PUBLIC SERVICE COMPANY OF NEW MEXICO

Sale and Leaseback Transactions
with respect to
Palo Verde Nuclear Generating Station
Units 1 and 2
(Docket Nos. STN-528 and STN-529)

Financial Information
with respect to
Prospective Equity Investors

June 10, 1986

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SECURITIES AND EXCHANGE COMMISSION
Washington, D.C. 20549

FORM 10-K
ANNUAL REPORT PURSUANT TO SECTION 13 OR 15(d) OF
THE SECURITIES EXCHANGE ACT OF 1934

84162

For the fiscal year ended December 31, 1985 — Commission file number 1-5945

THE CHASE MANHATTAN CORPORATION
(Exact name of registrant as specified in its charter)

Delaware	13-2633613
(State or other jurisdiction of incorporation or organization)	(I.R.S. Employer Identification No.)
1 Chase Manhattan Plaza, New York, New York	10081
(Address of principal executive offices)	(Zip Code)

Registrant's telephone number, including area code: 212-552-2222

PROCESSED BY RECEIVED MAR 25 1986 DISCLOSURE INCORPG.

Securities registered pursuant to Section 12(b) of the Act:

Title of each Class	Name of each Exchange on which Registered
Common Stock ($12.50 Par Value)	New York Stock Exchange
Preferred Stock, 6 3/4% Series B	New York Stock Exchange
Preferred Stock, 7.60% Series C	New York Stock Exchange
Preferred Stock, 10 1/2% Series D	New York Stock Exchange
Preferred Stock, Floating Rate Series E	New York Stock Exchange
Preferred Stock, Floating Rate Series F	New York Stock Exchange
4 7/8% Convertible Capital Notes Due 1993 of The Chase Manhattan Bank, N.A. Assumed by Registrant	New York Stock Exchange
6 1/2% Convertible Subordinated Debentures Due 1995	New York Stock Exchange
Floating Rate Subordinated Notes Due 1995	New York Stock Exchange
Floating Rate Notes Due 1999	New York Stock Exchange
Floating Rate Notes Due 2009	New York Stock Exchange
Floating Rate Subordinated Notes Due 1995	New York Stock Exchange
Extendable Notes Due 1997	New York Stock Exchange

Securities registered pursuant to Section 12(g) of the Act: None.

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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 X No ___

The number of shares outstanding of the registrant's Common Stock ($12.50 Par Value) was 78,732,123 shares at February 27, 1986 The aggregate market value of the voting stock held by non-affiliates of the registrant amounted to $3,325,000,000 at February 27, 1986.

DOCUMENTS INCORPORATED BY REFERENCE*

Documents	Part of Form 10-K Incorporated into
The Chase Manhattan Corporation Annual Report 1985	Part I, Part II, Part IV
The Chase Manhattan Corporation Proxy Statement for its 1986 Annual Meeting	Part III

* Such documents are incorporated herein only to the extent specifically set forth in response to an item herein.

PART I

Item 1. Business.

General Information

The Chase Manhattan Corporation (the "Company") is a bank holding company which was incorporated in 1969 and whose principal subsidiary is The Chase Manhattan Bank, N.A. Throughout this document the term "Corporation" refers to The Chase Manhattan Corporation and its subsidiaries and the term "Bank" refers to The Chase Manhattan Bank, N.A. and its subsidiaries. The Bank, which maintains its head office in New York City, provides a full range of commercial banking and trust services. Measured by total assets at December 31, 1985, the Bank was one of the largest commercial banks in the world and the third largest in the United States.

The Corporation has a number of other banking subsidiaries which also engage in a range of commercial banking activities. In addition, nonbanking subsidiaries of the Company engage in mortgage banking, commercial and consumer financing, discount brokerage, investment advisory and other financial services.

Domestic Activities

The Bank's domestic branch offices provide a wide variety of services which are designed to assist individuals and small businesses, as well as serve large domestic and multinational corporations. Consumer and small business services include numerous types of savings accounts, checking accounts and money market deposit accounts, as well as installment loans, lines of credit, accounts receivable and other asset-based financing services, Bank-by-Phone, electronic home banking and safe deposit facilities. The Company offers other consumer services including the issuance of Chase Manhattan VISA Travelers' Cheques. A subsidiary of the Company, The Chase Manhattan Bank (USA), N.A. ("CMB (USA)"), issues Chase Manhattan VISA credit cards and Chase Manhattan MasterCards.

Commercial lending divisions of the Bank, operating on an industry basis, provide financial services to customers in practically all industries. The Bank draws on the skill and expertise of lending and staff department officers to provide specialized services designed to meet customers' business needs. In addition, the Bank's global cash management system enables corporate and institutional customers to obtain directly multi-account balance and transaction information, transfer funds and manage debt and investment portfolios.

Approximately 3,000 correspondent banks located throughout the United States maintain deposit accounts with the Bank. In 1986, the Bank and Chase Lincoln First Bank, N.A. ("Chase Lincoln") will begin to operate an automated

clearing house (ACH) through a new subsidiary, the Chase Automated Clearing House, Inc. This will enable the Bank and Chase Lincoln to reduce operating costs and enhance the services provided to their customers.

The Trust Department of the Bank administers estates, personal trusts and pension and profit-sharing funds, and provides custody and investment advisory services. It acts as trustee of bond issues and unit trusts, serves as transfer agent or registrar for securities, paying agent for dividends and interest and agent for subscriptions and redemptions. It also provides a dividend reinvestment service for stockholders of publicly held corporations. Other subsidiaries of the Corporation including, Chase Lincoln, provide some or all of the foregoing services.

The Bank or one or more of its subsidiaries is active as a dealer in U.S. Government and state and municipal securities and is a major underwriter and distributor of state and local government securities. The Corporation's worldwide merchant banking activities are consolidated under Chase Manhattan Capital Markets (Holdings), Inc. ("Holdings"), a subsidiary of the Bank. Subsidiaries of Holdings offer merchant banking and investment banking services and engage in certain government and municipal finance activities.

CMB (USA), a wholly owned banking subsidiary of the Company, that commenced operations in 1982, extends credit and offers money market deposits to consumers nationwide from its office in the State of Delaware. Chase U.S. Consumer Services, Inc. ("CUSCS"), a wholly owned subsidiary of the Company, and its subsidiaries with offices located in eleven states, also extend consumer credit.

Rose & Company, a subsidiary of the Company acquired in 1983, offers discount brokerage services. Other subsidiaries of the Company, such as Chase Home Mortgage Corporation, are engaged in domestic real estate and mortgage financing and servicing activities.

A separate subsidiary of the Company, Chase Investors Management Corporation New York, provides investment-related research and investment advisory services for employee benefit funds, charitable foundations and foreign customers.

During the second quarter of 1985, the Company acquired six Ohio savings and loan institutions with total assets of approximately $450 million and merged and converted them into a wholly owned commercial bank named Chase Bank of Ohio. During the fourth quarter of 1985, the Company acquired three Maryland savings and loan institutions with total assets of approximately $700 million and merged and converted them into a wholly owned commercial bank named Chase Bank of Maryland.

During 1985 the Company entered into an agreement to acquire Continental Bancor of Phoenix, Arizona when permitted (October 1, 1986) under inter-state banking legislation adopted by Arizona. Separately, the Company through a subsidiary also acquired, in early 1986, Third Century Leasing Group (The Group) a supplier of office equipment leases with assets of $45 million, based in Moberly, Missouri. The Group is a separate division of Chase Commercial Corporation.

On July 1, 1984, Chase Manhattan National Corporation ("CMNC"), a wholly owned subsidiary of the Company, acquired Lincoln First Bank, N.A., renamed "Chase Lincoln First Bank, N.A." ("Chase Lincoln"), through the merger of its parent company, Lincoln First Banks Inc., into CMNC. Chase Lincoln, a commercial bank based in Rochester, New York, had over $4 billion in assets at the time of the acquisition. Subsequent to the merger, Chase Lincoln sold its downstate New York branch network to the Bank. At the same time, Chase Lincoln acquired the Bank's upstate branch network. At December 31, 1985, the Bank and Chase Lincoln had a combined total of 330 domestic branch offices in New York State.

International Activities

International commercial banking activities are conducted by the International Banking Sector of the Bank, headquartered in New York City, and foreign subsidiary and associated banks and trust companies. International banking activities are also conducted through Chase Bank International ("CBI"), an Edge Act banking subsidiary headquartered in Delaware with branches in Atlanta, Chicago, Houston, Los Angeles, Miami and San Francisco.

Through loans, letters of credit, acceptances, collections and foreign exchange services, the Bank assists both domestic and foreign customers in transacting business worldwide. The Bank maintains a comprehensive network of correspondent relationships with foreign commercial banks and serves as the principal depository in the U.S. for many foreign central banks.

A majority of the Bank's investments in banking and financial institutions and trust companies, which conduct their businesses outside the United States, are held through Chase Manhattan Overseas Banking Corporation ("CMOBC"). CMOBC is an Edge Act corporation with its principal office in Newark, Delaware. In April 1984, CMOBC acquired substantially all (approximately 68.5%) of the outstanding shares not already held by CMOBC, of Nederlandse Credietbank, N.V. ("NCB"), with headquarters in Amsterdam, The Netherlands, and with assets of approximately $4.2 billion, net of intercompany accounts with the Corporation.

In 1985, CMOBC acquired Banco de Finanzas of Madrid, Spain with total assets of approximately $265 million and six branch offices.

During 1985, a subsidiary of the Bank acquired a 29.9% limited partnership interest in Simon & Coates and a 5% limited partnership interest in Laurie, Milbank & Company. Simon & Coates and Laurie, Milbank & Company are London stockbrokers that are members of the London Stock Exchange. The Bank plans to increase its interest in each of the two firms to 100% in 1986, when permitted by the London Stock Exchange.

During 1985, the Bank and the Australian Mutual Provident Society ("AMP"), Australia's largest insurance company, received approval from the Australian regulatory authorities and the United States bank regulatory authorities and began to operate a full-service bank in Australia. CHASE AMP Bank, Ltd. in which CMOBC has a 50% interest, combines investment and commercial banking with securities trading, treasury services and consumer banking services.

Information with respect to the international earnings performance of the Corporation is included in "Management's Discussion and Analysis of Financial Condition and Results of Operations" beginning on page 22 and in Note 18: "International Activities", of the Notes to Financial Statements in The Chase Manhattan Corporation Annual Report 1985, which is filed herewith as Exhibit 13 (The Annual Report or Exhibit 13) and such information is incorporated herein by reference.

Competition

The Company, the Bank and their subsidiaries compete with various financial institutions, ranging from leading multinational bank holding companies and their subsidiaries to local thrift institutions, as well as securities brokers, underwriters, government agencies and other businesses providing financial services. The Bank and other banking subsidiaries of the Corporation compete for deposits with other banks and for other sources of funds with both bank and nonbanking institutions which are not subject to the same regulatory restrictions and which have intensified the competition for funds both domestically and abroad.

Staff

A comparison of the number of people employed by the Corporation at December 31, 1985, 1984 and 1983 is included in Management's Discussion and Analysis under the caption "Other Operating Expenses" on page 29 of the Annual Report and such information is incorporated herein by reference.

Statistical Information

The following statistical information concerning the financial condition and operating performance of the Corporation is included in the Annual Report and such information is incorporated herein by reference; page numbers below correspond to page numbers in the Annual Report.

Statistical Information	Page and Caption
Distribution of Assets, Liabilities and Stockholders' Equity; Interest Rates and Interest Differential	Page: 68 Caption: "Average Balances, Interest and Average Rates - Taxable Equivalent".
The Effect of Changes in Average Balances and Average Rates on Interest Income	Page: 26 Caption: "Net Interest Income - Taxable Equivalent Basis Increase (Decrease) Due to Changes in Average Balances and Rates".
Percentage of Total Assets and Total Liabilities Attributable to Foreign Activities on the Basis of Averages	Page: 24 Caption: "Domestic and International Operations-Average Assets by Geographic Region".

Statistical Information	Page and Caption
Investment Portfolio - Book Value by Category	Page: 67 Caption: "Consolidated Summary of Assets, Liabilities and Stockholders' Equity"
Carrying Value of Consolidated Investment Securities including Maturity Distributions, Weighted Average Yields and Estimated Market Values	Page: 39 Caption: "Investment Securities at December 31".
Loan Portfolio - Types of Loans	Page: 73 Caption: "Consolidated Loan Balances by Type and Percentage Distribution".
Maturities and Sensitivities of Loans to Changes in Interest Rates	Page: 72 Caption: "Selected Loan Maturities and Sensitivity to Changes in Interest Rates".
Risk Elements	Page: 37 Caption: "Nonaccrual, Reduced Rate and Past Due Loans". Page: 34 Caption: "Country Risk - Cross-Border Outstandings Which Exceed 1% of Total Assets" and "Cross-Border Outstandings Between .75% and 1% of Total Assets".
Summary of Loan Loss Experience	Page: 71 Caption: "Consolidated Analysis of Loan Loss Experience".
Allocation of the Reserve for Possible Loan Losses	Page: 28 Caption: "Allocation of the Reserve for Possible Loan Losses".
Deposits - Types of Deposits	Page: 68 Caption: "Average Balances, Interest and Average Rates - Taxable Equivalent".
Maturity Distribution of Time Certificates of Deposit	Page: 40 Caption: "Maturity Distribution of Time Deposits of $100,000 or More".
Return on Equity and Assets	Page: 74 Caption: "Financial Ratios".
Short-Term Borrowings	Page: 41 Caption: "Selected Funds Borrowed"

Supervision and Regulation

The Company is a bank holding company within the meaning of the Bank Holding Company Act of 1956, as amended (the "Act"), and is required to file with the Board of Governors of the Federal Reserve System (the "Federal Reserve Board") an annual report and such other information as may be required pursuant to the Act. The Company is subject to the examination power of the Federal Reserve Board.

Under the Act and Regulation Y of the Federal Reserve Board, as in effect on December 31, 1985, the Company, with certain exceptions, may not acquire direct or indirect ownership or control of more than 5% of the voting shares of any bank without the prior approval of the Federal Reserve Board. The Federal Reserve Board is not authorized to approve the acquisition of any bank unless it finds that any anticompetitive effects of the proposed acquisition are clearly outweighed by the probable effect of the transaction in meeting the convenience and needs of the community to be served. The Federal Reserve Board is prohibited from approving any application by a bank holding company to acquire voting shares of any bank in another state unless such acquisition is specifically authorized by the laws of such state or unless, under certain circumstances, such bank is a "failing bank". While an increasing number of states have adopted laws authorizing certain acquisitions by out-of-state bank holding companies, few states permit unrestricted entry by bank holding companies located in New York.

Pursuant to the Act, the Company may not engage in any business other than managing and controlling banks or furnishing certain services and may not acquire voting control of nonbanking corporations except those businesses or services which the Federal Reserve Board deems to be closely related to banking. Subject to obtaining the prior approval of the Federal Reserve Board, the Company also may acquire voting control of nonbanking corporations engaged in such activities. In making any such determination, the Federal Reserve Board is required to consider whether the performance of such activities by an affiliate of the Company can reasonably be expected to produce benefits to the public, such as greater convenience, increased competition, or gains in efficiency, that outweigh possible adverse effects, such as undue concentration of resources, decreased or unfair competition, conflicts of interest or unsound banking practices. Further, the Federal Reserve Board is empowered to differentiate between activities commenced de novo and activities commenced by acquisitions, in whole or in part, of going concerns.

The Bank, as a national banking association and member of the Federal Reserve System and Federal Deposit Insurance Corporation, is subject to supervision and regulation by the Comptroller of the Currency and the Federal Reserve Board. Such supervision and regulation includes periodic examinations of the Bank, periodic reporting requirements, limitations on the investment and other powers of the Bank and regulation of the establishment and operation of branches.

See Note 16 of Notes to Financial Statements on page 61 of the Annual Report for a description of the Bank's, Chase Lincoln's and CAB (USA's) legal

limitations pertaining to the amount of dividends that can be paid to the Company and the extent to which the Bank can finance or otherwise supply funds to its affiliates.

The Company, the Bank and their affiliates are also subject to restrictions with respect to issuing, floating and underwriting, or publicly selling or distributing, securities in the United States.

Regulations implementing the International Lending Supervision Act of 1983 ("ILSA") require federal banking agencies to jointly determine when and to what extent banking institutions are to establish and maintain special reserves against certain foreign loans or other foreign assets. Reserves are required whenever, in the judgement of the federal banking agencies, the quality of these loans or assets has been impaired by protracted inability of public or private borrowers in a foreign country to make payments on their external indebtedness or no definite prospects exist for orderly restoration of debt service. Such reserves are to be charged against current income and will not be considered as part of capital and surplus or allowances for possible loan losses for regulatory, supervisory, or disclosure purposes. In addition, no banking institution is allowed to charge, in connection with the restructuring of an international loan, any fee exceeding the administrative cost of restructuring unless it amortizes such fee over the effective life of the loan.

ILSA also directed the federal banking agencies to establish minimum levels of capital for banking institutions. (Capital requirements of bank regulators are discussed on pages 30 and 31 of Exhibit 13, under the caption "Capital Management."). Under regulations of the Board of Governors of the Federal Reserve System, the minimum acceptable ratio of total capital to total gross assets for multinational bank holding companies, such as the Corporation, is 6% and the minimum ratio of total primary capital to total gross assets has been established at 5.1/2%.

Effect of Government Policies.

The earnings of the Corporation are significantly influenced by fluctuations in economic activity, the general price level and relative prices throughout the world economy. In addition, fiscal and other policies adopted by the United States and foreign governments can have important consequences on the financial performance of the Corporation. In particular, the actions and policies of the Federal Reserve Board and foreign central banks exert a major influence on interest rates, credit conditions, exchange rates and asset prices. Recognizing the inherent difficulties of forecasting government behavior and asset prices, the Corporation endeavors to accurately assess and manage these economic and other risks which it faces in the conduct of its business.

Item 2. Properties.

The Company's Executive Office and the Bank's Head Office are located in a sixty-story building owned in fee by the Bank at 1 Chase Manhattan Plaza, New

York, New York which represents a significant portion of the value of banking premises owned by the Bank. Of total space of approximately two million square feet in this building, approximately two-thirds is occupied by the Bank and the Company and the remainder is leased to tenants. In 1984, the Bank purchased a 350,000 sq. ft. facility in Lake Success, Long Island for use as a processing center. The Bank also owns in fee other banking premises, principally in overseas locations such as England, Puerto Rico, Germany, Panama and Brazil.

The Bank leases space occupied by many of its branch offices and facilities used in its domestic and foreign operations. Leases of premises include a lease, expiring August 31, 2000, with options to renew to the year 2030, for approximately 1 million square feet on 21 floors in a fifty-story building at 1 New York Plaza, New York, New York. The Bank has an option to purchase the ground lease and the entire building at 1 New York Plaza on various dates in the future. The Lincoln First Tower, located in Rochester, New York is the leased headquarters of Chase Lincoln.

Item 3. Legal Proceedings.

Various actions and proceedings are pending against the Company, the Bank and certain of their subsidiaries in which claims for substantial money damages are asserted. Management of the Company, after consulting with legal counsel, is of the opinion that the ultimate effect on the Corporation of all pending actions and proceedings would not be material in relation to the financial position of the Corporation. These actions and proceedings include, GHR Companies, Inc. et al.v. Continental Illinois National Bank and Trust Company of Chicago, et al., (United States Bankruptcy Court, Southern District of Texas, Houston Division, commenced December 9, 1983) which is an adversary proceeding commenced by GHR Companies, Inc. and affiliated entities ("GHR") under Chapter 11 of the Bankruptcy Code against the Bank and other lenders to GHR in which GHR alleges that the Bank wrongfully controlled and dominated GHR and its affairs and seeks the disallowance of any claim filed by the Bank in the bankruptcy proceedings within which this proceeding was commenced, equitable subordination of any such claim, avoidance of alleged fraudulent transfers and other relief. Other adversary proceedings brought by GHR against the Bank and other lenders to GHR seeking substantially the same relief are pending in the same Court: GHR Companies, Inc. et al. v. Banque Paribas, et al., (U.S. Dist. Ct., S.D.N.Y., commenced December 13, 1983) is a case against the Bank and two other lenders to GHR in which it is alleged that the Bank violated Federal antitrust laws and Federal banking laws and that the Bank wrongfully controlled and dominated GHR and its affairs. Actual damages in the amount of $1 billion are sought and punitive damages are also demanded.

Item 4. Submission of Matters to a Vote of Security Holders.

The Company did not submit any matters to a vote of security holders during the last quarter of 1985.

PART II

Item 5. Market for Registrant's Common Equity and Related Stockholder Matters.

Information setting forth the high and low sales prices of the Common Stock for each quarterly period during the past two years, the approximate number of holders of Common Stock and the amounts of dividends declared on such Common Stock during the past two years is presented in tabular form on page 75 of Exhibit 13, "Stockholder Data", and such information is incorporated herein by reference. Information setting forth restrictions on the ability to pay dividends on the Company's Common Stock is presented in Note 14: "Common Stockholders' Equity" and Note 16: "Regulatory Limitations" of the Notes to Financial Statements on page 60 and 61, respectively, of Exhibit 13, and is incorporated herein by reference.

Item 6. Selected Financial Data.

Information concerning the Corporation's selected financial data is set forth on page 23 of Exhibit 13 under the caption "Summary of Selected Financial Data" and is incorporated herein by reference.

Item 7. Management's Discussion and Analysis of Financial Condition and Results of Operations.

Management's discussion and analysis of the Corporation's financial condition, results of operations and changes therein, is set forth on pages 22 through 41 of Exhibit 13, and is incorporated herein by reference.

Item 8. Financial Statements and Supplementary Data.

The consolidated statement of condition of The Chase Manhattan Corporation and Subsidiaries, at December 31, 1985 and 1984 as well as the related balance sheet of The Chase Manhattan Corporation (Company Only) at December 31, 1985 and 1984 and the related statements of income, changes in common stockholders' equity and changes in financial position for each of the years in the three year period ended December 31, 1985, together with the related notes and the report of Price Waterhouse, independent public accountants, thereon, contained on pages 44 through 50 and 55 through 65 of Exhibit 13, are incorporated herein by reference. Information related to the impact of inflation and changing prices on the Corporation's consolidated financial statements is contained on page 79 of Exhibit 13, under the caption "Financial Reporting and Analysis of the Effects of Changing Prices", and such information is incorporated herein by reference. Quarterly financial information for the two years ended December 31, 1985 is set forth on page 70 of Exhibit 13, and such information is incorporated herein by reference.

Item 9. Disagreements on Accounting and Financial Disclosure.

The Company has nothing to report under this item.

Part III

Item 10. Directors and Executive Officers of the Registrant.

The information called for by this item is set forth in the Proxy Statement of the Company for its 1986 Annual Meeting under the caption "Election of Directors", and such information is incorporated herein by reference. See also the information set forth below, which information, in accordance with the instructions to Item 401(b) of Regulation S-K, shall be deemed to be a portion of Part I of this Report on Form 10-K.

Executive Officers of the Company

The following is a list as of March 1, 1986 showing the names and ages of all principal executive officers of the Company and the position or office with the Company held by each of them and the date from which said office has been continuously held. There are no family relationships between any of the principal executive officers or directors. Under the By-Laws, the Chairman of the Board, the President and the Vice Chairmen of the Board hold office until the next annual organization meeting of the Board. All other officers hold office at the pleasure of the Board.

