MANAGEMENT DISCUSSION SECTION

Operator: Welcome to the E*TRADE Financial First Quarter 2010 Earnings Conference Call. At this time, all participants have been placed in a listen-only mode. Following the formal remarks we will open the call for Q&A. [Operator Instructions]

Thank you. It is now my pleasure to turn the floor over to Susan Hickey from E*TRADE Financial. Please, go ahead

Susan Hickey, Investor Relations

Good afternoon, and thank you for joining us for E*TRADE Financial's first quarter 2010 conference call. Joining me today are Steven Freiberg, E*TRADE's Chief Executive Officer; Bruce Nolop, our Chief Financial Officer and other members of E*TRADE's management team.

Before turning the call over to Steve, I would like to remind everyone that during this conference call, the company will be sharing with you certain projections or other forward-looking statements regarding future events or its future performance. E*TRADE Financial cautions you that certain factors, including risks and uncertainties referred to in the 10-Ks, 10-Qs and other documents E*TRADE files with the Securities and Exchange Commission could cause the company's actual results to differ materially from those indicated by its projections or forward-looking statements. This call will present information as of April 21, 2010. Please note that E*TRADE Financial disclaims any duty to update any forward-looking statements made in the presentation.

During this call, E*TRADE Financial may also discuss some non-GAAP financial measures in talking about its performance. These measures will be reconciled to GAAP either during the course of this call or in the company's press release, which can be found on its website at investor.etrade.com.

This call will be recorded. A replay of this call will be available via phone, webcast and podcast beginning today at approximately 7 PM Eastern Time. The call is being webcast live at investor.etrade.com. And no other recordings or copies of this call are authorized or may be relied upon.

And with that, I will now turn the call over to Steve Freiberg.

Steven J. Freiberg, Chief Executive Officer

Thank you, everyone, for joining us this afternoon. I am pleased to be participating in my first call as E*TRADE's Chief Executive Officer. To begin today's call, I would like to share a few thoughts and then Bruce will take you through the first quarter results. From there, I will add a few closing comments before we take your questions.

I have had a very busy and exciting first few weeks at E*TRADE learning more about the company, our people and our customers. This is a pivotal time for the company and I am energized by the opportunity to lead the organization through its next phase of growth and innovation.

My predecessors, Bob Druskin and Don Layton, the senior management team, and really the entire organization navigated the company through very challenging times and today with a solid brokerage business, complemented by an improvement balance sheet and its strengthened capital structure, E*TRADE is well positioned for grow and profitability.

I was attracted to the CEO role at E*TRADE for a number of reasons. I am a builder of businesses and I look forward to working with the team to build on the company's current momentum. In addition, I believe E*TRADE's focus on expanding customer relationships both with active traders and long-term investors aligns well with my experience in building consumer franchises, through enhanced value propositions, customer segmentation, product innovation and world class customer service. E*TRADE remains a respected company with a powerful financial services brand and as I spend time with our company and our people, I am even more confident about E*TRADE's opportunity to reach its full potential and I look forward to engaging with you on our progress.

As Bruce will describe, E*TRADE's first quarter performance exhibits several positive trends. Earnings are headed in the right direction. Our retail brokerage business continues to compete effectively, balance levels in our loan portfolio declined at a consistent rate with improving delinquency metrics, and for the first time in two years, E*TRADE Bank internally generated, rather than used, capital. These trends provide with us the flexibility to make investments that will drive our continued leadership as a trading and investing platform and our ongoing expansion in the long-term investor segment.

And with that brief introduction, I will turn the call over to Bruce.

Bruce P. Nolop, Executive Vice President and Chief Financial Officer

Thank you, Steve. We are pleased with our quarterly financial performance and the progress we continue to make in building out a comprehensive product and service offering that supports the needs of a broad range of investors. Before summarizing our financial results, I will review a few highlights of the quarter.

On the product side, a number of new customer offerings and enhancements were introduced. For long-term investors E*TRADE capital management introduced managed investment portfolios with a competitive fee structure and an accessible entry point of only $25,000. And Power E*TRADE Pro users now have access to an expanded feature set including streaming CNBC broadcasts.

In addition, E*TRADE Mobile Pro for the new iPad was recently released and we are proud that Apple highlighted our application on its download site and during its media briefings throughout the launch. We continued to lead the industry with tools that support today's increasingly mobile investor.

During the quarter, we also simplified our fee structure to enhance our value proposition to customers. We eliminated the 12.99 pricing tier, as well as incremental commissions that applied to certain trades. And effective in the second quarter, we are eliminating all of our account inactivity fees. We expect that these changes will reduce our revenue by approximately 50 million in 2010, but view the changes as an investment in customer satisfaction that we believe will reduce attrition rates over the long-term.

We were gratified that Barron's recognized our comprehensive customer experience in its 2010 Annual Online Broker Survey. Barron's awarded E*TRADE Securities four out of five stars, described us as a one-stop shopping destination, highlighted our mobile trading technology, and listed us among the best firms for long-term investing.

