quarter as well as a revenue mix change, with growth in non-compensable revenues this quarter.

The compensation ratio was 58%, down versus the fourth quarter. The TBT margin was 22%, profit before tax was $855 million. Total client assets were $2 trillion. Global fee-based asset inflows were $13.3 billion, fee-based assets under management increased to $803 billion at quarter end, representing 39% of client assets.

Global representatives were 15,915, down 1% to the fourth quarter. Deposits in our bank deposit program were $135 billion, down $3 billion versus the fourth quarter. Approximately $130 billion were held in Morgan Stanley banks. Wealth management lending balances continued to grow, reflecting the ongoing execution of our bank strategy.

Investment management revenues of $669 million were up 14% sequentially. In traditional asset management, revenues of $439 million were up 2% versus the fourth quarter. In Merchant Banking and real estate investing, revenues of $230 million were up compared with the fourth quarter driven by higher investment gain.

Non-interest expenses were $482 million, down 19% from the fourth quarter due to the change in compensation structure discussed last quarter.

Compensation expense was $273 million in the quarter reflecting a compensation ratio of 41%. Non-compensation expense was $209 million, down 2% from the fourth quarter. Profit before tax was $187 million in the first quarter. NCI was $17 million versus $12 million last quarter. Total assets under management increased to $406 billion driven by market appreciation.

Turning now to our outlook. In the first quarter the firm benefited from growing investor and corporate interest in global opportunities, with higher activity levels in the US complemented by a meaningful pickup in activity in Europe and Asia.

In investment banking, the M&A backlog is higher than a year ago, supported by the trends we have discussed previously; robust cross-border activity, activism and larger transactions across industries.

The underwriting pipeline similarly remains healthy, increasingly driven by acquisition activity. In sales and trading, we continue to benefit from the breadth of our strong, global franchise with renewed client interest in European and Asian markets, reflecting the varying stages of global recovery and the impact of central bank actions across product. The obvious factors that affect these results going forward are global events and the nature of volatility.

Our Wealth Management clients remain well engaged with their financial advisors. The key catalyst for higher activity is the level of US new issue activity, with the pipeline up versus Q1. Q1 levels also reflected client caution in anticipation of Federal Reserve rate moves which should play out throughout the year.

We are pleased to have achieved this starting point of our 22% to 25% margin target in a lower transaction environment, underscoring the great operating leverage in this business.

The outlook for our bank remains strong given the lending pipeline in our wealth management and institutional securities businesses. This enables us to continue to benefit from earnings upside, even without the benefit of rising rates.

Our goal with the roadmap we introduced several years ago was to address your many questions and be transparent through metrics and goalposts, so that our progress could be measured.

We had early confidence that the transformation of Morgan Stanley's business and balance sheet would deliver returns to all of our stakeholders, and I am proud that the levers we articulated are increasingly evident.

Beyond the business outlook we expect to benefit from lower funding costs and the impact of capital returns to shareholders. Although the path to a sustainable acceptable ROE is not a straight line from here, I am confident that the road is a clear one.

I will miss working with you and I'm grateful for the strong support and for the analysts on the call for your very constructive guidance and analysis. Thank you. It was a privilege to be in this role at this moment in Morgan Stanley's history. I thank my partner and boss, James Gorman, for the opportunity, but far more important for what our great team has accomplished.

We will now take your questions.

Question-and-Answer Session

Operator

[Operator Instructions] Your first question comes from the line of Guy Moszkowski with Autonomous Research.

Guy Moszkowski

Good morning, Ruth and James.

Ruth Porat

Good morning.

James Gorman

Morning.

Guy Moszkowski

First question I guess, is if you could give us a little bit more color on fixed income and commodities. Given that it seems like you've had a pretty high hurdle to deal with commodities not only having done well in the first quarter of last year, but also you having sold TransMontaigne.

Can you give us a little bit more color on how you managed to see revenue there actually up year-on-year?

Ruth Porat

Certainly. We had strong contribution from around the globe. Strength in EMEA across products with meaningfully higher client volumes. The bigger driver was strength in macro rates and FX were up nicely year over year; and, importantly, that's not withstanding a meaningfully lower balance sheet, and RWAs and fixed income were also lower; they were actually at $174 billion.

So through our target, we're keeping our target at $108 billion; but this really goes to what we've talked about over many quarters. Our focus is on centralized resource management, so nice performance there.

