KEYCORP /NEW/
Form 10-Q
May 03, 2018
UNITED STATES
SECURITIES AND EXCHANGE COMMISSION
Washington D.C. 20549

FORM 10-Q

QUARTERLY REPORT PURSUANT TO SECTION 13 OR 15(d)
OF THE SECURITIES EXCHANGE ACT OF 1934

For the Quarterly Period Ended March 31, 2018

Commission File Number 001-11302

Exact name of registrant as specified in its charter:

Ohio	34-6542451
State or other jurisdiction of incorporation or organization:	I.R.S. Employer Identification Number:

127 Public Square, Cleveland, Ohio	44114-1306
Address of principal executive offices:	Zip Code:

(216) 689-3000
Registrant's telephone number, including area code:

Indicate by check mark whether the registrant (1) has filed all reports required to be filed by Section 13 or 15(d) of the Securities Exchange Act of 1934 during the preceding 12 months (or for such shorter period that the registrant was required to file such reports), and (2) has been subject to such filing requirements for the past 90 days. Yes No

Indicate by check mark whether the registrant has submitted electronically and posted on its corporate Web site, if any, every Interactive Data File required to be submitted and posted pursuant to Rule 405 of Regulation S-T (§232.405 of this chapter) during the preceding 12 months (or for such shorter period that the registrant was required to submit and post such files). Yes No

Indicate by check mark whether the registrant is a large accelerated filer, an accelerated filer, a non-accelerated filer, smaller reporting company, or an emerging growth company. See the definitions of "large accelerated filer," "accelerated filer," "smaller reporting company," and "emerging growth company" in Rule 12b-2 of the Exchange Act. (Check one):

Large accelerated filer		Accelerated filer
Non-accelerated filer	(Do not check if a smaller reporting company)	Smaller reporting company
Emerging growth company		

If an emerging growth company, indicate by check mark if the registrant has elected not to use the extended transition period for complying with any new or revised financial accounting standards provided pursuant to Section 13(a) of the Exchange Act.

Indicate by check mark whether the registrant is a shell company (as defined in Rule 12b-2 of the Exchange Act). Yes No

Indicate the number of shares outstanding of each of the issuer's classes of common stock, as of the latest practicable date.

Common Shares with a par value of $1 each	1,061,663,471 shares
Title of class	Outstanding at April 30, 2018

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PART I. FINANCIAL INFORMATION

Item 2. Management's Discussion & Analysis of Financial Condition & Results of Operations

Introduction

This section reviews the financial condition and results of operations of KeyCorp and its subsidiaries for the quarterly periods ended March 31, 2018, and March 31, 2017. Some tables may include additional periods to comply with disclosure requirements or to illustrate trends in greater depth. When you read this discussion, you should also refer to the consolidated financial statements and related notes in this report. The page locations of specific sections and notes that we refer to are presented in the Table of Contents.

References to our "2017 Form 10-K" refer to our Form 10-K for the year ended December 31, 2017, which has been filed with the SEC and is available on its website (www.sec.gov) and on our website (www.key.com/ir).

Terminology

Throughout this discussion, references to "Key," "we," "our," "us," and similar terms refer to the consolidated entity consisting of KeyCorp and its subsidiaries. "KeyCorp" refers solely to the parent holding company, and "KeyBank" refers to KeyCorp's subsidiary bank, KeyBank National Association.

We want to explain some industry-specific terms at the outset so you can better understand the discussion that follows.

- We use the phrase continuing operations in this document to mean all of our businesses other than the education lending business and Austin. The education lending business and Austin have been accounted for as discontinued operations since 2009.
- Our exit loan portfolios are separate from our discontinued operations. These portfolios, which are in a run-off mode, stem from product lines we decided to cease because they no longer fit with our corporate strategy. These exit loan portfolios are included in Other Segments.
- We engage in capital markets activities primarily through business conducted by our Key Corporate Bank segment. These activities encompass a variety of products and services. Among other things, we trade securities as a dealer, enter into derivative contracts (both to accommodate clients' financing needs and to mitigate certain risks), and conduct transactions in foreign currencies (both to accommodate clients' needs and to benefit from fluctuations in exchange rates).
- For regulatory purposes, capital is divided into two classes. Federal regulations currently prescribe that at least one-half of a bank or BHC's total risk-based capital must qualify as Tier 1 capital. Both total and Tier 1 capital serve as bases for several measures of capital adequacy, which is an important indicator of financial stability and condition. As described under the heading "Regulatory capital requirements – Capital planning and stress testing" in the section entitled "Supervision and Regulation" that begins on page 8 of our 2017 Form 10-K, the regulators are required to conduct a supervisory capital assessment of all BHCs with assets of at least $50 billion, including KeyCorp. As part of this capital adequacy review, banking regulators evaluate a component of Tier 1 capital, known as Common Equity Tier 1, under the Regulatory Capital Rules. The "Capital" section of this report under the heading "Capital adequacy" provides more information on total capital, Tier 1 capital, and the Regulatory Capital Rules, including Common Equity Tier 1, and describes how these measures are calculated.

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The acronyms and abbreviations identified below are used in the Management's Discussion & Analysis of Financial Condition & Results of Operations as well as in the Notes to Consolidated Financial Statements (Unaudited). You may find it helpful to refer back to this page as you read this report.

ALCO: Asset/Liability Management Committee.
ALLL: Allowance for loan and lease losses.
A/LM: Asset/liability management.
AOCI: Accumulated other comprehensive income (loss).
APBO: Accumulated postretirement benefit obligation.
ASC: Accounting Standards Codification.
Austin: Austin Capital Management, Ltd.
BHCs: Bank holding companies.
Board: KeyCorp Board of Directors.
Cain Brothers: Cain Brothers & Company, LLC.
CCAR: Comprehensive Capital Analysis and Review.
CMBS: Commercial mortgage-backed securities.
CME: Chicago Mercantile Exchange.
CMO: Collateralized mortgage obligation.
Common Shares: KeyCorp common shares, $1 par value.
DIF: Deposit Insurance Fund of the FDIC.
Dodd-Frank Act: Dodd-Frank Wall Street Reform and Consumer Protection Act of 2010.
EBITDA: Earnings before interest, taxes, depreciation, and amortization.
EPS: Earnings per share.
ERISA: Employee Retirement Income Security Act of 1974.
ERM: Enterprise risk management.
EVE: Economic value of equity.
FASB: Financial Accounting Standards Board.
FDIC: Federal Deposit Insurance Corporation.
Federal Reserve: Board of Governors of the Federal Reserve System.
FHLB: Federal Home Loan Bank of Cincinnati.
FHLMC: Federal Home Loan Mortgage Corporation.
FICO: Fair Isaac Corporation.
First Niagara: First Niagara Financial Group, Inc. (NASDAQ: FNFG).
FNMA: Federal National Mortgage Association, or Fannie Mae.
FSOC: Financial Stability Oversight Council.
GAAP: U.S. generally accepted accounting principles.
GNMA: Government National Mortgage Association, or Ginnie Mae.
HelloWallet: HelloWallet, LLC.
ISDA: International Swaps and Derivatives Association.
KAHC: Key Affordable Housing Corporation.
KBCM: KeyBanc Capital Markets, Inc.
KCC: Key Capital Corporation.
KCDC: Key Community Development Corporation.
KEF: Key Equipment Finance.
KMS: Key Merchant Services, LLC.
KPP: Key Principal Partners.
KREEC: Key Real Estate Equity Capital, Inc.
LCR: Liquidity coverage ratio.
LIBOR: London Interbank Offered Rate.
LIHTC: Low-income housing tax credit.
LTV: Loan-to-value.
Moody's: Moody's Investor Services, Inc.
MRM: Market Risk Management group.
N/A: Not applicable.
NASDAQ: The NASDAQ Stock Market LLC.
NAV: Net asset value.
N/M: Not meaningful.
NOW: Negotiable Order of Withdrawal.
NPR: Notice of proposed rulemaking.
NYSE: New York Stock Exchange.
OCC: Office of the Comptroller of the Currency.
OCI: Other comprehensive income (loss).
OREO: Other real estate owned.
OTTI: Other-than-temporary impairment.
PBO: Projected benefit obligation.
PCI: Purchased credit impaired.
S&P: Standard and Poor's Ratings Services, a Division of The McGraw-Hill Companies, Inc.
SEC: U.S. Securities and Exchange Commission.
Series A Preferred Stock: KeyCorp's 7.750% Noncumulative Perpetual Convertible Preferred Stock, Series A.
TCJ Act: Tax Cuts and Jobs Act.
TDR: Troubled debt restructuring.
TE: Taxable-equivalent.
U.S. Treasury: United States Department of the Treasury.
VaR: Value at risk.
VEBA: Voluntary Employee Beneficiary Association.
VIE: Variable interest entity.

Forward-looking statements

From time to time, we have made or will make forward-looking statements within the meaning of the Private Securities Litigation Reform Act of 1995. These statements do not relate strictly to historical or current facts.

Forward-looking statements usually can be identified by the use of words such as "goal," "objective," "plan," "expect," "assume," "anticipate," "intend," "project," "believe," "estimate," or other words of similar meaning. Forward-looking stateme provide our current expectations or forecasts of future events, circumstances, results or aspirations. Our disclosures in this report contain forward-looking statements. We may also make forward-looking

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statements in other documents filed with or furnished to the SEC. In addition, we may make forward-looking statements orally to analysts, investors, representatives of the media, and others.

Forward-looking statements, by their nature, are subject to assumptions, risks, and uncertainties, many of which are outside of our control. Our actual results may differ materially from those set forth in our forward-looking statements. There is no assurance that any list of risks and uncertainties or risk factors is complete. Factors that could cause our actual results to differ from those described in forward-looking statements include, but are not limited to:

- deterioration of commercial real estate market fundamentals;
- defaults by our loan counterparties or clients;
- adverse changes in credit quality trends;
- declining asset prices;
- our concentrated credit exposure in commercial and industrial loans;
- the extensive regulation of the U.S. financial services industry;
- changes in accounting policies, standards, and interpretations;
- operational or risk management failures by us or critical third parties;
- breaches of security or failures of our technology systems due to technological or other factors and cybersecurity threats;
- negative outcomes from claims or litigation;
- failure or circumvention of our controls and procedures;
- the occurrence of natural or man-made disasters, conflicts, or terrorist attacks, or other adverse external events;
- evolving capital and liquidity standards under applicable regulatory rules;
- disruption of the U.S. financial system;
- our ability to receive dividends from our subsidiary, KeyBank;
- unanticipated changes in our liquidity position, including but not limited to, changes in our access to or the cost of funding and our ability to secure alternative funding sources;
- downgrades in our credit ratings or those of KeyBank;
- a reversal of the U.S. economic recovery due to financial, political or other shocks;
- our ability to anticipate interest rate changes and manage interest rate risk;
- deterioration of economic conditions in the geographic regions where we operate;
- the soundness of other financial institutions;
- tax reform and other changes in tax laws, including the impact of the TCJ Act;
- our ability to attract and retain talented executives and employees and to manage our reputational risks;
- our ability to timely and effectively implement our strategic initiatives;
- increased competitive pressure from banks and non-banks;
- our ability to adapt our products and services to industry standards and consumer preferences;
- unanticipated adverse effects of strategic partnerships or acquisitions and dispositions of assets or businesses;
- our ability to realize the anticipated benefits of the First Niagara merger; and
- our ability to develop and effectively use the quantitative models we rely upon in our business planning.