Name	Age	Position and Offices Held and Date from which Held
Willard C. Butcher	59	Chairman of the Board - April 21, 1981, Chief Executive Officer - January 1, 1980 and Director - January 19, 1972
Thomas G. Labrecque	47	President - April 21, 1981, Chief Operating Officer and Director - June 25, 1980
[illegible] t.R. Douglass	54	Vice Chairman of the Board - July 1, 1985 and Director
Arthur F. Ryan	43	Vice Chairman of the Board - July 1, 1985 and Director
Anthony P. Terracciano	47	Vice Chairman of the Board - July 1, 1985 and Director

Name	Age	Position and Offices Held and Date from which Held
A. Edward Allinson	51	Executive Vice President - April 1, 1983
James W. Bergford	59	Executive Vice President - February 17, 1971
Donald L. Boudreau	45	Executive Vice President - December 1, 1984
Richard J. Boyle	42	Executive Vice President - April 1, 1984
A. Wright Elliott	50	Executive Vice President - April 1, 1983
Michael P. Esposito, Jr.	46	Executive Vice President - April 1, 1983 and Controller - February 1, 1976
Joseph J. Harkins	54	Executive Vice President - January 1, 1986
Robert M. Lichten	45	Executive Vice President - December 1, 1984
Wolfgang Schoellkopf	53	Executive Vice President - October 1, 1980
L. Edward Shaw, Jr.	41	Executive Vice President - January 1, 1986 and General Counsel - February 1, 1983
Francis X. Stankard	54	Executive Vice President - December 18, 1974
Michael Urkowitz	42	Executive Vice President - December 1, 1984
Paul T. Walker	50	Executive Vice President - July 1, 1985

Except as noted below, each officer (i) has as his principal occupation the corresponding office with the principal subsidiary of the Company, the Bank, and (ii) for more than the last five years has been employed in such principal occupation or in other executive positions with the Bank, or other subsidiaries of the Company.

Mr. Shaw has served as General Counsel of the Company and the Bank since February 1, 1983. Since 1977, Mr. Shaw had been a member of the firm Milbank, Tweed, Hadley & McCloy, attorneys.Item 11. Management Remuneration.

Information in response to this item is set forth in the Proxy Statement of the Company for its 1986 Annual Meeting under the captions "Election of Directors", "Executive Compensation", "The Retirement Plan", "1978 Non-Qualified Stock Option Plan", "1982 Long-Term Incentive Plan", "The Thrift-Incentive Plan", "Other Incentive Plans", and "Transactions with Management and Others", and such information is incorporated herein by reference.

Item 12. Security Ownership of Certain Beneficial Owners and Management.

Information concerning beneficial ownership of equity securities of the Company by management is set forth under the caption "Stock Ownership" in the Proxy Statement of the Company for its 1986 Annual Meeting and such information is incorporated herein by reference.

Item 13. Certain Relationships and Related Transactions.

Information in response to this item is set forth in the Proxy Statement of the Company for its 1986 Annual Meeting under the caption "Transactions with Management and Others", and such information is incorporated herein by reference.

PART IV

Item 14. Exhibits, Financial Statement Schedules, and Reports on Form 8-K.

(a) (1) Financial statements have been included in Item 8 above.

(b) The Company filed a report on Form 8-K during the quarter ended December 31, 1985.

Date of Report	Items Reported
October 14, 1985	News release announcing the Corporation's earnings for the quarter ended September 30, 1985.

(c) The following exhibits are filed as a part of this report:

		Location in this Form 10-K
Exhibit 3A -	Restated Certificate of Incorporation of the Company (including certificates of designation, preferences and rights of series of Preferred Stock).	p. 17

		Location in this Form 10-K
Exhibit 3B -	Certificates of Change of Address of Registered Office and of Registered Agent.	p. 112
Exhibit 3C -	By-Laws of the Company.	p. 115
Exhibit 10A -	The Chase Manhattan 1982 Long-Term Incentive Plan.	p. 123
Exhibit 10B -	1978 Non-Qualified Stock Option Plan.	p. 138
Exhibit 10C -	Chase Manhattan Management Incentive Plan.	p. 154
Exhibit 10D -	Form of Director's Fee Deferral Agreement	p. 156
Exhibit 10E -	Supplemental Retirement Plan of The Chase Manhattan Bank, N.A.	p. 165
Exhibit 10F -	Supplement Benefit Plan of The Chase Manhattan Bank, N.A.	p. 167
Exhibit 10G -	Chase Lincoln First Bank, N.A. 1982 Incentive Stock Plan.	p. 169
Exhibit 11 -	Computation of Earnings Per Common Share.	p. 187
Exhibit 13 -	The Chase Manhattan Corporation Annual Report 1985 (except as to portions expressly incorporated herein, said Annual Report is included only for the information of the Commission.	p. 188
Exhibit 22 -	Subsidiaries of the Company.	p. 276
Exhibit 24 -	Consent of Accountants.	p. 277
Exhibit 25 -	Power of Attorney.	p. 278

Neither the Company nor any of its subsidiaries for which consolidated or unconsolidated financial statements are required to be filed are party to an instrument with respect to long-term debt where the securities authorized thereunder exceed 10% of the total assets of the Coporation.

In accordance with subsection (b)(4)(iii) of Item 601 of Regulation S-K, the Company hereby agrees to furnish to the Commission, on request, a copy of all instruments defining the rights of holders of long-term debt of the Company or any of its subsidiaries for which consolidated or unconsolidated financial statements must be filed.

All schedules normally required by Form 10-K are omitted because they are either not applicable, the data is not significant or the required information is set forth in the financial statements or in the notes related thereto.

Alexander D. Hargrave, William T. Coleman, Jr., Joan Ganz Cooney, Robert E. Flowerree, Howard C. Kauffmann, David T. Kearns, Richard W. Lyman, John D. Macomber, John H. McArthur, David T. McLaughlin, James E. Olson, Eliuni T. Pratt, Jr., Henry B. Schacht, Richard R. Shinn, Donald H. Trautlein, Ralph E. Ward	Directors	March 19, 1936

By: Michael P. Carlson
Attorney-in-Fact

Michael P. Esposito, Jr.
(Michael P. Esposito, Jr.)

Executive Vice President and Controller (Principal Financial Officer and Principal Accounting Officer) — March 19, 1986

Signatures

Pursuant to the requirements of the Securities Exchange Act of 1934, the Bank has duly caused this annual report to be signed on its behalf by the undersigned, thereunto duly authorized.

THE CHASE MANHATTAN BANK, N.A.
(Name of Bank)

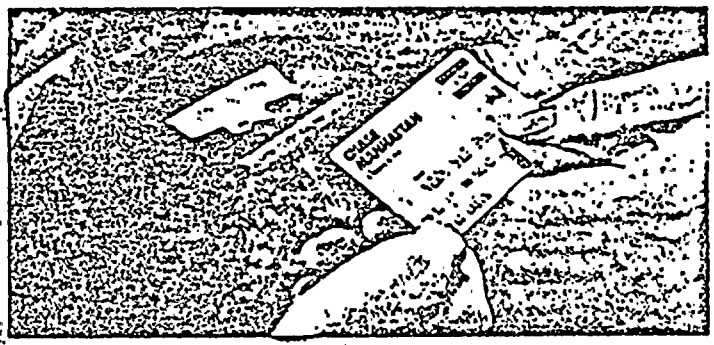
By _____
(Michael P. Esposito, Jr.)
(Executive Vice President and Controller)

March 19, 1986

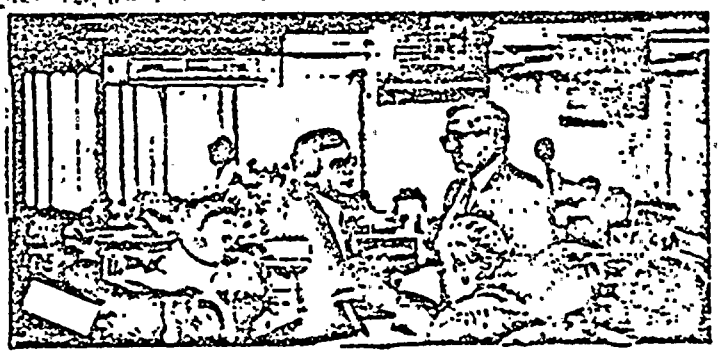
Pursuant to the requirements of the Securities Exchange Act of 1934, this report has been signed below by the following persons on behalf of the Bank and in the capacities and on the dates indicated.

Signature	Capacity	Date
_____ (Willard C. Butcher)	Director, Chairman of the Board (Principal Executive Officer)	March 19, 1986
_____ (Thomas G. Labrecque)	Director	
_____ (Robert R. Douglass)	Director	
_____ (Arthur F. Ryan)	Director	
_____ (Anthony P. Terracciano)	Director	

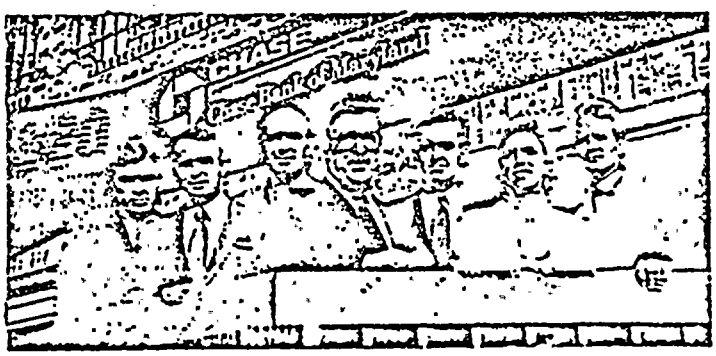
Consumer Banking

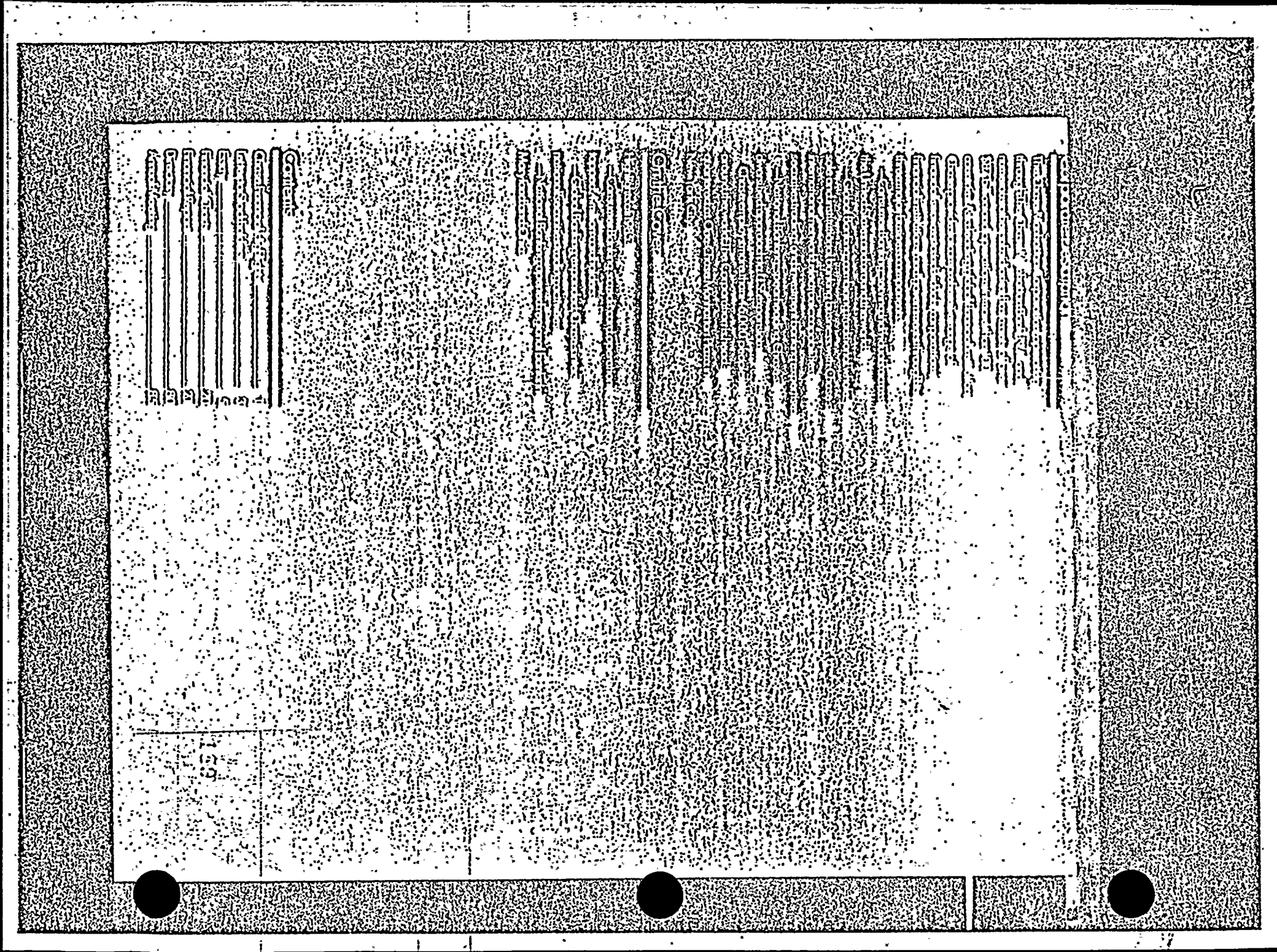


Global Banking



National Banking

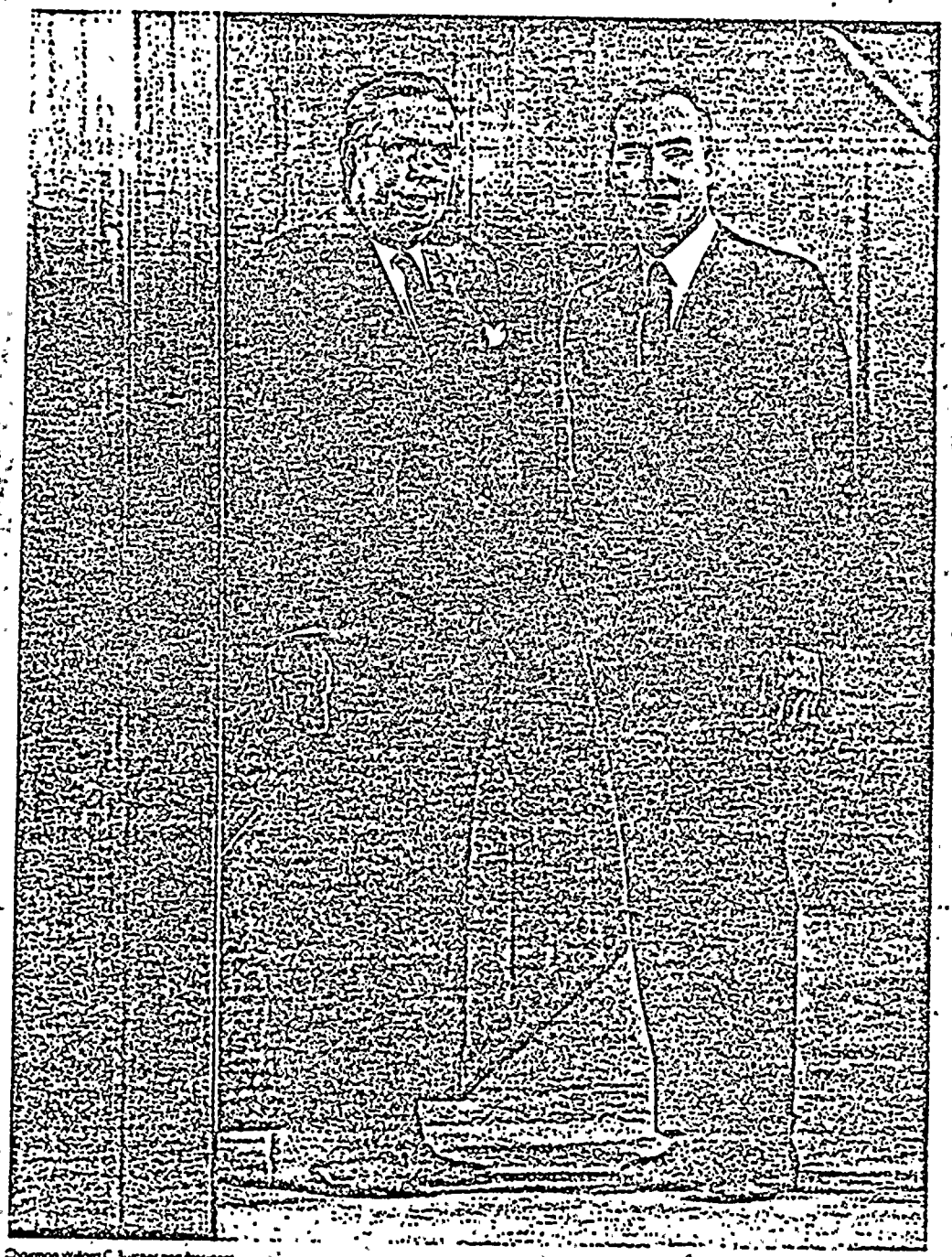




Chase Financial Highlights

	1985	1984	1983	Percentage Increase-Decrease 1985 vs. 1984	1984 vs. 1983
For the Year ($ in thousands)					
Net Interest Income	$2,748,730	$2,308,491	$2,169,055	19%	6%
Provision for Possible Loan Losses	435,000	365,000	285,000	19	28
Other Operating Income	1,315,731	929,584	864,211	42	8
Other Operating Expenses	2,731,878	2,244,526	2,045,561	22	10
Net Income	564,818	405,818	429,607	39	(6)
Per Common Share*					
Primary Earnings	$ 6.39	$ 4.51	$ 5.48	42%	(18)%
Fully Diluted Earnings	6.15	4.32	5.22	42	(17)
Cash Dividends Declared, Annually	1.90	1.82½	1.75	4	4
Cash Dividends Declared, Quarterly	.47½	.45½	.43¾	4	4
Common Stockholders' Equity at Year-end	49.19	45.81	43.91	7	4
Market Value at Year-end	36.31⅛	23.87½	22.75	52	5
Average Shares Outstanding (in thousands)	75,240	71,153	68,748	6	3
Financial Ratios					
Net Income as a Percentage of:					
Average Total Assets	.65%	.48%	.54%	35%	(11)%
Average Common Stockholders' Equity	13.6	10.1	13.1	35	(23)
Cash Dividends Paid on Common Stock as a Percentage of Net Income Applicable to Common Stock	29.6	40.3	31.9	(27)	26
At Year-end ($ in millions)					
Interest-Bearing Deposits Placed with Banks	$ 4,671	$ 4,355	$ 8,659	7%	(50)%
Investment Securities and Trading Account Assets	7,467	6,600	3,698	13	78
Loans	61,931	62,003	55,894	—	11
Reserve for Possible Loan Losses	908	761	564	19	35
Total Assets	87,685	86,883	81,921	1	6
Deposits	61,353	59,680	56,300	3	6
Long-Term Notes and Debentures	2,806	2,320	1,376	21	69
Redeemable Preferred Stock	62	62	150	—	(59)
Nonredeemable Preferred Stock	602	602	375	—	61
Common Stockholders' Equity	3,795	3,359	3,051	13	10
Capital Ratios at Year-end					
Primary Capital as a Percentage of Total Gross Assets	6.9%	6.4%	5.4%	8%	19%
Total Capital as a Percentage of Total Gross Assets	9.2	8.1	6.7	14	21

*Amounts restated to reflect two-for-one stock split declared January 15, 1986.



Chairman Willard C. Butcher and President
Thomas G. Labrecque

Letter to Stockholders

To Our Stockholders:

1985—a year of substantial progress.

That is the way we would characterize the performance of The Chase Manhattan Corporation last year. Importantly, this progress resulted from solid achievement in each major banking group.

In light of our earnings, the Board of Directors in January 1986 increased the regular quarterly cash dividend to $1.025 per share. At the same time, principally in response to the increase in the market price of our common stock, the Board declared a 2-for-1 split of the common stock in the form of a 100% stock dividend.

In 1985, the Corporation earned $565 million, up 39% from the $406 million earned in 1984. This translated into per common share earnings, after the stock split, of $6.39, up from the $4.51 earned in 1984. Both total and per common share earnings were records for the Corporation.

The year's financial highlights included:

—Return on average assets for the year was .65%, compared with .48% a year earlier.

—Return on average common stockholders' equity for the year was 13.6%, up from 10.1% in 1984.

—Net interest income on a taxable equivalent basis was almost $3 billion, up from $2.5 billion a year earlier.

—Operating income, including fees from products and services, foreign exchange trading income, and gains on the sale of investment securities, increased to $1.3 billion, up from the $930 million earned in 1984.

—Primary capital, as defined by the Federal Reserve Board, increased to $6 billion. At year-end, our primary capital to gross assets ratio stood at 6.87%, up from 6.37% at year-end 1984.

—Total capital increased to $8 billion. At year-end, our total capital to gross assets ratio stood at 9.23%, up from 8.11% at year-end 1984.

Business Highlights

As we indicated, the most encouraging aspect of our financial performance was that it resulted from solid earnings improvement in each of our three major banking groups—Consumer Banking, Global Banking, and National Banking. This year's annual report more fully describes our accomplishments in these three core businesses.

—In Consumer Banking, under Arthur F. Ryan, we expanded significantly our penetration of the profitable U.S. credit card market. We introduced a Chase MasterCard to complement Chase VISA, and at year-end, Chase ranked as the third largest bank credit card issuer in the United States.

Internationally, we launched a major initiative to expand our consumer banking business. We purchased Bank of America's credit card operation in Panama, for example, giving Chase the dominant share of that important consumer market. In Asia, we established a stand-alone Chase credit card operation in Hong Kong. And in Europe, we started up a consumer finance business in Italy.

The year was also a most successful one for our mortgage banking subsidiary, Chase Home Mortgage Corporation, and our consumer finance operation. Both units turned in profitable performances as they increased their roles in the nationwide consumer lending market.

You may recall that several years ago we set out to build, de novo, a substantial consumer finance business. We are pleased that this business has become profitable, and we plan to continue to develop this increasingly valuable asset.

—In Global Banking, under Anthony P. Terracciano, we modified our structure to further integrate our wholesale banking resources and expand our investment banking emphasis around the world.

By combining our securities trading operation with our corporate finance, international, corporate, and institutional businesses, we believe we have created a formidable and unique worldwide wholesale bank. In 1985, investment banking activities represented a major competitive strength and a significant source of profit growth.

At the same time, we enhanced our international network by opening our Chase AMP Bank Ltd. in Australia, in which we have a 50% interest with that nation's largest insurance company. Chase also purchased the Banco de Finanzas in Spain to develop Chase's presence in the consumer and capital markets in that important nation.

—In National Banking, under Robert R. Douglass, we acquired nine troubled savings and loan associations in Ohio and Maryland and converted them to full-service commercial banks, Chase Bank of Ohio and Chase Bank of Maryland.

Also during the year we agreed to acquire Continental Bank of Arizona, a high-quality institu-

tion with assets of $500 million. And in February 1986, we opened Chase Bank of Florida, becoming the first money center bank with a full-service commercial bank in the desirable Florida market.

We have launched this nationwide expansion effort despite continued Congressional foot-dragging on the interstate banking issue. Fortunately, the nation's forward-looking states have begun to open their borders to out-of-state bank holding companies. Chase has thus been able to advance—albeit slowly—toward our goal of creating a nationwide commercial banking franchise.

In the area of leasing, where we have become a leading vendor leasing bank, we increased our role in new and used aircraft and small-ticket leasing—also through acquisitions during the year.

Board of Directors

We welcomed four new members to Chase's Board of Directors during 1985. In April, H. Laurance Fuller, president of Amoco Corporation, joined the Board. In June, Messrs. Douglass, Ryan, and Terracciano were elected vice chairmen of the Board.

Also in June, John A. Hooper retired as vice chairman of the Board and Chase's credit policy executive. Jack Hooper contributed enormously to Chase's success during 37 years of service, and we are indebted to him.