Turning to our financial results, the company had a net loss of 48 million, or $0.02 per share during the quarter, which compares with a net loss of 67 million or $0.04 per share in the prior quarter, and a loss of 233 million or $0.41 per share, in the first quarter of 2009.

During the quarter, we generated 537 million of net revenue, which is an increase of 13 million from the prior quarter and an increase of 39 million or 8% from the same quarter a year ago. Our revenue this quarter included net interest income of 320 million, which was essentially flat compared with last quarter. This reflected a net interest spread of 2.96% on average interest-earning assets of 42.4 billion. Therefore, while average interest earning assets declined by 1.4 billion, a 10-basis point expansion in interest income spread allowed us to maintain a consistent level of net interest income.

Commission, fees and service charges, principal transactions and other revenue were 196 million. This was a 5% sequential decline compared with the fourth quarter which reflected lower retail trading activity as well as $0.10 decline in the average commission per trade.

The decline in the average commission included the impact of our recent pricing changes, which was partially offset by a more favorable customer mix this quarter. We enjoyed increased principal transactions this quarter in our market-making business. They were up 3 million from the prior quarter and 9 million from the prior year.

Our revenue this quarter also included 29 million of net gains on loans and securities. This net gain was greater than the 9 million of impairments during the quarter. Our total operating expense for the first quarter declined from the prior quarter by 23 million to 295 million. This included lower compensation, real estate owned and bad debt and restructuring expenses, which more than offset seasonal spending for advertising and market development. Our operating expense declined 4% compared with the first quarter of 2009, if we exclude FDIC insurance premiums and restructuring activities during both periods.

We are well on the way toward completing our previously announced plan to restructure our operations. We are exiting local market trading operations but will continue to offer customers residing outside of the U.S. the ability to trade in U.S. securities. We completed the sale of our German operation at the end of last year and in April, we consummated the sales of our local Nordic and U.K. businesses.

During the quarter, we recorded 3.4 million in international restructuring charges. Over the next two quarters, we expect to record approximately 1 million in restructuring charges including a $3 million credit during the second quarter and a $4 million charge during the third quarter.

The restructuring charges are lower than previously expected due to a gain on the sale of the U.K. business and lower than anticipated costs. With our restructuring largely completed, we will focus on U.S. metrics going forward as the international local activity will be phasing out over the next few quarters.

DARTs for our U.S. operations were 155,000 during the first quarter, which is down 2% from the prior quarter and 11% compared with the first quarter of 2009, a period of significant market volatility. Brokerage accounts were up 2,000 and we ended with 2.6 million accounts.
Net new asset flows into our brokerage business were a positive 2.2 billion during the quarter. Therefore, while the total number of brokerage accounts remained relatively constant, we believe the generation of net new assets indicates higher quality customer accounts. Customer assets in the U.S. were $159 billion at quarter end.

Net new assets were a positive 400 million during the quarter with the increase in brokerage assets more than offsetting the planned decline in customer bank assets. Brokerage customer cash increased by 1.4 billion to 21.8 billion, while bank customer cash declined by 1.8 billion, including the sale of approximately 1 billion of savings accounts to Discover. Customer margin receivables in the U.S. grew by 5% during the quarter and ended at 3.8 billion. This represented a 67% increase from a year ago.

Turning to the balance sheet, we made continued progress in the runoff of our loan portfolio with total loans declining by 1 billion during the quarter. Our loan loss provision declined for the sixth consecutive quarter from 292 million in the prior quarter to 268 million this quarter. Net charge-offs were 288 million, which was a $36 million decrease from the prior quarter. Because our provision was less than our charge-offs this quarter, our loan loss allowance declined by 20 million. Our loan loss reserve continues to be approximately 1.2 billion which is equal to 6% of total loans.

Delinquency trends continued to improve with quarter-over-quarter total special mention delinquencies declining by 4% and total at-risk delinquencies declining by 8%. We continue to be pleased with the impact that our loan modification program is having on our credit exposure and comfortable with our provision.

As Steve highlighted earlier, we were extremely pleased that the bank generated 48 million in regulatory risk-based capital during the quarter. And while we may not generate capital in every quarter, we do expect that the bank will generate capital for the full year 2010, marking a key milestone in our return to financial strength.

Our bank capital ratios continue to be substantially in excess of regulatory well capitalized thresholds. As of March 31, the Tier 1 capital ratio was 6.83% to total adjusted assets and 13.08% to risk-weighted assets.

Our sale of the savings accounts in particular allowed us to free up approximately 50 million in Tier 1 capital. We also ended the quarter with 947 million of risk-based total capital in excess of the level that our regulators define as well-capitalized.

We ended the quarter with 418 million in corporate cash, an increase of approximately 25 million from the prior quarter. We expect to receive during the second or third quarter a tax refund of approximately 100 million related to the legislation in 2009 that extended net operating loss carrybacks to five years. We expect that the parent company will retain 95 million of this cash with the remaining 5 million going to the bank. Given our improving financial position, we plan to pay cash for the May coupon on our Springing Lien Notes, although we will consider this decision more specifically as we approach the interest payment date.