Credit was up from a weak fourth quarter, although not at last year's levels. And then as you noted in commodities, Q1 is seasonally strong. And even with the sale of TMG, TransMontaigne, in last year's results we were up. And the performance was across the board. It was physical client flows, structured transactions for clients. So we saw strength across the board there.

Guy Moszkowski

Are you still looking to sell those storage and other physical businesses?

Ruth Porat

Well, as you've heard us say many times, we're committed to selling oil merchanting; and we'll let you know when we have something to say.

Guy Moszkowski

Okay. Great. And maybe a little bit of color on the reduction in the RWA in thick in the quarter. Can you give us a sense for how much of that was from runoff of some of the legacy positions that you've talked about in the past that don't generate revenue?

Ruth Porat

So included both active and passive mitigation. There was some benefit from market move as well. It was really all three.

Guy Moszkowski

Okay. That's helpful. And then final question on moves in the capital account. There's a lot of moving parts it seems like this quarter. We know that overall capital was kind of flat. But we can see in the average allocations that you provide that you moved or retained more capital in the institutional securities business.

And I was wondering if you could give us a little sense for, given the RWA movement, what's going on there?

Ruth Porat

So, you actually answered in your question. There were some ins and outs. But obviously given it is an average calculation, there are timing implications that flow through. And you can see, therefore, more capital moved up to ISG.

Guy Moszkowski

So we shouldn't necessarily expect that to remain in ISG as we move through the quarters of the year or is there something to do with continued regulatory changes that would drive those capital levels a little bit higher?

Ruth Porat

Well, over time it will. I mean, the required capital calculation is based on the capital regime in place today at any point time. So that does continue to be on a transitional basis. Over time, you'll see a reduction in some of the phased introductions.

So it will change over time, and more of that parent capital would be allocated across the businesses, but more of it going to ISG over time. But of course, that's a couple year period on the phase in.

Guy Moszkowski

Got it. Okay. Thanks very much for taking the questions and obviously for your service and your tremendous clarity of vision and explanation of everything over the last several years. We've appreciated working with you.

Ruth Porat

Thank you very much.

Operator

Your next question is from the line of Mike Mayo with CLSA.

Mike Mayo

Hi. First question for James. You have a 10% ROE target. You certainly achieved that in the first quarter. What is your target time frame to achieve the 10% ROE for the year?

James Gorman

Well, Mike, first of all, appreciate you noting the first quarter. We have, as you know, resisted giving you a formal time frame because obviously, the ROE is an output and it's a function of returns, both revenue and expenses, as well as it is of capital accretive over time and what our capital plans are. So we have resisted trying to put a formal date on it.

I can assure you everybody in this building would want it sooner rather than later. And the fact that we achieved it in a good environment but not an extraordinary environment in the first quarter and before many of the tailwinds that we have behind us are fully baked in, was very comforting.

We're not going to give you a formal date on this. We are intent on achieving a 10% ROE year over year and beyond that in the outgoing years. So we're off to a good start here in 2015, and let's hope we keep it up.

Mike Mayo

What is the 10.1% on a tangible basis?

James Gorman

It's 11.9, is that right Ruth?

Ruth Porat

Yes it is. Various numbers are we reported 14.2% translates to 16.6% on tangible. And so adjusting up for DVA and discrete tax benefits, equivalent ROTE rate of 11.9%.

Mike Mayo

And then a separate question. Your VaR stayed flatten from the fourth quarter when your VaR peers actually went up. What's your thought process there, did you leave money on the table, is that a lower risk profile? What's going on?

Ruth Porat

So, VaR is heavily weighted to changes in current market volatility. And as you know our VaR was flat, but what we're focused on is our VaR was flat on performance. We were very active with clients. We were able to achieve VaR efficiency. We reduced balance sheet in certain areas that were less constructive. We reallocated by client activity.

We have capacity to take VaR up. But you can see in the results, we had strong performance with flat VaR.

James Gorman

I think the key to this is we did not dial up risk to generate these earnings. Whether we left money on the table if things had turned out differently, some people might have said we left losses on the table. In this situation, we didn't dial up the risk. We delivered the earnings.

But obviously we have a very successful trading business in parts of this firm. And they will react to the market volatility as I said.