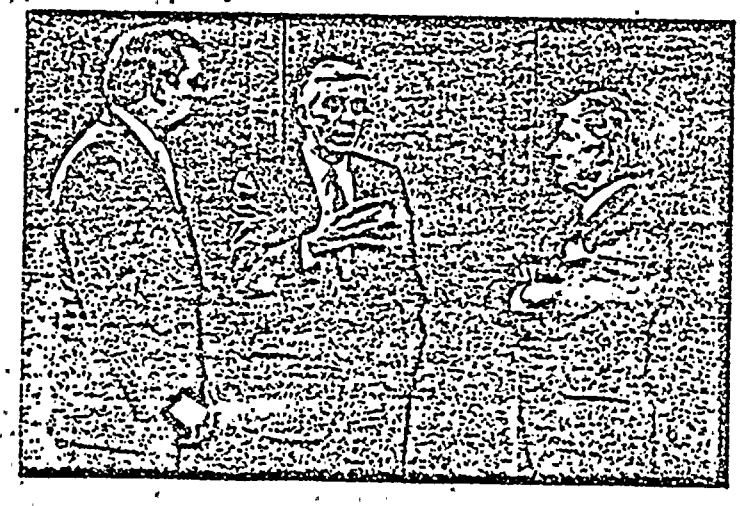
We also accepted the resignations of Philip Caldwell, who resigned after three years as a Board member to become senior managing director of Shearson, Lehman Brothers, and S. Bruce Smart, Jr., who resigned after nine years of service to Chase to become Under Secretary for International Trade for the U.S. Department of Commerce. We sincerely appreciate the efforts in behalf of Chase of both individuals and wish them well in their new roles.

The Challenge Ahead

Looking forward, 1986 promises to be a year of continuing challenge for The Chase Manhattan Corporation. Although we expect modest economic growth to continue in the United States and in much of the world, the impact of a disinflationary environment will continue to have both positive and negative effects on the world's economic structure. We believe Chase is in a particularly strong position today to deal with such an environment.

In this regard, we have placed considerable emphasis on and resources against the challenge of improving the quality of our lending portfolio—both the wholesale and consumer components. This is an important, continuing challenge for us in 1986. At the same time, we will continue to invest this year in the areas of our future growth—investment banking, electronic banking, domestic and international consumer banking, national expansion, and the like—and ensure that these investments help sustain ambitious growth into the 1990s.

The substantial progress that Chase achieved in 1985 positions us well for 1986—a year in which we look forward to continued solid performance.



Willard C. Butcher, Chairman and Chief Executive Officer

Thomas G. Labrecque, President and Chief Operating Officer

March 3, 1986

Vice Chairmen Arthur F. Ryan, Armando Terracciano, and Robert E. Douglass

Consumer Banking

Chase's consumer business spans the globe. In 1985, Consumer Banking managed consumer lending, residential mortgage banking, and discount brokerage businesses in 50 U.S. offices; a direct mail business including credit cards, installment loans, and deposit gathering; student loan, auto, and boat financing operations; home banking services; and activities in more than 20 countries.

Customers Respond to Direct Response Banking

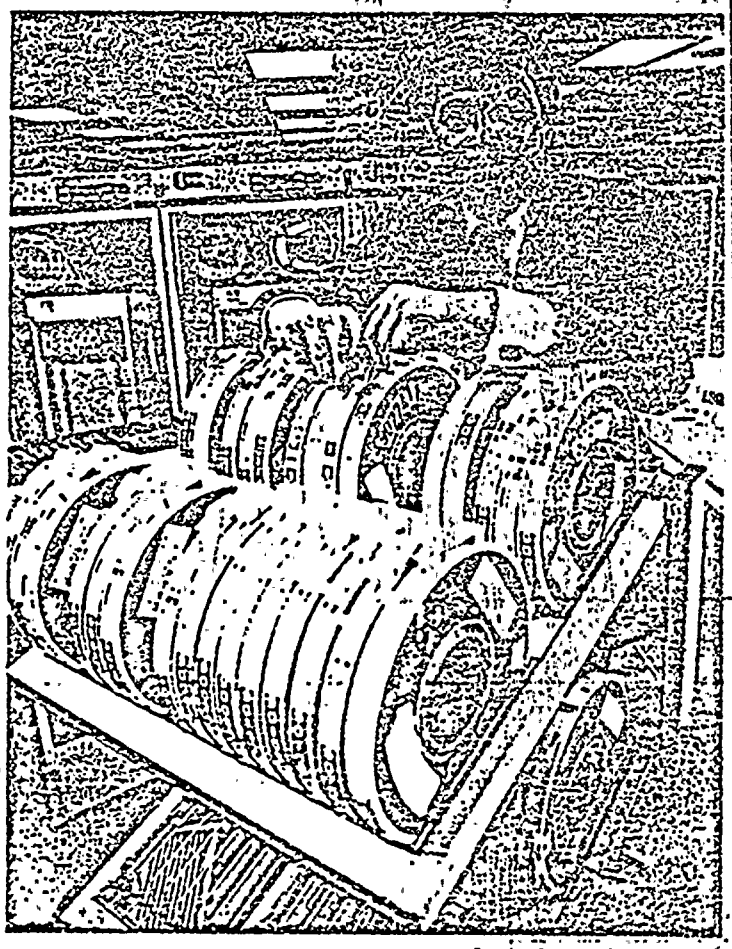
More and more consumers find that direct response banking, by mail and telephone, meets their needs for convenience and service. During 1985, Chase sent over 50 million direct mail solicitations and handled over 2 million telephone calls for its three major direct response product lines: credit cards, Chase Advantage Credit, and nationwide deposit gathering.

Among the world's leading credit card issuers, Chase aggressively expanded its business in 1985. In the United States, Chase added MasterCard to its VISA Classic and Premier World Card products. Adding over 1.5 million new cardmembers in 1985 brought total domestic credit card outstandings to more than $3 billion. Overseas, Chase launched its first foreign currency VISA card in Hong Kong; Chase AMP Ltd. introduced an Australian card; and, in January 1986, Chase acquired Bank of America's credit card portfolio in Panama.

A pioneer in adding extra benefits to save cardmembers time and money, Chase offers travel savings at hotels and motels, a computerized shopping service, and a low-cost road-and-tow service.

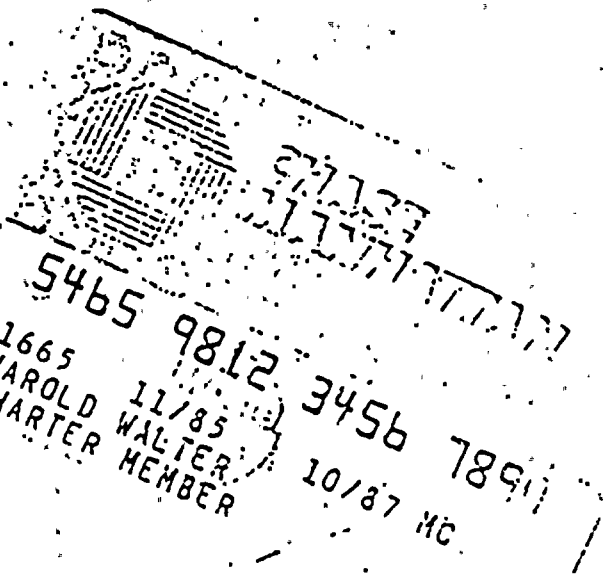
Chase Advantage Credit, a stand-alone, revolving line of credit up to $25,000, is Chase's second major direct response product. Nationwide mailings in 1985 drew over 200,000 new customers, and outstandings topped $800 million.

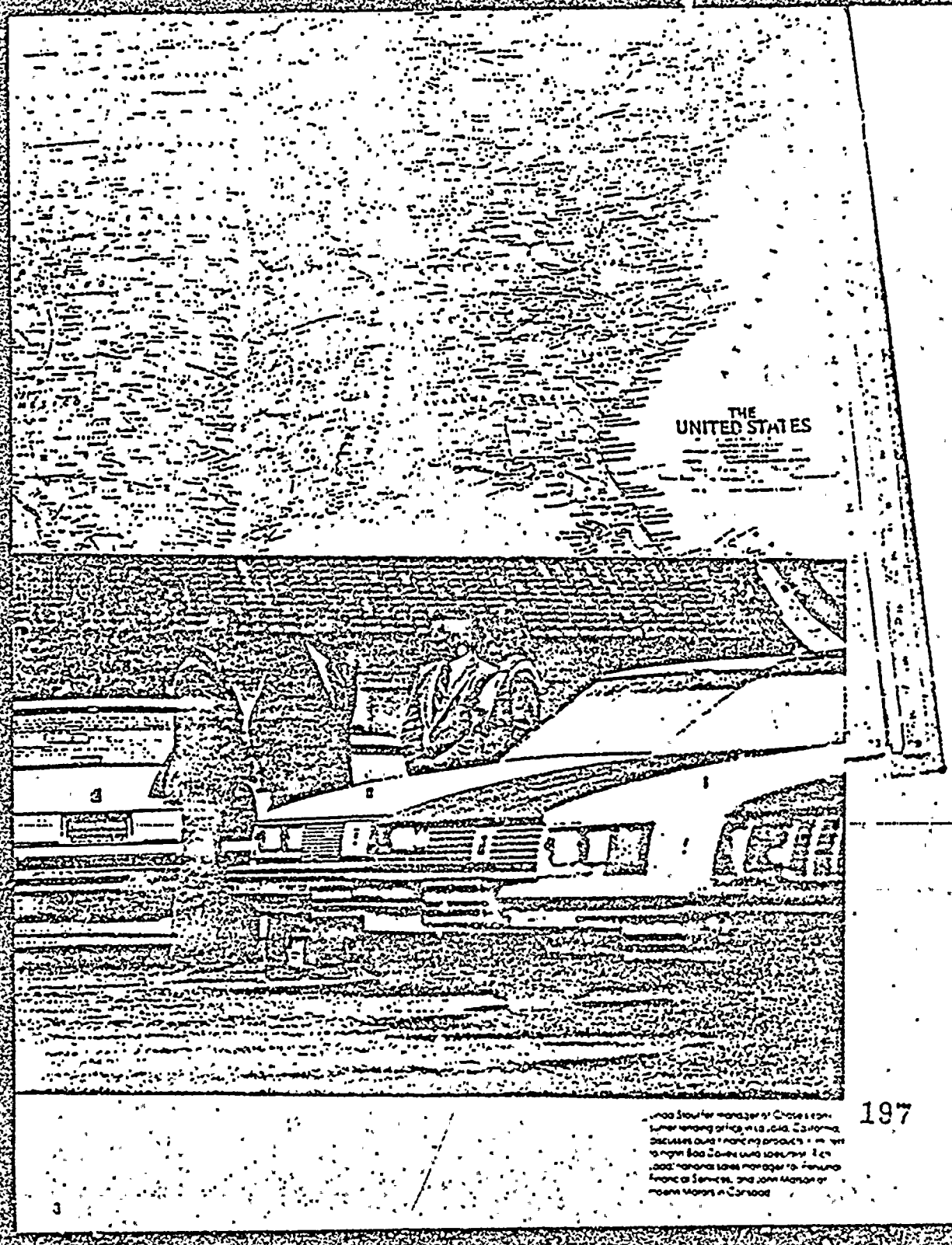
Chase also used telephone and mail to attract consumer deposits from all over the country to its Delaware subsidiary, Chase Manhattan Bank (USA). Chase (USA)'s Money Market Account offers an interest rate to consumers that outperforms the average of the top 50 U.S. commercial banks and thrifts. Last year, Chase (USA) began construction of a new Delaware headquarters facility to accommodate its growing business.



Consumer Operations Services Executive Jim Zegon visits Chase's Lake Success, New York, area facility. Almost three-quarters of Consumer Banking jobs are operations related.

Chase is the most largest issuer of bank credit cards in the United States





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Chase Home Mortgage President Fred Kapp visits with New Jersey homeowners.

Student Loan Executive Deborah Tobol visits with New York University Director of Financial Aid Ollie Bryant at NYU's Bobst Library.

Financing Consumer Needs: Shelter, Education, Transportation

From New York to San Diego, from Boca Raton to Minneapolis, Chase tailors consumer financial services to local markets, helping people meet their needs for shelter, education, transportation, and investment through its consumer products companies.

Chase Home Mortgage Corporation (CHMC) originated more than $770 million in residential mortgages in 1985 through its nationwide network of 25 offices. CHMC serviced a portfolio of almost $3 billion in residential mortgages and packaged approximately 30 different kinds of mortgages for sale in the secondary market.

In 1985, the Student Loan division began offering loans to parents; new loans for undergraduate, graduate, and professional students also joined the product roster.

With 24 offices in 11 states, Personal Financial Services (PFS) provides automobile lease and loan financing, real estate loans, boat loans, and unsecured lines of credit to consumers. Loan portfolios more than doubled in many offices in 1985.

Rose & Company, Chase's discount brokerage subsidiary, acquired the accounts of New York-based Porter, Alexander & Co., Incorporated, bolstering its presence on the East Coast. Rose & Company is linked to other Chase financial services through such products as Video Broker,® the securities trading segment of Spectrum, Chase's electronic home banking system.

Business with individuals will continue to contribute an increasing share of Chase's earnings. Chase is committed through its Consumer Banking group to serving the full-service financial needs of individuals around the world.

Global Banking

Global Banking unifies, in one wholesale business, Chase's traditional corporate and institutional relationships, its rapidly growing investment banking, foreign exchange, and securities trading operations, its technology-based service products, and a worldwide distribution network.

Redefining the Wholesale Banking Business

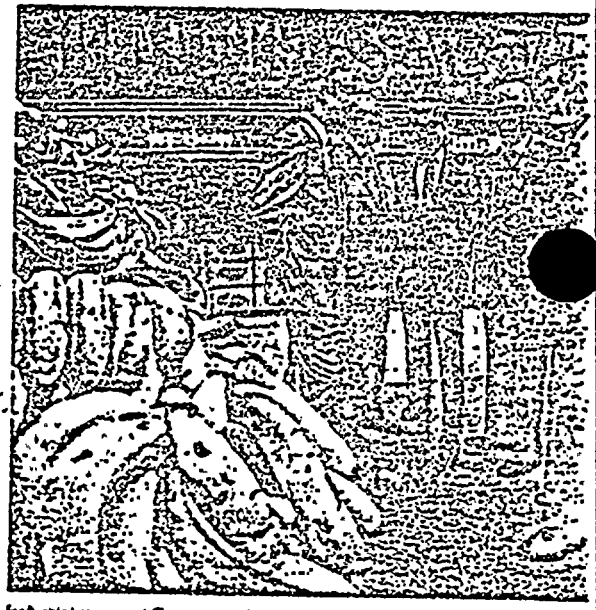
In 1985 Chase virtually redefined the wholesale banking business by marrying investment banking, commercial banking, and technology-based service products in one entity and delivering these products globally through an unrivaled worldwide network.

Broad product expertise, offices in more than 100 countries, leadership in electronic banking, and valuable long-standing relationships position Chase uniquely for the sea change occurring in the financial industry. Old distinctions between commercial and investment banking have blurred. Integrated global product delivery is the new game.

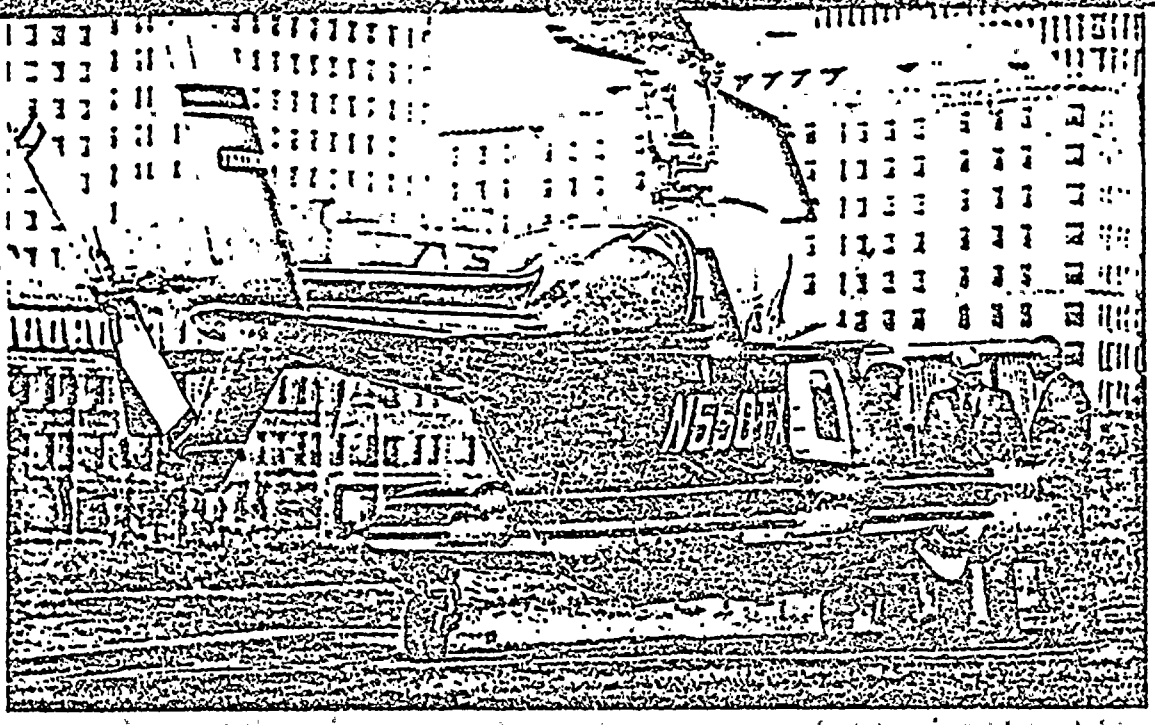
The recent sale for Textron Inc. of its Australian division, Valentine Sands Limited, exemplified Chase's distinct strengths in wholesale banking. When Textron, a U.S. customer of the Corporate Industries unit, gave Chase the mandate to sell its division, Corporate Industries marshaled the mergers and acquisitions expertise of Chase's investment banking unit in New York and the resources of Chase AMP Ltd. in Australia to close the sale.

As lead placement agent for a $220 million offering for the Puerto Rico Housing Finance Corporation, Chase brought together five distinct units in New York and Puerto Rico: the branch, the government securities trading desk in New York, the public finance team, the interest rate "swaps" area, and the investment bank in Puerto Rico.

As the lines between financial specialties fade and financial markets increasingly become more global, less than a handful of institutions possess such broad product strength and global reach. Chase is one of the few.



For Pueblo International, Chase arranged a $17 million industrial revenue bond to fund the construction of eight new supermarkets. From left: David Morrow, president of Pueblo; Harold Tapper, chairman; Ramon Cortes, Chase Manhattan Capital Markets Puerto Rico; Manuel Vallecillo, Pueblo vice chairman; and Ricardo Font, Chase Puerto Rico.



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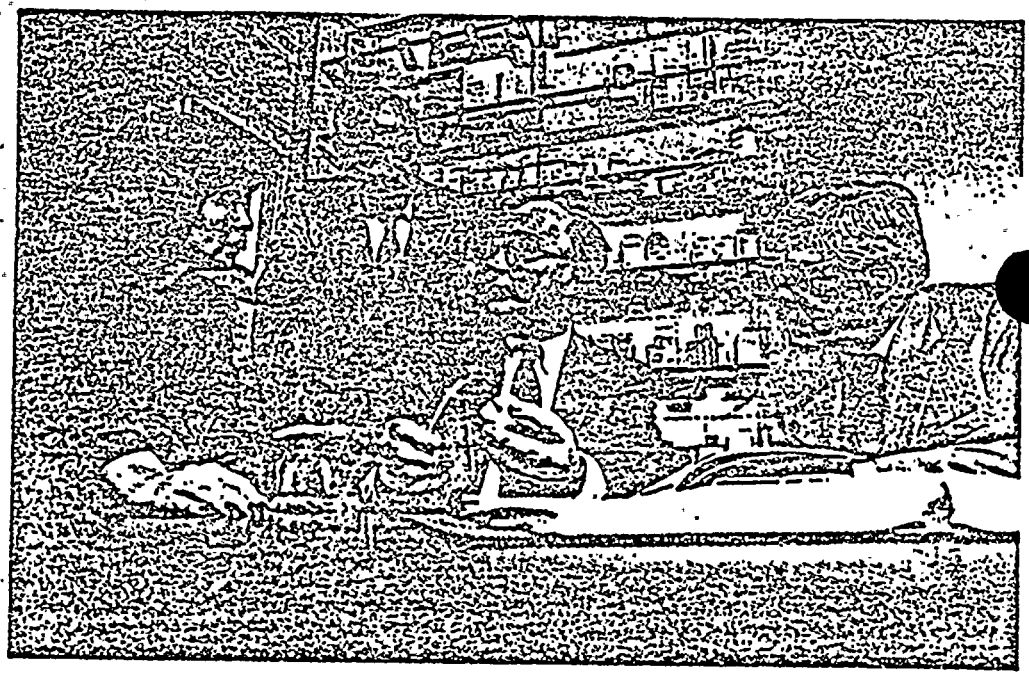
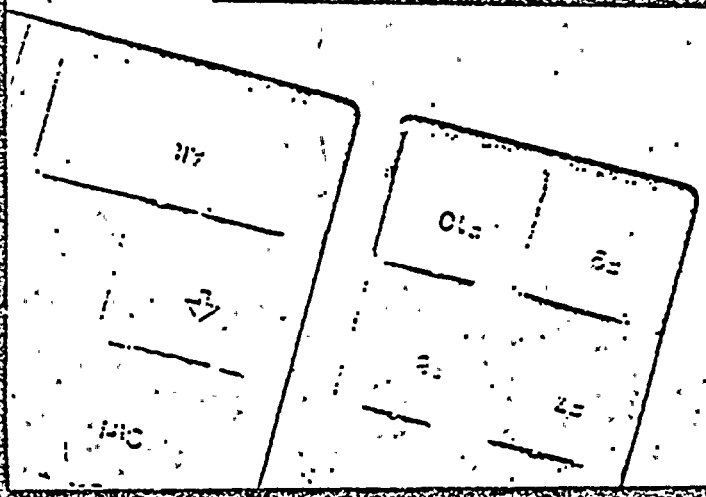
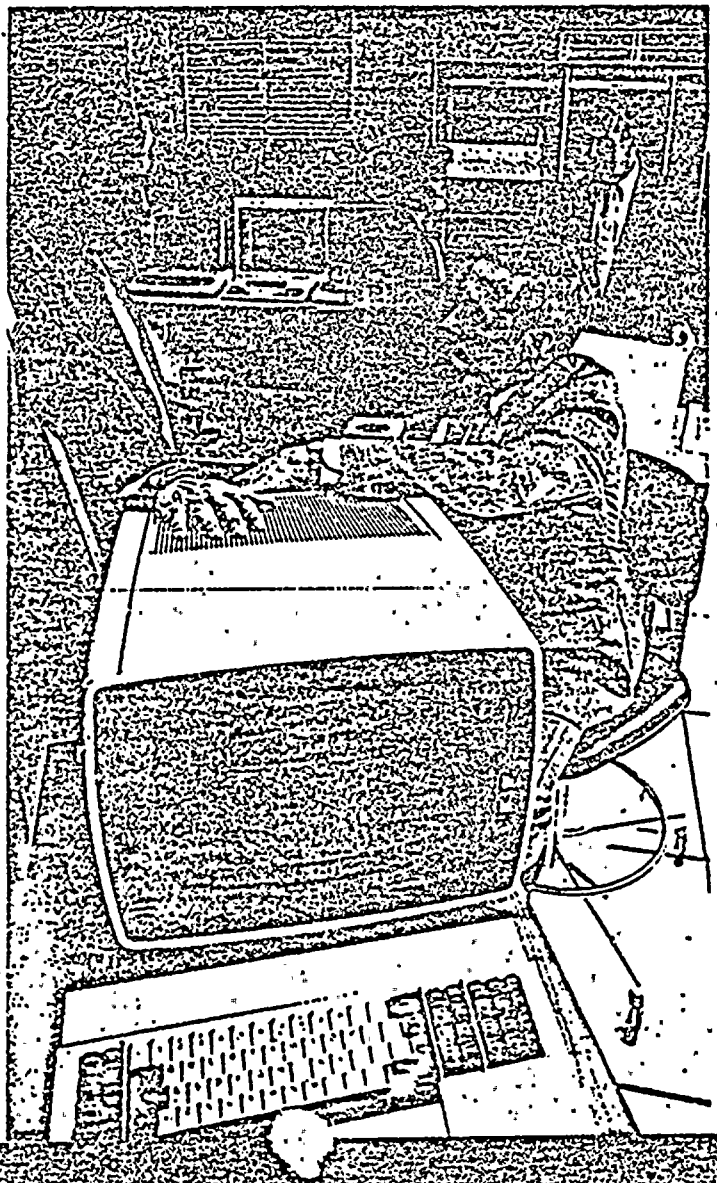


From left: Area Chairman of Corporate Industries, Pfizer Treasurer Jim Murray, Assistant Corporate Treasurer John Morrison, and Assistant Treasurer-International Paul Brady discuss international and domestic cash flows.