Finally, I would like to highlight a change that we are making in our financial reporting this quarter. In addition to the trading and investing and the balance sheet management segments, we are now providing increased visibility into our corporate expenses with the introduction of a new corporate segment. This new corporate segment includes unallocated expenses for finance, legal, human resource, and risk management functions as well as corporate interest expense.

In summary, we believe that our first quarter results demonstrate the strength in our core retail franchise and continued improvement in our overall financial condition. We welcome Steve to the organization and look forward to his leadership as we focus on growth and profitability.

And with that, I will turn the call back to Steve for closing remarks.

Steven J. Freiberg. Chief Executive Officer

Thank you, Bruce. Before opening the call for questions, let me share a few additional comments. Clearly we are on the right track in both our brokerage business and in our legacy loan portfolio and I am committed to continuing this positive trend.

As we generate capital and move towards profitability, our challenge is to invest in and grow our core brokerage business, manage legacy risk, and identify and prioritize opportunities for enhancing growth. I welcome this challenge and I am certain that the rest of our management team does, too.

And although it is still early days for me, I have several thoughts about E*TRADE's future. These include that we build on our heritage and strength as a technology leader to develop and/or embrace the next set of disruptive innovations, further leverage roughly involving research, segmentation, and decision science tools to drive more effective customer acquisition and retention and to expand customer relationships, particularly in the long-term investor segment. Enhance our product suite and customer interaction models to better serve our active trader and long-term investor segments and continue to support our brand and extend it more fully.

Not surprisingly, these themes support our strategy to extend our leadership in the active trader segment while continuing to expand our relationships with long-term investors. I look forward to the coming weeks and months as we develop and execute plans for E*TRADE's next stage of growth and as I said earlier, I look forward to engaging with you on our progress.

With that, operator, we are ready to take questions.

QUESTION AND ANSWER SECTION

Operator: [Operator Instructions] Our first question comes from William Tanona of Collins Stewart.

<Q – William Tanona>: Good morning, Steve. Good morning, Bruce, sorry, I should say, good evening. Question on delinquencies, particularly the 1.4; I was surprised to see that the early-stage delinquencies have actually stayed flat here for it looks like the last two to three quarters. And I was also I guess, surprised to see the later stage delinquencies increase here. It just seems like it's a trend that is not necessarily consistent with some of the other financial services companies that we have seen report as of late?

<A – Bruce Nolop>: This is Bruce, and one thing to remind everyone is that for first lien delinquencies, we have a month lag and so it's really the statistics for us is through February and some of the ones you may be comparing may be through March. Overall, we're very happy with the stabilization we're seeing in delinquencies and we expect the trends to continue and any additional information we have since the February time period would reinforce that belief.

<Q – William Tanona>: Okay. And then, in terms of the $1 billion in terms of loan reductions, there you mentioned that $700 million was principal reductions as well as prepayments. Can you quantify the difference between prepayments and principal reductions? And specifically how much of that is modifications?

<A – Bruce Nolop>: In terms of prepayments, it's – the lion's share of the reduction it's in the 700 million, a very small amount of actual maturities.

<Q – William Tanona>: Okay. And in terms of the $47 million of risk-based capital that was created as a result of changes that took place on the risk-weighted assets, can you help me understand exactly what changes took place to free up that capital?

<A – Bruce Nolop>: The primary change would be as the loan portfolio pays down – so that's reduced, the money is reinvested in agency securities so it's that difference in the risk weighting, which is a major part of it. In addition, we were able to use more of our deferred tax asset this quarter. And then just the relationship of the profitability of the bank versus the loan loss provision is more favorable than it had been.

<Q – William Tanona>: Okay. Thanks.

Operator: Your next question comes from Roger Freeman of Barclays.

<Q – Roger Freeman>: Hi, thanks. I guess, first, your comment on the – dropping the fees for inactive accounts, can you just help us think about that a little bit more? I understand, I guess you're looking for those as positive sources of reengagement at a later point but as you think of your balance sheet shrinkage objectives and the cash that is in those accounts, you have to hold capital against, does that counter at all some of your near term priorities?

<A – Bruce Nolop>: No. As the inactivity fee, we found, was just one of the primary customer dissatisfiers, and it was an irritant. And we wanted to make sure that we were doing everything we can to retain our accounts and not have anything that would be a dissatisfier to them and that will be the lion's share – or not lion's share but the majority of the 50 million will actually be the inactivity fee and so, you will see that coming in starting in the second quarter. But it's part of our overall strategy to focus on our online brokerage business and to grow our customer accounts and the quality of accounts.

<Q – Roger Freeman>: What's the profitability of an inactive client that doesn't use any of your services, doesn't trade, and will there be a specific action to reengage them?

<A – Bruce Nolop>: Sure. And the tendency is that often an account goes inactive for a period and they can be reactivated in terms of their level of engagement with us. And it affects not only the inactive ones. It's just a perception that we found that even some of our very best customers had a perception that that we had something that was not consistent with the other competitors in the online industry. And so just from a customer perception standpoint that has a benefit as well.