Mike Mayo

And then lastly, Ruth, you're yet one more banking executive to lead the industry. Any last comment about the regulation in the banking industry?

Ruth Porat

Well, I think that fundamental regulatory change was needed with the backdrop of 2008, and it was implemented. And I think there's been meaningful improvement in the stability and resiliency of the industry as a result with all that's been done. The higher capital levels, liquidity stress testing, recovery plans, resolution plans, governance -- all the changes in business activity.

I think if I look back over the last five years, some made those changes kicking and screaming. I think we were of the view that it was clear where it was going and it was needed and are proud of the changes we've made.

I think at this point given how much has been accomplished, it is time to pause, digest and assess. It will be good to have a timeout and see the impact on markets and see where there was an undershoot and an overshoot. And hopefully that's what we see going forward.

I think the main point is the industry is substantially more resilient, and that's a big accomplishment. It's a lot of work to get here for all of us. It may mean lower returns but it means a more resilient industry; and that's a positive place to be.

Mike Mayo

Thank you.

Ruth Porat

Thank you.

Operator

Your next question is from the line of Glenn Schorr with Evercore ISI.

Glenn Schorr

Hi, thanks. Ruth, you mentioned in your commentary on SIC about structure transactions being a contributor. I'm curious if that is only in commodities or if that was in other parts of the business and how big of a driver. And more importantly is that a sustainable appetite by clients, because we've all been waiting for that for a while.

Ruth Porat

I'm glad you asked that. It was a comment specific to commodities. In commodities, it was a combination of structured activity, the physical and trading activity. The majority of client facing flow in structured business, it was in the backdrop of what's gone on in the oil markets, it was good to see the volume of structured transactions. But as I said, I'm not going to do a forecast on.

Glenn Schorr

Okay. And does that mean – I don't want to put words in your mouth, but was the commodities contribution of the quarter larger than normal times just because of some of the things you mentioned plus the weather?

Ruth Porat

Well, commodities as you know well, is stronger in the first quarter. And so it was up some versus last quarter. But the bigger driver was the strength in macro with rates and foreign exchange up nicely year over year.

Glenn Schorr

Okay, cool. And then RWA down 4% for the firm sequentially, I think you said 6% in SIC. It's good; it's welcome. Is that not a number that we want to straightline, right?

Ruth Porat

I'm sorry, the number…

Glenn Schorr

Can it fall at that pace on an annualized basis?

Ruth Porat

So, two parts to that question. At 6% sync [ph] I noted that it's down to $174 billion; and we're retaining the target at $180 billion. We're very focused on RWA efficiency, and we've indicated there's another $25 billion that runs off post 2015.

And we're going to be very clinical and flexible in the way we allocate that capital across the franchise in a way that optimizes returns. But to your question, would we want you to straight line from there, I think I've answered that.

Glenn Schorr

Cool. Last one, easy one, share count was flat year on year, but you got a higher authorization. That's just math, right? We can count on maybe 2% shrinkage this year in the share count?

Ruth Porat

Yes, the main thing is we got a higher authorization and that we start executing on the share repurchase as we come out of the second quarter. And we expect to execute that radically over the time period.

Glenn Schorr

Thanks for everything, Ruth.

Ruth Porat

Thank you very much.

Operator

Your next question is from the line of Brennan Hawken with UBS.

Brennan Hawken

Good morning. Couple of quick ones here. Cap Markets, the equity strength. How much of that, I know you highlighted across regions, and you gave some great color, Ruth, on some of the various components.

How much of a tailwind was Europe this quarter, just given some of the strength and on the back of QE there?

Ruth Porat

Well as we've talked about on many quarters, we run the business with a nine box strategy product across the top cash derivatives in PB and then regions, Americas, EMEA and Asia. In the first quarter, every box was strong. The big theme, as I said, was increased investor interest outside of the US, and particularly US investors in the rest of the world.

We clearly saw a pick up in client engagement in the EU on the back of the CB actions, but we also saw cash share gains in Asia with a pickup in client activity on the Asia growth opportunity and relative value there. We had nice frets to the business.

The key question is the ongoing macro backdrop, as I said, and the nature of volatility. This quarter was characterized by LV trending volatility and a lot worked well. It was the best quarter in a long time. Looking forward, we'd anchor the outlook to what we've see over the last few years. But there were a lot of good things going on around the globe.

