MANAGEMENT DISCUSSION SECTION

Operator: Welcome to E*TRADE FINANCIAL Corporation's First Quarter 2006 Earnings Conference Call. [Operator Instructions].

I've been asked to begin this call with the following Safe Harbor statement. During this conference call the Company will be sharing with you certain projections or other forward-looking statements regarding future events or future performance. E*TRADE FINANCIAL cautions you that certain factors including risk and uncertainties referred to in the 10-Ks, 10-Qs, and other reports it periodically files with the Securities and Exchange Commission could cause the Company's actual results to differ materially from those indicated by its projections or forward-looking statements. In this call E*TRADE FINANCIAL will discuss some non-GAAP measures in talking about its performance, and you can find the reconciliation of those measures to GAAP in the Company's press release which can be found on its website at www.etrade.com.

This call is being recorded. A replay of this call will be available beginning at approximately 7 o'clock p.m. Eastern Time today through 11 o'clock p.m. Eastern Time on Wednesday, May 3rd. This call is also being webcast at www.etrade.com. No other recordings or copies of this call are authorized or may be relied upon. I'll now turn the call over to Mitchell Caplan, Chief Executive Officer of E*TRADE FINANCIAL Corporation who is joined by Jarrett Lilien, President and Chief Operating Officer and Robert Simmons, Chief Financial Officer. Mr. Caplan, please begin.

Mitchell H. Caplan, Chief Executive Officer

Thank you everybody for joining us today. Just over a year ago, we launched a new marketing campaign designed to build on the strengths of our existing brand while broadening what it means to global consumers. We created a new slogan that asks customers to challenge the ordinary and be extraordinary. At the same time, we asked our management team to do the same. We brought new ideas together to challenge the traditional value proposition and enhance the customer experience. We broadened the ways in which we create value for customers to include comprehensive, industry-leading cash management, credit, investing, and trading solutions. By deepening our customer relationships and leveraging our infrastructure to drive efficiency and growth across our global operations, we have and continue to create value for our shareholders.

As we look at how the franchise has done, particularly in the past year, it's truly extraordinary. Through the combination of organic growth initiatives and strategic acquisitions, the franchise has never been stronger. We have grown total client assets to nearly $200 billion on a base of over 4 million accounts. Across this increasing customer base, we are now generating meaningful product engagement beyond trading. We are seeing significant organic growth in cash, assets and credit, as we have created industry-leading functionality for these products. Through our integrated model, we are benefiting from these dynamics in both our retail and institutional segments.

As an example, consider the growth in cash alone we've experienced. Our base increased over 65% in the past year to a record in excess of $30 billion. While the benefits to our retail segment are apparent, our institutional segment continues to drive greater economics by leveraging this growth to significantly reduce our balance sheet funding costs. This link between retail and institutional has translated directly into spread expansion and record net interest income for the Company on a consolidated basis. Similarly, our growth in retail customer assets and trading activity continues to benefit our institutional equities business by providing greater order flow and deeper liquidity for our institutional clients.

In the last three years we have worked diligently to position the business to deliver growth and superior financial performance through various market environments. The results of this past quarter demonstrates the success of our model. We generated strong growth in our core business while accelerating that growth through the integration of additional assets, cash, credit and trading from our two recent acquisitions. As we drive further customer engagement from our existing and new customers, we continue to unlock the full value and opportunity of our integrated model. I am pleased to announce that in the first quarter, the company produced a record $598 million in total net revenues and record earnings of $0.36 per share. This excludes $0.03 in acquisition-related integration expenses as we guided to in December. Including these expenses, we generated GAAP EPS of $0.33, also a record. We delivered growth in all the key drivers of our business.

As we have executed on our vision of creating an integrated financial services company, we are just beginning to realize the power of our centralized technology, operations and service platform on a global basis. We are now in a place to leverage our success around customer assets, cash and credit in the US and extend these solutions to our international clients in Canada, Europe and Asia. We continue to see a tremendous opportunity to capitalize on the growing mass affluent population in the US where 44 million households remain relatively underserved. As we move outside of the US, we believe the opportunity is immense, particularly as we look to regions such as India and China. We have already seen some success internationally with regard to customer cash and this is even before we have begun to market these solutions. Moreover, credit relationships in these great regions remain largely untapped for us.

As we strive toward achieving global integration, our international operations not only differentiate us within the industry but more importantly they represent a natural extension of our model and a significant source of long-term growth. In sum, we are extremely pleased with how our model has and continues to deliver. As we seek to create value for customers and shareholders, we remain committed as a franchise and as a management team to challenge the ordinary and be extraordinary.