Any forward-looking statements made by us or on our behalf speak only as of the date they are made, and we do not undertake any obligation to update any forward-looking statement to reflect the impact of subsequent events or circumstances. Before making an investment decision, you should carefully consider all risks and uncertainties disclosed in our SEC filings, including this report on Form 10-Q and our subsequent reports on Forms 8-K, 10-Q, and 10-K and our registration statements under the Securities Act of 1933, as amended, all of which are or will upon filing be accessible on the SEC’s website at www.sec.gov and on our website at www.key.com/ir.

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Selected financial data

Our financial performance for each of the last five quarters is summarized in Figure 1.

Figure 1. Selected Financial Data

dollars in millions, except per share amounts	2018 First	2017 Fourth	Third	Second	First
FOR THE PERIOD					
Interest income	$1,137	$1,114	$1,109	$1,117	$1,050
Interest expense	193	176	161	144	132
Net interest income	944	938	948	973	918
Provision for credit losses	61	49	51	66	63
Noninterest income	601	656	592	653	577
Noninterest expense	1,006	1,098	992	995	1,013
Income (loss) from continuing operations before income taxes	478	447	497	565	419
Income (loss) from continuing operations attributable to Key	416	195	363	407	324
Income (loss) from discontinued operations, net of taxes	2	1	1	5	—
Net income (loss) attributable to Key	418	196	364	412	324
Income (loss) from continuing operations attributable to Key common shareholders	402	181	349	393	296
Income (loss) from discontinued operations, net of taxes	2	1	1	5	—
Net income (loss) attributable to Key common shareholders	404	182	350	398	296
PER COMMON SHARE					
Income (loss) from continuing operations attributable to Key common shareholders	$.38	$.17	$.32	$.36	$.28
Income (loss) from discontinued operations, net of taxes	—	—	—	—	—
Net income (loss) attributable to Key common shareholders [(a)]	.38	.17	.32	.37	.28
Income (loss) from continuing operations attributable to Key common shareholders — assuming dilution	.38	.17	.32	.36	.27
Income (loss) from discontinued operations, net of taxes — assuming dilution	—	—	—	—	—
Net income (loss) attributable to Key common shareholders — assuming dilution [(a)]	.38	.17	.32	.36	.27
Cash dividends paid	.105	.105	.095	.095	.085
Book value at period end	13.07	13.09	13.18	13.02	12.71
Tangible book value at period end	10.35	10.35	10.52	10.40	10.21
Market price:					
High	22.15	20.44	19.37	19.10	19.53
Low	19.04	17.64	16.47	16.91	16.54
Close	19.55	20.17	18.82	18.74	17.78
Weighted-average common shares outstanding (000)	1,056,037	1,062,348	1,073,390	1,076,203	1,068,609
Weighted-average common shares and potential common shares outstanding (000) [(b)]	1,071,786	1,079,330	1,088,841	1,093,039	1,086,540
AT PERIOD END					
Loans	$88,089	$86,405	$86,492	$86,503	$86,125
Earning assets	122,961	123,490	122,625	121,243	120,261
Total assets	137,049	137,698	136,733	135,824	134,476
Deposits	104,751	105,235	103,446	102,821	103,982

Long-term debt	13,749	14,333	15,100	13,261	12,324
Key common shareholders’ equity	13,919	13,998	14,224	14,228	13,951
Key shareholders’ equity	14,944	15,023	15,249	15,253	14,976
PERFORMANCE RATIOS — FROM CONTINUING OPERATIONS					
Return on average total assets	1.25 %	.57 %	1.07 %	1.23 %	.99 %
Return on average common equity	11.76	5.04	9.74	11.12	8.76
Return on average tangible common equity [(c)]	14.89	6.35	12.21	13.80	10.98
Net interest margin (TE)	3.15	3.09	3.15	3.30	3.13
Cash efficiency ratio [(c)]	62.9	66.7	62.2	59.3	65.8
PERFORMANCE RATIOS — FROM CONSOLIDATED OPERATIONS					
Return on average total assets	1.24 %	.57 %	1.06 %	1.23 %	.98 %
Return on average common equity	11.82	5.07	9.77	11.26	8.76
Return on average tangible common equity [(c)]	14.97	6.39	12.25	13.98	10.98
Net interest margin (TE)	3.13	3.07	3.13	3.28	3.11
Loan-to-deposit [(d)]	86.9	84.4	86.2	87.2	85.6
CAPITAL RATIOS AT PERIOD END					
Key shareholders’ equity to assets	10.90 %	10.91 %	11.15 %	11.23 %	11.14 %
Key common shareholders’ equity to assets	10.16	10.17	10.40	10.48	10.37
Tangible common equity to tangible assets [(c)]	8.22	8.23	8.49	8.56	8.51
Common Equity Tier 1	9.99	10.16	10.26	9.91	9.91
Tier 1 risk-based capital	10.82	11.01	11.11	10.73	10.74
Total risk-based capital	12.73	12.92	13.09	12.64	12.69
Leverage	9.76	9.73	9.83	9.95	9.81
TRUST ASSETS					
Assets under management	$39,003	$39,588	$38,660	$37,613	$37,417
OTHER DATA					
Average full-time-equivalent employees	18,540	18,379	18,548	18,344	18,386
Branches	1,192	1,197	1,208	1,210	1,216

(a) EPS may not foot due to rounding.

(b) Assumes conversion of Common Share options and other stock awards as applicable.

(c) See Figure 2 entitled “GAAP to Non-GAAP Reconciliations,” which presents the computations of certain financial measures related to “tangible common equity” and “cash efficiency.” The table reconciles the GAAP performance measures to the corresponding non-GAAP measures, which provides a basis for period-to-period comparisons.

(d) Represents period-end consolidated total loans and loans held for sale divided by period-end consolidated total deposits.

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Figure 2 presents certain non-GAAP financial measures related to “tangible common equity,” “return on tangible common equity,” “cash efficiency ratio,” certain financial measures excluding notable items, and “Common Equity Tier 1 under the Regulatory Capital Rules (estimates).”

Notable items include certain revenue or expense items that may occur in a reporting period which management does not consider indicative of ongoing financial performance. Management believes it is useful to consider certain financial metrics with and without merger-related charges and/or other notable items in order to enable a better understanding of Company results, increase comparability of period-to-period results, and to evaluate and forecast those results.

The tangible common equity ratio and the return on tangible common equity ratio have been a focus for some investors, and management believes that these ratios may assist investors in analyzing Key’s capital position without regard to the effects of intangible assets and preferred stock. Since analysts and banking regulators may assess our capital adequacy using tangible common equity, we believe it is useful to enable investors to assess our capital adequacy on these same bases. Figure 2 reconciles the GAAP performance measures to the corresponding non-GAAP measures.

Beginning in the first quarter of 2018, we no longer separately report merger-related charges. Prior to that, we reported merger-related charges as a result of our purchase of First Niagara on August 1, 2016. The definitive agreement and plan of merger to acquire First Niagara was originally announced on October 30, 2015. For every quarter of 2017, merger-related charges are included in the total for "notable items." The table below shows the computation of return on average tangible common equity excluding notable items, pre-provision net revenue excluding notable items, cash efficiency ratio excluding notable items, and return on average assets from continuing operations excluding notable items. Management believes that eliminating the effects of the merger-related charges and other notable items made it easier to analyze the results by presenting them on a more comparable basis.

Figure 2 also shows the computation for and reconciliation of pre-provision net revenue, which is not formally defined by GAAP. We believe that eliminating the effects of the provision for credit losses makes it easier to analyze our results by presenting them on a more comparable basis.

The cash efficiency ratio is a ratio of two non-GAAP performance measures. Accordingly, there is no directly comparable GAAP performance measure. The cash efficiency ratio excludes the impact of our intangible asset amortization from the calculation. We also disclose the cash efficiency ratio excluding notable items. We believe these ratios provide greater consistency and comparability between our results and those of our peer banks. Additionally, these ratios are used by analysts and investors as they develop earnings forecasts and peer bank analysis.

Non-GAAP financial measures have inherent limitations, are not required to be uniformly applied, and are not audited. Although these non-GAAP financial measures are frequently used by investors to evaluate a company, they have limitations as analytical tools, and should not be considered in isolation, nor as a substitute for analyses of results as reported under GAAP.

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Figure 2. GAAP to Non-GAAP Reconciliations

		Three months ended				
dollars in millions		3/31/2018	12/31/2017	9/30/2017	6/30/2017	3/31/2017
Tangible common equity to tangible assets at period-end						
Key shareholders' equity (GAAP)		$14,944	$15,023	$15,249	$15,253	$14,976
Less:	Intangible assets [a]	2,902	2,928	2,870	2,866	2,751
	Preferred Stock [b]	1,009	1,009	1,009	1,009	1,009
	Tangible common equity (non-GAAP)	$11,033	$11,086	$11,370	$11,378	$11,216
Total assets (GAAP)		$137,049	$137,698	$136,733	$135,824	$134,476
Less:	Intangible assets [a]	2,902	2,928	2,870	2,866	2,751
	Tangible assets (non-GAAP)	$134,147	$134,770	$133,863	$132,958	$131,725
	Tangible common equity to tangible assets ratio (non-GAAP)	8.22 %	8.23 %	8.49 %	8.56 %	8.51 %
Notable items						
Merger-related charges		—	$(56)	$(36)	$(44)	$(81)
Impacts of tax reform and related actions		—	(30)	—	—	—
Merchant services gain		—	—	(5)	64	—
Purchase accounting finalization, net		—	—	—	43	—
Charitable contribution		—	—	—	(20)	—
Total notable items		—	$(86)	$(41)	$43	$(81)
Income taxes		—	(26)	(13)	16	(30)
Reevaluation of certain tax related assets		—	147	—	—	—
Total notable items after tax		—	$(207)	$(28)	$27	$(51)
Average tangible common equity						
Average Key shareholders' equity (GAAP)		$14,889	$15,268	$15,241	$15,200	$15,184
Less:	Intangible assets (average) [c]	2,916	2,939	2,878	2,756	2,772
	Preferred Stock (average)	1,025	1,025	1,025	1,025	1,480
	Average tangible common equity (non-GAAP)	$10,948	$11,304	$11,338	$11,419	$10,932
Return on average tangible common equity from continuing operations						
Net income (loss) from continuing operations attributable to Key common shareholders (GAAP)		$402	$181	$349	$393	$296
Plus:	Notable items, after tax	—	207	28	(27)	51
	Net income (loss) from continuing operations attributable to Key common shareholders after notable items (non-GAAP)	$402	$388	$377	$366	$347
Average tangible common equity (non-GAAP)		10,948	11,304	11,338	11,419	10,932
Return on average tangible common equity from continuing operations (non-GAAP)		14.89 %	6.35 %	12.21 %	13.80 %	10.98 %
Return on average tangible common equity from continuing operations excluding notable items (non-GAAP)		14.89	13.62	13.19	12.86	12.87
Return on average tangible common equity consolidated						
Net income (loss) attributable to Key common shareholders (GAAP)		$404	$182	$350	$398	$296
Average tangible common equity (non-GAAP)		10,948	11,304	11,338	11,419	10,932
Return on average tangible common equity consolidated (non-GAAP)		14.97 %	6.39 %	12.25 %	13.98 %	10.98 %
Pre-provision net revenue						