Brennan Hawken

Okay. Thanks for that color. And then thinking about Wealth Management here, can you give maybe a little color? It's early, but on any potential impact from the Department of Labor proposal?

Ruth Porat

So, respect to the DOL proposal, it's still in the comment period' there are a number of open items to address. Based on our best interpretation of the proposal at this point, we don't expect a meaningful impact on our business. We do expect some changes in activity, and we do expect more compliance-related costs.

Brennan Hawken

Okay. And then I know the loan growth environment is sort of tough. But sequential loan growth slowed somewhat, and it looked like PLA slowed more than mortgage. Was there anything driving that, and should we ratchet down expectations for loan growth? Or was that more sort of like a single quarter type of a slowdown there?

Ruth Porat

Yes. Loan growth is still very much on plan, consistent with what James went through on the fourth quarter. We talked a lot about prudent loan grow. There is some seasonality with PLA in mortgages in the first quarter.

But we have a healthy and diversified pipeline and expect it to continue to deliver steady prudent loan growth. The main point to talk about is two sizable franchises with diversified assets. We have ample opportunities for loan growth.

Brennan Hawken

Terrific. Last one from me. Any chance to quantify the legal charge in both overall firm and in the securities business?

Ruth Porat

No, we commented that non-comp expense was up a bit here due in part to legal; but we're not breaking it out.

Brennan Hawken

Okay.

James Gorman

The main takeaway on that is that the big legal stuff relating to the crisis we feel is behind us. We are dealing with some of the one-off smaller events as we move forward here.

Brennan Hawken

Thanks for that, James. Congrats to you, Ruth. Best of luck on your switch over to the left coast there.

Ruth Porat

Thank you very much.

Operator

Your next question is from the line of Michael Carrier with Bank of America/Merrill Lynch.

Michael Carrier

Ruth, one more on equities. And not really focused on the quarter but if I look over the last four or six quarters, it seems like the traction of the progress has just been continuous. And it's been pretty consistent across products, across geographies.

I just want to get a sense, when you look at what's going on in the equity business and when you look at some of the pressures on the business and on the regulatory environment with clients, are you seeing more market share in areas where you guys are differentiating versus the customers or versus competitors?

And is there any nuance between the high touch, the low touch or anything else? It just seems like the consistency in the traction has been very consistent across the past two years.

Ruth Porat

So we are of the view, and I've talked about this on prior calls, of the view that we're benefiting from a lot of investments in the business over many years. So it's back to early technology investments in the business that enable us to execute on behalf of clients in all market environments and do so on a cost efficient basis, where we're driving returns for stakeholders as well.

It goes to the quality and content of the team, so that it very much is high tech, high touch and the breadth of the franchise. Talk about the nine box strategy because it's so core to way the team runs it, and with this maniacal focus within each box.

But then as we talked about over many years now, a focus on what are the adjacencies, so that has we go deeper with clients in certain areas they go deeper with us. It is a very tightly run business, but its delivering results.

James Gorman

I'd just add to that, Mike, that remember coming out of the financial crisis our prime brokerage business clearly took a hit. And that is being rebuilt. I think over time, essentially gained share. The strength of that business has been a real additive.

And secondly, these businesses do well in a large part because of the quality of the leadership team running them. And we've had a very stable and strong, deep leadership team running now [ph] these business for several years, and I think that makes a difference.

Michael Carrier

Okay. That's helpful. You have set out the ROE target, and you hit around that area this quarter. And, James, it sounds like when you talked about dialing up the risk, it wasn't one of those quarters where everything worked. There was obviously good progress, but it could've been better.

I just want to get a sense of when you guys look at some of the things that can improve in terms of the Wealth Management pretax margin, things that you have control of, it still seems a little surprising when I think about a 10% ROE and then I look at your business. 20% is fixed income, and then 80% is equities, banking and wealth management and investment management. Things that we generally think of a higher ROE.

When I think about going over the next couple quarters, years, besides the things that you have control of, are there other things on the capital side or the balance sheet side that will continue to boost that ROE?

I know the ROTE is higher; it's around 12% versus the 10%. I just wanted to get your sense on what will be the drivers to improve that, besides the margin in the wealth management business.

James Gorman

Well, let me take a cut at that, and I'm sure Ruth will add on. Firstly, I think a lot of folks really haven't given much attention to the E part of this equation. When we started as a team five years ago, our E was around $40 billion; it's now around $68 billion, I think. So if we were still operating with the same equity we had five years ago, our ROE would actually be in the order of magnitude of 15%, our ROET well above that.