<Q – Roger Freeman>: Got it. Okay. And then on the provision for loan loss you might have said this, I might have missed it. Why did it pick up in the HELOC portfolio so much in the quarter?

<A – Bruce Nolop>: Right. The way it works is that the provisioning is based on your actual experience and then you forecast on that basis and it so happens that this quarter, the loan modification program was more skewed toward home equity than toward our first lien. I am sorry, I reversed that – more for first lien and less home equity. And the home equity went down because we were putting in some operational changes and that had the effect of reducing that activity during the quarter and first liens is an area that we have been gradually increasing. So that effect creates a disproportion compared to what had been the experience and that flows through your loan provision. Since that time, we've returned to more normalized mix of loan modifications including an increase in home equity modifications and therefore going forward, we fully expect starting with the second quarter to be back to a normalized provisioning and you will see home equity and first lien return to their more normal trends. And overall, we expect that the provisioning for the year will not differ from where we began with our expectations.

<Q – Roger Freeman>: Okay, but does that mean the last few quarters the decline in provisioning has really been more just a function of modifying loans and some pushing out the potential problems?

<A – Bruce Nolop>: No. It's really the function of the change, and we, in our analysis, concluded that although you have some differences in the absolute amounts of provisioning, in terms of the trend, that it doesn't have an impact on provisioning or on the delinquencies.

<Q – Roger Freeman>: Okay. Last point – last question quickly – customer mix – you made a comment it was more favorable this quarter. What was that in reference to?

<A – Bruce Nolop>: Yeah. The primary one was that we had more transactions in our corporate services group, which is in the stock plan administration. And it's more exercises of restricted stock that they sell the stock into the market. And that's a higher profitable trade.

<Q – Roger Freeman>: Oh, interesting. And is that – do you think its going to end up being a seasonal thing in particular with more restricted stock being used for comp -

<A – Bruce Nolop>: Yeah. That's probably something that more and more will take into account that there does seems to be more restricted stock that vests in the first quarter and people are tending to sell their stock when it vests. The other one in the mix I would mention is we had an uptick in options as well, which is another favorable.

<Q – Roger Freeman>: Yeah, okay. Great, thanks.

<A – Bruce Nolop>: Yeah.

Operator: Your next question from Rich Repetto of Sandler O'Neill.

<Q – Richard Repetto>: Yes, good evening and welcome, Steve. Hopefully you come in at an upswing here, for sure.

<A – Steven Freiberg>: Thanks, Rich.

<Q – Richard Repetto>: I guess to follow up on this – on the question that Roger asked on the provisioning. To be blunt, I don't fully understand because I see you overprovided, even though the charge-offs in home equity have sort of continued down on a trend downward. So I guess – would you expect charge-offs later on because of these modifications to increase?

<A – Bruce Nolop>: Rich, what I'll suggest is have Paul Brandow, our Chief Risk Officer, elaborate further and just see what color he can add.

<A – Paul Brandow>: I will give you an explanation now and then maybe if you have some questions later on, perhaps we can handle them there. But this is really an effect of the interplay between the two different reserves that are involved with loans, the FAS 5 reserve and the one that is specific to TDRs. The way we do a forecast, right, we need to make an assessment of the amount of modifications that are going to be done, which would, in turn, then create the FAS – both the FAS 5 and the TDR and the FAS 114 reserve. Because modifications for home equity were lower in the first quarter and since our forecasting is based on our most recent experience, that tended to leave more of our loans in a non-modified state which would be showing up in higher FAS 5 reserves. Since we now have returned to a much more normal level of home equity loans, we expect that effect, in effect, to dissolve over the next quarter or two. And so by the end of the year, assuming again that the modification activity stays at what is now the return to higher pays, it should return to what we expected at the beginning of the year.

<Q – Richard Repetto>: Okay. We certainly can spend some time offline going through that. But moving on, the expenses, nice reduction quarterly sequentially in expenses, and Bruce, the other line came down dramatically from, I think, 40, 38 to 21 million. Could you give us some color what was going in that line and why it came down?

<A – Bruce Nolop>: Yes. There are a couple of things. One is you had a lower REO expense that occurred and that's because of stabilization of home prices had a favorable impact on that expense line. And then bad debts that the fourth quarter of 2009, it was an abnormally high amount of charges that went through that line. And we're back to normal bad debt levels.

<Q – Richard Repetto>: Got you. Okay. And the very last question, the focus on the core brokerage, and everybody knows that has been the strength here with the company through the downswing, the economic downswing. We did take – I guess the question is, there was sort of an uptick in attrition. There was a net loss of accounts in March. I was just trying to see – I'm also looking back at the prior quarter, and it looks like the accounts are different than in the last press release. So is there some accounting thing going on with the brokerage accounts or – and what do you attribute the attrition in March to?