Net interest income (GAAP)	$944	$938	$948	$973	$918
Plus: Taxable-equivalent adjustment	8	14	14	14	11
Noninterest income (GAAP)	601	656	592	653	577
Less: Noninterest expense (GAAP)	1,006	1,098	992	995	1,013
Pre-provision net revenue from continuing operations (non-GAAP)	$547	$510	$562	$645	$493
Plus: Notable items	—	86	41	(43)	81
Pre-provision net revenue from continuing operations excluding notable items (non-GAAP)	547	596	603	602	574
Cash efficiency ratio					
Noninterest expense (GAAP)	$1,006	$1,098	$992	$995	$1,013
Less: Intangible asset amortization	29	26	25	22	22
Adjusted noninterest expense (non-GAAP)	$977	$1,072	$967	$973	$991
Less: Notable items	—	85	36	60	81
Adjusted noninterest expense excluding notable items (non-GAAP)	$977	$987	$931	$913	$910
Net interest income (GAAP)	$944	$938	$948	$973	$918
Plus: Taxable-equivalent adjustment	8	14	14	14	11
Noninterest income (GAAP)	601	656	592	653	577
Total taxable-equivalent revenue (non-GAAP)	$1,553	$1,608	$1,554	$1,640	$1,506
Plus: Notable items	—	1	5	(103)	—
Adjusted noninterest income excluding notable items (non-GAAP)	$1,553	$1,609	$1,559	$1,537	$1,506
Cash efficiency ratio (non-GAAP)	62.9%	66.7%	62.2%	59.3%	65.8%
Cash efficiency ratio excluding notable items (non-GAAP)	62.9	61.3	59.7	59.4	60.4
Return on average total assets from continuing operations excluding notable items					
Income from continuing operations attributable to Key (GAAP)	$416	$195	$363	$407	$324
Plus: Notable items, after tax	—	207	28	(27)	51
Income from continuing operations attributable to Key excluding notable items, after tax (non-GAAP)	$416	$402	$391	$380	$375
Average total assets from continuing operations (GAAP)	$134,915	$135,255	$134,356	$132,491	$132,741
Return on average total assets from continuing operations excluding notable items (non-GAAP)	1.25%	1.18%	1.15%	1.15%	1.15%

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Figure 2. GAAP to Non-GAAP Reconciliations, continued

dollars in millions	Three months ended March 31, 2018
Common Equity Tier 1 under the Regulatory Capital Rules (estimates)	
Common Equity Tier 1 under current Regulatory Capital Rules	$ 12,086
Adjustments from current Regulatory Capital Rules to the fully phased-in Regulatory Capital Rules:	
Deferred tax assets and other intangible assets [d]	—
Common Equity Tier 1 anticipated under the fully phased-in Regulatory Capital Rules [e]	$ 12,086
Net risk-weighted assets under current Regulatory Capital Rules	$ 120,986
Adjustments from current Regulatory Capital Rules to the fully phased-in Regulatory Capital Rules:	
Mortgage servicing assets [f]	700
All other assets	319
Total risk-weighted assets anticipated under the fully phased-in Regulatory Capital Rules [e]	$ 122,005
Common Equity Tier 1 ratio under the fully phased-in Regulatory Capital Rules [e]	9.91 %

(a) For the three months ended March 31, 2018, December 31, 2017, September 30, 2017, June 30, 2017, and March 31, 2017, intangible assets exclude $23 million, $26 million, $30 million, $33 million, and $38 million, respectively, of period-end purchased credit card relationships.
(b) Net of capital surplus.
(c) For the three months ended March 31, 2018, December 31, 2017, September 30, 2017, June 30, 2017, and March 31, 2017, average intangible assets exclude $24 million, $28 million, $32 million, $36 million, and $40 million, respectively, of average purchased credit card relationships.
(d) Includes the deferred tax assets subject to future taxable income for realization, primarily tax credit carryforwards, as well as intangible assets (other than goodwill and mortgage servicing assets) subject to the transition provisions of the final rule.
(e) The anticipated amount of regulatory capital and risk-weighted assets is based upon the federal banking agencies' Regulatory Capital Rules (as fully phased-in on January 1, 2019); we are subject to the Regulatory Capital Rules under the "standardized approach."
(f) Item is included in the 10%/15% exceptions bucket calculation and is risk-weighted at 250%.

Long-term financial targets

Our long-term financial targets are as follows:

- Generate positive operating leverage and a cash efficiency ratio in the range of 54.0% to 56.0%;
- Maintain a moderate risk profile by targeting a net loan charge-offs to average loans ratio in the range of .40% to .60%; and
- Achieve a return on tangible common equity ratio in the range of 15.00% to 18.00%.

Figure 3 shows the evaluation of our long-term financial targets for the three months ended March 31, 2018.

Figure 3. Evaluation of Our Long-Term Targets

	Key Metrics [a]	1Q18	Targets
Positive operating leverage	Cash efficiency ratio [b]	62.9 %	54.0 - 56.0%

Moderate Risk Profile	Net loan charge-offs to average loans	.25 %	.40 - .60%
Financial Returns	Return on average tangible common equity [b]	14.89%	15.00 - 18.00%

(a) Calculated from continuing operations, unless otherwise noted.
(b) Non-GAAP measure; see Figure 2 entitled "GAAP to Non-GAAP Reconciliations" for reconciliation.

Strategic developments

Our actions and results during the first three months of 2018 supported our corporate strategy described in the "Introduction" section under the "Corporate strategy" heading on page 38 of our 2017 Form 10-K.

- Total revenue was up 3.1% compared to the first quarter of last year driven by a higher net interest margin, solid loan growth, and strong performance from our fee-based businesses. Excluding purchase accounting accretion, net interest income was up $43 million from the first quarter of 2017, driven by higher interest rates and well-managed deposit betas. The growth in average loans for the first quarter of 2018 was primarily in our commercial and industrial portfolio which was up 6.8% from a year ago, reflecting broad-based growth in commercial and industrial loans with middle-market clients. We had a record first quarter for investment banking and debt placement fees of $143 million, an increase of 12.6% from the year-ago quarter, as we benefited from the acquisition of Cain Brothers as well as continued growth in our core franchise.
- Net loan charge-offs were .25% of average loans for the first three months of 2018, down from .27% for the same period one-year ago and below our targeted range. Total net loan charge-offs decreased during the first three months of 2018 compared to the year-ago period. Total loans charged off decreased in our commercial lease financing, home equity loan, and consumer indirect loan portfolios. Partially offsetting these decreases in loan charge-offs were increases in total loans charged off in our commercial and industrial and real estate — residential mortgage loan portfolios. Total loan loss recoveries were down slightly from the year-ago quarter.

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- Capital management remains a priority for 2018. As previously reported, share repurchases of up to $800 million were included in the 2017 capital plan, which is effective through the second quarter of 2018. We completed $199 million of Common Share repurchases, including $156 million of Common Share repurchases in the open market and $43 million of Common Share repurchases related to employee equity compensation programs, in the first quarter of 2018 under this authorization.
- Consistent with our 2017 capital plan, the Board declared a quarterly dividend of $.105 per Common Share for the first quarter of 2018. In the second quarter of 2018, the Board plans to consider a potential increase in our quarterly common share dividend, up to $.12 per share.
- On March 29, 2018, we announced that we had entered into a definitive agreement to sell Key Insurance & Benefits Services, Inc. to USI Insurance Services. We acquired Key Insurance & Benefits Services, Inc. as a part of the 2016 merger with First Niagara. The transaction is subject to regulatory approvals and other customary closing conditions and is expected to close in the second quarter of 2018.

Demographics

We have two major business segments: Key Community Bank and Key Corporate Bank.

Key Community Bank serves individuals and small to mid-sized businesses by offering a variety of deposit and investment, lending, mortgage and home equity, credit card, and personalized wealth management products and business advisory services. Key Community Bank offers personal property and casualty insurance, such as home, auto, renters, watercraft, and umbrella policies. Key Community Bank also purchases retail auto sales contracts via a network of auto dealerships. These products and services are provided through our relationship managers and specialists working in our 15-state branch network, which is organized into ten internally defined geographic regions: Washington, Oregon/Alaska, Rocky Mountains, Indiana/Northwest Ohio/Michigan, Central/Southwest Ohio, East Ohio/Western Pennsylvania, Atlantic, Western New York, Eastern New York, and New England. In addition, some of these product capabilities are delivered by Key Corporate Bank to clients of Key Community Bank.

Key Corporate Bank is a full-service corporate and investment bank focused principally on serving the needs of middle market clients in seven industry sectors: consumer, energy, healthcare, industrial, public sector, real estate, and technology. Key Corporate Bank delivers a broad suite of banking and capital markets products to its clients, including syndicated finance, debt and equity capital markets, commercial payments, equipment finance, commercial mortgage banking, derivatives, foreign exchange, financial advisory, and public finance. Key Corporate Bank is also a significant servicer of commercial mortgage loans and a significant special servicer of CMBS. Key Corporate Bank delivers many of its product capabilities to clients of Key Community Bank.

Further information regarding the products and services offered by our Key Community Bank and Key Corporate Bank segments is included in this report in Note 18 (“Line of Business Results”).

Supervision and regulation

The following discussion provides a summary of recent regulatory developments and should be read in conjunction with the disclosure included in our 2017 Form 10-K under the heading “Supervision and Regulation” in Item 1. Business and under the heading “II. Compliance Risk” in Item 1A. Risk Factors.

Regulatory capital requirements

The final rule to implement the Basel III international capital framework (“Basel III”) was effective January 1, 2015, with a multi-year transition period ending on December 31, 2018 (“Regulatory Capital Rules”). The Basel III capital framework and the U.S. implementation of the Basel III capital framework are discussed in more detail in Item 1.

Business of our 2017 Form 10-K under the heading "Supervision and Regulation - Regulatory capital requirements."

Under the Regulatory Capital Rules, standardized approach banking organizations, such as KeyCorp and KeyBank, are required to meet the minimum capital and leverage ratios set forth in Figure 4 below. At March 31, 2018, Key had an estimated Common Equity Tier 1 Capital Ratio of 9.91% under the fully phased-in Regulatory Capital Rules. Also at March 31, 2018, based on the fully phased-in Regulatory Capital Rules, Key estimates that its capital and leverage ratios, after adjustment for market risk, would be as set forth in Figure 4.

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Figure 4. Pro Forma Ratios vs. Minimum Capital Ratios Calculated Under the Fully Phased-In Regulatory Capital Rules

Ratios (including capital conservation buffer)	Key March 31, 2018 Pro forma		Minimum January 1, 2018		Phase-in Period	Minimum January 1, 2019	
Common Equity Tier 1 [(a)]	9.91	%	4.5	%	None	4.5	%
Capital conservation buffer [(b)]			—		1/1/16-1/1/19	2.5	
Common Equity Tier 1 + Capital conservation buffer			4.5		1/1/16-1/1/19	7.0	
Tier 1 Capital	10.73	%	6.0		None	6.0	
Tier 1 Capital + Capital conservation buffer			6.0		1/1/16-1/1/19	8.5	
Total Capital	12.64	%	8.0		None	8.0	
Total Capital + Capital conservation buffer			8.0		1/1/16-1/1/19	10.5	
Leverage [(c)]	9.76	%	4.0		None	4.0	

(a) See Figure 2 entitled "GAAP to Non-GAAP Reconciliations," which presents the computation of Common Equity Tier 1 capital under the fully phased-in regulatory capital rules.