So we've been through a major repositioning of this firm in the regulatory environment. The key has been to put ourselves in a position where we had enough capital, where we wouldn't be going, needing to go out and raise capital, accrete excess capital and so on. And ultimately, the test of that would be successful CCAR capital distributions.

We've now had three years where we've lifted our dividend from $0.20 to $0.40, now $0.60 a year. Lifted our buyback from 500 to 1 billion to now 2.5 billion, and we expect to increase capital actions in the years ahead. The E part of this equation, I think, deserves a little bit of attention.

On the R side, two things are going on. One, we have a very, very focused non-comp expense program we've had in process for a few years, which has a huge team here, led by Charlie Chasen here. They are very focused on that. We're not going to let go or let hold of the non-comp side.

And on the comps side, it's pretty clear. We said the ISG comp to revenue ratio would be below 40%, and indeed it was. And we're bringing down the comp to revenue ratio for the other businesses as we build scale.

Then you look at where the opportunities are, and they are many, frankly. We're not yet in a global economy which is by any means robust. The Wealth Management full transition to the managed product hasn't yet occurred. The bank loan products, we've still got tremendous capacity there. We haven't seen the interest rate hike, which we're going to get at some point in the future.

The M&A and ECM businesses clearly will pick up as the global economies pickup, and I could go on with a long list. I'm giving a long answer because it's a complicated, multifaceted thing.

But I would look at all of those, starting with the move to non-comp, the comp to revenue commitments, capital plans and then follow with the particular revenue drivers in each of the businesses that exist today and are likely to exist in the changing, high rate environment going forward.

Michael Carrier

Okay. Makes sense. Thanks a lot.

James Gorman

Sure.

Operator

And your next question is from the line of Christian Bolu with Credit Suisse.

Christian Bolu

Good morning, James. Good morning, Ruth.

James Gorman

Morning.

Christian Bolu

James, on the regulatory environment, the SEC seems to be focused on the potential abuse of fee-based accounts, so-called reverse churning. Given Morgan Stanley's fee-based accounts have more than doubled since 2009, I'd be curious as to what kind of controls or checks you have in place to ensure the proper use of fee-based accounts at Morgan Stanley

James Gorman

Well, this is one of those questions which, depending on the environment, you could ask it one way or the other. A lot of people spend their time complaining about the churning on transaction type accounts, which is why the fee-based industry has really evolved. Where clients, certain clients, have wanted the certainty of knowing they pay one fee, and with that they either do none or as much transaction activity as they want to do. So it seems to me it would be a very natural market segmentation.

There will be some clients for example, people with large restricted stock positions, which that would probably not be something they want to do. But from many others who want a more advice driven relationship, it obviously is. Whether its transaction activity or fee-based activity, we have an enormous compliance operation in our wealth management division, driven down to the branch level.

Both at the personal touch level and also at the model-driven level, where we look for exceptions, which looks at suitability, concentration risk and all the other things that you would expect to make sure that the clients are properly served at the pricing that they're getting.

Christian Bolu

Okay. That’s helpful. A question on the tax strategy. I think tax benefit seems to be recurrent theme quarter after quarter. At a very high level, could you explain the firm's tax strategy and how we should conceptually think about any tax benefits going forward.

Ruth Porat

Well, this quarter was the result of a legal entity simplification consistent with resolution. We would still guide you to around 30% as the effective tax rate on a go-forward basis.

Christian Bolu

Okay, there's no wide tax strategy or anything in that nature we should think about?

Ruth Porat

No. As I said, this was legal entity simplification; and I guide you at 30%.

Christian Bolu

Okay. A couple of cleanup questions. On the M&A backlog, I believe you said it was up year over year. How does a look on a link quarter basis?

Ruth Porat

It is up year-over-year and that is the way we've been looking at it.

Christian Bolu

Okay. And then on the funding cost benefits, how should we think about the allocation between FIC and equities?

Ruth Porat

So, as we've talked about a number of calls, we allocate funding, balance sheet, liquidity based down to the product level. And it's really based on the asset mix, and so that's the real driver of it.

We haven't broken that out, but it's going to benefit across sales and trading. And it's a nice tailwind that is increasingly building through 2016 year.