<A – Bruce Nolop>: Sure. In March, you have the inactivity fee comes in, so you typically would find that that would have an impact in the last month of the quarter. And as we discussed a little earlier, in some ways, this is getting rid of the less valuable accounts. And so more and more what we look at is the overall quality of the accounts and that's, from our point of view, the best metric is the 2.2 billion in net new assets that came in. So while we want to grow the number of accounts, we are probably even more focused on the net new assets. And because of things like inactivity fees and other factors, you'll have changes that we, should help going forward.

<Q – Richard Repetto>: And just on the accounting, I'm looking at the last press release that said 2.7 million brokerage accounts, was there change--

<A – Bruce Nolop>: Yeah, the change was that in – as I mentioned, we were going to focus on U.S. metrics going forward. And so we're excluding the international local accounts. And so we're trying to be apples-to-apples. And going forward, it should get a little less confusing, but for a while we're going through the transition.

<Q – **Richard Repetto>:** Understood. Thanks, guys.

Operator: Your next question comes from Keith Walsh of Citi.

<**Q – Keith Walsh>:** Good morning, everybody – good evening, sorry. Getting a little confused here. First for Bruce, just opportunity for more loan sales and specifically, what's the gap you're seeing these days around the market value versus what you've marked these loans to? And then I've got a couple follow-ups.

<**A – Bruce Nolop>:** Yeah rather than quote specific prices, I would say that we continue to monitor the market. And what we see are the prices in the secondary market are still below the intrinsic value. And so we do not see the potential to do anything material in terms of additional loan sales.

<**Q – Keith Walsh>:** I mean what's the trend on that gap, though? What have we seen over the last six to eight months?

<**A – Bruce Nolop>:** With that I think for the additional color, I'll call on Bob Burton, who is President of the E*TRADE Bank to comment.

<**A – Robert Burton>:** We're seeing some narrowing of that difference between what we believe the intrinsic value is in the market and we are looking, for example, to take advantage of opportunities to potentially securitize some of the loans in the portfolio. But we still think there's a ways before that gap narrows to the point where we would even contemplate additional sales.

<**Q – Keith Walsh>:** Okay. And then second question for Bruce – maybe if you could just remind us upward movement on short-term rates, why your two larger competitors it has positive EPS leverage and for you guys, it's actually slightly negative.

<**A – Bruce Nolop>:** Yeah, I can't comment on the balance sheet of the competitors, but for us, we manage the balance sheet to be neutral in terms of the impact of interest rate movements, and even since last quarter, we have become more neutral. So with a change in short-term rates, at this point, we don't see any effect on our interest income. And that's a combination of just the way that the mix of assets and liabilities are constructed as well as hedging activities, which the people in our bank treasury department manage.

<**Q – Keith Walsh>:** Okay. And then the third question just for Steven around strategy here, what attracted you to this job specifically, what do you view as your immediate priorities as we move throughout 2010? Thanks.

<**A – Steven Freiberg>:** Keith, just to frame it – one, the industry at large, which essentially is the brokerage and financial services, has always been an interest of mine and I've spent 10 out of my 30 years on that side of the house. And I've always basically enjoyed it and enjoyed basically building franchises within the category.

Secondarily, E*TRADE in particular, as I said earlier, is at a pivotal point, and I've spent also a good part of my career in turnarounds and I'm very optimistic at this point about the opportunity that E*TRADE specifically presents. I also enjoy consumer-oriented franchises. We've got a terrific brand, a very strong core business. We have the potential to expand that core business into other segments that I think hold significant potential. And we have to work through, as it is clearly evident, some of the challenges of the past, which is, in fact, the legacy asset book, and so we can't lose sight or we can't basically let up the vigilance around that. So that in itself – and again just to remind the group, it's been all of about three weeks. So that I'm beginning to get a better understanding of both the opportunity, the issues and risks associated with the franchise but on balance, I couldn't think of a better company at a better time to join.

<Q – Keith Walsh>: Great. Thank you.

Operator: The next question comes from Matt Snowling of FBR Capital Markets.

<Q – Matt Snowling>: Hi, good evening. Just maybe a question on the net interest margin, it came in a little higher than we were looking for, is that just simply the effect of redeploying the cash on the balance sheet in higher rates, higher rates security?

<A – Bruce Nolop>: Sure. There's really three reasons. One is, as you mentioned that we were able to put more cash into securities. Secondly, we have a higher margin balance, which is a very much lucrative balance. And third is the mix of our deposits. It became more skewed towards brokerage cash rather than bank cash and that in turn lowers our cost of funding, which gets translated into a higher margin.

<Q – Matt Snowling>: Okay. And maybe going back to your interest rate sensitivity, you mentioned you were neutral right now?

<A – Bruce Nolop>: Yes.

<Q – Matt Snowling>: To rates. But is the model itself still asset sensitive in that and you've just hedged out some of the sensitivity in the near term?

<A – Bruce Nolop>: I tell you, again, I think this is when I'll call on Bob Burton, who is the President of the Bank, to explain further about how we manage that.

<A – Robert Burton>: Yeah, in general, although we certainly engage in hedging activity to customize our position, the balance sheet is generally moving closer and closer to neutral as the loan portfolio pays off. And so we have the rift generated by the loan portfolio and by our securities portfolio, offset by the value creation as interest rates move from our large internal deposit base. So as a rule, it leans towards being basically neutral.