(b) Capital conservation buffer must consist of Common Equity Tier 1 capital. As a standardized approach banking organization, KeyCorp is not subject to the countercyclical capital buffer of up to 2.5% imposed upon an advanced approaches banking organization under the Regulatory Capital Rules.

(c) As a standardized approach banking organization, KeyCorp is not subject to the 3% supplemental leverage ratio requirement, which became effective January 1, 2018.

Revised prompt corrective action framework

The federal prompt corrective action ("PCA") framework under the FDIA groups FDIC-insured depository institutions into one of five prompt corrective action capital categories: "well capitalized," "adequately capitalized," "undercapitalized," "significantly undercapitalized," and "critically undercapitalized." In addition to implementing the Basel III capital framework in the United States, the Regulatory Capital Rules also revised the prompt corrective action capital category threshold ratios applicable to FDIC-insured depository institutions such as KeyBank, with an effective date of January 1, 2015. The revised Prompt Corrective Action Framework table in Figure 5 identifies the capital category thresholds for a "well capitalized" and an "adequately capitalized" institution under the Prompt Corrective Action Framework.

Figure 5. "Well Capitalized" and "Adequately Capitalized" Capital Category Ratios under Revised PCA Framework

Prompt Corrective Action Ratio	Capital Category Well Capitalized [(a)]		Adequately Capitalized	
Common Equity Tier 1 Risk-Based	6.5	%	4.5	%
Tier 1 Risk-Based	8.0		6.0	
Total Risk-Based	10.0		8.0	
Tier 1 Leverage [(b)]	5.0		4.0	

(a) A "well capitalized" institution also must not be subject to any written agreement, order, or directive to meet and maintain a specific capital level for any capital measure.

(b) As a "standardized approach" banking organization, KeyBank is not subject to the 3% supplemental leverage ratio requirement, which became effective January 1, 2018.

We believe that, as of March 31, 2018, KeyBank (consolidated) satisfied the risk-based and leverage capital requirements necessary to be considered "well capitalized" for purposes of the PCA framework. However, investors should not regard this determination as a representation of the overall financial condition or prospects of KeyBank because the prompt corrective action framework is intended to serve a limited supervisory function. Moreover, it is

important to note that the prompt corrective action framework does not apply to BHCs, like KeyCorp.

Recent regulatory capital-related developments

On September 27, 2017, the federal banking agencies issued a joint proposal to simplify certain aspects of the Regulatory Capital Rules for standardized approach banking organizations (the "Simplification Proposal"), including Key. In anticipation of the Simplification Proposal, on August 22, 2017, the agencies issued a companion proposal to extend the current capital treatment for certain items that are part of the Simplification Proposal and also subject to the multi-year transition period for the Regulatory Capital Rules, which ends on December 31, 2018 (the "Transitions Proposal"). The Transitions Proposal was published as a final rule in the Federal Register on November 21, 2017, and is expected to alleviate the burden that would have resulted from the continued phase-in of those capital requirements as the agencies seek public comment on and work to finalize the Simplification Proposal. The Simplification Proposal and the Transitions Proposal are discussed in more detail in Item 1. Business of our 2017 Form 10-K under the heading "Supervision and Regulation - Regulatory capital requirements - Recent regulatory capital-related developments."

In December 2017, the Basel Committee released its final revisions to Basel III. The revisions seek to restore credibility in the calculation of risk-weighted assets and improve the comparability of regulatory capital ratios across banking organizations. The revisions are discussed in more detail in Item 1. Business of our 2017 Form 10-K under

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the heading "Supervision and Regulation - Regulatory capital requirements - Recent regulatory capital-related developments."

The U.S. federal banking agencies released a statement announcing their support for the Basel Committee's efforts, but cautioned that they will consider how to appropriately incorporate these revisions into the Regulatory Capital Rules, and that any proposed changes based on the Basel Committee revisions would be subject to notice-and-comment rulemaking. In view of the prohibition under the Dodd-Frank Act on the use of credit ratings in federal regulation, there is some uncertainty as to whether or how the agencies would implement the ratings-based aspects of the Basel Committee revisions to Basel III, as well as any other aspect of the Basel Committee revisions that permit the U.S. agencies to exercise home-country discretion, for example, due to differences in accounting or market practices, and legal requirements.

Subsequently, in February 2018, the Basel Committee released for public consultation a proposal to update the Pillar 3 disclosure framework, to more appropriately align it to the changes adopted under the Basel Committee's final revisions to Basel III. The public consultation period ends on May 25, 2018. Before any action is taken by the federal banking agencies with respect to the revised Pillar 3 disclosure framework, it first must be adopted in final form by the Basel Committee, and the federal agencies must determine whether and to what extent they will implement the final revisions to Basel III released by the Basel Committee in December 2017.

Capital planning and stress testing

On December 7, 2017, the Federal Reserve released for public comment a package of proposals that would increase the transparency of its stress testing program while maintaining the Federal Reserve's ability to test the resilience of the nation's largest, most complex banks. The proposals responded to public and industry calls for more transparency around the CCAR program. The proposals are discussed in more detail in Item 1. Business of our 2017 Form 10-K under the heading "Supervision and Regulation - Regulatory capital requirements - Recent developments in capital planning and stress testing."

In a separate release, published April 10, 2018, the Federal Reserve invited comment on a proposal to integrate certain aspects of the Federal Reserve's Regulatory Capital Rules with the CCAR and stress test rules, in order to simplify the overall capital framework that is currently applicable to banking organizations subject to the capital plan rule (including KeyCorp). Under the proposal, the Federal Reserve would (1) amend the capital conservation buffer requirement under the Regulatory Capital Rules by replacing the static risk-weighted assets component of the buffer with a new measure, the stress capital buffer, which would be based on the results of an individual banking organization's annual supervisory stress test; (2) introduce a stress leverage buffer requirement that would replace the existing Tier 1 leverage requirement under CCAR; (3) modify certain assumptions under the supervisory stress test; (4) remove the 30% dividend payout ratio limitation as a criterion for heightened supervisory scrutiny of an organization's capital plan; and (5) eliminate the CCAR quantitative objection.

Under the proposed rule, a banking organization would not be subject to any limitations on capital distributions and discretionary bonus payments if it satisfies all minimum capital requirements and its capital conservation requirement (as amended to incorporate the stress capital buffer), stress leverage buffer requirement, and, if applicable, the advanced approaches capital conservation buffer requirement and supplementary leverage ratio standard (the latter two of which do not apply to KeyCorp). If it is adopted as a final rule, the proposal would be effective December 31, 2018; however, the stressed capital buffer and stress leverage buffer requirements would generally not be effective until October 1, 2019. Key expects that the proposal would have a marginally favorable impact on its capital requirements.

Liquidity requirements

In October 2014, the federal banking agencies published a final rule to implement the Basel III liquidity coverage ratio ("Basel III LCR") for U.S. banking organizations (the "Liquidity Coverage Rules") that establishes a minimum LCR for certain internationally active bank and nonbank financial companies (excluding KeyCorp) and a modified version of the LCR ("Modified LCR") for BHCs and other depository institution holding companies with over $50 billion in consolidated assets that are not internationally active (including KeyCorp). KeyBank will not be subject to the LCR or the Modified LCR under the Liquidity Coverage Rules unless the OCC affirmatively determines that application to KeyBank is appropriate in light of KeyBank's asset size, level of complexity, risk profile, scope of operations, affiliation with foreign or domestic covered entities, or risk to the financial system.

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Under the Liquidity Coverage Rules, KeyCorp must calculate a Modified LCR on a monthly basis, and was required to satisfy a minimum Modified LCR requirement of 100% by January 1, 2017. At March 31, 2018, Key's Modified LCR was above 100%. In the future, KeyCorp may change the composition of our investment portfolio, increase the size of the overall investment portfolio, and modify product offerings to enhance or optimize our liquidity position.

Net stable funding ratio

The federal banking agencies commenced the U.S. implementation of the Basel III net stable funding ratio ("NSFR") in April and May 2016, with the release of a proposed rule to implement a NSFR requirement for certain internationally active banking organizations (excluding KeyCorp) and a modified version of the minimum NSFR requirement ("Modified NSFR") for BHCs and other depository institution holding companies with over $50 billion in consolidated assets that are not internationally active (including KeyCorp), together with quarterly public disclosure requirements. The proposed rule would require banking organizations to satisfy a minimum NSFR requirement of 1.0 on an ongoing basis. However, banking organizations subject to the Modified NSFR (like KeyCorp) would be required to maintain a lower minimum amount of available stable funding, equal to 70% of the required stable funding under the NSFR. The proposed rule was scheduled to be effective on January 1, 2018; however, it has not been adopted in final form. The comment period for the NPR expired on August 5, 2016. If the proposed NSFR requirement is adopted as a final rule, then similar to actions taken in connection with the implementation of the Liquidity Coverage Rules, KeyCorp may adjust its balance sheet or modify product offerings to enhance its liquidity position.

Resolution and recovery planning

BHCs with at least $50 billion in total consolidated assets, like KeyCorp, are required to periodically submit to the Federal Reserve and FDIC a plan discussing how the company could be rapidly and efficiently resolved if the company failed or experienced material financial distress. Insured depository institutions with at least $50 billion in total consolidated assets, like KeyBank, are also required to submit a resolution plan to the FDIC. These plans are due annually, usually by December 31 of each year. For 2015, these resolution plans, the third required from KeyCorp and KeyBank, were submitted on December 1, 2015. KeyCorp and KeyBank were not required to submit resolution plans for 2016 because the FDIC and Federal Reserve deferred such requirement (for 38 firms, including KeyCorp) until December 2017 and the FDIC deferred such requirement (for a number of insured depository institutions, including KeyBank) until July 1, 2018. On December 1, 2017, KeyCorp submitted its resolution plan to the Federal Reserve and the FDIC. The Federal Reserve and FDIC make available on their websites the public sections of resolution plans for the companies, including KeyCorp and KeyBank, that submitted plans. The public section of the resolution plans of KeyCorp and KeyBank is available at http://www.federalreserve.gov/supervisionreg/resolution-plans.htm and https://www.fdic.gov/regulations/reform/resplans/.

On September 28, 2016, the OCC released final guidelines that establish standards for recovery planning by certain large OCC-regulated institutions, including KeyBank. The guidelines require such institutions to establish a comprehensive framework for evaluating the financial effects of severe stress events, and recovery actions an institution may pursue to remain a viable, going concern during a period of severe financial stress. Under the final guidelines, an institution's recovery plan must include triggers to alert the institution of severe stress events, escalation procedures, recovery options, and a process for periodic review and approval by senior management and the board of directors. The recovery plan should be tailored to the complexity, scope of operations, and risk profile of the institution. Because KeyBank had average total consolidated assets of greater than $100 billion but less than $750 billion as reported on KeyBank's Consolidated Reports of Condition and Income for the four most recent consecutive quarters prior to January 1, 2017, it was required to be in compliance with the guidelines not later than January 1, 2018. We believe that KeyBank is in compliance with the guidelines.