Christian Bolu

Okay. Thank you. And just lastly, like the sentiments of my peers, it's been a pleasure working with you, Ruth. You're definitely going to be missed.

Ruth Porat

Thank you very much.

Christian Bolu

Thank you.

James Gorman

I feel like all of you are going to start selling tick stocks.

Operator

And your next question comes from the line of Steven Chubak with Nomura.

Steven Chubak

Certainly pleased to see the ISG comp leverage really show through in the quarter in light of the revenue strength. I was just wondering how we should think about the comp leverage versus the full-year target of 39%, assuming you can actually deliver revenue growth for the full year?

Ruth Porat

So when we set the comp ratio, it's with a full-year outlook. So the 38% is the full-year outlook. Again, that's all things equal. That's the way it's set.

We remain very committed to rewarding those who drive returns. And we think with the steps we've taken on comp structure and the operating leverage in the business, this is a full-year outlook -- again, all things equal.

Steven Chubak

Okay. And then maybe switching over to the capital side for a moment. We're certainly pleased to see the significant build in the leverage ratio in the quarter. When parsing the individual components of that ratio, it looks like the improvement was really driven by a reduction in SLR add-ons more so than anything else.

And I was just wondering if you could speak to what the current level is of those SLR add-ons, and maybe how we should be thinking about sources of future mitigation potential.

Ruth Porat

Well from the benefit this quarter was really both numerator and denominator. You're absolutely right; in the denominator, we have work streams against all the various gross ups, and we had reductions in net long CDS sold.

And we're benefiting from compression activity, which I would say industry wide has become more business as usual, which we think is a real positive.

We were early on that, and it's good to see it has been broadly embraced. The numerator clearly benefited from earnings in our preferred issuance early in the quarter. So we remain focused on all of the items that are possible and logical for mitigation.

Compression, as I said, but across the board, remain focused on ensuring that if we're using balance sheet, where we're using balance sheet. It continues to provide the kind of returns commensurate with the capital that's being required here. And so it's, again, a deep focus; but it's both a numerator and a denominator benefit.

Steven Chubak

Okay. Thanks, Ruth. And then just lastly on the Wealth Management side and specifically the new long-term deposit target of $200 billion, which Greg spoke to at a recent investor conference. In the past you've highlighted some metrics where maybe your under penetrated relative to peers to help drive future growth.

And was hoping, in the context of this specific target, whether you could highlight any specific metrics which would support that additional growth towards that $200 billion.

Ruth Porat

Well, we've talked about, I say it so often, I'm sure you're tired of hearing it, but we're focused on prudent loan growth across both wealth management and institutional securities. We do believe we have meaningful upside from here, given the scale of the client base and the relative penetration, in particular in wealth management. We've talked about that. The $200 billion deposit target is really married to our expected loan demand over the next several years.

And so the execution plan on deposit growth, as we looked at what is the loan potential given these two large franchises, the expectation for deposit growth was two phases. The contractual on boarding from city, and as I think you know, that ends this quarter, the second quarter of 2015, but we are in an excess deposit position.

Our loan to deposit ratio is at 51%. And even if we load in standby liquidity to support loans, the ratio is at 74%. So we do have a nice runway before we need additional deposits to support loan growth.

And then as we've talked about on the fourth-quarter call and as Greg commented on, we have substantial organic deposit growth opportunity given our client base. We still have a large portion of cash held away.

But it's really calculated with a lens to what is the loan growth opportunity across Wealth Management and institutional securities. And we see quite of bit of opportunity from here against which we will execute over time, prudently, leading with credit risk management.

Steven Chubak

Okay. Thanks, Ruth. That's really helpful. And congrats on the new role and best of luck at future opportunity.

Ruth Porat

Thank you very much.

Operator

Your next question is from the line of Matthew O'Connor with Deutsche Bank.

Ruth Porat

Good morning.

Matthew O'Connor

You had mentioned earlier about long-term debt cost coming down and I think implied you're still early on in that process. Maybe if you could just size how much benefit you've had so far from that and try and shape how much opportunity is still in front of us.

Ruth Porat

Well, as we indicated from peak financing costs to end of 2016, it's down about 25%. And the benefit comes in as we refinance debt that was issued post crisis, given our credit spreads are meaningfully tighter. And so as we see more of that we refinance, the greater the benefits. That's why it lags in over time.