<Q – Matt Snowling>: Does that assume that you reprice your deposits in line with rising rates?

<A – Robert Burton>: Well, it certainly makes – there's certainly a series of assumptions we have to make about how sensitive our deposits are to moving and we use historical numbers to look at that.

<Q – Matt Snowling>: Okay. Thanks.

Operator: Your next question comes from Michael Carrier of Deutsche Bank.

<Q – Michael Carrier>: Thanks. Just a question on the net new brokerage accounts. You had this quarter, you had a little less than 2,000, last quarter it was negative. Just trying to figure it out because in the industry when you look at some of your peers, they are showing two-year highs in terms of net-new brokerage accounts and organic growth. I know when I look at your spending on the marketing, it's a little bit lower, but trying to understand if there's anything else going on there in terms of the new growth?

<A – Bruce Nolop>: Two comments I'd make, one is that if you recall in January, we had some eschevement and so 6,000 accounts were eliminated through that process and that was not something that was in prior quarters, if you compare.

And secondly is that, we find that new accounts are very largely correlated with volatility. And so this is a period of lower volatility. And I'd just comment that already when you've seen some increase in the market volatility that we can see the impact from that immediately and so that's something that probably is a more telling factor in the slower growth.

<Q – Michael Carrier>: Okay, and then secondly, just on the outlook for the commissions and the inactive fees, if I look at the 50 million that you're projecting for the year, just trying to understand how much of that was in the first quarter versus -

<A – Bruce Nolop>: Sure. Yeah. First quarter, the impact was about 4 million. And for the next three quarters, it will be 15 million, approx, per quarter, which gets you up to the 50 million.

<Q – Michael Carrier>: Okay. Thanks a lot.

Operator: Your next question from Mike Vinciquerra of BMO Capital Markets.

<Q – Michael Vinciquerra>: Thank you. Just following up on Mike's question there on the commission rate, you did say that the majority of the lost $50 million is going to come from the inactivity fees, right? So there's not going to be much of an impact on that – the commission rate itself.

<A – Bruce Nolop>: Yeah. I can give you a feel for that. For the quarter, we estimate that it was about a $0.33 impact and again, that was offset to a large degree by mix. And going forward, that would be more in the range of about $0.50.

<Q – Michael Vinciquerra>: Okay, great. And then the corporate services side, I mean as stock prices have risen certainly more people have incentive to sell restricted stock if it's vested, so does that help to support potentially more activity from that segment?

<A – Bruce Nolop>: Sure. Yeah. I'm going to have Mike Curcio, who is the head of our brokerage operations and also corporate services reports to him, so maybe he can add some color.

<A – Michael Curcio>: Yeah, absolutely. As markets have come up and individual stocks have come up, there's become more and more value in options than we see left in DARTs through the corporate service channel because more options are exercised, more restricted stock is sold and that's a positive there and it's on our commissions because the commissions are much higher than the rack rate.

<Q – Michael Vinciquerra>: Great, thank you, Mike. And then just one other thing, Bruce, on the net interest margins that you didn't mention as far as the lift in the quarter. I noticed your repo rates fell pretty substantially, is this reflective of tighter credit spreads in the marketplace or how did that kind of come about? It's pretty significant quarter over quarter.

<A – Bruce Nolop>: Again, this is one I'm going to refer to Bob Burton.

<A – Robert Burton>: Certainly, some of it is related to the market but in addition, early last year, we locked in a lot of longer-term repo arrangements that are expiring and as they expire, we've been able to reduce our cost of repo.

<Q – Michael Vinciquerra>: Great. So that sounds like it's a sustainable level now with these in the low twos now.

<A – Robert Burton>: That's what we would expect.

<Q – Michael Vinciquerra>: Great. Thanks, guys.

Operator: Your next question comes from Howard Chen of Credit Suisse.

<Q – Howard Chen>: Hi, good afternoon, everyone.

<A – Bruce Nolop>: Hi.

<Q – Howard Chen>: Steve, your commentary was pretty constructive on the outlook for the organic growth of the franchise. I'm just curious as the new CEO, thoughts on the feasibility and appetite of a strategic sale of the franchise?

<A – Steven Freiberg>: We expected that question could come up. Let me just emphasize Howard – and I do appreciate the question – that we have a thriving online brokerage business. We've strengthened our financial position and I believe we have the opportunity to grow and prosper as a stand-alone company and I think that sums it up.

<Q – Howard Chen>: Okay. Thanks. Just wanted to hear it from you. And then second, any latest thoughts on what the appropriate size of the balance sheet and balance sheet composition is for the longer term franchise?

<A – Steven Freiberg>: Again, just to reiterate, it's been all of three weeks. I think the trend that the business has followed to this point is correct, which essentially is a combination of reducing the legacy at-risk assets, de-risking the company on a whole host of fronts, and as we develop a broader, longer-term strategic plan for the company, which is part of one of my year-end priorities I think that will be a derivative of the plan overall. So it will be a combination of relative size, diversification of the franchise, level of risk that we're willing to take on with an expectation of kind of earnings and returns. So it's very early to give you an absolute outside the context of a broader set of strategies but that is a high priority for all of us so that we can frame, essentially, the future of this company.