Deposit insurance and assessments

As required under the Dodd-Frank Act, in March 2015, the FDIC approved a final rule to impose a surcharge on the quarterly deposit insurance assessments of insured depository institutions having total consolidated assets of at least $10 billion (like KeyBank). The surcharge is 4.5 cents per $100 of the institution's assessment base (after making certain adjustments). The final rule became effective on July 1, 2016. As of July 1, 2016, KeyBank must pay a surcharge to assist in bringing the reserve ratio to the statutory minimum of 1.35%. Surcharges will continue through the quarter that the DIF reserve ratio reaches or exceeds 1.35%, but not later than December 31, 2018. If the reserve ratio does not reach 1.35% by December 31, 2018 (provided it is at least 1.15%), the FDIC will impose a shortfall assessment on March 31, 2019, on insured depository institutions with total consolidated assets of $10 billion or more (like KeyBank).

In December 2016, the FDIC issued a final rule that imposes recordkeeping requirements on insured depository institutions with two million or more deposit accounts (including KeyBank) in order to facilitate rapid payment of insured deposits to customers if the institutions were to fail. The rule requires those insured depository institutions to: (i) maintain complete and accurate data on each depositor's ownership interest by right and capacity for all of the institution's deposit accounts; and (ii) develop the capability to calculate the insured and uninsured amounts for each deposit owner within 24 hours of failure. The FDIC will conduct periodic testing of compliance with these requirements, and institutions subject to the rule must submit to the FDIC a certification of compliance, signed by the KeyBank chief executive officer, and deposit insurance coverage summary report on or before the mandatory compliance date and annually thereafter. The final rule became effective on April 1, 2017, with a mandatory compliance date of April 1, 2020. The FDIC has been releasing Frequently Asked Questions for Part 370 on a rolling basis, and has committed to continue this practice as institutions subject to the rule present issues associated with its implementation that require FDIC consultation.

Supervision and governance

On August 3, 2017, the Federal Reserve published an NPR to align its supervisory rating system for large financial institutions, including KeyCorp, with the post-crisis supervisory programs for these firms (the "LFI Rating System"). If adopted in final form, the LFI Rating System would provide a supervisory evaluation of whether an institution possesses sufficient operational strength and resilience to maintain safe and sound operations through a range of conditions, and assess an institution's capital planning and positions, liquidity risk management and positions, and governance and controls. Institutions subject to the LFI Rating System would be rated using the following scale: Satisfactory, Satisfactory Watch, Deficient-1, and Deficient-2, with the Satisfactory Watch rating intended to be used as a transitory rating to allow an institution time to remediate a concern identified during the supervisory evaluation.

The governance and controls component of the LFI Rating System is the subject of two separate, but related proposals: (1) proposed guidance regarding supervisory expectations for boards of directors of large financial institutions; and (2) proposed guidance regarding core principles for effective senior management, business management, and independent risk management and controls for large financial institutions.

On January 4, 2018, the Federal Reserve released the final component of the proposed LFI Rating System — proposed guidance regarding core principles for effective senior management, business management, and independent risk management and controls for large financial institutions. The proposals and guidance are discussed in more detail in Item 1. Business of our 2017 Form 10-K under the heading "Supervision and Regulation - Other Regulatory Developments under the Dodd-Frank Act - Supervision and governance."

ERISA fiduciary standard

In April 2016, the Department of Labor published final rules and amendments to certain prohibited transaction exemptions regarding which service providers would be regarded as fiduciaries under ERISA for making investment advice recommendations to: (i) certain retirement plan fiduciaries, participants, or beneficiaries; and (ii) owners or beneficiaries of individual retirement accounts and health savings accounts, among other retirement plans. The purpose of the rules is to place fiduciary obligations, rather than the lesser legal obligations that currently apply, on these service providers. Accordingly, the rules subject any financial institution making recommendations for either the purchase or sale of investments in or rollover of the respective retirement plan to certain fiduciary obligations under ERISA such as an impartial conduct standard and not selling certain investment products whose compensation may raise a conflict of interest for the advisor without entering into a contract providing certain disclosures and legal remedies to the customer. Under the Department of Labor’s original rules, the impartial

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standard requirement for financial institutions and their advisors was to become effective April 10, 2017. However, in response to a Presidential Order, the Department of Labor extended the effective date to June 9, 2017. The contract provisions were required to be in place by January 1, 2018. However, on November 29, 2017, the Department of Labor extended the applicability of the contract rules until July 1, 2019, while it continues to review requested comments concerning whether to modify, further delay, or rescind these rules in whole or in part. On March 15, 2018, the United States Court of Appeals for the Fifth Circuit invalidated the rule in its entirety. Other federal courts have upheld the rule. It is unclear what impact these decisions will have on the rules.

Results of Operations

Earnings overview

The following chart provides a reconciliation of net income from continuing operations attributable to Key common shareholders for the three months ended March 31, 2017, to the three months ended March 31, 2018 (dollars in millions):
The following discussion explains the key factors that caused these elements to change.

Net interest income

One of our principal sources of revenue is net interest income. Net interest income is the difference between interest income received on earning assets (such as loans and securities) and loan-related fee income, and interest expense paid on deposits and borrowings. There are several factors that affect net interest income, including:

- the volume, pricing, mix, and maturity of earning assets and interest-bearing liabilities;
- the volume and value of net free funds, such as noninterest-bearing deposits and equity capital;
- the use of derivative instruments to manage interest rate risk;
- interest rate fluctuations and competitive conditions within the marketplace;
- asset quality; and
- fair value accounting of acquired earning assets and interest-bearing liabilities.

To make it easier to compare both the results across several periods and the yields on various types of earning assets (some taxable, some not), we present net interest income in this discussion on a “TE basis” (i.e., as if all income were taxable and at the same rate). For example, $100 of tax-exempt income would be presented as $126, an amount that, if taxed at the statutory federal income tax rate of 21%, would yield $100. Prior to 2018, $100 of tax-exempt income would be presented as $154, an amount that, if taxed at the previous statutory federal income tax rate of 35%, would yield $100.

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Figure 6 shows the various components of our balance sheet that affect interest income and expense, and their respective yields or rates over the past five quarters. This figure also presents a reconciliation of TE net interest income to net interest income reported in accordance with GAAP for each of those quarters. The net interest margin, which is an indicator of the profitability of the earning assets portfolio less cost of funding, is calculated by dividing annualized TE net interest income by average earning assets.
TE net interest income was $952 million for the first quarter of 2018, and the net interest margin was 3.15%, compared to TE net interest income of $929 million and a net interest margin of 3.13% for the first quarter of 2017, reflecting the benefit from higher interest rates and low deposit betas. First quarter 2018 net interest income included $33 million of purchase accounting accretion, a decline of $20 million from the first quarter of 2017. In 2018, we expect net interest income to be in the range of $3.95 billion to $4.05 billion.

Average loans were $86.9 billion for the first quarter of 2018, an increase of $794 million compared to the first quarter of 2017, reflecting broad-based growth in commercial and industrial loans with middle-market clients, as well as strength in auto lending as the company expands into existing geographies and dealer relationships. In addition, reductions in commercial real estate loans over the past year reflect significantly higher debt placements and paydowns. For 2018, we anticipate average loans to be in the range of $88.5 billion to $89.5 billion.

Average deposits totaled $102.6 billion for the first quarter of 2018, an increase of $478 million compared to the year-ago quarter. Certificates of deposits and other time deposits increased $1.5 billion, reflecting strength in Key's retail banking franchise and growth from commercial relationships. Additionally, consumer noninterest-bearing balances grew 10% from the prior year. NOW and money-market deposit accounts declined $792 million, partially driven by a shift to higher-yielding deposit products and the managed exit of certain higher cost corporate and public sector deposits. For 2018, we anticipate average deposits to be in the range of $104.5 billion to $105.5 billion.

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Figure 6. Consolidated Average Balance Sheets, Net Interest Income, and Yields/Rates from Continuing Operations

	First Quarter 2018			Fourth Quarter 2017		
dollars in millions	Average Balance	Interest [a]	Yield/ Rate [a]	Average Balance	Interest [a]	Yield/ Rate [a]
ASSETS						
Loans [b], [c]						
Commercial and industrial [d]	$42,733	$ 434	4.11 %	$41,289	$ 417	4.01 %
Real estate — commercial mortgage	14,085	165	4.76	14,386	167	4.60
Real estate — construction	1,957	22	4.64	1,967	23	4.55
Commercial lease financing	4,663	41	3.53	4,687	45	3.86
Total commercial loans	63,438	662	4.23	62,329	652	4.15
Real estate — residential mortgage	5,479	54	3.95	5,474	54	3.95
Home equity loans	11,877	134	4.56	12,128	134	4.39
Consumer direct loans	1,766	33	7.53	1,782	32	7.15
Credit cards	1,080	30	11.32	1,061	30	11.14
Consumer indirect loans	3,287	35	4.29	3,232	36	4.42
Total consumer loans	23,489	286	4.91	23,677	286	4.80
Total loans	86,927	948	4.41	86,006	938	4.33
Loans held for sale	1,187	12	4.10	1,420	13	3.81
Securities available for sale [b], [e]	17,889	95	2.06	18,447	93	1.97
Held-to-maturity securities [b]	12,041	69	2.30	11,121	61	2.20
Trading account assets	907	7	2.99	898	6	2.72
Short-term investments	2,048	8	1.51	3,684	12	1.29
Other investments [e]	723	6	2.96	725	5	2.80
Total earning assets	121,722	1,145	3.78	122,301	1,128	3.66
Allowance for loan and lease losses	(875)			(871)		
Accrued income and other assets	14,068			13,825		
Discontinued assets	1,304			1,358		
Total assets	$136,219			$136,613		
LIABILITIES						
NOW and money market deposit accounts	$53,503	46	.34	$53,601	40	.29
Savings deposits	6,232	5	.29	6,372	3	.24
Certificates of deposit ($100,000 or more)	6,972	27	1.58	6,776	26	1.50
Other time deposits	4,865	13	1.12	4,771	13	1.05
Total interest-bearing deposits	71,572	91	.51	71,520	82	.45
Federal funds purchased and securities sold under repurchase agreements	1,421	4	1.11	360	—	.08
Bank notes and other short-term borrowings	1,342	6	1.87	693	3	1.72
Long-term debt [f], [g]	12,465	92	2.95	13,140	91	2.76
Total interest-bearing liabilities	86,800	193	.90	85,713	176	.81
Noninterest-bearing deposits	30,984			32,278		
Accrued expense and other liabilities	2,241			1,994		
Discontinued liabilities [g]	1,304			1,359		
Total liabilities	121,329			121,344		
EQUITY						
Key shareholders’ equity	14,889			15,268		
Noncontrolling interests	1			1		

Total equity	14,890			15,269		
Total liabilities and equity	$136,219			$136,613		
Interest rate spread (TE)			2.88 %			2.85 %
Net interest income (TE) and net interest margin (TE)		952	3.15 %		952	3.09 %
TE adjustment [b]		8			14	
Net interest income, GAAP basis		$ 944			$ 938	

(a) Results are from continuing operations. Interest excludes the interest associated with the liabilities referred to in (g), calculated using a matched funds transfer pricing methodology.

(b) Interest income on tax-exempt securities and loans has been adjusted to a TE basis using the statutory federal income tax rate in effect for that period.

(c) For purposes of these computations, nonaccrual loans are included in average loan balances.

(d) Commercial and industrial average balances include $120 million, $119 million, $117 million, $117 million, and $114 million of assets from commercial credit cards for the three months ended March 31, 2018, December 31, 2017, September 30, 2017, June 30, 2017, and March 31, 2017, respectively.