With that, I'd like now to turn the call over to Jarrett.

Robert Jarrett Lilien, President and Chief Operating Officer

Thanks, Mitch. Our results for the first quarter proved the power of our model and truly demonstrate our unique ability to leverage our retail performance through our institutional business to generate superior results. We have long said that at the center of our model is the global retail customer through an integrated technology, operations and service platform, we are best positioned to leverage customer engagement across cash, credit, investing and trading solutions.

Around this time last year we rolled out our first iteration of E*TRADE Complete focused on driving broader customer engagements, an important product complete with our Intelligent Cash Optimizer. Since its launch, we have experienced tremendous organic growth in customer cash. By organic growth we mean inflows from customers above and beyond acquisitions. These balances grew $800 million in the third quarter of last year followed by $1 billion in the fourth quarter of last year and $1.6 billion last quarter. The first quarter results represent a 22% annualized growth rate on our enterprise customer cash, which now represents 65% of our enterprise liabilities.

Combined with the trends we are seeing through our quick transfer functionality, this organic growth is extremely encouraging. During the quarter we processed over 750,000 customer initiated quick transfers with almost $3 being transferred in for every $2 out. Interestingly, the largest cash inflows came from bulge bracket firms and national brick and mortar financial institutions. This continued trend of E*TRADE as a destination for cash solidifies our view that our value propositions are resonating well in the marketplace.

Turning to credit, in mid-February we further enhanced Complete with a launch of our intelligent Lending Optimizer. This optimizer allows customers to realize value by demonstrating the most efficient ways to borrow. For the quarter, 8% of traffic to the intelligent lending optimizer resulted in credit application inquiries. While early in its deployment, we hope this optimizer will create deeper credit relationships with our customers, especially as they respond to the changing interest rate environment. In investing, continuing our leadership and commitment to innovation, we launched the intelligent Investing Optimizer allowing customers to maximize their investment portfolio based upon their own goals and risk preferences. In addition, we rolled out a series of enhancements for our retail investors answering the growing need for more sophisticated research and product functionality.

As we continue to enhance the customer experience, we seek to attract and retain higher quality wealth building customers. In the first quarter, total client assets increased 8%. Adjusting for market appreciation, we saw sequential asset growth of 3.5%, representing an annualized growth rate of 14%. In trading, we had a very strong quarter as well. Within our 181,000 total retail DARTs, US volumes were up 41% from the prior quarter, and 115% from a year ago. Even more impressive was the further growth in our international and options trades. Continuing to outpace domestic growth, international trading increased 43% versus Q4. Option-related DARTs grew 53% sequentially and now represent 12% of aggregate DART volume, up from 11% in the fourth quarter. We view the growth in international and options businesses not only as proof that our value proposition is resonating, but also that the model is expanding. We are pleased by the performance of our trading products as they benefit from an 85% incremental operating margin and allow for additional upside in stronger equity market environments.

Our average commission in the first quarter was $12.10. This is lower than our guided range of 12.25 to 12.40 for the year. The disparity resulted from two factors. First was the free trade offer extended to Harrisdirect customers upon conversion. The cost associated with this offer was $0.13 to our average commission rate and was a part of the overall $0.03 of acquisition integration expenses in the quarter. Excluding the impact of this offer, our average commission rate would have been $12.23. The second factor was our success in retaining more Brown customers in model coupled with a higher level of engagement. Given our outlook for the remainder of the year, we continue to view our initial guidance range as a fair estimate.

Turning to our institutional results, we are pleased with a record performance which directly correlated to our heightened levels of retail customer engagement. You will recall that our retail customer cash and credit relationship each play an integral part in balance sheet management. Leveraging these retail customer flows, we generated record net interest income after provision of $315 million. This was driven by an enterprise net interest spread of 286 basis points and average interest earning assets in excess of $41 billion. With respect to moving Clearing under the bank, we are confident that we will be receiving the economic benefit associated with this by midsummer as originally forecasted.

We continue to guide to a spread of approximately 286 basis points for the balance of the year as a result of several factors. While acknowledging the expected benefit from moving Clearing under the bank as well as the potential upside from continued growth in customer cash and credit, uncertainties related to the current rate environment and the shape of the yield curve persist. In addition, as we grow the balance sheet for the remainder of the year, the majority of the assets will be comprised of our traditional mix of mortgages, HELOC, and margin. Further looking at institutional, our equities business also continues to benefit from its link to our retail segment. This business benefited from the increase in retail trading activity that we experienced in the quarter, driving an increase in institutional principal transaction revenue and institutional commissions.