Chase works with Pfizer Inc. to manage Pfizer's daily cash position worldwide using the Chase InfoCash MicroSystem. Foreground: Global Electronic Banking Executive Phil Giaquinto and Pfizer Assistant Treasurer Bill Harvey. Background: Leslie Bomar, Chase cash management specialist, and Roy Liberatore, Pfizer's director of cash management.



Tapping Technology to Create New Products

Chase moved electronic banking forward in 1985 with CHESS, a unique technology-based, risk management product. The Chase Electronic Swaps System—a dual service product—typifies Chase's integration of service and investment banking products with global electronic delivery capabilities.

Chase designed the product, the first of its kind, for companies with outstanding short-term debt in excess of $200 million or with significant cash reserves. CHESS creates a global data base of interest and exchange rates that makes swaps effective for short-term hedging. Introduced in New York, Hong Kong, London, and Tokyo, CHESS makes pricing and trading possible 24 hours a day, around the world. The excellent initial response to CHESS was testimony to Chase's technological capabilities in the investment banking area.

Chase added other new products in 1985, including an electronic letter of credit and a tool to manage foreign exchange contracts, raising to more than 40 Chase's electronic treasury, trade, cash management, securities, and payments products. An electronic link between Chase and some 3,000 customers in 25 countries cuts across time zones, reduces costs, and provides information for hedging foreign exchange investments, monitoring trade agreements, and trading securities.

New electronic products like CHESS that cross traditional lines between service, transaction, and investment banking products are part and parcel of the new world of global wholesale electronic banking that Chase is helping to redefine.

Answering the Challenge of a Global Financial Marketplace

The world is rapidly becoming one electronically connected global financial marketplace. And Chase stands at the forefront of that evolution. With important trading operations in cities such as London, New York, and Tokyo, Chase is ideally positioned—able to trade many products in many markets, around the clock, around the world.

In London last year, Chase added to its securities trading capabilities with the acquisition of two stockbrokers—Laurie, Milbank & Co. and Simon & Coates. The two firms add British government securities, or "gilts," and U.K. equities to a product line that includes foreign exchange, money markets, Eurosecurities, U.S. government issues, and financial futures.

In New York, Chase's investment banking unit amplified its capabilities in mergers and acquisitions, private placements, syndications, and classic corporate finance advisory services. Last year, Chase executed more than 300 interest rate and currency exchange agreements, called "swaps," totaling $7 billion in volume.

Responding to the growing importance of the Japanese market, Chase expanded its investment banking presence in Tokyo. In 1985, Chase arranged more than $1 billion in private placements with Japanese financial institutions.

Fourteen securities trading centers and 15 investment banking locations in Asia, Europe, and North and South America enhance Chase's power to place securities and to deliver investment banking services from private placements to futures.

Chase's growing investment banking and securities trading capabilities linked by state-of-the-art technology position Chase to face the challenge of a global marketplace with financial strength, professional confidence, and the commitment to be a major force in all key markets and products.

Walt Schoellkopf, trading and Securities executive, and Ron Reading, head of U.K. and Eurosecurities, on the trading floor at One Chase Manhattan Plaza.

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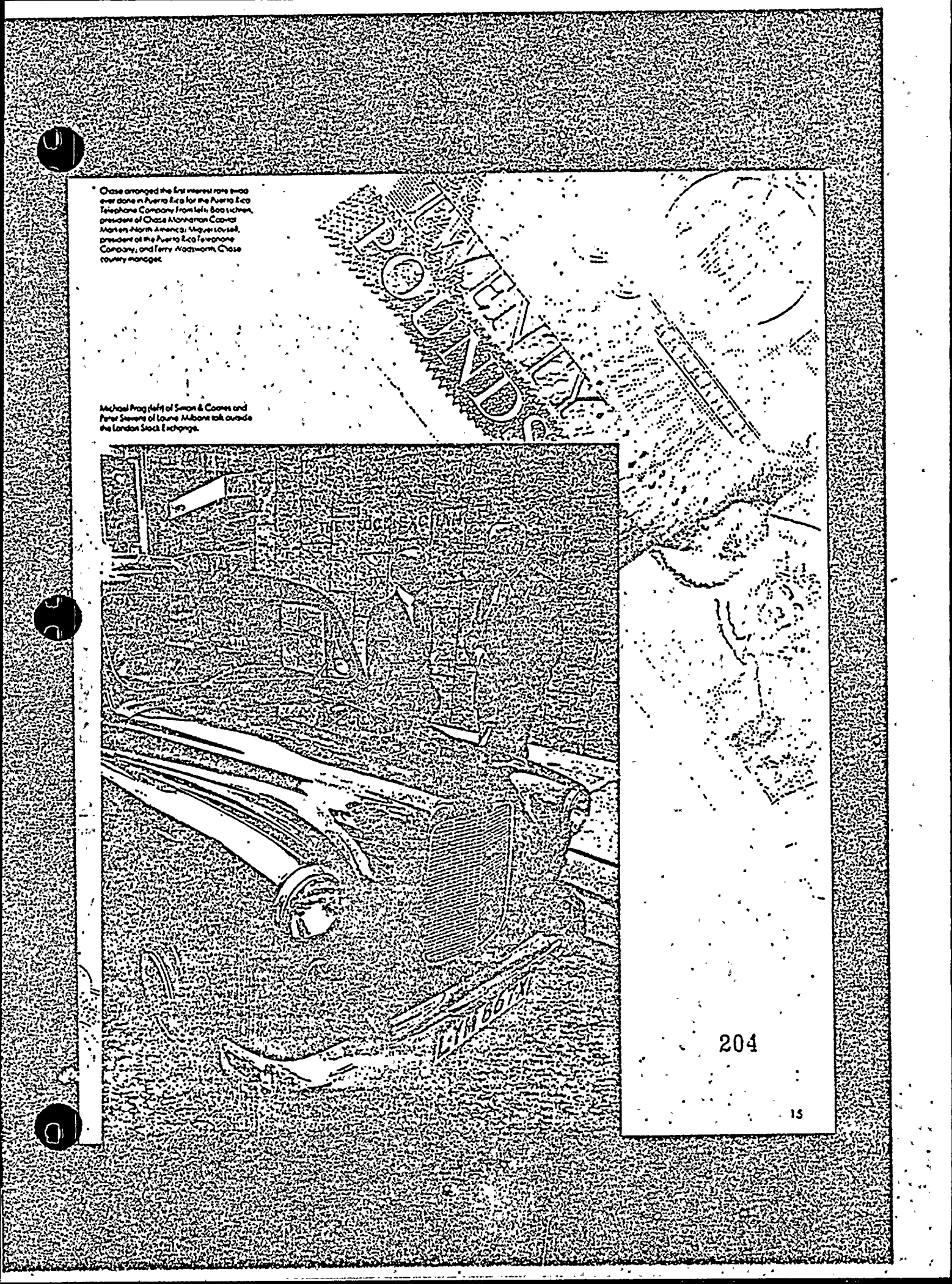
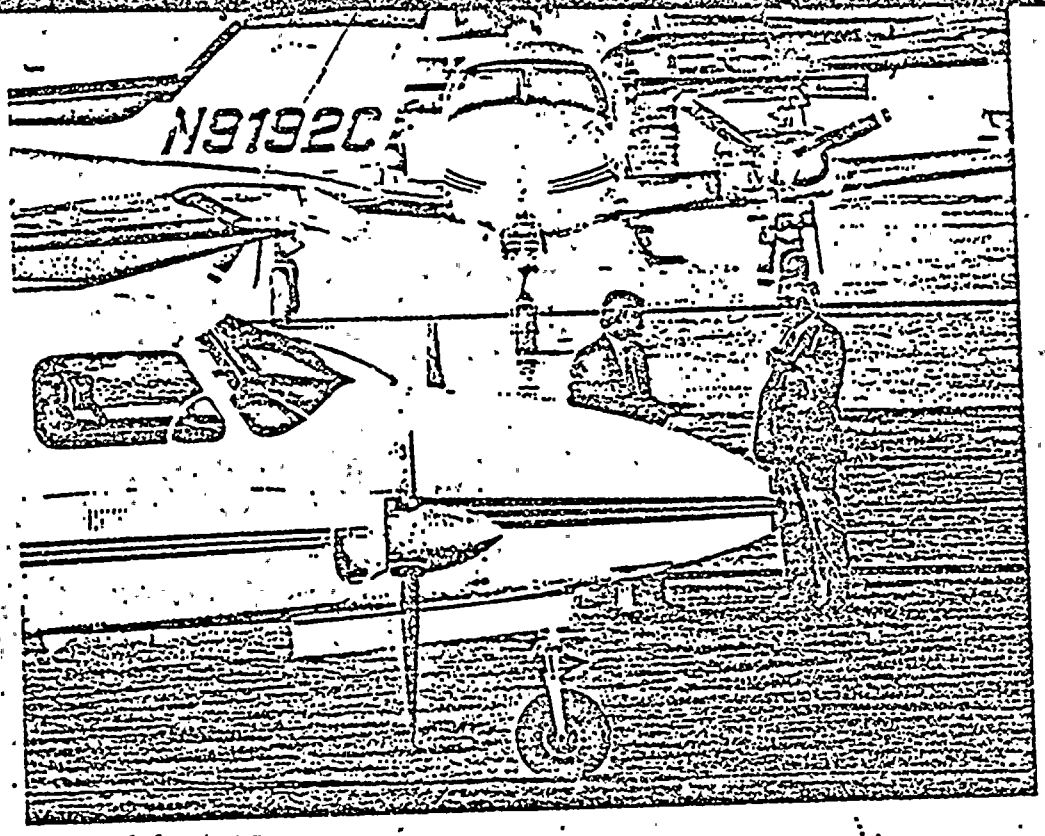


Chase arranged the first interest rate swap ever done in Puerto Rico for the Puerto Rico Telephone Company from left, Bob Lichten, president of Chase Manhattan Capital Markets-North America; Miguel Lovaid, president of the Puerto Rico Telephone Company; and Terry Wadsworth, Chase country manager.

Michael Prag (left) of Simon & Coates and Peter Stevens of Laurie Milbank talk outside the London Stock Exchange.



Don Nunemaker, CMLC special products division executive, and Tom Harvell, general manager of Chase Aircraft Finance Company, visit the company aircraft in Loveland, Florida.

Bob Jorgensen, CMLC vendor leasing division executive right, with Cig ar Equipment Corporation facility in Marlboro, Massachusetts, with Jay Schmidt, DEC U.S. pension fund manager. DEC provides financing through CMLC to purchasers of their computer equipment.

CHASE COMMERCIAL CORPORATION
IS PLEASED TO ANNOUNCE THE ACQUISITION
OF THE ON-GOING BUSINESS AND
CERTAIN ASSETS OF

PIPER ACCEPTANCE COMPANY

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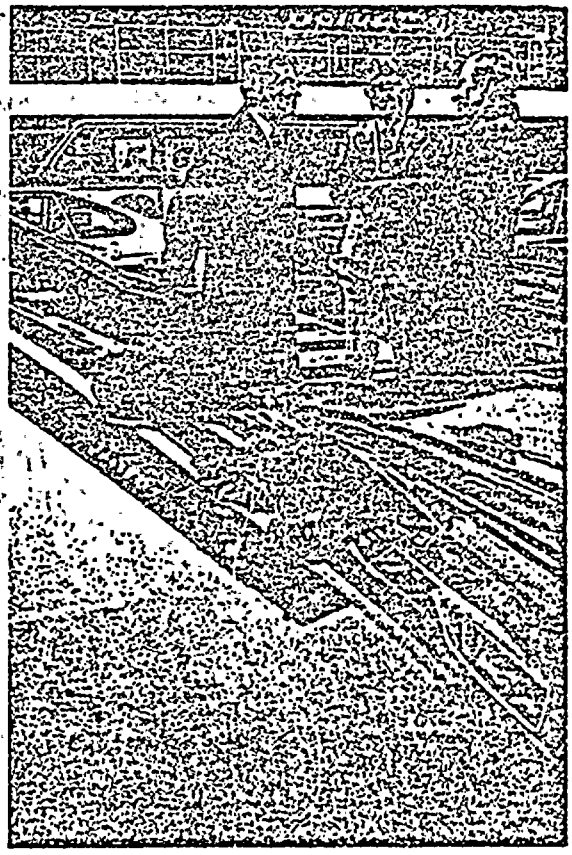
National Banking

National Banking is responsible for accelerating the development of Chase's business across the United States. The group is made up of regional banking, leasing, real estate finance, and trust, investment, and information services businesses. In 1985, Chase added regional banks in Ohio and Maryland, agreed to purchase a bank in Arizona, and acquired two leasing businesses.

CMLC provides specialized financing services to corporate clients including The Hertz Corporation. From left: Hertz Treasurer Dana Brady, CMLC Marketing Officer Peggie Smith, and CMLC President Theodore L. Dziedzic.



Leasing Looks to New Markets

Leasing is an expanding business for Chase and one of the Corporation's targets for strategic investment in 1985. Chase Manhattan Leasing Company (CMLC) entered new markets and broadened its range of leasing services through two acquisitions last year.

Building on its already strong position in vendor leasing, CMLC acquired certain assets and the ongoing business of Piper Acceptance Corporation. The Aircraft Finance Group, created as a result of this acquisition, provides both a private label vendor program for Piper Aircraft Corporation and direct financing for new and used general aviation aircraft of other manufacturers and dealers around the country.

Third Century Leasing, a high-volume supplier of small-ticket leases, was acquired by CMLC in February 1986, moving Chase into yet another specialty leasing niche. Third Century uses cost-effective telemarketing to sell its leasing services to over 500 dealers and distributors of office equipment located throughout the United States.

Formed in 1974 to serve Chase's major manufacturing customers, CMLC in just 11 years has grown to 400 people servicing more than 100,000 individual lease customers from offices in 12 U.S. cities. Last year alone, the company funded more than $900 million in new equipment lease business; at year-end, outstandings totaled approximately $1.5 billion.

Leasing will continue to be an attractive financing vehicle for quality companies in many industries. Looking ahead, CMLC will continue to enter new leasing markets while expanding its existing business.

Regional Banks Break New Ground

Five giant steps have moved Chase closer to its goal of establishing a nationwide commercial banking network. Chase Bank of Ohio, a full-service commercial bank, opened for business in June. In November, Chase formed a second out-of-state bank, Chase Bank of Maryland. Also in the fall, Chase agreed to acquire Continental Bank, Arizona's sixth largest bank.

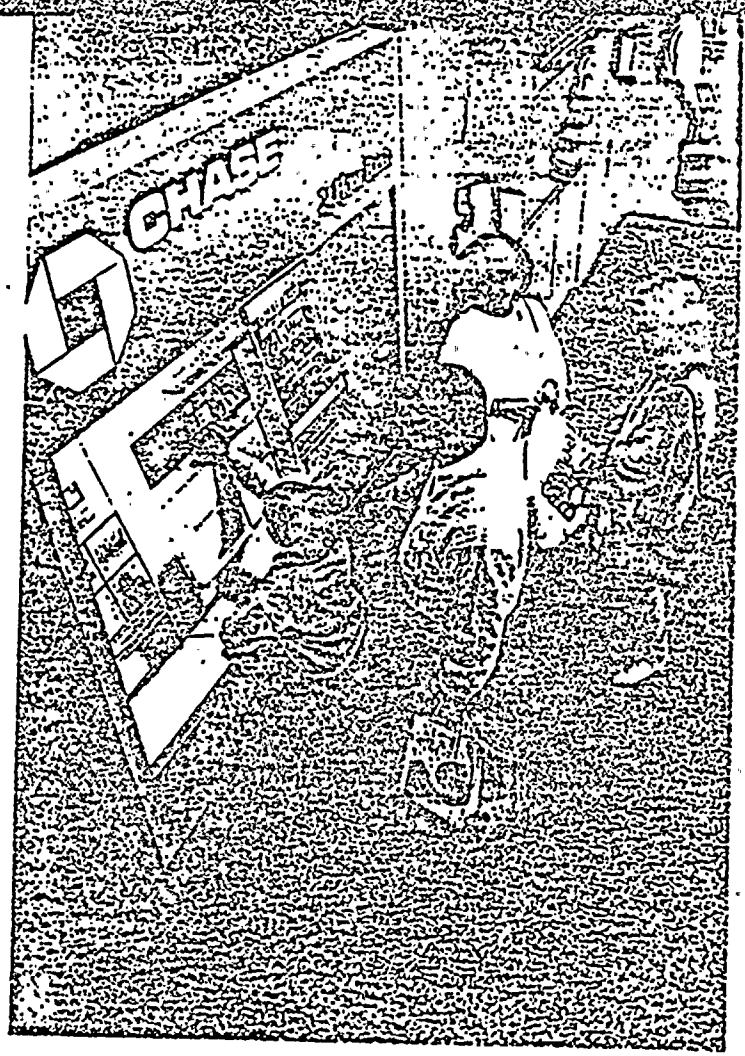
And in February 1986, Chase Bank of Florida opened its doors, the first full-service commercial bank to be established in Florida by a money center bank.

Finally, Chase brought its consumer, small business banking, and middle market businesses together in the metropolitan New York market. The new organization means that commercial banking teams can meet both the business and personal banking needs of local companies and their employees.

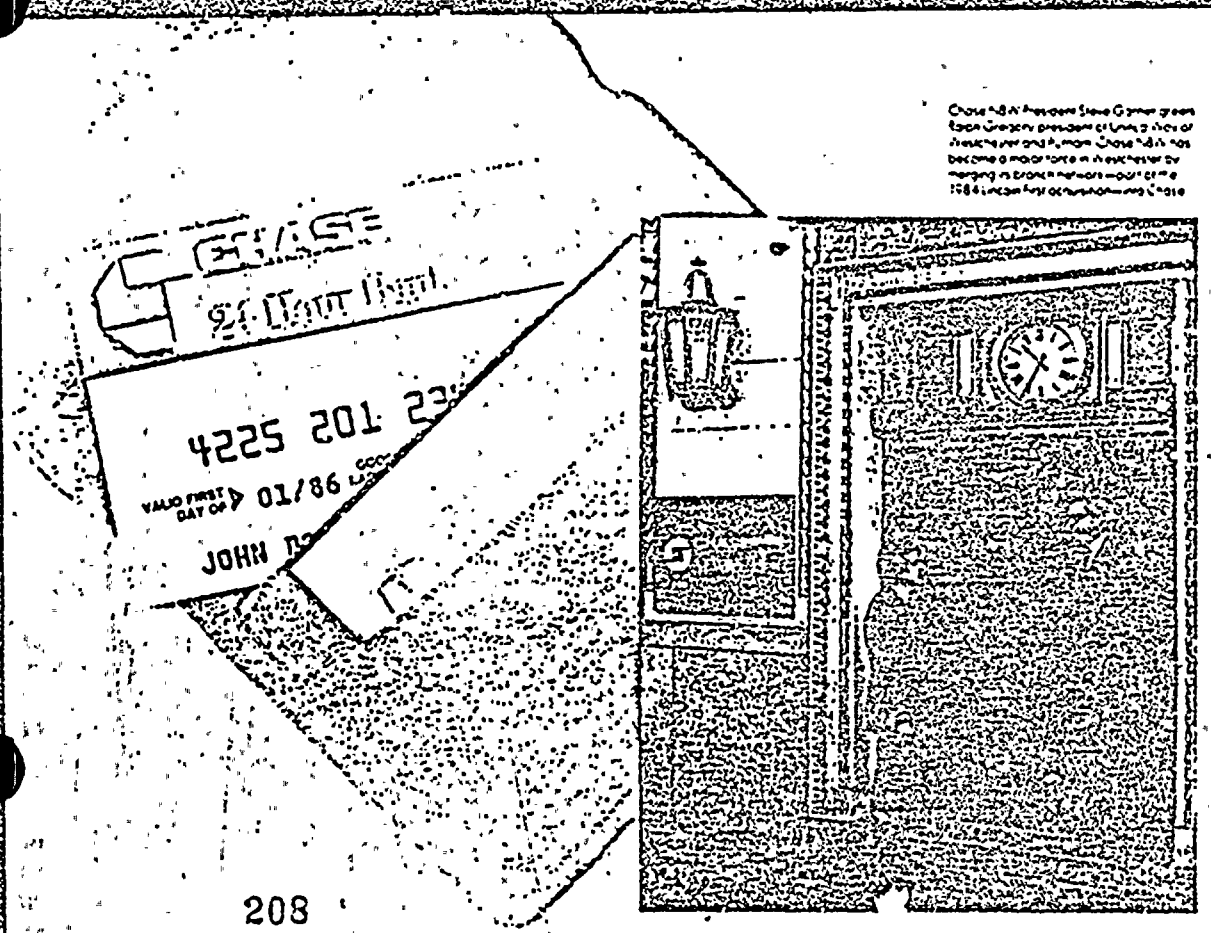
The restructured Metropolitan Community Bank provides customers Chase's big bank advantages—innovative products, competitive rates, operating efficiency, and international reach—through local full-service community banks. In upstate New York, for example, Chase Lincoln First continued to prove its value as a profitable acquisition.

Breaking new ground in Ohio, Maryland, Arizona, and Florida, Chase has laid the foundation for a nationwide network of banking offices.

This network offers opportunities for other Chase businesses such as Real Estate Finance. With an established position in prime markets, Real Estate's loan volume and earnings exceeded corporate targets in 1985. Going forward, Chase's combination of regional expertise and investment banking capabilities will enhance Real Estate Finance's ability to meet customers' needs.



Membership in the NYCE, Plus, and VISA ATM networks gives Chase customers access to cash at more than 7,500 worldwide locations, including the state of Massachusetts, New York.