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Figure 6. Consolidated Average Balance Sheets, Net Interest Income, and Yields/Rates from Continuing Operations

Third Quarter 2017			Second Quarter 2017			First Quarter 2017		
Average Balance	Interest [(a)]	Yield/ Rate [(a)]	Average Balance	Interest [(a)]	Yield/ Rate [(a)]	Average Balance	Interest [(a)]	Yield/ Rate [(a)]
$41,416	$ 414	3.97 %	$40,666	$ 409	4.04 %	$40,002	$ 373	3.77 %
14,850	169	4.51	15,096	187	4.97	15,187	164	4.39
2,054	23	4.51	2,204	31	5.51	2,353	26	4.54
4,694	46	3.89	4,690	50	4.33	4,635	44	3.76
63,014	652	4.11	62,656	677	4.34	62,177	607	3.95
5,493	54	3.92	5,509	52	3.77	5,520	54	3.94
12,314	136	4.41	12,473	135	4.31	12,611	131	4.22
1,774	33	7.26	1,743	31	7.07	1,762	30	6.97
1,049	30	11.34	1,044	29	11.04	1,067	29	11.06
3,170	37	4.64	3,077	38	5.02	2,996	37	4.91
23,800	290	4.85	23,846	285	4.77	23,956	281	4.75
86,814	942	4.31	86,502	962	4.46	86,133	888	4.17
1,607	17	4.13	1,082	9	3.58	1,188	13	4.28
18,574	91	1.96	17,997	90	1.97	19,181	95	1.95
10,469	55	2.12	10,469	55	2.09	9,988	51	2.04
889	7	2.74	1,042	7	3.00	968	7	2.75
2,166	6	1.21	1,970	5	.96	1,610	3	.79
728	5	2.46	687	3	1.87	709	4	2.26
121,247	1,123	3.68	119,749	1,131	3.78	119,777	1,061	3.57
(868)			(864)			(855)		
13,977			13,606			13,819		
1,417			1,477			1,540		
$135,773			$133,968			$134,281		
$53,826	37	.27	$54,416	34	.25	$54,295	32	.24
6,697	5	.25	6,854	4	.21	6,351	1	.10
6,402	21	1.31	6,111	19	1.23	5,627	16	1.16
4,664	9	.81	4,650	9	.77	4,706	9	.76
71,589	72	.40	72,031	66	.36	70,979	58	.33
456	—	.23	466	—	.23	795	1	.32
865	3	1.49	1,216	4	1.43	1,802	5	1.06
12,631	86	2.75	11,046	74	2.68	10,833	68	2.54
85,541	161	.75	84,759	144	.68	84,409	132	.63
31,516			30,748			31,099		
2,057			1,782			2,048		
1,417			1,477			1,540		
120,531			118,766			119,096		
15,241			15,200			15,184		
1			2			1		
15,242			15,202			15,185		
$135,773			$133,968			$134,281		

	2.93	%		3.10	%		2.94	%
962	3.15	%	987	3.30	%	929	3.13	%
14			14			11		
$ 948			$ 973			$ 918		

(e) Yield is calculated on the basis of amortized cost.
(f) Rate calculation excludes basis adjustments related to fair value hedges.
(g) A portion of long-term debt and the related interest expense is allocated to discontinued liabilities as a result of applying our matched funds transfer pricing methodology to discontinued operations.

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Figure 7 shows how the changes in yields or rates and average balances from the prior year period affected net interest income. The section entitled "Financial Condition" contains additional discussion about changes in earning assets and funding sources.

Figure 7. Components of Net Interest Income Changes from Continuing Operations

	From three months ended March 31, 2017 to three months ended March 31, 2018		
in millions	Average Volume	Yield/ Rate	Net Change [a]
INTEREST INCOME			
Loans	$ 8	$ 52	$ 60
Loans held for sale	—	(1)	(1)
Securities available for sale	(7)	7	—
Held-to-maturity securities	11	7	18
Trading account assets	—	—	—
Short-term investments	1	4	5
Other investments	—	2	2
Total interest income (TE)	13	71	84
INTEREST EXPENSE			
NOW and money market deposit accounts	—	14	14
Savings deposits	—	4	4
Certificates of deposit ($100,000 or more)	4	7	11
Other time deposits	—	4	4
Total interest-bearing deposits	4	29	33
Federal funds purchased and securities sold under repurchase agreements	1	2	3
Bank notes and other short-term borrowings	(2)	3	1
Long-term debt	11	13	24
Total interest expense	14	47	61
Net interest income (TE)	$ (1)	$ 24	$ 23

(a) The change in interest not due solely to volume or rate has been allocated in proportion to the absolute dollar amounts of the change in each.

Provision for credit losses

Our provision for credit losses was $61 million for the three months ended March 31, 2018, compared to $63 million for the three months ended March 31, 2017. The decrease of $2 million in our provision for credit losses was related to a decrease in net loan-charge offs during the first quarter of 2018 compared to one year ago. In 2018, we expect the provision to slightly exceed net loan charge-offs to provide for loan growth.

Noninterest income

As shown in Figure 8, noninterest income was $601 million for the first quarter of 2018, compared to $577 million for the year-ago quarter. Noninterest income represented 39% of total revenue for the three months ended March 31, 2018, compared to 38% for the three months ended March 31, 2017. In 2018, we expect noninterest income to be in

the range of $2.5 billion to $2.6 billion.

The following discussion explains the composition of certain elements of our noninterest income and the factors that caused those elements to change.

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Figure 8. Noninterest Income

(a) Other noninterest income includes operating lease income and other leasing gains, corporate services income, corporate-owned life insurance income, consumer mortgage income, mortgage servicing fees, net gains (losses) from principal investing, and other income. See the "Consolidated Statements of Income" in Item 1. Financial Statements of this report.

Trust and investment services income

Trust and investment services income consists of brokerage commissions, trust and asset management fees, and insurance income. The assets under management that primarily generate these revenues are shown in Figure 9. For the three months ended March 31, 2018, trust and investment services income decreased $2 million, or 1.5%, compared to the same period one year ago, primarily due to a decrease in fixed income brokerage commissions.

A significant portion of our trust and investment services income depends on the value and mix of assets under management. At March 31, 2018, our bank, trust, and registered investment advisory subsidiaries had assets under management of $39.0 billion, compared to $37.4 billion at March 31, 2017. As shown in Figure 9, the increase in assets under management was primarily attributable to market growth over the past twelve months.

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Figure 9. Assets Under Management

in millions	March 31, 2018	December 31, 2017	September 30, 2017	June 30, 2017	March 31, 2017
Assets under management by investment type:					
Equity	$23,629	$ 24,081	$ 23,342	$22,824	$22,522
Securities lending	837	947	876	807	1,095
Fixed income	11,098	10,930	11,009	10,819	10,497
Money market	3,439	3,630	3,433	3,163	3,303
Total assets under management	$39,003	$ 39,588	$ 38,660	$37,613	$37,417

Investment banking and debt placement fees

Investment banking and debt placement fees consists of syndication fees, debt and equity financing fees, financial adviser fees, gains on sales of commercial mortgages, and agency origination fees. Investment banking and debt placement fees increased $16 million, or 12.6%, from the year-ago quarter, primarily related to the Cain Brothers acquisition during the fourth quarter of 2017, as well as continued growth in our core franchise. In the first quarter of 2018, commercial mortgage banking and mergers and acquisitions advisory fees contributed to the strong performance.

Cards and payments income

Cards and payments income, which consists of debit card, consumer and commercial credit card, and merchant services income, decreased $3 million, or 4.6%, from the year-ago quarter. Cards and payments income and other expense both declined due to the adoption of the new revenue recognition accounting standard. The new accounting standard had no net impact to income during the first quarter of 2018. Excluding the impact of the new revenue recognition accounting standard, cards and payments increased $8 million from the year-ago quarter driven by strength in our core products and the impact of the Key Merchant Services acquisition in the second quarter of 2017.

Service charges on deposit accounts

Service charges on deposit accounts increased $2 million, or 2.3%, for the three months ended March 31, 2018, compared to the same period one year ago. The increase from the three months ended March 31, 2017, was driven by an increase in account analysis fees.

Other noninterest income

Other noninterest income includes operating lease income and other leasing gains, corporate services income, corporate-owned life insurance income, consumer mortgage income, mortgage servicing fees, net gains (losses) from principal investing, and other income. Other noninterest income increased $11 million, or 6.7%, from the year-ago quarter. Operating lease income and other leasing gains contributed to the increase, up $9 million from the year-ago period, driven by higher originations. Corporate services income grew $8 million related to higher loan and derivative trading income. These increases were partially offset by a decline in other income.

Noninterest expense

As shown in Figure 10, noninterest expense was $1.0 billion for the first quarter of 2018 and first quarter of 2017. Figure 10 gives a breakdown of our major categories of noninterest expense as a percentage of total noninterest expense for the three months ended March 31, 2018. In 2018, we expect noninterest expense to be in the range of $3.85 billion to $3.95 billion.

Beginning in the first quarter of 2018, we no longer separately report merger-related charges.

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Figure 10. Noninterest Expense

(a) Other noninterest expense includes equipment, operating lease expense, marketing, FDIC assessment, intangible asset amortization, OREO expense, net, and other expense. See the "Consolidated Statements of Income" in Item 1. Financial Statements of this report.

(a) See Figure 2 entitled “GAAP to Non-GAAP Reconciliations,” which presents the computations of certain financial measures related to “cash efficiency.” The table reconciles the GAAP performance measures to the corresponding non-GAAP measures, which provides a basis for period-to-period comparisons.

Figure 11. Merger-Related Charges

dollars in millions	Three months ended March 31, 2018	2017
Personnel	$ —	$ 30
Net occupancy	—	5
Business services and professional fees	—	5
Computer processing	—	5
Marketing	—	6
Other nonpersonnel expense	—	30
Noninterest expense	—	81
Total merger-related charges	$ —	$ 81

Personnel

As shown in Figure 12, personnel expense, the largest category of our noninterest expense, increased by $38 million, or 6.8%, for the first quarter of 2018 compared to the year-ago quarter. This increase was largely due to recent acquisitions, as well as accelerated technology investments and higher performance-based compensation.

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Figure 12. Personnel Expense

	Three months ended March 31,		Change	
dollars in millions	2018	2017	Amount	Percent
Salaries and contract labor	$339	$324	$15	4.6 %
Incentive and stock-based compensation	145	127	18	14.2
Employee benefits	105	96	9	9.4
Severance	5	9	(4)	(44.4)
Total personnel expense	$594	$556	$38	6.8 %
Merger-related charges	—	30	(30)	N/M
Total personnel expense excluding merger-related charges	$594	$526	$68	12.9 %

Net occupancy

Net occupancy expense decreased $9 million, or 10.3%, for the first quarter of 2018, compared to the same period one year ago. This decrease was primarily due to lower property reserve and rental expenses.

Other noninterest expense

Other noninterest expense includes equipment, operating lease expense, marketing, FDIC assessment, intangible asset amortization, OREO expenses, and other miscellaneous expense categories. Other noninterest expense decreased $23 million, or 8.7%, from the year-ago quarter. Other expense declined from a year ago, primarily driven by a $20 million philanthropic contribution made in the first quarter of 2017. These declines are partially offset by higher marketing expense, higher operating lease expenses driven by increased volumes, and costs related to recent acquisitions.