I'd now like to spend a few minutes on the status of our deal integrations. In January we completed the Harrisdirect conversion. The Brown conversion is now scheduled for early May and it will be operationally less complicated as the platforms are substantially similar. With respect to attrition, the economic drivers for both transactions; assets, cash, credit and DARTs, all remain above plan. Specifically, as of the quarter end, Harrisdirect economic attrition with 6.6% and Brown with a 2%, both against our 15% modeled level. As evidenced in our Q1 results, the economic attrition we've experienced is being more than offset by deepening engagement from our new Harrisdirect and Brown customers.

Given the increased engagement trends across all accounts and products, we will continue to invest in our service platform. When we announced each of these acquisitions, we discussed we would retain the entire service platforms from both companies to help strengthen our overall service offering. Our view of the costs associated with achieving this was predicated on the volumes and engagement levels forecasted at that time. Since then, we have seen a greater level of engagement across our entire customer base. As a result we see a need to make an additional investment in service to support the higher customer activity levels. To that end, we have begun to hire additional service representatives. This investment will ensure that all E*TRADE FINANCIAL customers, new and old, enjoy improved service as they continue further engagement with us.

The first quarter was a great one for the Company. We made significant progress in expanding customer relationships, driving growth in our operating metrics both domestically and internationally, while delivering solid financial performance. With that, I'll turn the call over to Rob for the financial details.

Robert J. Simmons, Chief Financial Officer

Okay, thanks Jarrett. Our first quarter financial results built on a record year in 2005 and delivered another quarter of record performance. During the quarter we remained focused and disciplined in executing on our core strategic plan while accelerating that plan through the integration of our recent acquisitions. This combination not only produced record revenue and earnings, but also record results across many of the key drivers of our business. First quarter total net revenue increased 43% year-over-year and 25% sequentially to a record $598 million. Net interest income after provision increased 79% year-over-year and 30% sequentially to a record $315 million.

As we have achieved greater balance sheet integration over the past year, we have more effectively monetized the growth in customer cash and credit balances. As a result, net interest income has become a larger portion of a growing revenue base and now represents 53% of revenue, up from 42% just a year ago. Non-interest income which includes retail and institutional commissions, fees, and other revenue also continued to grow, increasing 17% year-over-year and 20% sequentially. The year-over-year growth in reported non-interest income is the result of a 60% increase in commissions and a 43% increase in other revenue offset by a 74% decrease in gain on sale of loans and security – securities. Rather than originating and selling loans, we have improved the customer experience by putting more origination volume on balance sheet. This allows us to retain the customer relationship while driving growth and spread related revenue. The shift away from gain on sale has favorably impacted the overall quality of our earnings. Our model is designed to generate a growing base of recurring revenue as customers engage in assets, cash and credit solutions. As witnessed in the first quarter, our model also maintains strong leverage to growth in trading activity.

Turning now to expenses. In the first quarter we continued to deliver prudent control and operational efficiency within our core operations while integrating our acquisitions of Harrisdirect and BrownCo. Total expenses excluding corporate interest were $355 million. Our first quarter results included acquisition-related integration expenses that we outlined in December. Most of these expenses appeared in professional services and compensation and impacted our earnings by $0.03 per share. We have carved out these items for discussion purposes as well as for our guidance as they are not truly reflective of the full integration of the operations and the synergies of the acquisitions. Evaluating our results with this in mind, we can see that the model continued to deliver great operating leverage. In fact, each of our operating expense line items, including compensation, clearing and servicing costs, communications, marketing, professional services, all declined as a percentage of revenue in the quarter. Compensation and benefits is now at 19% of revenue, down from 21% in the fourth quarter and over 22% a year ago. Given the combination of our controls and the increased scale in the model, we generated a record 44% operating margin in the quarter, excluding the acquisition integration related expenses. We achieved operating margin improvement even as we increased our marketing spend by $3 million sequentially. Illustrating the leverage in the model, 74% of the sequential growth in revenue in the quarter fell directly to our segment income. The model is working and delivering impressive earnings generation for every new dollar of revenue.

Before concluding, I'd like to spend a minute on our earnings outlook for the remainder of the year. As stated in our press release, we increased the high and low end of our earnings guidance for 2006 by $0.05. This increase is predicated on a number of factors. First, it reflects the strength of our first quarter results. Second, it considers the fact that we are only three months post conversion on Harrisdirect and still pre-conversion on BrownCo. While current indications around the combined attrition levels are encouraging, we believe it is prudent to maintain our current assumptions until we have greater clarity after converting BrownCo. Third, we remain hesitant to extrapolate Q1 market volume trends, and we will update our expected DART range at the mid-year point when we have a better view of activity through the spring and summer. Fourth, our revised guidance reflects the higher than originally forecasted share count as a result of the performance of the stock. At the current stock price, we are experiencing a higher diluted share count as a result of employee stock options and the mandatory convertible notes issued last year. The impact of this increased share count was not contemplated in the initial guidance we provided in December. Fifth and finally, we remain committed to investing in service as an integral component of our asset gathering and franchise building initiative as Jarrett outlined earlier.