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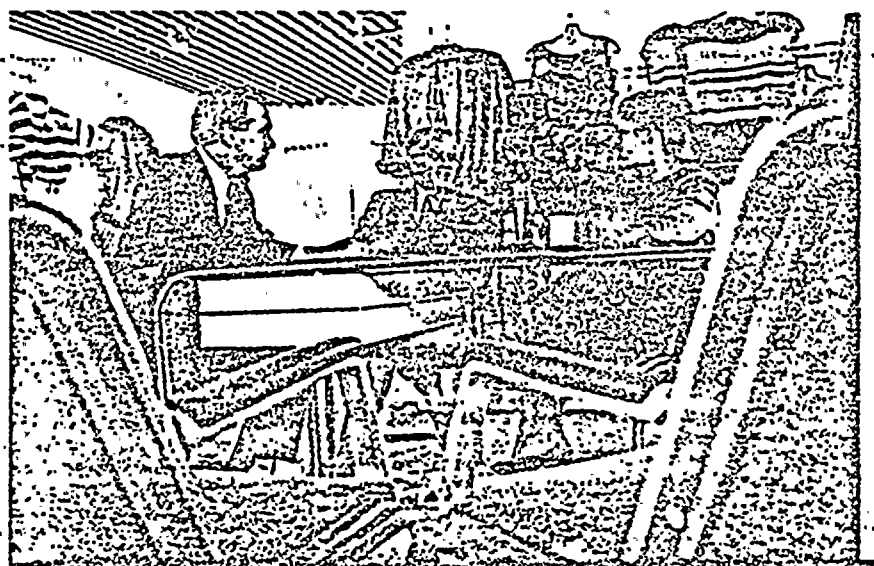
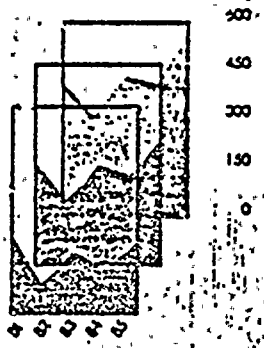
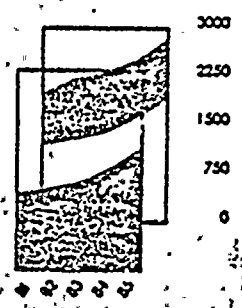


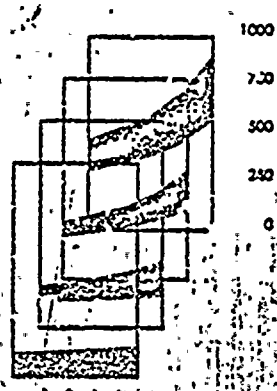
Net Income e , a Percentage of Average Total Assets, Average Common Stockholders' Equity
$ in Millions
- Net Income
- Return on Average Assets (ROA)%
- Return on Average Common Stockholders' Equity (ROE)%



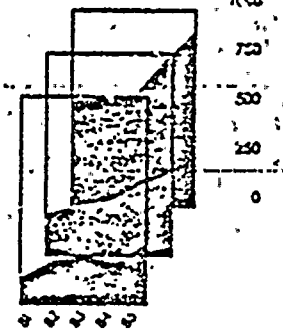
Net Interest Income—Taxable Equivalent Basis ($ in Millions)
- Overseas Offices
- Domestic Offices



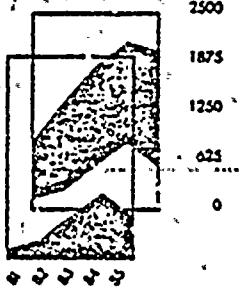
Fee-based Income ($ in Millions)
- Other Fees
- Consumer Banking Fees
- Trust & Fiduciary Investment Fees
- International Business Fees



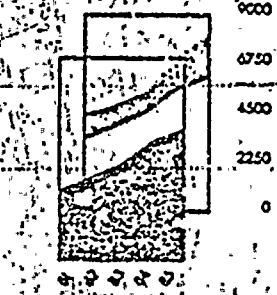
Reserve for Possible Loan Losses, Provision for Possible Loan Losses and Net Charge-offs ($ in Millions)
- Reserve for Possible Loan Losses
- Provision for Possible Loan Losses
- Net Charge-offs



Nonaccrual and Restructured Loans ($ in millions)
- Credit Crescent
- Country Crescent



Period-end Capital ($ in Millions)
- Total Capital
- Primary Capital



Reserve Balances as a Percentage of Loans at Year-end

	81	82	83	84	85
%	1.25	1.01	1.01	1.03	1.47

	81	82	83	84	85
Primary Capital %	4.17	4.73	5.44	6.37	6.87
Total Capital %	5.73	6.01	6.69	8.11	9.23

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Net Income

Summary of Selected Financial Data

	1985	1984	1983	1982	1981
For the Year ($ in millions)					
Net Interest Income	$ 2,749	$ 2,308	$ 2,169	$ 2,024	$ 1,772
Provision for Possible Loan Losses	435	365	285	263	211
Other Operating Income	1,316	930	864	698	609
Other Operating Expenses	2,732	2,245	2,09[illegible]	2,135	1,606
Net Income	565	406	43[illegible]	307	412
Average Common Shares Outstanding* (in thousands)	75,240	71,153	68,745	67,157	65,454
Per Common Share*					
Net Income*					
Primary	$ 6.39	$ 4.51	$ 5.48	$ 3.86½	$ 5.78
Fully Diluted	6.15	4.32	5.22	3.64	5.37
Cash Dividends Declared	1.90	1.82½	1.75	1.70	1.55
Stockholders' Equity at Year-end	49.19	45.81	43.91	40.71	39.18
Market Value at Year-end	36.31¼	23.87½	22.75	24.50	26.93¼
At Year-end ($ in millions)					
Loans	$61,931	$62,003	$55,894	$55,532	$51,331
Total Assets	87,685	86,683	81,921	80,863	77,839
Long-Term Notes and Debentures	2,806	2,320	1,376	1,046	944
Redeemable Preferred Stock	62	62	150	150	280
Nonredeemable Preferred Stock	602	602	375	375	125
Common Stockholders' Equity	3,795	3,359	3,051	2,761	2,593
Financial Ratios					
Return on Average Total Assets	.65%	.48%	.54%	.40%	.55%
Return on Average Common Stockholders' Equity	13.6	10.1	13.1	9.8	15.9
Primary Capital as % of Total Gross Assets	6.87	6.37	5.44	4.73	4.17
Total Capital as % of Total Gross Assets	9.23	8.11	6.69	6.01	5.73

*Amounts reflect the 2-for-1 common stock split effected in the form of a 100% stock dividend declared on January 15, 1986, to stockholders of record on January 31, 1986, and distributed on February 13, 1986.

Consolidated net income was a record $565 million for 1985, up $159 million, or 39%, from the $406 million earned in 1984, and up $135 million from 1983's level of $430 million. In comparison with 1984, earnings for 1985 included increased net interest income and higher other operating income, including substantial increases in virtually all fee-based income categories. In foreign exchange trading income and in gains from the sale of investment securities. Partially offsetting this strong income performance were increased operating expenses and a higher provision for possible loan losses. Net income for 1985 reflects the full year impact of the acquisitions of Nederlandse Credietbank N.V. (NCB) and Lincoln First Banks Inc. (Lincoln) while 1984 included only the impact after the mid-year consolidations of the two entities. Accordingly, net income for the first half of 1985 was favorably impacted by approximately $72 million from these acquisitions.

On a per common share basis, consolidated net income was $6.39 in 1985, compared with $4.51 in 1984 and $5.48 in 1983. Fully diluted net income per common share was $6.15 in 1985, compared with $4.32 in 1984 and $5.22 in 1983.

Net income per common share amounts in 1985 reflect the issuance of common shares pursuant to: the 1984 Lincoln acquisition, the dividend reinvestment and stock purchase plan, payment of interest in common shares on Floating Rate Subordinated Notes (Due 1996) and conversions of convertible capital notes and debentures. The 1985 per common share amounts also reflect the full year impact of increased preferred stock dividend requirements, primarily attributable to the Floating Rate Series F Nonredeemable Preferred Stock issued in conjunction with the 1984 acquisition of Lincoln. Series F preferred dividends had been initially set at $3.10 per share for each of the quarterly dividend periods ended May 31, 1985 and thereafter are adjusted based on a formula.

Chase's Consolidated Statements of Income for the years 1985, 1984 and 1983 are presented on page 45. Summary income statements by quarter for 1985, 1984 and 1983 are presented on page 70. The effects of general increases in the price level (inflation) on selected financial data are presented on page 79.

Average total assets were $86.3 billion in 1985, a 1% increase over 1984 and a 9% increase over 1983. Chase's return on average total assets (ROA) based on net income was .65% in 1985. The ROA was .48% for 1984 and .54% for 1983. The return on average common stockholders' equity (ROE) based on net income applicable to common stock, was 13.6% in 1985. The ROE for 1984 was 10.1% and for 1983 was 13.1%. Cash dividends per common share increased to $1.90 in 1985, up from $1.82½ in 1984 and $1.75 in 1983. In January 1986, for the eighth consecutive year, Chase's Board of Directors approved an increase in the quarterly common dividend. The increase, to $.51¼ per share, equates to an annual rate of $2.05 per share.

On January 15, 1986, Chase's Board of Directors declared a 2-for-1 stock split effected in the form of a 100% stock dividend on Chase's common stock, distributable on February 13, 1986, to stockholders of record on January 31, 1986. Average common shares outstanding, earnings per common share and cash dividends declared for 1985 and prior years have been restated to reflect the 2-for-1 stock split. For further information see Note 2 of Notes to Financial Statements: Common Stock Split.

In the second quarter of 1985, Chase acquired six Ohio savings and loan institutions, with total assets of approximately $450 million, and converted them into a commercial bank named Chase Bank of Ohio (Chase Ohio). In the fourth quarter of 1985, Chase acquired three Maryland savings and loan institutions, with total assets of approximately $700 million, and converted them into a commercial bank named Chase Bank of Maryland (Chase Maryland). Both acquisitions were accounted for as purchases. Statements of condition at year-end 1985 for Chase Ohio and Chase Maryland are presented on page 78.

During 1985, Chase made other acquisitions, including Banco de Finanzas, of Madrid, Spain, with total assets of approximately $265 million. These other acquisitions were also accounted for as purchases.

Domestic and International Operations

Average assets by geographic region are shown in the following table:

Average Assets by Geographic Region

In millions	United States	Asia	Europe	Middle East and Africa	Western Hemisphere	Total International	Total Corporation
Cash and Due from Banks[1]	$ 4,333	$ 855	$ 3,413	$ 44	$ 930	$ 5,242	$ 9,575
Investment Securities	4,358	117	790	10	262	1,179	5,537
Loans (Net of Loan Loss Reserve)	28,849	6,971	10,378	1,596	12,909	31,854	60,703
Customers' Liability on Acceptances	326	1,507	1,304	100	788	3,699	4,025
Other Assets	4,142	352	1,219	75	663	2,309	6,451
Total Assets—1985	$42,008	$ 9,802	$17,104	$1,825	$15,552	$44,283	$86,291
Percentage of Total	49%	11%	20%	2%	18%	51%	100%
Total Assets—1984	$37,608	$11,165	$17,449	$2,435	$16,684	$47,733	$85,341
Percentage of Total	44%	13%	20%	3%	20%	56%	100%
Total Assets—1983	$33,277	$10,645	$16,209	$2,520	$16,420	$45,794	$79,071
Percentage of Total	42%	13%	21%	3%	21%	58%	100%

[1]Includes Interest-Bearing Deposits Placed with Banks.

Note: No foreign country accounted for more than 10% of average consolidated total assets in 1985, 1984 or 1983. Average international liabilities, principally deposits, represented 62% of average total liabilities in 1985, compared with 65% in 1984 and 63% in 1983.

Domestic Earnings, representing results of operations in the United States, were $371 million in 1985, compared with $299 million in 1984 and $249 million in 1983. Domestic earnings accounted for 66% of consolidated net income in 1985, compared with 74% in 1984 and 58% in 1983.

In comparison with both 1984 and 1983, domestic earnings for 1985 were favorably affected by higher net interest income, increased fee-based income, net gains from the sale of investment securities and the full year impact of the Lincoln acquisition. These favorable factors were partially offset by increased operating expenses and a higher provision for possible loan losses. Domestic net interest income increased primarily due to a higher volume of interest-earning assets, resulting in part from the Lincoln acquisition, to generally lower interest rates paid on interest-bearing liabilities and a higher level of net noninterest-bearing demand deposits.

Domestic other operating income increased 49%, or $261 million in 1985 to $797 million, compared with $536 million for 1984 and $492 million for 1983. The Lincoln acquisition accounted for $65 million of this increase, including the impact of approximately $40 million in the first six months of 1985. Domestic fee-based income increased from $405 million in 1983 and from $501 million in 1984 to $656 million in 1985, primarily due to the continued growth of Chase's consumer credit card, trust and fiduciary and investment banking activities and to the impact of the Lincoln acquisition. Domestic nonfee-based income was $141 million in 1985, an increase of $106 million over 1984 and of $54 million over 1983. Domestic nonfee-based income for 1985 included net investment securities gains of $90 million, up $77 million from 1984 and up $68 million from 1983.

The domestic provision for loan losses for 1985 was $330 million, compared with $215 million in 1984 and $135 million in 1983. The increase of $115 million and $195 million, respectively, primarily reflected actual experience and anticipated higher levels of domestic consumer charge-offs due to Chase's expanding consumer lending activities. Domestic operating expenses increased to $1,659 million in 1985 from $1,261 million in 1984 and from $1,134 million in 1983. Excluding both the impact of approximately $79 million in the first six months of 1985 resulting from the acquisition of Lincoln, and the $49 million special recovery in 1984 related to the 1982 Drysdale loss, 1985 domestic operating expenses increased 21% over 1984 and 39% over 1983. See page 29 for further information on Other Operating Expenses.

International Earnings[2], which include the operating results of Chase's overseas offices as well as international business activities conducted from the Head Office in New York and other domestic offices, were $194 million in 1985, up 80% from $107 million in 1984 and up 7% from $181 million in 1983. The substantial increase in 1985 international earnings caused the percentage contribution of international earnings to consolidated net income to increase to 34% in 1985, compared with 26% in 1984 and 42% in 1983.

Further information regarding international activities is contained in Note 18 of Notes to Financial Statements as well as in the Country Risk section of this analysis.

International earnings for 1985 increased compared with 1984 and 1983 due primarily to increases in net interest income caused by wider interest rate spreads and increases in other operating income. International fee-based income increased to $253 million in 1985 from $215 million in 1984 and from $196 million in 1983. Investment banking, global trust and custody activities and letters of credit fee income increased while fee income from acceptances declined. Nonfee-based international income increased to $266 million in 1985 from $179 million in 1984 and from $185 million in 1983, due largely to strong foreign exchange trading income, gains from the sales of real estate and substantially all of Chase's interest in Diamond Lease Company Ltd., both in Japan, and pre-tax net foreign exchange translation gains on investments in overseas branches, subsidiaries and associated companies. These increases in nonfee-based income were partially offset by reduced equity income from Chase's investments in overseas associated banking institutions.

The international provision for loan losses for 1985 was $105 million, compared with $150 million in 1984 and 1983. International operating expenses increased to $1,073 million in 1985 from $984 million in 1984 and from $911 million in 1983. Excluding the impact of approximately $36 million in the first six months of 1985 resulting from the consolidation of NCB, 1985 expenses increased 5% over 1984 and 14% over 1983, reflecting the effect of expense management programs and more favorable foreign exchange rates in 1985.

[2]Estimated based on internal allocations and allowances. See Note 18 of Notes to Financial Statements: International Activities.

The contribution to 1985 international earnings from operations in Europe was $41 million, compared with $16 million in 1984 and $33 million in 1983. Net interest income and fee-based income, particularly international business, commercial banking and global custody fees, and nonfee-based income, mainly foreign exchange trading income, increased in 1985 compared with 1984. These increases were partially offset by higher operating expenses in 1985, resulting in part from the consolidation of NCB. In 1985, earnings in the United Kingdom, The Netherlands, West Germany, Belgium and Switzerland increased compared with 1984, while earnings from Italy and Sweden declined.

Operations in the Western Hemisphere (other than the United States) contributed $109 million to international earnings in 1985, compared with $66 million in 1984 and $75 million in 1983. In 1985, net interest income from this area increased compared with 1984 primarily due to wider interest rate spreads and improved collections of interest on nonaccrual loans. The provision for loan losses for this area declined in 1985 compared with 1984 and fee-based income increased modestly from the 1984 level, primarily due to an increase in investment banking fees. Nonfee-based income increased in 1985 due to pre-tax net foreign exchange translation gains on investments in overseas branches, subsidiaries and associated companies, compared with losses on such investments in 1984. The increase in nonfee-based income was partially offset by a decrease in equity income from Chase's investments in overseas associated banking institutions. In 1985, earnings from activities in Argentina, Puerto Rico and Ecuador increased compared with 1984, while earnings from Peru, Colombia, the Bahamas and local activities in Brazil declined.

Operations in the Middle East and Africa contributed a loss of $6 million to international earnings in 1985, compared with net income of $4 million in 1984 and $24 million in 1983. In 1985, net interest income and fee-based income from this area increased over the 1984 level. However, nonfee-based income in 1985 declined significantly compared with 1984 and 1983, primarily due to a substantial decrease in equity income from Chase's investments in overseas associated banking institutions. Also, nonfee-based income in 1983 included $25 million from Chase's settlement with Iran. In addition, a higher level of net loan charge-offs in 1985, compared with 1984 and 1983 contributed to the 1985 loss recorded in this area.

Operations in Asia contributed $50 million to 1985 international earnings, compared with $21 million in 1984 and $49 million in 1983. Net interest income and fee-based income increased moderately compared with 1984 and 1983. Nonfee-based income increased in 1985, compared with 1984 and 1983, primarily due to a gain of $22 million ($15 million after taxes) from the sale of substantially all of Chase's investment in Diamond Lease Company Ltd., and a gain of $23 million ($15 million after taxes) on the sale of real estate, both in Japan, and from increased foreign exchange trading income. Operating expenses in 1985 increased compared with 1984. In 1985, earnings from activities in Japan, Hong Kong and Singapore increased compared with 1984, while earnings in Australia, India and the Philippines declined.

Net Interest Income—Taxable Equivalent Basis[1]

Net interest income on a taxable equivalent basis was $2,994 million in 1985, an increase of 18% over 1984 and of 25% over 1983. Net interest income increased over 1984 primarily due to a higher volume of interest-earning assets and wider interest rate spreads resulting from the declining interest rate environment. In addition, net interest income benefited from Chase's increased activities in the interest rate and currency swap markets. In 1985, average interest-earning assets were $74.2 billion, up $1.9 billion, or 3%, from 1984, and up $7.9 billion, or 12%, compared with 1983.

The following table presents a reconciliation of net interest income on a taxable equivalent basis and on a financial statement basis.

Net Interest Income—Taxable Equivalent Adjustment

($ in millions)	1985	1984	1983
Domestic Offices			
Net Interest Income—			
Taxable Equivalent Basis	$1,914	$1,611	$1,377
Taxable Equivalent Adjustment	213	198	156
Net Interest Income (Financial Statement Basis)	$1,701	$1,413	$1,221
Overseas Offices			
Net Interest Income—			
Taxable Equivalent Basis	$1,080	$ 926	$ 970
Taxable Equivalent Adjustment	32	31	22
Net Interest Income (Financial Statement Basis)	$1,048	$ 895	$ 948
Corporation Consolidated			
Net Interest Income—			
Taxable Equivalent Basis	$2,994	$2,537	$2,347
Taxable Equivalent Adjustment	245	229	178
Net Interest Income (Financial Statement Basis)	$2,749	$2,308	$2,169

[1]Taxable equivalent amounts have been adjusted by applying a combined U.S. federal, state and local income tax rate of approximately 51%, 59% and 60% for 1985, 1984 and 1983, respectively, to recognize the differential between interest income that is exempt from taxes and interest income that is fully taxable.

Over the past five years, net interest income on a taxable equivalent basis increased at a 12% annual compound growth rate as a result of generally higher net interest rate spreads and a growing volume of interest-earning assets. During this five-year period, net interest income as a percentage of gross interest-earning assets fluctuated between a low of 3.25% for 1981 and a high of 4.03% for 1985, while the average for the five-year period was 3.54%.

Net interest income on a taxable equivalent basis in domestic offices totaled $1,914 million in 1985, up 19% compared with $1,611 million in 1984, and up 39% from $1,377 million in 1983. The 1985 increase was primarily attributable to a higher volume of interest-earning assets, partly applicable to the Lincoln acquisition, to generally lower interest rates paid on interest-bearing liabilities and a higher level of net noninterest-bearing demand deposits. Compared with 1984, domestic net interest income for 1985 included a lower amount of cash collections of interest on nonperforming loans. The 1985 average volume of interest-earning assets in domestic offices was $31.2 billion, up 13% compared with $27.7 billion in 1984 and up 30% from $24.0 billion in 1983.

Net interest income on a taxable equivalent basis in overseas offices totaled $1,080 million in 1985, up 17% compared with $926 million in 1984 and up 11% compared with $970 million in 1983. Overseas net interest income increased in 1985, compared with 1984 due primarily to wider net interest rate spreads, and compared with 1983 due primarily to a higher level of noninterest-bearing funding sources.

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The table below presents net interest income on a taxable equivalent basis and related interest rate spreads for the last three years for domestic offices, overseas offices and the consolidated Corporation.

Net Interest Income and Interest Rate Spreads—Taxable Equivalent Basis

	Domestic Offices					
	1985		1984		1983	
($ in millions)	Amount	Rate	Amount	Rate	Amount	Rate
Interest Earned	$3,714	11.88%	$3,558	12.90%	$2,871	11.98%
Interest Paid*	1,800	8.10	1,957	9.99	1,494	9.03
Net Interest Income	$1,914	3.78%	$1,601	2.91%	$1,377	2.95%
—as a % of Gross Interest-Earning Assets		6.12%		5.82%		5.75%

	Overseas Offices					
	1985		1984		1983	
	Amount	Rate	Amount	Rate	Amount	Rate
Interest Earned	$4,949	11.52%	$5,612	12.58%	$4,966	11.72%
Interest Paid*	3,869	9.52	4,686	10.83	3,996	9.74
Net Interest Income	$1,080	2.00%	$ 926	1.75%	$ 970	1.98%
—as a % of Gross Interest-Earning Assets		2.52%		2.08%		2.29%

	Consolidated Corporation					
	1985		1984		1983	
	Amount	Rate	Amount	Rate	Amount	Rate
Interest Earned	$8,663	11.68%	$9,160	12.70%	$7,837	11.81%
Interest Paid	5,669	9.02	6,643	10.57	5,490	9.53
Net Interest Income	$2,994	2.66%	$2,537	2.13%	$2,347	2.28%
—as a % of Gross Interest-Earning Assets		4.03%		3.51%		3.[illegible]

*Includes appropriate allocations for the cost of time deposits received by overseas offices for domestic use and the cost of domestic monies raised for use in overseas offices.

The following table presents the effects of changes in average balances and interest rates of major categories of assets and liabilities on net interest income on a taxable equivalent basis.

Net Interest Income—Taxable Equivalent Basis Increase (Decrease) Due to Changes in Average Balances and Rates[1]

	1985 vs. 1984			1984 vs. 1983		
($ in millions)	Balance	Rate	Total	Balance	Rate	Total
Interest-Earning Assets						
Interest-Bearing Deposits Placed with Banks	$(194)	$ (94)	$(288)	$ (79)	$121	$ 42
Federal Funds Sold and Securities Purchased Under Resale Agreements	43	(15)	28	14	6	20
Trading Account Assets	39	(11)	28	(11)	13	2
Investment Securities	149	37	186	65	(40)	25
Loans:						
Domestic Offices	281	(229)	52	437	208	645
Overseas Offices	(149)	(474)	(523)	333	276	609
Total Interest-Earning Assets	269	(786)	(517)	759	584	1,343
Interest-Bearing Liabilities						
Deposits:						
Domestic Offices	252	(328)	(76)	299	117	416
Overseas Offices	(231)	(413)	(644)	178	314	492
Federal Funds Purchased and Securities Sold Under Repurchase Agreements	(40)	(46)	(86)	(89)	82	(7)
Other Borrowed Money	(92)	(122)	(214)	62	104	166
Long-Term Notes and Debentures	74	(28)	46	74	12	86
Total Interest-Bearing Liabilities	37	(937)	(974)	524	629	1,153
Net Interest Income—Taxable Equivalent Basis	$ 305	$ 151	$ 457	$ 235	$ (45)	$ 190

[1]Changes not solely due to balances or to interest rates have been allocated equally to balances and interest rates.

Provision for Possible Loan Losses and Net Loan Charge-offs

The provision for possible loan losses for 1985 increased to $435 million, up $70 million from the $365 million recorded in 1984 and up $150 million from the $285 million recorded in 1983. The increase in the 1985 provision for possible loan losses was due to the higher level of net loan charge-offs, and the continuing uncertain conditions in certain developing countries, and in anticipation of higher levels of domestic consumer charge-offs due to the rapid growth of the domestic consumer loan portfolio.

Net loan charge-offs for 1985 were $320 million, up $105 million and $66 million compared with 1984 and 1983, respectively. Domestic net loan charge-offs were $234 million for 1985, a $72 million increase from 1984 and a $79 million increase from 1983, and represented 73%, 75% and 61% of total net loan charge-offs for 1985, 1984 and 1983, respectively. Domestic consumer net loan charge-offs, primarily attributable to credit card activities, were $131 million for 1985, up $73 million from 1984 and up $97 million from 1983, and represented 56% of domestic net loan charge-offs for 1985. Included in 1985 domestic net loan charge-offs was approximately $3 million of net charge-offs of loans acquired through the former Penn Square Bank, N.A., down from $43 million and $40 million in 1984 and 1983, respectively. Details on loan charge-offs and recoveries by loan type may be found on page 71, Consolidated Analysis of Loan Loss Experience.