<Q – Howard Chen>: Okay. Great. Thanks. And then final question, loan portfolio seems to be running off, credit behaving as you expect or better than expected. I guess as the environment becomes more normal, just any broad thoughts on when that inflection point and franchise profitability happens?

<A – Steven Freiberg>: At this point, one, we're not predicting it. All again, I will just emphasize that the trends have been positive and we expect, as you've described it, those broad macro trends to continue and within that frame, we believe that we can continue to produce the positive results, the positive trend. But predicting precisely when we would cross to profitability is something we would not really provide at this point.

<Q – Howard Chen>: Okay, great. Thanks so much for taking my questions.

Operator: Your next question comes from Joel Jeffrey of KBW.

<Q – Joel Jeffrey>: Just a quick question, I think you said earlier that most of the rundown in the loan portfolio was due to prepayments. Now, if we get into a higher rate environment, do you continue to see that trend as being sustainable?

<A – Bruce Nolop>: You want to comment on that, Bob? Bob Burton?

<A – Robert Burton>: Sure. Certainly we continue to expect that we will continue to see prepayment. Obviously we're going to move with the industry and to the extent that prepayments flow we expect to see that. However, remember that our portfolio is older and we think that's a constant benefit across a number of factors in that age is going to help us.

<Q – Joel Jeffrey>: Okay. Great. And then it looked like advertising was up quarter-on-quarter and typically seasonally up in the first quarter of the year but given your new sort of heavy focus on brokerage side of the business, is this an elevated trend we can continue to see? Or do you think it will resort back to more traditional seasonal levels?

<A – Bruce Nolop>: Well, what we said at the beginning of the year is we expected the overall spending on advertising and market development to be roughly equal to modestly above 2009 and that continues to be what we expect. But we are having it more broadly spaced throughout the year than we did last year.

<Q – Joel Jeffrey>: Okay. Great. And then just lastly, in terms of your working capital needs, how much working capital do you guys need to run the business on an annual basis?

<A – Bruce Nolop>: Well, in terms of the brokerage company, it's – in connection with the Bank as well, and maybe I can answer it that way that we look at 1 to 2 billion of cash that we would maintain in the Bank and that would be the level and we're slightly above that amount right now.

<Q – Joel Jeffrey>: Okay, great. Thanks.

Operator: Your next question comes from Daniel Harris of Goldman Sachs.

<Q – Daniel Harris>: Hi, good evening, guys. One of the things I wanted to touch on was the market making business. It looks like the shares you're trading are going well way up and obviously it was a difficult market for market making in the quarter with volatility declining. But how do you see that part of your business moving going forward?

<A – Bruce Nolop>: Yeah. This is a really good story. As I mentioned, the transactions are up and so with that, I am going to let Mike Curcio, who supervises this business as well maybe elaborate on what is a real gem for us right now.

<A – Michael Curcio>: Sure, Bruce. We're seeing some really good trends now that we're past our crisis and we invested in our business, making it more automation in all the NMS stocks. We're getting a lot more external customers, so that's really where you're seeing the growth, especially in the bulletin boards. But we've also seen a nice lift in the NMS business as well and we feel that trend will continue as long as market conditions are the way they are and they could even increase if we get more volatility. So we're very excited about that business.

<Q – Daniel Harris>: Okay, and sort of on a similar vein, can you sort of remind us what are the obligations and opportunities you guys have to increase payment for order flow as we move further away from some of the things that have occurred over the last few years?

<A – Bruce Nolop>: Well, as you know, the agreement that we have with Citadel expires at the end of the year and we will be looking at alternatives for the order flow. And we'll be comparing different alternatives and obviously need to make a decision before then. But at this point, don't have anything to report.

<Q – Daniel Harris>: Okay. And then just lastly, I know that there was some moving parts in the first mortgage and the HELOC book on the provision rates. But in terms of the first mortgage portfolio, we are starting to see some stabilization in the charge-offs. I don't know where, obviously the number goes next quarter, but we were trending that you were building the reserves prior to this quarter. You said that that probably flip-flops next quarter. I mean at what point do you think you'll start releasing reserves in that first lien portfolio, or do you seeing any signs of what actually lead us to think that's sooner rather than later?

<A – Bruce Nolop>: Again, Paul Brandow, our Chief Risk Officer response?

<A – Paul Brandow>: I think you almost answered my question for me. We do agree that trends in the home equity portfolio have been more favorable in the first lien. But first lien also has declined quite consistently over the past 12 months at a slower pace than home equity, because as we mentioned before, it's a less seasoned portfolio and furthermore we had first mortgages with relatively low LTVs and it's taken a longer time for some of those to become delinquent.