Matthew O'Connor

And do you have what the blended rate of your long-term debt is, the $155 billion?

Ruth Porat

I don't have that with me.

Matthew O'Connor

Okay.

Ruth Porat

It's in the filings, I don't have it with me.

Matthew O'Connor

Okay. But just I mean, conceptually, are we halfway through - your spreads have been coming in quite a bit, market rates have been coming down, even just the past year here so. I think there's still additional opportunity to bring those rates down.

Ruth Porat

There is a decent opportunity. Some of the debt that we refinanced was put on pre-crisis, and so we've only recently begun to tap into that portion of it that was put on post crisis. At a certain point, it was actually more of a headwind.

It's been turning recently to become a tailwind, and that's why we called it out when we did. We delayed to call it out and at the point at which we were starting, not to refinance the early 2000 debt, but what was put on post crisis. That's why it's a delayed benefit here. Delayed posts are the contraction we've seen in our credit spreads.

Matthew O'Connor

Okay. That makes sense. All right, thank you.

Ruth Porat

Thank you.

Operator

Your next question is from the line of Jim Mitchell with Buckingham Research.

James Mitchell

Hey, good morning. Just maybe a follow-up on the capital question. You are substantially above on your common equity tier 1 ratio; but on the SLR, you're just slightly above the minimum. How do you think about the interplay of the leverage versus the common equity, to a point where you can start to return even more of the common equity to maximize returns?

Is there a lot more to go on the denominator in the leverage ratio, or does it mean potentially more preferred to maximize shareholder returns? How do you think about that dynamic over time, and what kind of a cushion do you think you need on the SLR?

Ruth Porat

So, I've already answered part of it in response to an earlier question which is, we've talked frequently about the way to maximize return and capital over the longer term is to have steady increases. No discontinuous moves in the request for return of capital.

And we're very pleased to have the ability this year, at the $3.1 billion share repurchase over the five quarter period and the dividends up 50%. So when we look at the requirement, there are clearly a number of them. Interest rate capital, it's SLR, it's the CCAR process itself, it's how you think about the stress losses.

SLR obviously was not in CCAR in the last round. But we have a forward-looking lens as we think about the business, where we consider all of those factors. And as we looked to optimize the opportunity across the franchise, both from a returns perspective and the ability to return capital, we look through each one of those lenses.

At this point though, as I said, SLR hasn't been included in the CCAR that would govern how much we can return. But that obviously hasn't stopped us implementing strong work streams to mitigate the gross up in the denominator, as we've already talked about on this call.

We look at all. You have to look at all; you can't just tip to one versus the other. Again, it's with a lens that we want to ensure we're providing balance sheet capital behind client activity and doing it in the most constructive way. But it's complicated. There's no question with the multiplicity of requirements. But that's what we've been managing against.

James Mitchell

So hear but on the CCAR, your constraining factors were more of the tier 1 ratio's, right, the leverage the total capital? So I'm just trying to get a sense. Do you think there's a lot more to do on the denominator side or do you think it would make more sense to issue more preferred to deal with that? Or do you think you have enough time to make more efficiencies on the balance sheet side? That's what I'm just trying to get at

Ruth Porat

Okay, sorry. On that, part of it is the CCAR process itself. We were pleased this year that on one input to the overall calculation, PP&R, the estimate by the Federal Reserve increased. We believe that reflects the greater consistency we have in earnings. We put a lot of effort behind trying to clarify that, and we're pleased that it picked up.

And when you look at what were some of the things that took the total capital calculation lower, the leverage lower, there was a difference between estimates firm and Federal Reserve on balance sheet growth or RWAs over the period. And our view is that the test is a learning process, even though there's not that much transparency in it and that it's really about addressing some of those elements of it.

So that's one component, trying to narrow the gap between the Federal Reserve's estimate and the firm's estimate on things like balance sheet growth. You know, is the fair value firm and we don't see that kind of balance sheet growth.

And then on the second part of it, of course ensuring we are being very clinical and direct on balance sheet use in other elements of it. We look at all preferred and sub debt as ways to optimize capital over time, and we'll continue to do so. We've been doing that for the last couple of years.

James Gorman

Just think about where we've come from. The SLR, we're at about 4.2%; a year ago, we were at 5.1%. With some of the actions we took, we intentionally depleted our capital in the last several months, including the charge relating to the Attorney General action, Department of Justice, and the charge related to our deferrals.