Net pre-tax gains or losses on securities and real estate properties acquired in satisfaction of debts previously contracted are not reflected in net loan charge-offs. Included in 1985 other income were net pre-tax gains of $11 million from the disposition of securities acquired in satisfaction of debts previously contracted, compared with $7 million in 1984 and $34 million in 1983. Net gains on the disposition of real estate properties acquired in satisfaction of loans, after valuation adjustments on properties held at year-end, were $12 million in 1985, compared with net gains of $18 million in 1984 and net losses of $6 million in 1983. Gains and losses on dispositions and valuation adjustments of real estate properties acquired are reflected in other expenses.

Net loan charge-offs, loan loss experience ratios and the estimated allocation of the provision for possible loan losses attributable to domestic and international activities for the past five years are summarized in the following table.

Net Loan Charge-offs and Loan Loss Experience Ratios

($ in millions)	1985	1984	1983	1982	1981
Net Loan Charge-offs					
Domestic—Consumer[a]	$131	$ 59	$ 35	$ 34	$ 32
—Commercial and Other	103	103	121	117	76
Total Domestic	234	162	156	151	108
International	86	53	99	79	18
Total	$320	$215	$255	$230	$126
Loan Loss Experience Ratios[b]					
Domestic—Consumer[a]	1.60%	1.07%	.79%	.85%	.94%
—Commercial and Other	.49	.48	.66	.63	.47
Total Domestic	.80	.60	.68	.67	.56
International	.27	.16	.32	.27	.06
Consolidated	.52	.36	.47	.44	.26
Allocation of the Provision for Possible Loan Losses					
Domestic	$330	$415	$135	$163	$161
International	105	150	150	100	50
Total	$435	$365	$285	$263	$211

[a] Loans to individuals for personal expenditures and 1-4 family residential properties.

[b] Net loan charge-offs as a percentage of average loans.

The preceding allocation of the provision for possible loan losses between domestic and international activities has been prepared based on subjective estimates, as further discussed in the following section, Reserve for Possible Loan Losses.

Reserve for Possible Loan Losses

Implicit in lending activities is the fact that losses will be experienced and that the amount of such losses will vary from time to time, depending upon the risk characteristics of the portfolio as affected by worldwide economic conditions and the financial experience of borrowers. The reserve for possible loan losses, which provides for the risk of losses inherent in the lending process, is increased by the provision for possible loan losses charged to expenses and decreased by the amount of net loan charge-offs. There is no precise method of predicting specific losses or amounts which ultimately may be charged off on particular segments of the loan portfolio. The conclusion that a loan may become uncollectible, in whole or in part, is a matter of judgment. Similarly, the adequacy of the reserve for possible loan losses can be determined only on a judgmental basis, after full review, including consideration of:

—Economic conditions and their effects on particular countries, industries and specific borrowers;

—Borrowers' financial data, together with industry data, competition, the borrowers' management capabilities, evaluations of the underlying collateral for secured lending including, when appropriate, independent appraisals of real estate properties, and other factors;

—A continuing evaluation of the loan portfolio and off-balance sheet credit exposures, including monitoring by lending officers and credit supervisory personnel of loans which are identified as being of less than acceptable quality. In addition, periodic examinations are conducted in lending areas by the Credit Audit Division of Chase's General Auditing department;

—Monthly in-depth appraisal of loans which present a possibility of loss. If, as a result of such monthly appraisals, a loan is judged to be not collectible, the carrying value of the loan is reduced, in accordance with internal policy, to that portion which is considered to be collectible.

In addition to the continuing internal assessment of the loan portfolio, the consolidated financial statements are examined by Chase's independent public accountants, whose examination includes a review of the adequacy of the reserve for possible loan losses. Also, examinations of Chase's loan portfolio are conducted periodically by the federal banking authorities.

The reserve for possible loan losses is maintained as a general reserve without any internal allocation to the components of the loan portfolio. When potential losses on specific loans are identified, the portion deemed uncollectible is charged off. However, an allocation of the reserve has been prepared based on subjective estimates which take into account historical loss data and Management's views as to the relative risk characteristics of the portfolio.

The year-end 1985 reserve allocation to international loans of $400 million, up $25 million from year-end 1984, reflected the continuing uncertain global economic conditions, particularly in certain developing countries, and the continuing high but somewhat reduced level of nonaccrual loans. The year-end 1985 allocation to domestic commercial loans, which increased by $10 million, reflected Management's continued concern over the uneven economic recovery in the United States. The allocation to domestic consumer loans was increased substantially by $95 million to $175 million at year-end 1985 in anticipation of higher levels of charge-offs consistent with the rapid growth of the domestic consumer loan portfolio and conditions currently prevailing in the consumer credit markets.

The allocation of the reserve account will change whenever Management determines that the risk characteristics of the loan portfolio have changed. It should not be construed that the amount allocated to a particular segment is the only amount available for future charge-offs that might occur within that segment, since the reserve is a general reserve available against the total loan portfolio. In addition, the amounts so allocated by segment may not be indicative of future charge-off trends. In the opinion of Management, the reserve for possible loan losses at December 31, 1985, is adequate to absorb anticipated losses in the loan portfolio at that date. Chase's independent public accountants have concurred with Management's opinion.

At December 31, 1985, the balance in the reserve for possible loan losses was $908 million, compared with $761 million at year-end 1984 and $564 million at year-end 1983. At year-end 1985, the reserve for possible loan losses represented 1.47% of loans, compared with 1.23% and 1.01% at year-end 1984 and 1983, respectively. The following table presents the allocation of the reserve for possible loan losses at year-end 1985 compared with the prior four year-ends.

Allocation of the Reserve for Possible Loan Losses

	December 31,				
($ in millions)	1985	1984	1983	1982	1981
Allocated Portion of Reserve:					
Domestic:					
Real Estate Loans	$ 25	$125	$ 20	$ 25	$ 25
Commercial and Industrial Loans	235	225	150	160	150
Loans to Individuals for Personal Expenditures	175	80	55	50	50
Lease Financings	15	15	10	10	10
International	400	375	300	275	250
Total Allocated Portion	850	720	535	520	485
Unallocated Portion	58	41	29	38	56
Total Reserve for Possible Loan Losses	$908	$761	$564	$558	$541

Other Operating Income

Other operating income totaled $1,316 million in 1985, up 42% from $930 million in 1984 and up 52% from $864 million in 1983, as reflected in the following table.

Other Operating Income

($ in millions)	1985	1984	1983
Fee-Based Income*			
International Business Fees	$ 162	$152	$144
Trust and Fiduciary Investment Fees	193	154	120
Consumer Banking Fees	209	145	113
Other Fee-Based Income	345	265	224
Total Fee-Based Income	$ 909	$716	$601
Non-fee-Based Income			
Foreign Exchange Trading Income	$ 173	$119	$117
Trading Account Profits	31	29	24
Investment Securities Gains (Losses)	98	17	25
Other Nonfee-Based Income	105	49	97
Total Nonfee-Based Income	$ 407	$214	$263
Total Other Operating Income	$1,316	$930	$864

*Reclassified for comparative purposes.

Fee-Based Income

In 1985, fee income from trust and fiduciary investment services increased 25% over 1984 and 61% over 1983. The increase in 1985 reflected the impact of approximately $23 million resulting from the Lincoln acquisition and growth in Chase's global custody services and specialty investment services offered by Chase Investors Management Corporation in New York. Consumer banking fees increased 44% compared with 1984 and 80% compared with 1983. This increase was primarily attributable to continued growth of the VISA credit card business. Other fee-based income included income from investment banking activities, information services, mortgage banking and commercial banking activities. Investment banking fees increased 60% and 108% compared with 1984 and 1983, respectively, due to substantial increases in fee income from mergers and acquisitions, loan syndication and overseas underwriting activities, leasing and financial advisory services. In addition, during 1985 the Investment Banking Group consummated approximately 300 interest rate and currency swap transactions aggregating approximately $7 billion in notional principal. Fee income from interest rate and currency swaps in 1985 increased substantially compared with 1984. Other fees generated from information services, mortgage banking and commercial banking activities increased 23% over 1984 and 44% over 1983.

Nonfee-Based Income

Foreign exchange trading income for 1985 was $173 million, compared with $119 million in 1984 and $117 million in 1983. The approximately 45% increase in foreign exchange trading income from 1983 to 1985 reflected the global effectiveness of Chase's network in the highly competitive foreign exchange environment. Chase is a major market maker in all of the world's freely traded currencies and through its global network of trading centers is able to timely and accurately execute foreign exchange transactions for customers and to arbitrage the various spot, forward, futures and options markets.

Trading account profits, including profits from dealer bond and precious metals trading activities, were $31 million in 1985, compared with $29 million in 1984 and $24 million in 1983. In addition to increased profitability, substantial gains were achieved in underwriting presence and global securities distribution.

Net investment securities gains increased substantially to $98 million, up $81 million from 1984, and up $73 million compared with 1983, reflecting declining interest rates and favorable market conditions prevailing throughout most of 1985.

Other nonfee-based income includes equity income from associated companies (20% to 50% owned by Chase), net gains on the disposition of assets, net foreign exchange translation gains and losses, and miscellaneous income. The increase in other nonfee-based income, from $49 million in 1984 to $105 million in 1985, includes a pre-tax gain of $22 million from the sale of substantially all of Chase's interest in Diamond Lease Company Ltd. and a $23 million pre-tax gain from the sale of real estate, both in Japan. Other nonfee-based income in 1983 included $26 million resulting from Chase's settlement with Iran. Net gains, before income taxes, from the disposition of securities acquired in satisfaction of debts previously contracted totaled $11 million in 1985, compared with $7 million in 1984 and $34 million in 1983. Equity income from associated banking institutions declined $7 million from 1984. Net foreign exchange translation gains on Chase's investments in overseas branches, subsidiaries and associated companies were approximately $5 million in 1985 compared with losses of $4 million in 1984 and of $40 million in 1982. On an after-tax basis, net foreign exchange translation losses were approximately $9 million, $15 million and $27 million in 1985, 1984 and 1983, respectively.

Other Operating Expenses

Other operating expenses were $2,732 million in 1985, up 22% from 1984 and 34% from 1983, as shown in the following table. Included in 1984 other operating expenses was a special recovery of $49 million ($20 million after taxes) as a result of Chase's settlements with certain defendants in the action the Bank brought against Drysdale Securities Corporation, Drysdale Government Securities, Inc. and others in 1982 and the net recovery realized on certain other transactions relating to the Drysdale situation. Excluding both this 1984 special recovery and the first six months 1985 impact of the consolidations of NCB and Lincoln, 1985 other operating expenses would have been up 14% over 1984 and up 28% over 1983. The impact of the acquisitions of NCB and Lincoln on the first six months of 1985 increased operating expenses by $115 million.

Other Operating Expenses

($ in millions)	1985	1984	1983
Salaries and Employee Benefits	$1,451	$1,219	$1,122
Net Occupancy	284	245	213
Equipment Rentals, Depreciation and Maintenance	203	171	139
Other Expenses	794	659	572
Special (Recovery)	—	(49)	—
Total Other Operating Expenses	$2,732	$2,245	$2,046

Salaries and employee benefits were $1,451 million in 1985, up $232 million from 1984 and up $329 million from 1983. The increase in 1985 was due to normal staff merit increases and higher profit sharing and other incentive compensation expenses, principally as a result of substantially improved earnings. In addition, 1985 staff expenses reflect recent acquisitions including among others, the acquisitions of Lincoln, NCB and Chase Chia, and $15 million in aggregate severance payments made in certain overseas locations. Pension expense for Chase's major plan was $19 million in 1985, compared with $17 million in 1984 and $33 million in 1983. The reductions from 1983 pension expense were principally due to revisions in the interest rate assumptions in 1984 to more accurately reflect recent experience and future expectations.

All other items of operating expense, including net occupancy, equipment costs and other expenses, increased by $206 million, or 19%, in 1985 to $1,281 million, compared with $1,075 million in 1984 and $924 million in 1983. The increase in 1985 other operating expenses primarily reflects continued investments in equipment, systems technology and product innovation, and expansion in existing and new markets, partially offset by savings realized from expense management programs instituted to reduce unproductive and marginal activities and other discretionary types of spending.

The number of employees at year-end 1985 was higher by 2,850 employees, or 7%, than in 1984 and 25% higher than in 1983. The increase in 1985, compared with 1983 is substantially attributable to the acquisitions of NCB and Lincoln. The following table sets forth both the number of domestic employees and a geographic distribution of employees in overseas offices.

Number of Employees at Year-end

	1985	1984	1983
Domestic Offices*	29,570	26,800	23,130
Overseas Offices			
Asia	3,450	3,320	3,140
Europe*	6,480	6,410	3,745
Middle East and Africa	550	600	645
Western Hemisphere	6,400	6,470	6,550
Total Overseas Offices	16,880	16,800	14,100
Total Employees	46,450	43,600	37,230

*Domestic offices include approximately 4,000 employees in 1985 and 3,430 in 1984 resulting from the acquisitions of Lincoln Chase Chia and Chase Manhard. Overseas offices include 2,335 employees in 1985 and 2,330 in 1984 resulting from the acquisitions of NCB and Banco de Finanzas.

Provision for Income Taxes

The provision for income taxes applicable to net income increased to $333 million in 1985 from $223 million in 1984 and $273 million in 1983, primarily due to an increase in income before taxes, partially offset by an increase in income exempt from federal income taxes. In 1985, New York State and City adopted a new income tax law affecting banking institutions. The effect of the new law, while favorable, was not material to Chase's 1985 net income.

The amount of income tax reflected on the tax line of the financial statements may create an erroneous impression that Chase is subject to a lower income tax burden than are other types of business corporations. Actually, Chase and other commercial banking institutions in effect pay additional amounts which are equivalent to income taxes by accepting lower yields on federally tax-exempt municipal obligations and by virtue of the required maintenance of interest-free reserves with Federal Reserve Banks.

The following table presents both the direct and indirect 1985 taxes borne by Chase and the resulting effective income tax rate:

Overall Effective Income Taxes—1985

($ in millions)	Pre-tax Income	Tax	Net Income
Financial Statements, as published	$ 898	$333	$565
Exempt Obligations Implicit Tax	233	233	0
Federal Reserve Bank Indirect Tax*	59	59	0
Financial Statements, pro forma	$1,190	$625	$565
Effective Tax Rate		53%	

*Computed using Chase's average cost of domestic interest-bearing funds on $746 million maintained by Chase in interest-free reserves with Federal Reserve Banks.

Liquidity and Interest Sensitivity Management

The central role of Chase's liquidity management is to ensure that Chase has possession of and access to sufficient liquid funds to meet the normal transaction requirements of its customers, to take advantage of market opportunities requiring flexibility and speed and to provide a cushion against unforeseeable and unforeseen liquidity needs. The need for a disciplined and comprehensive program for liquidity management has been heightened substantially by economic developments in recent years. Movements in economies of major countries around the world are significantly more synchronized and financial markets are more closely integrated.

In recent years the deregulation of interest rate ceilings on most domestic deposits of under $100,000 and the permission granted to banks by federal authorities to offer money market deposit accounts, combined with effective marketing programs to acquire these deposits, have favorably affected liquidity management by creating significant new sources of funds. Also enhancing liquidity management were the acquisition of Lincoln, which has access to a significant consumer deposit network in New York State, and the issuance in the third quarter of 1983 and the second quarter of 1985 of Floating Rate Extendable Notes Due 1992 and 1997, respectively. Chase has been able to utilize these new sources of funds to reduce its traditional reliance on large-denomination negotiable certificates of deposit from an average of $2.7 billion in 1983 to $1.4 billion in 1984 and $.9 billion in 1985.

As an essential part of its liquidity management, Chase continues to place a high priority on closely monitoring its worldwide mix of asset and liability positions and maintaining its ability to adjust these positions throughout its worldwide network. This network provides diverse sources of funding and lending that enable Chase to choose the most cost-efficient means to execute business strategies.

In addition to its liquid assets and short-term liabilities, Chase also utilizes interest rate futures contracts to manage interest rate risk exposure as part of its global asset/liability management strategies and for liquidity management.

The following table shows selected average liquid assets and short-term liabilities for the years 1985, 1984 and 1983.

Selected Liquid Assets and Short-Term Liabilities

($ in millions—Averages)	1985	1984	1983
Selected Liquid Assets			
Interest Bearing Deposits Placed with Banks	$5,100	$7,000	$ 7,800
U.S. Treasury Securities	1,800	1,500	1,700
Foreign Government Securities	900	500	300
Federal Funds Sold and Securities Purchased Under Resale Agreements	1,200	800	600
Loans to Brokers and Dealers in Securities	600	600	600
Bankers' Acceptances in Portfolio	500	500	600
Average Total Assets	$86,200	$85,300	$79,100
Selected Short-Term Liabilities			
Non-Interest-Bearing Demand Deposits in Domestic Offices	$ 6,300	$ 5,500	$ 5,300
Non-Interest-Bearing Deposits in Overseas Offices	1,400	1,200	1,200
Federal Funds Purchased and Securities Sold Under Repurchase Agreements	4,500	5,200	6,100
Eurodollar and Eurocurrency Deposits with Original Maturities of Seven Days or Less	3,800	4,000	4,200
Commercial Paper of the Company	3,200	3,200	3,600
Negotiable Certificates of Deposit in Domestic Offices	900	1,400	2,700
Average Total Liabilities	$82,100	$81,600	$75,700

In managing liquidity, Management takes into account bank regulatory limitations on the ability of a national bank to pay dividends to its parent holding company. See Note 16 of Notes to Financial Statements: Regulatory Limitations.

Capital Management

The capital management function at Chase is a continuous process which consists of planning capital for both current financial positions and anticipated future growth. Key to this process is internal generation of primary capital through earnings retention and net increases to the reserve for possible loan losses. During 1985, internally generated primary capital totaled $454 million, up from the $332 million generated in 1984, and included a $122 million net increase in the reserve for possible loan losses. The annual rate of primary capital generation from internal sources was 8.1% in 1985, compared with 7.4% in 1984, and 6.6% in 1983.

Three external sources of equity generation are derived from issuance of common stock to existing investors in Chase pursuant to the Dividend Reinvestment and Stock Purchase Plan; shares issued upon conversions of the two outstanding convertible debt issues, the 4¼% Convertible Capital Notes Due 1993 and the 6¼% Convertible Subordinated Debentures Due 1996; and shares issued in payment of interest on Floating Rate Subordinated Notes Due 1996. During 1985, common stockholders reinvested $39 million of dividends in 717,000 new shares, a participation rate of approximately 27% of eligible shares. This compares with $33 million and 770,000 shares during 1984, a participation rate of approximately 25%. (Numbers of shares are before giving effect to the 2-for-1 stock split declared on January 15, 1986.)

Chase's primary capital increased by $510 million to $6,090 million at year-end 1985 from the $5,580 million level at year-end 1984, as shown in the accompanying tables. In 1984, Chase issued $400 million in floating rate subordinated notes that qualified as primary capital and $227 million in non-redeemable preferred stock. At year-end 1985, Chase's primary capital to total gross assets ratio was 6.87%, well in excess of the 5.5% minimum ratio established in 1984 by Chase's principal banking regulators, and up 50 basis points from the 6.37% ratio at year-end 1984.

Total capital includes, in addition to the elements of primary capital, secondary capital which is comprised of redeemable preferred stock and long-term debt. Chase augmented its secondary capital in April, May and November 1985 with the issuance of French francs 250 million (approximately $45 million) of Floating Rate Bonds Due 1993, $250 million of Floating Rate Subordinated Notes Due 2000 and $175 million of Floating Rate Subordinated Notes Due 1997, respectively. The net increases in secondary capital, combined with the net increases in primary capital, resulted in an increase in total capital during 1985 of $1,069 million. Total capital at year-end 1985 was $8,176 million compared with $7,107 million at year-end 1984. At year-end 1985, Chase's total capital to total gross assets ratio was 9.22%, also well in excess of the 6.0% minimum ratio established in 1984 by Chase's principal banking regulators and up 112 basis points from the 8.11% ratio at year-end 1984.

The following table shows changes in summary and total capital during 1985, 1984 and 1983.

Summary of Changes in Capital for 1985, 1984 and 1983

$ in millions (Totals may not add due to rounding)	1985	1984	1983
Primary Capital at Beginning of Year	$5,580	$4,486	$3,848
Primary Capital Generated from Internal Sources			
Retained Earnings (Net of FX Translation)	332	200	248
Net Change in Reserve for Possible Loan Losses	122	132	6
Total Primary Capital from Internal Sources	454	332	254
Primary Capital Generated from External Sources			
Floating Rate Series F Preferred Stock	—	227	—
Reserve for Possible Loan Losses of Acquired Subsidiaries	24	65	—
Net Gain on Retirement of Series B and C Preferred Stock	—	28	—
Promise to Equalize Floating Rate Notes Due 1995—Payment to Note Fund	(37)	(33)	—
—Net of Note Fund	—	—	342
Floating Rate Subordinated Notes Due 1996	(54)	346	—
Common Stock Issued Pursuant to:			
Floating Rate Subordinated Notes Due 1996	34	20	—
Acquisition of Lincoln	—	19	—
Conversion of Convertible Notes and Debentures	27	8	15
Dividend Reinvestment Plan	39	33	26
Exercise of Stock Options	4	—	1
Minority Interest in Consolidated Subsidiaries	—	(1)	—
Total Primary Capital from External Sources	56	762	384
Net Primary Capital Generation	$110	1,094	638
Primary Capital at Year-end	$6,090	$5,580	$4,486
Secondary Capital at Beginning of Year	$1,527	$1,034	$1,046
Retirement of Series B and C Preferred Stock	—	(88)	—
Long-Term Debt of Acquired Subsidiaries	—	114	—
Issuance of Notes and Debentures	462	886	350
Accretion on Zero Coupon Notes	9	8	7
Exchanges and Conversions	(27)	(8)	(15)
Repurchases and Retirement of Notes	(10)	(26)	—
Foreign Exchange Translation Adjustments	52	(30)	(9)
Long-Term Notes Excluded from (Included in) Primary Capital	73	(363)	(347)
Net Change in Secondary Capital	559	493	(12)
Secondary Capital at Year-end	$2,086	$1,527	$1,034
Total Capital at Beginning of Year	$7,107	$5,520	$4,894
Net Capital Additions	1,069	1,587	626
Total Capital at Year-end	$8,176	$7,107	$5,520

The following table shows the year-end primary capital and total capital accounts for 1985, 1984 and 1983.

Primary and Secondary Capital[1]

$ in millions	December 31 1985	1984	1983
Primary Capital			
Common Stockholders' Equity	$3,795	$3,359	$3,051
Minority Interest in Consolidated Subsidiaries	3	3	4
Common Stock Equity Contracts	150	150	150
Promise to Equalize Floating Rate Notes Due 1995 (Net of Note Fund)	270	309	342
Floating Rate Subordinated Notes Due 1996[2]	362	396	—
Reserve for Possible Loan Losses	908	761	564
Nonredeemable Preferred Stock	602	602	375
Total Primary Capital	6,090	5,580	4,486
Secondary Capital			
Redeemable Preferred Stock	62	62	150
Long-Term Notes and Debentures	2,606	2,329	1,376
Long-Term Notes Included in Primary Capital	(782)	(863)	(492)
Total Secondary Capital	2,086	1,527	1,034
Total Capital	$8,176	$7,107	$5,520

[1] Federal Reserve Board definition revised May 1985. Primary capital consists of common stockholders' equity, minority interest in equity of consolidated subsidiaries, perpetual preferred stock, mandatory convertible securities (including mandatory stock purchase contracts) and the reserve for possible loan losses. Secondary capital consists of limited life preferred stock and long-term debt.

[2] Principal amount less value of interest paid in shares of common stock of the Company.

Selected ratios monitored by management are shown below.