The net result of these factors is our $0.05 increase in guidance. Within these factors, there are sources of upside as well as offsets to our earnings production in 2006. On the positive side of this equation is approximately $0.15 of higher earnings expected in 2006 from the outperformance of the first quarter plus the impact of cash, margins, debt, balance sheet size, spread and DARTs, all at the high end of our guidance range. Against this, we have headwinds of approximately $0.04 associated with the higher share count and $0.06 related to our investment in service. The net of all this is the $0.05 increase in guidance. As we continue to monitor deal-related attrition, the interest rate environment, customer cash and credit growth, as well as the equity market environment, we plan to provide an earnings update in July or as appropriate.

And with that, I'd like to open the call for questions. Operator?

QUESTION AND ANSWER SECTION

Operator: [Operator Instructions]. Your first question comes from Rich Repetto with Sandler O'Neill.

<Q – Richard Repetto>: Yeah hi guys, can you hear me?

<A – Mitchell Caplan>: Hey, Rich. Perfectly.

<Q – Richard Repetto>: Congratulations, excellent quarter.

<A – Mitchell Caplan>: Thanks a lot.

<Q – Richard Repetto>: First thing is the cash inflows, that's a number that just jumps out at you. And I guess, Jarrett, you talked about the bulge bracket and traditional brick and click, brick and mortar clients bringing more cash. Can you – is there any more color to this – more specifics to say, you know, is it coming from Harrisdirect higher balance accounts or BrownCo higher balance accounts more than the rest of your customer base or is it spread out? And how consistent do you think this inflow of cash will be throughout the year?

<A – Mitchell Caplan>: Jarrett?

<A – Robert Jarrett Lilien>: Sure, yeah, Rich. It's very much across the board. We're seeing it – and that's what's really encouraging about it. With Harris and Brown, we're finding as these customers see the product mix that we have, that they are engaging more with us, and that engagement is really offsetting what we're losing from the accounts that are leaving us. So that's very encouraging. But then on top of it, is it continues to be a strong trend that is, a value proposition that is just ringing home with our customers, our existing customers, and they continue to bring more cash, and they continue to engage more with us across the board.

<A – Mitchell Caplan>: Yeah, and I guess the only thing I'd add, Richard, is that we are seeing a 1.6 billion. We were actually quite pleased by that given that 100% of that was organic growth in the quarter. I think, you're beginning to see more and more of the effect of the Cash Optimizer which is embedded in the E*TRADE Complete product. As Jarrett said, you're definitely seeing additional engagement from both Harrisdirect and Brown, we hadn't modeled any of that when we announced the deals, as you know, because it was just too, too hard to try to model what could be prospective cross sells, but we are succeeding and certainly hope to, given the kinds of accounts that we acquired, their average balances. But we're also seeing it in the new accounts that we're bringing in, you know, three, four times the value of those that are leaving, as well as with our current base. And we're seeing them, across the board from a lot of the bulge bracket firms, whether it's places like, you know, Morgan Stanley, Merrill Lynch, Citi, UBS, really pretty much all of the bulge bracket firms. I mean, I think that's sort of the new battleground for us given our business model and what we're trying to achieve in terms of growth.

<A – Robert Jarrett Lilien>: I guess just kicking this dead horse to death, the other place where we're seeing some nice inflows, are from the – as we were saying, the sort of bricks and mortar banks. So, not only is the value proposition really ringing home with investing customers and the traditional brokerage firms, but we're also seeing, assets and trading and cash coming directly from some of the more traditional big banks as well.

<A – Mitchell Caplan>: Yeah, I think at very decent size balances. So the goal here is to try to again engage with that investing base customer, recognizing that they've got savings of cash, 10 to 15% of their total assets somewhere. And our, obviously, call to action is bring it to E*TRADE FINANCIAL. Do we think it's sustainable? We certainly are hoping for that, and that's how we intend to execute.

Operator: [Operator Instructions]. At this time we have no questions.

Mitchell H. Caplan, Chief Executive Officer

Okay, thanks everybody for joining us and we will keep you updated.

Operator: This concludes today's E*TRADE Q1 2006 earnings conference call. You may now disconnect.