Income taxes

We recorded tax expense from continuing operations of $62 million for the first quarter of 2018 and $94 million for the first quarter of 2017.

Our federal tax expense differs from the amount that would be calculated using the federal statutory tax rate, primarily because we generate income from investments in tax-advantaged assets, such as corporate-owned life insurance and credits associated with renewable energy and low-income housing investments, and make periodic adjustments to our tax reserves. Tax expense for the three months ended March 31, 2018, and March 31, 2017, was affected by net discrete income tax benefits of $26 million and $19 million, respectively. Excluding those benefits, the tax expense for the first quarter of 2018 was $88 million.

Additional information pertaining to how our tax expense (benefit) and the resulting effective tax rates were derived is included in Note 14 (“Income Taxes”) beginning on page 156 of our 2017 Form 10-K.

Line of Business Results

This section summarizes the financial performance of our two major business segments (operating segments): Key Community Bank and Key Corporate Bank. Note 18 (“Line of Business Results”) describes the products and services offered by each of these business segments, provides more detailed financial information pertaining to the segments,

and explains “Other Segments” and “Reconciling Items.”

Figure 13 summarizes the contribution made by each major business segment to our “taxable-equivalent revenue from continuing operations” and “income (loss) from continuing operations attributable to Key” for the three-month periods ended March 31, 2018, and March 31, 2017.

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Figure 13. Major Business Segments — Taxable-Equivalent Revenue from Continuing Operations and Income (Loss) from Continuing Operations Attributable to Key

dollars in millions	Three months ended March 31, 2018	2017	Change Amount	Percent
REVENUE FROM CONTINUING OPERATIONS (TE)				
Key Community Bank	$973	$905	$68	7.5 %
Key Corporate Bank	559	578	(19)	(3.3)
Other Segments	22	29	(7)	(24.1)
Total Segments	1,554	1,512	42	2.8
Reconciling Items [(a)]	(1)	(6)	5	N/M
Total	$1,553	$1,506	$47	3.1 %
INCOME (LOSS) FROM CONTINUING OPERATIONS ATTRIBUTABLE TO KEY				
Key Community Bank	$196	$147	$49	33.3 %
Key Corporate Bank	207	180	27	15.0
Other Segments	19	21	(2)	(9.5)
Total Segments	422	348	74	21.3
Reconciling Items [(a)]	(6)	(24)	18	N/M
Total	$416	$324	$92	28.4 %

(a) Reconciling items consist primarily of the unallocated portion of merger-related charges and items not allocated to the business segments because they do not reflect their normal operations.

Key Community Bank summary of operations

As shown in Figure 14, Key Community Bank recorded net income attributable to Key of $196 million for the first quarter of 2018, compared to $147 million for the same period one year ago.

TE net interest income increased in the first quarter of 2018 compared to the first quarter of 2017, primarily attributable to the benefit from higher interest rates and growth in loans. Average loans and leases increased from the year-ago quarter largely driven by a $1.1 billion, or 6.1%, increase in commercial and industrial loans. Average deposit balances increased from the year-ago quarter driven by increases in certificates of deposits and other time deposits.

The provision for credit losses increased slightly from the year-ago quarter while net loan charge-offs were flat as overall credit quality was stable.

Noninterest income was up from the year-ago quarter, driven by higher assets under management from market growth, as well as increases across several fee categories. During the first quarter of 2018, cards and payments income and other expense both declined due to the adoption of the new revenue recognition accounting standard resulting in no net impact to income. Excluding the impact of the new revenue recognition accounting standard, cards and payments income increased from the year-ago quarter driven by strength in our core products and the impact of the Key Merchant Services acquisition in the second quarter of 2017.

Noninterest expense increased from the year-ago quarter, as personnel expense increased $17 million driven by recent acquisitions and ongoing investments, including our residential mortgage platform and HelloWallet. Nonpersonnel expense increased $26 million driven by technology development costs, marketing expenses, higher volume related expenses, and the impact of recent acquisitions, including HelloWallet and Key Merchant Services.

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Figure 14. Key Community Bank

dollars in millions	Three months ended March 31, 2018	2017	Change Amount	Percent
SUMMARY OF OPERATIONS				
Net interest income (TE)	$688	$628	$60	9.6 %
Noninterest income	285	277	8	2.9
Total revenue (TE)	973	905	68	7.5
Provision for credit losses	48	46	2	4.3
Noninterest expense	668	625	43	6.9
Income (loss) before income taxes (TE)	257	234	23	9.8
Allocated income taxes (benefit) and TE adjustments	61	87	(26)	(29.9)
Net income (loss) attributable to Key	$196	$147	$49	33.3 %
AVERAGE BALANCES				
Loans and leases	$47,680	$47,085	$595	1.3 %
Total assets	51,681	51,063	618	1.2
Deposits	79,945	79,148	797	1.0
Assets under management at period end	$39,003	$37,417	$1,586	4.2 %

ADDITIONAL KEY COMMUNITY BANK DATA

dollars in millions	Three months ended March 31, 2018	2017	Change Amount	Percent
NONINTEREST INCOME				
Trust and investment services income	$104	$98	$6	6.1 %
Services charges on deposit accounts	76	75	1	1.3
Cards and payments income	51	55	(4)	(7.3)
Other noninterest income	54	49	5	10.2
Total noninterest income	$285	$277	$8	2.9 %
AVERAGE DEPOSITS OUTSTANDING				
NOW and money market deposit accounts	$44,291	$44,780	$(489)	(1.1)%
Savings deposits	5,056	5,268	(212)	(4.0)
Certificates of deposits ($100,000 or more)	4,961	3,879	1,082	27.9
Other time deposits	4,856	4,692	164	3.5
Noninterest-bearing deposits	20,781	20,529	252	1.2
Total deposits	$79,945	$79,148	$797	1.0 %
HOME EQUITY LOANS				
Average balance	$11,763	$12,456		
Combined weighted-average loan-to-value ratio (at date of origination)	70 %	70 %		
Percent first lien positions	60	60		
OTHER DATA				
Branches	1,192	1,216		
Automated teller machines	1,569	1,594		

Key Corporate Bank summary of operations

As shown in Figure 15, Key Corporate Bank recorded net income attributable to Key of $207 million for the first quarter of 2018, compared to $180 million for the same period one year ago.

TE net interest income decreased in the first quarter of 2018 compared to the first quarter of 2017, primarily attributable to lower spreads on earning assets and lower purchase accounting accretion. Average loans and leases increased from the year-ago quarter largely driven by a $1.2 billion, or 5.2%, increase in commercial and industrial loans. Average deposit balances decreased from the year-ago quarter driven by the managed exit of higher cost corporate and public sector deposits.

The provision for credit losses and net loan charge-offs both decreased slightly from the year-ago quarter as overall credit quality continued to improve.

Noninterest income was up from the year-ago quarter, driven by higher investment banking and debt placement fees related to the acquisition of Cain Brothers as well as continued growth in our core franchise. Operating lease income and other leasing gains increased due to higher originations, and corporate services income increased due

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to higher derivatives revenues. These increases were partially offset by a decline in other noninterest income related to lower gains from certain real estate investments.

Noninterest expense increased from the year-ago quarter, largely driven by higher operating lease expense and intangible asset amortization.

Figure 15. Key Corporate Bank

dollars in millions	Three months ended March 31, 2018	2017	Change Amount	Percent
SUMMARY OF OPERATIONS				
Net interest income (TE)	$272	$304	$(32)	(10.5)%
Noninterest income	287	274	13	4.7
Total revenue (TE)	559	578	(19)	(3.3)
Provision for credit losses	14	18	(4)	(22.2)
Noninterest expense	314	304	10	3.3
Income (loss) before income taxes (TE)	231	256	(25)	(9.8)
Allocated income taxes and TE adjustments	24	76	(52)	(68.4)
Net income (loss)	$207	$180	$27	15.0
Net income (loss) attributable to Key	$207	$180	$27	15.0 %
AVERAGE BALANCES				
Loans and leases	$38,260	$37,688	$572	1.5 %
Loans held for sale	1,118	1,097	21	1.9
Total assets	45,549	44,124	1,425	3.2
Deposits	20,815	21,002	(187)	(.9)%

ADDITIONAL KEY CORPORATE BANK DATA

dollars in millions	Three months ended March 31, 2018	2017	Change Amount	Percent
NONINTEREST INCOME				
Trust and investment services income	$29	$37	$(8)	(21.6)%
Investment banking and debt placement fees	141	124	17	13.7
Operating lease income and other leasing gains	27	21	6	28.6
Corporate services income	43	38	5	13.2
Service charges on deposit accounts	13	12	1	8.3
Cards and payments income	11	9	2	22.2
Payments and services income	67	59	8	13.6
Mortgage servicing fees	17	16	1	6.3
Other noninterest income	6	17	(11)	(64.7)
Total noninterest income	$287	$274	$13	4.7 %

Other Segments

Other Segments consist of Corporate Treasury, Key's Principal Investing unit, and various exit portfolios. Other Segments generated net income attributable to Key of $19 million for the first quarter of 2018, compared to $21 million for the same period last year.

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Financial Condition

Loans and loans held for sale

Figure 16. Breakdown of Loans at March 31, 2018

(a) Other consumer loans include Consumer direct loans, Credit cards, and Consumer indirect loans. See Note 3 ("Loans and Loans Held for Sale") Item 1. Financial Statements of this report.

At March 31, 2018, total loans outstanding from continuing operations were $88.1 billion, compared to $86.4 billion at December 31, 2017. For more information on balance sheet carrying value, see Note 1 ("Summary of Significant Accounting Policies") under the headings "Loans" and "Loans Held for Sale" on page 100 of our 2017 Form 10-K.

Commercial loan portfolio

Commercial loans outstanding were $64.8 billion at March 31, 2018, an increase of $2.0 billion, or 3.3%, compared to December 31, 2017, primarily driven by an increase in commercial and industrial loans. Figure 17 provides our commercial loan portfolios by industry classification at March 31, 2018, and December 31, 2017.