Selected Capital Ratios

	December 31 1985	1984	1983
Primary Capital as a Percent of:			
Loans	9.03%	9.00%	8.03%
Risk Assets[3]	7.93	8.65	6.83
Total Gross Assets[4]	6.87	6.37	5.44
Total Capital as a Percent of:			
Loans	13.20	11.46	9.88
Risk Assets[3]	10.11	8.72	7.18
Total Gross Assets[4]	9.23	8.11	6.69
Common Stockholders' Equity as a Percent of Total Gross Assets[4]	4.28	3.83	3.70
Total Stockholders' Equity as a Percent of Total Gross Assets[4]	5.03	4.59	4.34
Total Preferred Stock as a Percent of Common Stockholders' Equity	17.49	19.77	17.21
Mandatory Convertible Securities as a Percent of Other Primary Capital	14.73	18.10	12.22

[3] Risk Assets are defined as Total Gross Assets less Cash and Due from Banks and U.S. Treasury and Federal Agency Securities.

[4] Total Gross Assets are defined as Total Assets plus the Reserve for Possible Loan Losses.

In January 1986, the Board of Governors of the Federal Reserve System issued, and requested comments on, a new proposal for risk-based Primary Capital Guidelines. These guidelines would replace proposed guidelines, which incorporate some off-balance sheet commitments, and be used in conjunction with the current primary capital: primary capital to total gross assets guideline to determine minimum capital requirements. Since the initial Federal Reserve release has not examined risk-based capital guidelines, the impact of the proposal cannot be explicitly determined. However, Chase's management believes that Chase's capital is fully adequate and that it would continue to be so under the newly proposed risk-based capital guidelines, if adopted.

Loan Portfolio

Chase's loan portfolio was $61.9 billion at year-end 1985 and $62.0 billion at year-end 1984. Average loan balances were $61.5 billion in 1985, a $1.8 billion increase from $59.7 billion in 1984. The average rate earned, on a taxable-equivalent basis, on the loan portfolio during 1985 was 11.83% compared with 12.99% for 1984.

Chase continued to expand its capacity to sell loans through its Asset Sales Program. The sales volume of short- and medium-term loans exceeded $24 billion in 1985, up from $3 billion in 1984. At year-end 1985, total assets were reduced by loan sales of approximately $2.4 billion compared with $2.1 billion at year-end 1984. Asset Sales enable Chase to more competitively meet customer credit needs while functioning as a financial intermediary between suppliers and users of funds.

Chase's loan portfolio in domestic offices increased from $[illegible] billion at year-end 1984 to $27.9 billion at year-end 1985. The increase was largely due to the increased loan volume experienced in the domestic consumer sector, primarily because of Chase's consumer marketing thrust. At year-end 1985, Chase's domestic consumer loans for personal expenditures were $7.4 billion, up 39% from $5.3 billion at year-end 1984. The average interest rate earned on domestic consumer loans for personal expenditures was 15.70% for 1985, compared with 16.32% for 1984.

The consumer financial products provided by Chase include credit card activities, revolving credit lines, guaranteed student loans, cash reserve checking, installment loans and 1-4 family residential mortgage loans. Chase has several subsidiaries which offer these credit products and services to consumers. Among these are Chase U.S. Consumer Services, Inc. and its subsidiaries (CUSCS) which establish direct relationships with consumers in selected markets throughout the United States. CUSCS's network has been expanded to comprise 25 locations in 11 states at year-end 1985, with loans of approximately $855 million compared with $410 million at year-end 1984. In 1985, the recently formed Chase Auto Leasing Corporation was transferred from The Chase Manhattan Bank, N.A. to CUSCS, with loans of approximately $70 million at year-end 1985. The Chase Manhattan Bank (USA), N.A. (Chase (USA)), a banking subsidiary in Delaware, provides consumer credit and deposit products nationwide through direct mail marketing. At December 31, 1985, Chase (USA) had outstanding consumer loans of $4.6 billion, an increase of approximately $2.7 billion compared with the previous year-end. Included in this increase was approximately $920 million in credit card loans at year-end 1985 as a result of the transfer of the VISA portfolio to Chase (USA) from The Chase Manhattan Bank, N.A. In the second and fourth quarters of 1985, Chase increased its consumer deposit base with the acquisition of several Ohio and Maryland thrift institutions which formed Chase Ohio and Chase Maryland, respectively. At December 31, 1985, Chase Ohio and Chase Maryland had outstanding consumer loans of approximately $170 million and $175 million, respectively. Statements of condition for Chase (USA), Chase Ohio and Chase Maryland are on page 73.

Domestic consumer mortgage loans for 1-4 family housing were $2.7 billion at year-end 1985, up approximately $747 million compared with the previous year-end. The average rate earned on these 1-4 family mortgage loans was 10.76% in 1985, compared with 12.02% in 1984.

Lease financings in domestic offices aggregated $1.5 billion at December 31, 1985, compared with $1.0 billion at December 31, 1984. In 1985, lease financings in domestic offices averaged approximately $1.1 billion compared with approximately $800 million for 1984. This growth is the result of Chase's strategic thrust in this important business segment. For 1985, the average interest rate earned, on a taxable equivalent basis, on domestic lease financings was 11.71% compared with 11.22% for 1984.

Real estate loans, excluding 1-4 family mortgages, in domestic offices aggregated $3.7 billion at December 31, 1985, compared with $3.1 billion at December 31, 1984. In 1985, such real estate loans in domestic offices averaged approximately $3.1 billion compared with approximately $2.8 billion for 1984. For 1985, the average interest rate earned on these domestic real estate loans was 10.94% compared with 12.92% for 1984.

At year-end 1985, the balance of commercial and industrial loans in domestic offices was $3.8 billion, compared with $10.0 billion at year-end 1984. The year-end to year-end decline in commercial and industrial loan volume is primarily attributable to refinancings by corporate borrowers in the external markets and to the Asset Sales Program. Chase's prime rate averaged 9.93% for 1985, compared with 12.04% for 1984 and 10.78% for 1983. Included in average loans in overseas offices was approximately $5.6 billion of loans to U.S. commercial borrowers, compared with $5.5 billion of such loans for 1984. During 1985, the average balance of loans which were exempt from U.S. federal income taxes, principally loans to state and political subdivisions, was $1.2 billion, up approximately $400 million from 1984. The average rate earned on these loans, on a taxable equivalent basis, was approximately 14% and 17% for 1985 and 1984, respectively.

Chase's loan volume in overseas offices decreased from $32.1 billion at year-end 1984 to $31.0 billion at year-end 1985. On an average basis, loans recorded in overseas offices, excluding approximately $5.6 billion of loans to domestic obligors, accounted for 50% of Chase's total loan portfolio for 1985, compared with 53% for 1984. The average yield on loans booked in Chase's overseas offices was 11.61% for 1985, compared with 12.91% for 1984 and 12.12% for 1983. Real estate loans in overseas offices totaled $2.8 billion at year-end 1985, of which approximately $1.5 billion, or 53%, was for 1-4 family mortgages. At year-end 1985, foreign currency denominated loans constituted approximately 35% of total overseas loans. A breakdown by type of loans recorded in overseas offices at year-end 1985 is presented on page 73.

The following table sets forth the distribution of domestic and international loans at December 31, 1985 and 1984, based on the domicile of the obligors.

Loans Based on Domicile of Obligors—Year-end ($ in millions)	1985	1984
Domestic Loans		
Recorded in Domestic Offices	$27,510	$24,390
Recorded in Overseas Offices	5,010	5,750
Total Domestic Loans	32,520	30,140
International Loans		
Recorded in Domestic Offices	400	420
Recorded in Overseas Offices	29,010	31,440
Total International Loans	29,410	31,860
Total Loans	$61,930	$62,000

Average international loans, based on the domicile of the obligor, including loans to foreign obligors booked in domestic offices, were $322 billion in 1985, down 1% from the $327 billion in 1984. A breakdown of average international loans, by type of borrower, for the three most recent years follows:

Average International Loans—By Type

In millions, based on month-end balances	1985	1984	1983
Commercial and Industrial Loans	$20,410	$20,780	$20,560
Loans to Banks	3,310	3,930	4,260
Loans to Foreign Governments and Official Institutions	3,910	3,800	2,290
Real Estate Loans	1,810	1,570	1,160
Loans to Other Financial Institutions	640	770	810
Loans to Individuals for Personal Expenditures	1,120	840	490
Lease Financings	260	180	120
Other Loans	970	980	1,160
Total International Loans, Gross	$32,430	$32,850	$30,870
Less: Unearned Discount	190	150	130
Total International Loans	$32,240	$32,700	$30,740

Schedules on Selected Loan Maturities and Sensitivity to Changes in Interest Rates and on year-end and average loan balances by type are presented on pages 72 and 73.

Risk Elements

Risk elements in the portfolio are described in the Country Risk, the Non-accrual, Restructured Loans and Past Due Loans, and the Loan Concentrations sections as follows:

Country Risk

International lending requires not only the normal credit analysis associated with the decision to extend financing to a particular customer but also an assessment of "country risk." Country risk arises from economic, social and political factors that might affect a borrower's ability to repay in the currency of the loan. Cross-border loans are those which borrowers must repay in a currency other than their local currency or to a lender in a different country. One of the important factors associated with cross-border lending is the possibility that a country's foreign exchange reserves may be insufficient to permit timely repayment of cross-border loans by borrowers domiciled in that country, even if borrowers possess sufficient local currency. In addition, foreign government decisions and other related events can affect business activities in a country and an client's ability to repay its loans.

Chase has a systematic country assessment process by which it analyzes and monitors the political, social and economic environment in all the countries in which it conducts business or in which its borrowers reside. These in-depth assessments, performed by a team of economists and political analysts in conjunction with local Chase management, are utilized by Chase within its planning cycle for such countries as well as in Chase's system of managing total country exposure.

The following two tables illustrate Chase's policy of portfolio diversification by which exposures are spread over a wide spectrum of geographic regions, individual countries and economic structures. The first table presents the distribution of international loans by country classification, including loans at overseas offices and international loans booked at domestic offices, based on the domicile of the ultimate obligor, at December 31, 1985, 1984 and 1983, respectively. As evidenced by the table, the majority of Chase's exposure is to borrowers in various industrial countries and countries classified as primary product exporters. The distribution by classification has not substantially changed over the three-year period.

Structure of International Loans by World Economic Development[1]

	1985					1984			1983		
		Foreign Currency Loans									
	Local Currency	Original Maturity Under 1 Year	Original Maturity Over 1 Year	Translatability US $	Total	Local Currency	Foreign Currency Translatability US $	Total	Local Currency	Foreign Currency Translatability US $	Total
Industrial Countries	$6,990	$2,200	$3,360	$5,700	$ 11,750	$6,030	$ 7,350	$14,030	$4,640	$ 8,030	$ 13,270
Centrally Planned Economies	—	—	30	30	30	—	70	70	—	90	90
Other Countries											
Fuel Exporters	120	1,300	2,740	4,040	4,160	120	4,380	4,500	90	4,250	4,340
Primary Product Exporters	850	1,600	4,190	5,790	6,640	790	6,060	6,850	850	5,800	6,650
Exporters of Manufactures	1,440	950	950	1,900	2,850	1,340	1,650	2,990	1,100	1,540	2,640
Services and Commerce	140	190	590	780	920	140	950	1,090	130	900	1,030
Total	$9,540	$6,270	$12,860	$19,130	$25,390	$8,540	$20,460	$29,000	$6,810	$21,550	$28,360

[1] Country classifications are based on international bank fund definitions, except for centrally planned economies and certain territories and dependencies which do not maintain independent foreign exchange reserves.

The second table shows those countries in which Chase had cross-border outstandings which exceed 1% of [illegible] total assets at December 31, 1985, 1984 and 1983, respectively, including a breakdown by type of borrower within each country.

Cross-Border Outstandings Which Exceed 1% of Total Assets

$ in millions

As of December 31,	Country Name	Total Outstandings	% of Total Assets	Governments and Official Institutions	Banks and Other Financial Institutions	Commercial and Industrial	Other Borrowers	Other Outstandings
1985	Japan	$3,020	3.4%	$ —	$1,270	$1,450	$120	$180
	Brazil	2,820	3.2	500	700	1,380	120	120
	United Kingdom	2,740	3.1	460	680	1,270	170	160
	Mexico	1,680	1.9	320	490	840	110	80
	West Germany	1,420	1.6	110	340	870	100	80
	Venezuela	1,250	1.4	190	210	800	80	70
	France	930	1.1	10	470	280	100	70
	Argentina	920	1.1	180	120	580	10	30
1984	Japan	2,980	3.4	50	1,180	1,660	80	10
	United Kingdom	2,840	3.3	450	820	1,420	160	410
	Brazil	2,830	3.3	440	800	1,280	130	180
	Mexico	1,750	2.0	340	440	860	80	30
	West Germany	1,690	1.9	110	380	1,160	120	80
	France	1,380	1.6	180	560	640	80	20
	Venezuela	1,280	1.5	180	230	810	40	20
	Korea	1,230	1.4	10	340	680	110	90
1983	Japan	4,870	6.0	80	2,660	2,110	70	50
	United Kingdom	3,130	3.8	280	1,410	1,290	80	280
	Brazil	2,560	3.1	320	740	1,240	80	180
	France	2,120	2.6	60	1,490	410	110	50
	West Germany	1,920	2.3	110	440	1,280	180	20
	Mexico	1,550	1.9	280	280	860	10	60
	Korea	1,340	1.6	140	740	660	10	10
	Venezuela	1,220	1.5	140	220	780	80	10
	Italy	1,220	1.5	20	770	370	50	10
	Canada	970	1.2	10	450	470	30	10

Note: Cross-border outstandings are defined for the purpose to include: total loans including accrued interest, acceptances, interbank placings, other interest-bearing investments, and any other monetary assets denominated in dollars or other non-local currency. Government entities that are majority-owned are classified by type of borrower based on the industry of the business enterprise.

The following table presents those countries in which Chase had cross-border outstandings of between .75% and 1% of its total assets at year-end 1985, 1984 and 1983.

Cross-Border Outstandings Between .75% and 1% of Total Assets

	December		
($ in millions)	1985	1984	1983
.75% through 1% Range	$655 to $830	$650 to $870	$610 to $820
Countries	Korea	Argentina Indonesia Italy	Argentina Australia Hong Kong Indonesia
Total Outstandings	$840	$1,250	$1,240

Because of slowing growth in the industrialized countries, particularly the United States, and declining commodity prices, exports from the heavily-indebted developing countries showed little tendency to increase in 1985. There was thus some reduction in the overall trade surplus of the heavily-indebted developing countries last year. The flow of new bank credits to these countries also declined. To address this situation, at the joint annual meeting of the International Monetary Fund (IMF) and the International Bank for Reconstruction and Development (IBRD), the U.S. Government proposed a Program for Sustained Growth, an initiative aimed at strengthening the international debt strategy to improve prospects for growth in the debtor countries.

Throughout 1985, Chase continued its close cooperation with the international banking community, the IMF, the IBRD and other multilateral organizations in addressing the debt service problems of Latin American and other countries. The recent U.S. initiative is aimed at consolidating the efforts of each of these countries with those of both creditor and debtor countries in building stronger economies and arriving at resolution of debt service difficulties. Despite the close cooperation and efforts to resolve these payment difficulties, as long as uncertainties with respect to these countries remain, it is possible that additional amounts of Chase's cross-border outstandings could be placed in or returned to a nonaccrual status.

The following section discusses recent developments in the principal rescheduling countries in which [illegible] as cross-border outstandings exceeding 1% of its total assets.

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Brazil

At December 31, 1985, Chase's cross-border outstandings in Brazil were approximately $2.8 billion, including extensions of credit to public and private sector borrowers of approximately $1.7 billion and $1.0 billion, respectively, compared with $1.5 billion and $1.2 billion, respectively, at December 31, 1984. Approximately 17% of Chase's Brazilian cross-border outstandings at December 31, 1985, was related to short-term trade financing.

At the request of the Central Bank of Brazil, international commercial banks agreed to extend the term of the $9.8 billion (Chase share $371 million) facility for trade finance and the $5.4 billion (Chase share $118 million) of interbank deposits, which were part of the 1984 financing package, through January 17, 1986. The Central Bank of Brazil also advised international commercial banks of interim measures it placed in effect with respect to commercial bank cross-border medium-term debt maturing after January 1, 1985, up to and including January 17, 1986. Borrowers were instructed to deposit the cruzeiro equivalent of principal payments falling due during that period in the Central Bank of Brazil. Subject to payment being made, the Central Bank has opened interest-bearing, U.S. dollar denominated, deposit accounts in the amount of the principal maturity in favor of the lender and guaranteed by the Federal Republic of Brazil.

The Bank Advisory Committee for Brazil and the Brazilian authorities continued to discuss the possible terms pertaining to the restructuring of the 1985 maturities as well as new trade and interbank facilities. While progress has been made, agreement was not reached before the expiration of the interim measures described above. On January 18, 1986, the Government of Brazil and the Central Bank advised the Bank Advisory Committee of an extension of the above interim arrangements to cover medium-term debt maturing on or after January 18, 1986, and on or before March 15, 1986, and requested its creditor banks to continue to maintain trade and deposit outstandings at the level of their previous commitments. The Bank Advisory Committee, of which Chase is a member, supports the continuance of these interim arrangements and has requested the international banking community to do likewise.

The Bank Advisory Committee and the Central Bank of Brazil will prepare a proposal to be sent to all creditor banks before March 15, 1986, encompassing the restructure of the 1985 maturities and arrangements for the interim deposit of 1986 maturities (both of which may eventually be included in a multi-year debt restructuring) and maintenance of trade and interbank facilities through 1986. The Government of Brazil and the Central Bank have also requested that interest rates on the 1985 and 1986 interim deposits be adjusted retroactively from the effective date of the restructuring through January 18, 1986, to reflect the interest rates eventually agreed upon for the restructured debt provided that a specific proposal is issued to the international banking community by March 15, 1986, and that such rates are specified in it.

In 1985, Chase reported total income on cross-border outstandings to Brazilian borrowers of approximately $342 million. During 1985, approximately $345 million in interest payments was received in cash.

No material principal payments were received during 1985 on cross-border outstandings to Brazilian borrowers other than approximately $250 million pursuant to the interim deposit arrangement described above.

The amount of Chase's cross-border nonaccrual loans to borrowers in Brazil at December 31, 1985, was approximately $7 million. This amount is included in the table on page 37. The negative impact of these nonaccrual loans on Chase's net income for the year ended December 31, 1985, was insignificant.

In light of continuing uncertainties regarding Brazil, it is possible that additional amounts of Chase's cross-border outstandings to borrowers in Brazil could be placed in nonaccrual status.

Mexico

At December 31, 1985 and 1984, Chase's cross-border outstandings in Mexico aggregated approximately $1.7 billion, included in this amount were extensions of credit to public and private sector borrowers of approximately $1.3 billion and $400 million, respectively.

Multi-Year Debt Restructuring agreements have been entered into and signed for Mexico and encompass: a) an amendment of the 1983 $5.0 billion new money Credit Agreement with Mexico and a prepayment of $1.2 billion principal amount (Chase share $30 million) loaned thereunder, b) the multi-year restructure of maturities of Mexican public sector debt to commercial banks falling due in 1985 through 1990 (approximately $20.1 billion), c) the extension of the 1987 through 1990 maturities (approximately $23.6 billion) under the existing restructure agreements negotiated in 1982 and d) adjustment of interest rates on the restructured debt. The effect of the Debt Restructuring would be to reduce the amounts of maturities falling due during 1985-1990 and to establish a more manageable amortization schedule beginning in 1986 and ending in 1998. The documentation necessary to implement the Debt Restructuring was completed and signed but has not yet become effective.

In March 1985, prepayment was made of $250 million (Chase share $6 million) of the amount loaned under the 1983 $5.0 billion new money Credit Agreement with Mexico as amended in 1985. In October 1985, at the request of the Mexican Government, payment of the remaining $950 million balance (Chase share $24 million) was extended for six months.

The interest rate adjustments, which are to be effective retroactive to January 1, 1985, will result in a change in the interest rate on Chase's approximately $930 million share (after the estimated remaining prepayment of approximately $24 million) in the Multi-Year Debt Restructuring. Approximately $665 million of Chase's share currently carries a weighted average spread of approximately 1⅛% over the prevailing prime rate and approximately $265 million currently carries a weighted average spread of approximately ⅞% over the London Interbank Offered Rate (LIBOR). Following the restructuring, the estimated weighted average spread on Chase's $930 million share will be approximately ⅞% over LIBOR for 1985, and Chase reported total income on its share on that basis in 1985. Under the terms of the restructuring, this estimated weighted average spread is scheduled to increase over time to 1⅛% over LIBOR in 1992 through 1998.

A 1984 $3.8 billion commercial bank loan (Chase share $100 million) is not included in the Multi-Year Debt Restructuring agreements. During 1985, Chase loaned the remaining $26 million of its share under this commitment at a spread of 1⅛% over prime.

During 1985, Chase's cross-border outstandings to public sector borrowers in Mexico were substantially unchanged at approximately $1.3 billion and were current as to payment of principal and interest. Chase reported approximately $129 million as income on such outstandings for the year ended December 31, 1985. During 1985, approximately $139 million in interest payments was received in cash. In 1985, Chase received minimal principal repayments on cross-border outstandings to Mexican public sector borrowers.

The amount of Chase's cross-border nonaccrual loans to Mexican private sector borrowers was approximately $123 million at December 31, 1985. This amount is included in the table on page 37. The negative impact of such nonaccrual loans on Chase's net income was approximately $2 million after taxes for the year ended December 31, 1985.

In light of continuing uncertainties regarding Mexico, including conditions currently prevailing in the world petroleum markets, it is possible that additional amounts of Chase's cross-border outstandings to borrowers in Mexico could be placed in nonaccrual status.

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Venezuela

At December 31, 1985 and 1984, Chase's cross-border outstandings in Venezuela aggregated approximately $1.3 billion, included in that amount were extensions of credit to public sector and private sector borrowers totaling approximately $900 million and $400 million, respectively.

The Government of Venezuela and the Bank Advisory Committee of Venezuela completed negotiation of the terms of restructuring agreements covering the proposed restructuring of approximately $21.2 billion of Venezuelan public sector debt. The restructuring agreements call for a down payment of approximately $730 million (Chase share approximately $26 million) and the restructuring of all maturities falling due between March 22, 1983, and December 31, 1988. The remaining approximately $20.5 billion principal would be repaid over a 12-year period ending on June 30, 1997. The restructuring agreements have been distributed to the international banking community. Approximately $800 million of Chase's cross-border outstandings to the Venezuelan public sector would be restructured under these agreements. The restructured principal will be repriced on the effective date of the restructuring and the effect on Chase will be approximately as follows:

Principal Amount ($ in millions)	Average Interest Rate* Before Restructuring	Interest Rate After Restructuring
$600	Prime plus 2.61%	LIBOR plus 1.25%
200	LIBOR plus 1.29%	

*At December 31, 1985, weighted by principal outstanding.

At December 31, 1985, Chase's cross-border Venezuela public sector loans were current as to payment of principal and interest. The following table compares the amount of interest income reported in 1985 related to the principal to be restructured with that which would have been reported on a pro forma basis had that principal been restructured as of January 1, 1985:

($ in millions)

Principal to be Restructured	Actual Interest Income Reported	Pro Forma Interest Income Accrual Basis After Restructuring
$900	$86	$77

Chase reported total income on cross-border outstandings to Venezuelan public and private sector borrowers of $136 million for the year ended December 31, 1985. Of this amount, $86 million related to the principal to be restructured. During 1985, Chase received $141 million in interest payments in cash on cross-border outstandings to borrowers in Venezuela. Minimal principal payments were received during the year ended December 31, 1985.

The amount of Chase's cross-border nonaccrual loans to private sector borrowers in Venezuela was approximately $200 million at December 31, 1985, compared with $95 million at December 31, 1984. This amount is included in the table on page 37. The negative impact of such nonaccrual loans on Chase's net income for the year ended December 31, 1985, was approximately $4 million after taxes.