The good news is we're above 5% now. We have several years to stave up 5%. We have several years to work the balance sheet and, as necessary, use preferred securities. So we have a long runway to keep this in motion, and we're pretty confident we can stay above 5% and do the things that Ruth talked about.

James Mitchell

Absolutely. Thanks.

Operator

Your next question is from the line of Devin Ryan with JMP Securities.

Devin Ryan

Just a couple quick follow ups here. So on the bank and strong loan demand, is it reasonable to think that you could skew more towards loans than you presented? I think you've given roughly 60% loans as a percent of assets by 2016 end. Is that the optimal mix; or, if the demand is there, could we see that mix look more lending heavy?

Ruth Porat

Just 13 weeks ago, James refreshed our outlook on the six-point plan and provided we added another year on the bank outlook to give you a sense of the asset mix. And the real point of doing that was so that you could model, when you expect a rate increase. We're giving you our outlook on asset mix, and there's no updates there on what was reviewed last quarter.

Devin Ryan

Okay. All right, great. And then just coming back to the strength in EMEA in the quarter. It sounds like that was more trading heavy in the trading businesses. Were there any specific areas that really experienced improvement? Does that tone of activity still feel good, and do you see that spilling into other businesses?

Ruth Porat

I've indicated it was in both equities and in fixed income in macro products. But as I noted, it was not just Europe. We saw a focus on the opportunity in Asia as well. It's an early start to the quarter here. As we typically say at this point, a couple of weeks is not a quarter.

Devin Ryan

Okay. Thanks very much.

Ruth Porat

Thank you.

Operator

Your next question is from the line of Matt Burnell with Wells Fargo Securities.

Matt Burnell

Good morning. Thanks for taking my question. Ruth, I wanted to focus one more question on the debt opportunity and specifically on the legacy trust to preferreds that you have outstanding.

I think your plan previously was to potentially redeem most, if not all, of those this year. I'm wondering what the timing is on that based on your CCAR results this past go around?

Ruth Porat

We did include the redemption of trust in CCAR because it's expensive relative to where it stands today. The rules are complicated, but we do remain focused on eliminating the drag. That was the piece we withdrew. We did not change our requested return of capital. The $3.1 billion share repurchase and the dividend increase of 50% weren't altered. And we're pleased to attest qualitatively.

Matt Burnell

Okay. And then just in terms of investment banking trends, obviously very strong quarter across the franchise in trading. To James's earlier point, you're not hitting on all cylinders, and banking within ISG was a little bit less strong.

Can you give us some color as to your outlook as to the potential opportunities or strengths within EMEA and Asia, specifically within the banking business?

James Gorman

I think firstly, just looking at the banking franchise, it's a terrific franchise. We actually had a strong quarter; some others had very strong quarters, all power to them. We have a good pipeline. Obviously, it's a lumpier business in any 13-week period than some of the other businesses, so you're going to expect a little more bouncing around. No concerns there.

We are seeing a pickup in Europe. Asia has been slow. Japan was a little slow earlier in the year, but we're starting to see some cross-border activity there. Well-positioned strong franchises in Japan and China. So I think the outlook remains very firm.

Matt Burnell

Okay. Thanks very much.

Ruth Porat

Thank you.

James Gorman

I think that brings this call to an end. I just wanted to take a moment to thank our dear friend Ruth, wish her well. I'm also sorry to see the analysts are now moving to the West Coast, following her. We'll have to pick up some others over here.

But on a more serious note, she's been a great partner. Has sat in the office next to me for five years, and done a terrific job in helping get this firm back from the depths of the financial crisis. And it takes a great team. Ruth had a great team working with her. She followed also a terrific CFO, who helped us navigate the crisis during extraordinarily stressful period, Tom Kelleher. And she now precedes another new CFO, as I said John Pruzan, who I think will also be terrific.

And throughout it all, we've had a deputy CFO that many of you have not heard on these calls, but has been in many of the meetings. Paul Wirth has been an extraordinary able and steady hand now through the last three CFOs we've had at this firm, so great team. Thank you Ruth. We wish you well. And don't forget us.

We're going to leave Ruth with something to remind her of Morgan Stanley, not that she would ever forget us. But we wish her the best. Thanks, everybody, for a good call.