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Figure 17. Commercial Loans by Industry

March 31, 2018 dollars in millions	Commercial and industrial	Commercial real estate	Commercial lease financing	Total commercial loans	Percent of total	
Industry classification:						
Agricultural	$ 687	$ 149	$ 90	$ 926	1.4	%
Automotive	2,206	483	61	2,750	4.2	
Business products	2,053	151	51	2,255	3.5	
Business services	2,786	154	236	3,176	4.9	
Commercial real estate	6,061	10,242	22	16,325	25.2	
Construction materials and contractors	1,702	331	175	2,208	3.4	
Consumer discretionary	3,697	579	555	4,831	7.5	
Consumer services	2,990	952	214	4,156	6.4	
Equipment	1,542	131	112	1,785	2.7	
Financial	4,765	62	338	5,165	8.0	
Healthcare	3,396	2,173	367	5,936	9.2	
Materials manufacturing and mining	1,903	99	132	2,134	3.3	
Media	404	22	38	464	.7	
Oil and gas	1,217	45	50	1,312	2.0	
Public exposure	2,745	52	1,029	3,826	5.9	
Technology	599	10	8	617	1.0	
Transportation	1,444	227	782	2,453	3.8	
Utilities	3,505	6	338	3,849	5.9	
Other	611	—	—	611	1.0	
Total	$ 44,313	$ 15,868	$ 4,598	$ 64,779	100.0	%

December 31, 2017 dollars in millions	Commercial and industrial	Commercial real estate	Commercial lease financing	Total commercial loans	Percent of total	
Industry classification:						
Agricultural	$ 742	$ 156	$ 100	$ 998	1.5	%
Automotive	2,156	474	73	2,703	4.3	
Business products	1,845	148	52	2,045	3.3	
Business services	2,711	158	245	3,114	5.0	
Commercial real estate	5,595	10,392	23	16,010	25.5	
Construction materials and contractors	1,693	320	162	2,175	3.5	
Consumer discretionary	3,646	565	542	4,753	7.6	
Consumer services	3,005	937	262	4,204	6.7	
Equipment	1,505	137	118	1,760	2.8	
Financial	4,081	62	341	4,484	7.1	
Healthcare	3,246	2,233	389	5,868	9.4	
Materials manufacturing and mining	1,819	113	133	2,065	3.3	
Media	364	21	42	427	.7	
Oil and gas	1,095	21	51	1,167	1.9	
Public exposure	2,783	52	1,055	3,890	6.2	
Technology	579	3	8	590	.9	
Transportation	1,418	242	890	2,550	4.1	
Utilities	3,067	6	340	3,413	5.4	
Other	509	8	—	517	.8	

Total	$ 41,859	$ 16,048	$ 4,826	$ 62,733	100.0 %

Commercial and industrial. Commercial and industrial loans are the largest component of our loan portfolio, representing 50% of our total loan portfolio at March 31, 2018, and 48% at December 31, 2017. This portfolio is approximately 83% variable rate and consists of loans originated in both Key Corporate Bank and Key Community Bank to large corporate, middle market, and small business clients.

Commercial and industrial loans totaled $44.3 billion at March 31, 2018, an increase of $2.5 billion, or 5.9%, compared to December 31, 2017. The growth was broad-based and spread across most industry categories, including increased lending in the financial, commercial real estate, and utilities industries, which combined accounted for approximately 65% of the growth at March 31, 2018.

Commercial real estate loans. Our commercial real estate portfolio includes both mortgage and construction loans, and is originated through two primary sources: our 15-state banking franchise, and KeyBank Real Estate Capital, a national line of business that cultivates relationships with owners of commercial real estate located both within and beyond the branch system. Approximately 69% of our average commercial real estate loans are generated by our KeyBank Real Estate Capital line of business. Nonowner-occupied properties, generally properties for which at least 50% of the debt service is provided by rental income from nonaffiliated third parties, represented 79% of total commercial real estate loans outstanding at March 31, 2018. Construction loans, which provide a stream of funding for properties not fully leased at origination to support debt service payments over the term of the contract or project, represented 12% of commercial real estate loans at period end.

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At March 31, 2018, commercial real estate loans totaled $15.9 billion, which includes $1.9 billion of construction loans. Compared to December 31, 2017, this portfolio decreased $180 million, or 1.1%. We continue to focus primarily on owners of completed and stabilized commercial real estate in accordance with our relationship strategy.

As shown in Figure 18, our commercial real estate loan portfolio includes various property types and geographic locations of the underlying collateral. These loans include commercial mortgage and construction loans in both Key Community Bank and Key Corporate Bank.

Figure 18. Commercial Real Estate Loans

	Geographic Region										
dollars in millions	West	Southwest	Central	Midwest	Southeast	Northeast	National	Total	Percent of Total	Construction	Commercial Mortgage
March 31, 2018											
Nonowner-occupied:											
Retail properties	$220	$ 129	$118	$191	$205	$834	$313	$2,010	12.7 %	$ 255	$ 1,755
Multifamily properties	441	234	770	409	802	1,982	238	4,876	30.7	1,107	3,769
Health facilities	98	—	55	157	211	886	453	1,860	11.7	75	1,785
Office buildings	251	13	87	121	165	1,017	64	1,718	10.8	125	1,593
Warehouses	71	25	20	101	68	343	92	720	4.5	37	683
Manufacturing facilities	9	—	5	2	22	72	66	176	1.1	9	167
Hotels/Motels	39	—	26	—	1	194	34	294	1.9	5	289
Residential properties	—	—	—	3	19	166	—	188	1.2	76	112
Land and development	23	—	5	3	3	69	—	103	.7	74	28
Other	5	—	29	13	2	335	205	589	3.7	6	584
Total nonowner-occupied	1,157	401	1,115	1,000	1,498	5,898	1,465	12,534	79.0	1,769	10,765
Owner-occupied	881	10	268	547	44	1,584	—	3,334	21.0	102	3,232
Total	$2,038	$ 411	$1,383	$1,547	$1,542	$7,482	$1,465	15,868	100.0 %	$ 1,871	$ 13,997
December 31, 2017											
Total	$2,071	$ 387	$1,320	$1,730	$1,939	$7,758	$843	$16,048		$ 1,960	$ 14,088
March 31, 2018											
Nonowner-occupied:											
Nonperforming loans	—	—	—	$1	$10	$11	—	$22	N/M	—	$ 22
Accruing loans past due 90 days or more	$—	—	—	—	—	10	—	10	N/M	1	9
Accruing loans past due 30 through 89 days	—	—	—	2	3	43	—	48	N/M	$ 34	14

West –	Alaska, California, Hawaii, Idaho, Montana, Oregon, Washington, and Wyoming
Southwest –	Arizona, Nevada, and New Mexico
Central –	Arkansas, Colorado, Oklahoma, Texas, and Utah
Midwest –	Illinois, Indiana, Iowa, Kansas, Michigan, Minnesota, Missouri, Nebraska, North Dakota, Ohio, South Dakota, and Wisconsin
Southeast –	Alabama, Delaware, Florida, Georgia, Kentucky, Louisiana, Maryland, Mississippi, North Carolina, South Carolina, Tennessee, Virginia, Washington D.C., and West Virginia
Northeast –	Connecticut, Maine, Massachusetts, New Hampshire, New Jersey, New York, Pennsylvania, Rhode Island, and Vermont
National –	Accounts in three or more regions

Consumer loan portfolio

Consumer loans outstanding decreased by $362 million, or 1.5%, from December 31, 2017, driven by continued declines in the home equity loan portfolio, largely the result of pay downs on home equity lines of credit.

The home equity portfolio is comprised of loans originated by our Key Community Bank within our 15-state footprint and is the largest segment of our consumer loan portfolio, representing 50% of consumer loans outstanding at March 31, 2018.

As shown in Figure 14, we held the first lien position for approximately 60% of the Key Community Bank home equity portfolio at both March 31, 2018, and March 31, 2017. For loans with real estate collateral, we track borrower performance monthly. Regardless of the lien position, credit metrics are refreshed quarterly, including recent FICO scores as well as updated loan-to-value ratios. This information is used in establishing the ALLL. Our methodology is described in Note 1 ("Summary of Significant Accounting Policies") under the heading "Allowance for Loan and Lease Losses" beginning on page 102 of our 2017 Form 10-K.

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Figure 19. Consumer Loans by State

March 31, 2018	Real estate — residential mortgage	Home equity loans	Consumer direct loans	Credit cards	Consumer indirect loans	Total
State						
New York	$ 1,204	$3,054	$ 379	$385	$ 746	$5,768
Ohio	435	1,619	382	239	298	2,973
Washington	662	1,772	223	99	14	2,770
Pennsylvania	323	775	68	45	233	1,444
California	49	34	16	4	50	153
Connecticut	811	416	19	19	151	1,416
Colorado	227	522	78	33	3	863
Oregon	342	918	82	43	3	1,388
Texas	4	23	8	3	22	60
New Jersey	22	23	13	3	514	575
Other	1,394	2,564	490	195	1,257	5,900
Total	$ 5,473	$11,720	$ 1,758	$1,068	$ 3,291	$23,310
December 31, 2017						
Total	$ 5,483	$12,028	$ 1,794	$1,106	$ 3,261	$23,672

Loan sales

As shown in Figure 20, during the first three months of 2018, we sold $2.7 billion of loans. Sales of loans classified as held for sale generated net gains of $44 million in the first three months of 2018.

Among the factors that we consider in determining which loans to sell are:

- our business strategy for particular lending areas;
- whether particular lending businesses meet established performance standards or fit with our relationship banking strategy;
- our A/LM needs;
- the cost of alternative funding sources;
- the level of credit risk;
- capital requirements; and
- market conditions and pricing.

Figure 20 summarizes our loan sales for the first three months of 2018 and all of 2017.

Figure 20. Loans Sold (Including Loans Held for Sale)

in millions	Commercial	Commercial Real Estate	Commercial Lease Financing	Residential Real Estate	Total
2018					
First quarter	$ 141	$ 2,251	$ 66	$ 284	$2,742
Total	$ 141	$ 2,251	$ 66	$ 284	$2,742
2017					
Fourth quarter	$ 88	$ 3,394	$ 81	$ 275	$3,838

Third quarter	337	2,534	93	279	3,243
Second quarter	205	2,097	14	230	2,546
First quarter	49	2,011	83	194	2,337
Total	$ 679	$ 10,036	$ 271	$ 978	$11,964

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Figure 21 shows loans that are either administered or serviced by us, but not recorded on the balance sheet; this includes loans that were sold.

Figure 21. Loans Administered or Serviced

in millions	March 31, 2018	December 31, 2017	September 30, 2017	June 30, 2017	March 31, 2017
Commercial real estate loans	$246,089	$238,718	$224,361	$218,667	$218,387
Residential mortgage	4,585	4,582	4,458	4,345	4,272
Education loans	888	932	974	1,019	1,067
Commercial lease financing	873	862	856	833	916
Commercial loans	498	488	458	446	427
Total	$252,933	$245,582	$231,107	$225,310	$225,069

In the event of default by a borrower, we are subject to recourse with respect to approximately $3.4 billion of the $252.9 billion of loans administered or serviced at March 31, 2018. Additional information about this recourse arrangement is included in Note 15 (“Contingent Liabilities and Guarantees”) under the heading “Recourse agreement with FNMA.”

We derive income from several sources when retaining the right to administer or service loans that are sold. We earn noninterest income (recorded as “mortgage servicing fees”) from fees for servicing or administering loans. This fee income is reduced by the amortization of related servicing assets. In addition, we earn interest income from investing funds generated by escrow deposits collected in connection with the servicing loans. Additional information about our mortgage servicing assets is included in Note 8 (“Mortgage Servicing Assets”).

Securities

Our securities portfolio totaled $30.1 billion at March 31, 2018, compared to $30.0 billion at December 31, 2017. Available-for-sale securities were $17.9 billion at March 31, 2018, compared to $18.1 billion at December 31, 2017. Held-to-maturity securities were $12.2 billion at March 31, 2018, and $11.8 billion at December 31, 2017.

As shown in Figure 22, all of our mortgage-backed securities, which include both securities available for sale and held-to-maturity securities, are issued by government-sponsored enterprises or GNMA and traded in liquid secondary markets. These securities are recorded on the balance sheet at fair value for the available-for-sale portfolio and at amortized cost for the held-to-maturity portfolio. For more information about these securities, see Note 5 (“Fair Value Measurements”) under the heading “Qualitative Disclosures of Valuation Techniques,” and Note 6 (“Securities”).

Figure 22. Mortgage-Backed Securities by Issuer

in millions	March 31, 2018	December 31, 2017
FHLMC	$5,896	$ 5,897