Having said that we would expect the positive trend to continue, perhaps at this more moderate pace that we've seen over the past few months. But to the point that was mentioned before, in the quarter the special mention delinquencies were more or less flat, but there were improvements in the roll rates of other categories. Actually we did see more significant declines in the later stage buckets. So, again, we won't predict when exactly that means that we would flip, but we're pretty confident that's coming not too far away.

<Q – Daniel Harris>: But -- so the big provision bill that you -- or the big reserve bill that you had in the fourth quarter that, probably shouldn't expect anything much more than that, given the trends we're seeing and maybe getting better? That's as far as I understand what you're saying. So thanks very much.

<A>: You're welcome.

Operator: Your next question comes from Faye Elliott of Banc of America/Merrill Lynch.

<Q – Faye Elliott>: Hi, thank you. Good afternoon. I think I might be repeating the previous question. But I just wanted to make sure for modeling sake I understand I guess your philosophy on your provision and your reserve. And it looks like your reserves to EOP loans and your reserve to, I'm sorry, MPAs was going up across categories and actually as a whole. And I guess I'm still not clear whether you're saying that you're ready to lower that provision such that these numbers can start coming down, these ratios can start coming down a little bit.

<A – Bruce Nolop>: Yeah, this is Bruce, and the one thing I would say at the outset is our philosophy, really isn't the governing factor; that we apply consistent procedures and a very rigorous modeling. And so just I don't want you to think that this is a subjective process and with that, I'll let Paul respond.

<A – Paul Brandow>: The only thing I was going add to what Bruce said was keep in mind that we have a steadily declining portfolio, so other things being equal would drive the ratios up.

<Q – Faye Elliott>: Right, but, and I expected that would be the reason. But if you have a continually declining portfolio, then would you provision less to drive those – to allow those ratios to start coming down given the trends that we're seeing?

<A – Paul Brandow>: But I think the effect would be that or the result would be that but as Bruce alluded to before, our process for providing for loans, and reserving for loans is based on a consistent procedure, which starts with an estimation of losses going forward, based on a number of factors including the loan level performance of our own portfolio. So, yes, what you say is going to happen over time, but we get at with it a different set of analysis.

<Q – Faye Elliott>: Okay. Thank you.

Operator: [Operator Instructions] Your next question come from Roger Freeman of Barclays.

<Q – Roger Freeman>: Hi, yeah, just a couple follow-ups. On the – with respect to the wholesale funding, I think it was a question earlier about where you're putting maturing loans and you're buying MBS securities. What about further reduction of say FHLD loans since that has a higher cost to it?

<A – Bruce Nolop>: Yeah. I think we've communicated before and I'll just make sure everyone understands that the wholesale funding, we have a couple of constraints that limit our ability to reduce that amount of funding. First, on the home loan bank loans, any reduction there would require a prepayment penalty so essentially, pulls interest cost forward. And that has a negative impact on capital. So it's something we do when we can, but it's not something we can do regularly. And then with respect to the repo financing, the constraint there is there are hedging arrangements that are associated and that would be pretty significant financial impact if we tried to reduce.

<Q – Roger Freeman>: Just on that one – I know you have talked about that in the past -- what's the average duration on the swap hedges on the repo portfolio? At some point, do those run off?

<A – Bruce Nolop>: Eventually, but it's a long duration.

<Q – Roger Freeman>: Okay.

<A – Bruce Nolop>: My memory is bit more like four or five years, and then maturity is like 10.

<Q – Roger Freeman>: Okay. Got it. But I just one thing, on repo I think the balance actually went – sorry FHLB actually went up in the quarter. 2.761 versus 2.749?

<A>: Yes, just 2 million.

<Q – Roger Freeman>: Yes. It wasn't much. Yes. I was wondering why it would go up at all.

<A – Bruce Nolop>: Our bank treasurer, any comment on that, Mike Peasy?

<A>: Home loan bank line has a certain amount which is just overnight. It is a very small amount.

<Q – Roger Freeman>: Okay.

<A>: There are a lot of intraday fluctuations there between the cash side of the balance sheet on the asset side and the funding side and so you will see small amount of variability. There – you shouldn't expect to see any large growth.

<Q – Roger Freeman>: Okay. All right.

<A – Bruce Nolop>: Definitely, no change in strategy.

<Q – Roger Freeman>: Got it. Okay. Makes sense. All right, just on a lighter note. Would you say you've got more advertising benefit out of this frivolous Lohan lawsuit than any expenses?

<A – Bruce Nolop>: Well, we won't comment on that, but I would just say overall we have got a lot of free media from the whole Super Bowl campaign that made that a very worthwhile -

<Q – Roger Freeman>: Yes.

<A – Bruce Nolop>: As the CFO, I appreciate that return on investment.

<Q – Roger Freeman>: Got it. Yes. Okay, thanks.

Operator: This concludes the question-and-answer portion of today's call. I will now turn the conference back over to Mr. Steven Freiberg for any closing remark.

Steven J. Freiberg, Chief Executive Officer

Okay. Thank you for joining us tonight. We feel very good about the progress we made in the first quarter, and we look forward to speaking with you again next quarter. Good evening.

Operator: Thank you. This concludes your conference. You may now disconnect.