In light of continuing uncertainties regarding Venezuela, including conditions currently prevailing in the world petroleum markets, it is possible that additional amounts of Chase's cross-border outstandings to borrowers in Venezuela could be placed in nonaccrual status.

Argentina

At December 31, 1985, Chase's cross-border outstandings in Argentina aggregated approximately $920 million, compared with $845 million in 1984. Included in the 1985 amount were extensions of credit of approximately $600 million and $300 million, respectively, to public and private sector borrowers, compared with $520 million and $300 million at December 31, 1984. Approximately $333 million and $125 million, respectively, of principal maturities owing to Chase from public and private sector borrowers would be rescheduled under the Argentine Republic 1984-1985 Financing Plan (Financing Plan).

The Financing Plan was signed in August 1985 and provides for: a) a new ten-year $3.7 billion term credit facility and $500 million four-year trade and deposit facility (Chase share $129 million and $18 million, respectively), b) the restructure of principal maturities of public sector debt originally falling due during 1982 through 1985 over a 10- to 12-year period (Chase share $333 million), c) the restructuring of maturities over a ten-year period of private sector indebtedness originally due in 1984 and 1985, together with certain 1982 and 1983 maturities not already covered by existing agreements (Chase share $125 million), d) committed one-year facilities for trade financing (Chase share $20 million) and e) one-year agreements to maintain interbank outstandings (Chase share $53 million).

The principal to be restructured was repriced under the Financing Plan and the effect on Chase was approximately as follows:

Principal Amount ($ in millions)	Average Interest Rate* Before Restructuring	Interest Rate After Restructuring
$404	LIBOR plus 2.14%	LIBOR plus 1.37
54	Prime plus 1.55%	

*At December 31, 1985, weighted by principal outstanding.

On September 30, 1985, the Argentine Central Bank repaid the $750 million (Chase share $29 million) which was outstanding under the 1983 $1 billion bridge loan, which was guaranteed by the Republic of Argentina, and drew down $1.7 billion (Chase share $59 million) of the new $3.7 billion ten-year term credit facility and all of the new $500 million (Chase share $18 million) four-year trade and deposit facility. An additional $200 million (Chase share $29 million) was disbursed under the $3.7 billion ten-year term credit facility in the fourth quarter of 1985.

Other than the $29 million repaid by the Argentine Central Bank under the bridge loan, Chase received minimal principal payments on cross-border outstandings to Argentine borrowers in 1985.

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During 1985, Chase's cross-border outstandings to borrowers in Argentina increased approximately $75 million. Chase reported total income on cross-border outstandings to Argentine borrowers of $116 million for the year ended December 31, 1985. Of that amount, $59 million of interest income (including $10 million of past due interest applicable to the prior year) related to principal to be restructured under the Financing Plan. During 1985, Chase received $118 million in interest payments in cash on cross-border outstandings to Argentine borrowers.

The following table compares the amount of interest income reported in 1985 related to the principal to be restructured with that which would have been reported on a pro forma basis had the principal to be restructured been on a full accrual basis in 1985 and that which would have been reported had that principal been restructured as of January 1, 1985:

($ in millions)			
Principal to be Restructured	Actual Interest Income Reported	Pro forma Interest Income Assuming Full Accrual Basis	
		Before Restructuring	After Restructuring
$458	$59	$49	$45

Cross-border nonaccrual loans to Argentine borrowers decreased by $410 million to approximately $155 million at year-end 1985 from $565 million at year-end 1984.

Nonaccrual loans to Argentine borrowers are included in the accompanying table. The decrease in cross-border nonaccrual loans reflects the $29 million principal payment in September and the approximately $380 million of loans to public sector borrowers which was returned to accrual status in the fourth quarter of 1985. The remaining approximately $155 million in cross-border nonaccrual loans is to Argentine private sector borrowers. The impact of nonaccrual loans to Argentine borrowers on Chase's net income for the year ended December 31, 1985, was insignificant.

In light of continuing uncertainties regarding Argentina, it is possible that additional amounts of Chase's cross-border outstandings to borrowers in Argentina could be placed in nonaccrual status.

Nonaccrual, Reduced Rate and Past Due Loans

Nonaccrual loans, on which interest income accruals have been suspended, and reduced rate loans, on which interest income is accrued at a rate lower than that originally contracted, totaled $2.0 billion at year-end 1985 and $2.2 billion at year-end 1984. Nonaccrual loans attributable to international lending activities, primarily in Latin America, decreased $166 million, partially offset by an increase of $36 million in domestic nonaccrual loans. Cross-border loans to Argentine public sector borrowers of approximately $380 million were returned to accrual status in the fourth quarter of 1985.

Chase's policy is to discontinue the accrual of interest income on loans, other than consumer loans, where reasonable doubt exists as to timely collectibility, or if payment of principal or interest is contractually past due 90 days or more and the loan is not well secured and in the process of collection. Past due consumer loans are generally charged off according to an established delinquency schedule which does not exceed 180 days.

The following table sets forth the distribution of nonaccrual and reduced rate loans based on the domiciles of the obligors.

Nonaccrual and Reduced Rate Loans

	December 31				
($ in millions)	1985	1984	1983	1982	1981
Nonaccrual Loans:					
Domestic Loans:					
Real Estate Loans	$ 199	$ 174	$ 133	$ 64	$ 64
Loans to financial institutions	7	7	7	45	37
Commercial and industrial loans	551	540	631	433	222
Other loans	17	17	19	9	3
Total Domestic Loans	774	738	790	551	326
International Loans:					
Real Estate Loans	51	65	89	116	65
Loans to Governments and Official Institutions	93	170	26	7	9
Loans to Banks and Other Financial Institutions	104	87	68	77	25
Commercial and Industrial Loans	949	1,053	775	456	154
Other Loans	34	22	21	10	66
Total International Loans	1,231	1,397	979	666	319
Total Nonaccrual Loans	$2,005	$2,135	$1,769	$1,217	$ 645

	December 31,				
($ in millions)	1985	1984	1983	1982	1981
Reduced Rate Loans:					
Domestic Loans:					
Real Estate Loans	$ 4	$ 17	$ 25	$ 109	$ 151
Loans to financial institutions	7	1	54	61	59
Commercial and industrial loans	19	9	7	1	37
Total Domestic Loans	30	27	86	171	247
International Loans:					
Real Estate Loans	—	—	—	6	—
Loans to Governments and Official Institutions	—	1	—	17	15
Commercial and Industrial Loans	—	4	15	16	—
Total International Loans	—	5	15	39	15
Total Reduced Rate Loans	$ 30	$ 32	$ 101	$ 210	$ 262
Total Nonaccrual and Reduced Rate Loans	$2,035	$2,167	$1,970	$1,427	$ 907
—as a % of Total Loans	3.3%	3.5%	3.3%	2.6%	1.8%

The decrease in the negative impact of nonaccrual and reduced rate loans for 1985 compared with 1984, as set forth in the following table, resulted primarily from lower interest rates.

Negative Impact of Nonaccrual and Reduced Rate Loans

	Total Loans		Domestic Loans		International Loans	
$ in millions	1985	1984	1985	1984	1985	1984
Interest Income Which Would Have Been Recorded Under Original Terms	$224	$278	$ 83	$ 85	$141	$193
Interest Income Actually Reported	105	122	18	21	87	101
Reduction in Interest Income:						
Before Applicable Taxes	$119	$156	$ 65	$64	$ 54	$ 92
After Applicable Taxes	58	76	32	27	26	46

Accruing loans which are contractually past due 90 days or more are loans which are both well secured or guaranteed by financially responsible third parties and are in the process of collection. The amount of accruing loans past due 90 days or more at year-end 1985, 1984 and 1983, including $113 million, $68 million, and $43 million, respectively, of consumer loans, is presented in the accompanying table.

Accruing Loans Past Due 90 Days or More	December 31			
($ in millions)	1985	1984	1983	1982
Domestic Loans	$136	$ 93	$ 60	$ 86
International Loans	75	99	75	113
Total Accruing Loans Past Due 90 Days or More	$211	$192	$135	$199

Chase's policy, similar to that of most major bank holding companies, is to discontinue the accrual of interest income on loans as to which reasonable doubt exists with respect to the timely collectibility of interest or principal. Where there are "serious doubts" as to the ability of the borrower to comply with present loan repayment terms, such loans also are placed in nonaccrual status. With respect to loans which are current as to payments of principal and interest but have a somewhat higher than normal risk of becoming nonaccrual or reduced rate in the near future, Chase would estimate such loans as totaling approximately $270 million, or .4% of total loans, at year-end 1985, compared with $205 million, or .3%, at year-end 1984. At December 31, 1985, approximately $185 million of these loans was owed by domestic borrowers and approximately $85 million was owed by international borrowers. In addition, in connection with the acquisition of troubled thrift institutions (formed into Chase Maryland), approximately $113 million of investments in and advances to real estate related entities was acquired. These transactions were recorded at estimated net realizable values at date of acquisition. Consistent with past experience, Chase anticipates that some loans in nonaccrual or reduced rate status at year-end 1985 will be returned to accrual status or be repaid in 1986.

As shown below, real estate properties acquired in satisfaction of loans, which are included in other assets, increased $10 million, from $90 million at year-end 1984 to $100 million at year-end 1985.

Analysis of Changes in Real Estate Properties Acquired in Satisfaction of Loans

$ in millions	1985	1984	1983	1982	1981
Balance at Beginning of Year	$ 90	$70	$103	$ 84	$136
Increases:					
Consolidation of Acquired Subsidiaries	3	24	—	—	—
Foreclosures, Asset Swaps and Other, Net	47	76	23	57	9
Advances	1	5	—	—	3
Decreases:					
Dispositions and Write-downs	41	85	56	38	64
Balance at End of Year	$100	$90	$ 70	$103	$ 84

The net effect on earnings for the most recent five years resulting from operating expenses, net of related income, with respect to real estate properties acquired in satisfaction of loans is presented in the accompanying table:

Real Estate Properties Acquired in Satisfaction of Loans

($ in millions)	1985	1984	1983	1982	1981
Direct Operating Expenses Reported in Other Expenses	$12	$18	$ 18	$ 15	$ 15
Income (Net of Write-downs) Reported in Other Expenses	14	25	—	—	61
Income (Expenses) of Real Estate Properties Acquired, Net of Related Income	2	7	(18)	(15)	(21)
Income Tax (Benefit)	1	4	(9)	(7)	(10)
Net After-Tax Income (Expense)	$ 1	$ 3	$ (9)	$ (8)	$ (11)

In addition, approximately $43 million of other assets was acquired in satisfaction of loans during 1985 compared with $7 million in 1984. Operating expenses net of income earned from these other assets had a negligible impact on net income.

Loan Concentrations

On a global basis, no single industry group's aggregate borrowings from Chase exceeded 10% of the total loan portfolio at December 31, 1985.

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Investment Securities

Net gains from the sale of investment securities, included in noninterest income, were $98 million pre-tax ($49 million after taxes) in 1985, up substantially from $17 million and $25 million pre-tax ($8 million and $11 million after taxes) in 1984 and 1983, respectively. Included in the 1985 sales of investment securities were pre-tax gains on U.S. Treasury securities of $67 million, compared with $9 million and $16 million in 1984 and 1983, respectively. See Note 4 of Notes to Financial Statements for additional information on the Investment Securities Portfolio.

The following table presents the carrying values, estimated market values and yields of investment securities at year-end 1985, 1984 and 1983. Average balances, interest income and average interest rates earned for the past three years are presented on pages 68 and 69.

Investment Securities at December 31.

	1985					1984	1983
($ in millions)	Within 1 Yr.	After 1 but Within 5 Yrs.	After 5 but Within 10 Yrs.	After 10 Yrs.	Total	Total	Total
U.S. Treasury							
Carrying Value	$ 46	$1,389	$400	$ 4	$1,839	$1,735	$ 985
Market Value	47	1,446	410	4	1,907	1,748	983
Yield	10.91%	9.88%	9.11%	7.56%	9.73%	11.11%	11.60%
Federal Agency							
Carrying Value	$ 4	$ 263	$ 38	$ 25	$ 330	$ 193	$ 153
Market Value	5	272	38	23	338	193	137
Yield	11.21%	9.85%	10.03%	10.77%	9.92%	11.58%	9.53%
State and Political Subdivisions							
Carrying Value	$228	$ 592	$429	$1,161	$2,410	$2,103	$1,353
Market Value	225	592	424	1,051	2,292	1,863	1,316
Yield	10.41%	12.35%	13.84%	14.25%	13.35%	14.60%	13.26%
Other Bonds, Notes and Debentures							
Carrying Value	$433	$ 688	$224	$ 64	$1,409	$1,071	$ 587
Market Value	423	692	231	57	1,403	1,057	553
Yield	9.89%	8.15%	9.92%	8.72%	8.99%	8.89%	9.62%

Note: Interest income is adjusted for amortization of premium and accretion of discount and divided by total carrying value to derive the yields. Yields are stated on a taxable equivalent basis, applying a combined federal, state and local tax rate of approximately 51%, 59% and 60% in 1985, 1984 and 1983, respectively. The annualized taxable equivalent adjustments for the four maturity ranges shown above are approximately $10 million, $33 million, $28 million and $77 million, respectively. Average life for 1985—7 years and 2 months; 1984—7 years and 8 months; 1983—8 years and 2 months.

Included in the caption State and Political Subdivisions are investments in securities issued by New York State, New York City and their related agencies and independent authorities with carrying values totaling $613 million and $800 million at December 31, 1985 and 1984, respectively. The maturities and estimated market values of such New York obligations held in the investment portfolio at December 31, 1985, are set forth in the following table.

New York Investment Securities

	Carrying Value				
($ in millions)	Within 1 Year	After 1 but Within 5 Years	After 5 Years	Total	Estimated Market Value
Municipal Assistance Corporation	$—	$—	$269	$269	$295
Securities Issued or Guaranteed by or Obligating New York City	5	12	55	72	55
New York State and Financially Related Agencies	55	18	145	218	182
Revenue Obligations of Independent Authorities	3	11	40	54	47
Total	$63	$41	$509	$613	$579

Except for securities of the U.S. Government and of New York City and New York State, including their related agencies and independent authorities, there was no individual issuer whose investment portfolio securities exceeded 10% of Chase's Preferred Stock and Common Stockholders' Equity at December 31, 1985.

In 1982, the Company made a $50 million aggregate investment in preferred stock of Equimark Corporation and Equibank which it carried in its investment portfolio. The investment included an option to acquire Equibank, a Pittsburgh based bank doing business primarily in western Pennsylvania. In 1985, the Company disposed of its investment in preferred stock of Equimark for $25 million, terminated its option to acquire Equibank, agreed to a revision of the terms of its $25 million investment in preferred stock of Equibank to make it nonredeemable and received $2 million in cash and also warrants to acquire 4.9% of Equimark's common stock.

Interest-Bearing Deposits Placed with Banks

Chase places deposits with other banks, principally at overseas offices, primarily for earnings and liquidity purposes. Interest earned on these deposits decreased 37% from $769 million in 1984 to $486 million in 1985, primarily due to a decrease in the average interest rate earned from 11.03% to 9.48% and a decrease in the average balance of $1.9 billion from 1984. Year-end 1985 deposit balances placed with banks increased by approximately $300 million from the year-end 1984 level of $4.4 billion. The following table presents the maturity distribution of overseas deposit placings at December 31, 1985 and 1984.

Overseas Interest-Bearing Deposits Placed with Banks Time Remaining to Maturity

	December 31,	
($ in millions)	1985	1984
3 Months or Less	$3,700	$3,300
Over 3 through 6 Months	600	800
Over 6 through 12 Months	100	100
Over 12 Months	100	100
Total Overseas Interest-Bearing Deposits Placed with Banks	$4,500	$4,300

Deposits

Deposits represent Chase's principal source of funds. Chase's deposit base consists of demand deposits, certificates of deposit, savings and money market accounts and other time deposits. Total deposits were $61.4 billion at December 31, 1985, compared with $59.7 billion at year-end 1984. Total deposits averaged $60.2 billion for 1985, an increase of $1.6 billion from the 1984 average. Total domestic deposits increased approximately $3.7 billion from year-end 1984 to $32.6 billion at December 31, 1985, principally due to a substantial increase in money market deposits and other deregulated deposit accounts. Another factor contributing to the increase was the acquisition of Lincoln, accompanied by the subsequent promotion activities begun in 1984, for Chase's and Lincoln's downstate New York branch networks. These events have enabled Chase to increase the balance of its money market accounts and deregulated certificates of deposit to $12.4 billion at year-end 1985, up from $11.2 billion and $6.7 billion at year-end 1984 and 1983, respectively. This rapid growth in deregulated consumer deposits has increased the stability of Chase's overall deposit base. Since year-end 1983, the growth in these deposits primarily represented new funds for Chase. Total domestic deposit balances averaged $28.1 billion for 1985, compared with $24.3 billion for 1984. Chase's average overseas deposits decreased from $34.3 billion in 1984 to $32.1 billion in 1985. Overseas deposits were primarily in amounts in excess of $100,000 and represented deposits received principally from corporate and institutional customers.

Domestic Noninterest-Bearing Deposits

	December 31,		Daily Averages		
($ in millions)	1985	1984	1985	1984	1983
Gross Noninterest-Bearing Deposits	$13,500	$11,149	$9,822[a]	$8,843[a]	$8,731
Less: Due from Banks and Cash Items in the Process of Collection	4,114	2,901	2,864	2,870	3,015
Net Domestic Noninterest-Bearing Deposits	$ 9,386	$ 8,248	$6,958	$5,973	$5,716

[a] Includes approximately $635 million in 1985 and $325 million in 1984 of average deposits resulting from the 1984 mid-year consolidation of Lincoln.

Although cash items in the process of collection are reflected on a net basis in the preceding table, such items are included as assets and liabilities in Chase's financial statements on a gross basis. In recent years, there has been considerable discussion between the major banking institutions and the accounting profession with respect to the historical practice of treating cash items in the process of collection arising from checks credited to depositor accounts (termed "deposit float") as an asset and liability even though such credits are conditional upon the collection of the checks. Chase is of the opinion that this historical practice should be changed to provide for the reclassification of deposit float as an offset against deposits. Chase believes there is strong support for this position in both the banking community and the accounting profession and, therefore, is hopeful that the appropriate accounting and regulatory rule-making bodies will review this matter in 1986. The netting of domestic deposit float would have reduced Chase's total assets at December 31, 1985, by approximately $3.0 billion. If Chase netted deposit float, its year-end 1985 primary capital to total gross assets ratio would have been 7.11% rather than 6.87% and its return on average assets would have been .67% rather than .65%.

The balances and maturity distributions of certificates of deposit and other time deposits in denominations of $100,000 or more are presented in the following table.

Maturity Distribution of Time Deposits of $100,000 or More

	December 31, 1985		
($ in millions)	Certificates of Deposit	Other Time Deposits	Total
Domestic Offices:			
3 Months or Less	$2,790	$ 1,310	$ 4,100
Over 3 through 6 Months	410	80	490
Over 6 through 12 Months	160	20	180
Over 12 Months	150	280	430
Total Domestic Offices	$3,510	$ 1,690	$ 5,200
Total Overseas Offices	$2,130	$18,610	$20,740

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Funds Borrowed

Funds borrowed principally include federal funds purchased, securities sold under repurchase agreements, commercial paper, term federal funds, notes payable, including notes repayable at the option of their holders, and notes rediscounted by overseas offices.

Funds borrowed in 1985 averaged $11.4 billion, down 10% from $12.6 billion in 1984. Domestic average borrowings decreased 12%, primarily due to a decrease in federal funds purchased and securities sold under repurchase agreements, down approximately $526 million to an average of $4.6 billion.

Funds borrowed in overseas offices averaged approximately $1.4 billion in 1985, up from $1.3 billion in 1984. The average interest rate paid on these borrowings was 22.74% in 1985, compared with 20.97% in 1984. The increase of 177 basis points in the average rate paid in 1985 reflects the extraordinarily high level of local interest rates prevailing in certain South American countries. Further information on Chase's borrowings is presented in Note 10 of Notes to Financial Statements: Other Borrowed Money.

The following table summarizes Federal Funds Purchased and Securities Sold Under Repurchase Agreements, Commercial Paper of the Company and Term Federal Funds Purchased in 1985, 1984 and 1983.

Selected Funds Borrowed

($ in millions)	1985	1984	1983
Federal Funds Purchased and Securities Sold Under Repurchase Agreements			
Balance at End of Period	$4,132	$4,480	$3,741
Daily Average Balance Outstanding During Year	$4,804	$5,204	$6,116
Maximum Balance Outstanding as of Any Month-end During Year	$6,108	$5,675	$8,223
Daily Average Interest Rate During Year	9.61%	10.52%	9.07%
Average Interest Rate on Balance at End of Year	14.69%	8.70%	10.23%
Commercial Paper of the Company			
Balance at End of Period	$3,352	$4,341	$4,157
Daily Average Balance Outstanding During Year	$2,163	$3,824	$3,636
Maximum Balance Outstanding as of Any Month-end During Year	$4,115	$4,849	$4,473
Daily Average Interest Rate During Year	8.19%	10.47%	9.26%
Average Interest Rate on Balance at End of Year	7.83%	8.86%	9.75%
Term Federal Funds Purchased			
Balance at End of Period	$ 480	$ 384	$ 956
Daily Average Balance Outstanding During Year	$ 389	$ 680	$ 843
Maximum Balance Outstanding as of Any Month-end During Year	$ 562	$1,107	$1,121
Daily Average Interest Rate During Year	8.90%	11.17%	9.37%
Average Interest Rate on Balance at End of Year	9.49%	10.27%	9.85%

Fourth Quarter 1985 Versus Fourth Quarter 1984

Results of operations for the fourth quarters of 1985 and 1984 are shown in the table below.

Fourth Quarter Ended December 31,			
($ in millions)	1985	1984	Percentage Increase
Net Interest Income	$733	$654	12%
Provision for Possible Loan Losses	125	90	39
Other Operating Income	381	265	44
Other Operating Expenses	744	630	18
Income Taxes	94	79	20
Net Income	$151	$120	25%
Return on Average Assets	.69%	.55%	
Return on Average Common Stockholders' Equity	14.4%	11.4%	

Consolidated net income for the fourth quarter of 1985 was $151 million, compared with $120 million for the fourth quarter of 1984 and $149 million for the third quarter of 1985. In comparison with the fourth quarter of 1984, fourth quarter 1985 earnings included increased net interest income and higher other operating income, partially offset by increased operating expenses and a larger provision for possible loan losses.

Net interest income on a taxable equivalent basis for the fourth quarter of 1985 was $799 million, compared with $724 million for the fourth quarter of 1984. The increase in net interest income in the fourth quarter of 1985 was due substantially to the improved net interest rate spread of 4.25%, up 37 basis points from the 3.88% recorded in the fourth quarter of 1984. Interest-earning assets averaged $74.6 billion for the fourth quarter of 1985, compared with $74.2 billion for the fourth quarter of 1984.

The 1985 fourth quarter provision for possible loan losses was $125 million, compared with $90 million for the fourth quarter of 1984. Net loan charge-offs were $104 million and $59 million for the fourth quarters of 1985 and 1984, respectively. Domestic net loan charge-offs for the fourth quarter of 1985 were approximately $80 million, an increase of approximately $40 million over the fourth quarter of 1984. The increases in domestic net loan charge-offs were substantially attributable to expanding domestic consumer lending activities.

Other operating income for the fourth quarter of 1985 was $381 million, up 44% from the $265 million earned in the same period of 1984. Fee-based income was $262 million, compared with $203 million for the fourth quarter of 1984. Fourth quarter 1985 fee-based income included income from trust and fiduciary activities of $53 million, up 24% from the $43 million recorded in the same period of 1984 and fee income from investment banking activities which increased 129% compared with the same period in 1984. Foreign exchange trading income was $46 million, compared with $37 million for the fourth quarter of 1984. Profits from bond trading account activities were $11 million, compared with $14 million for the fourth quarter of 1984. Included in the fourth quarter 1985 other operating income was a $23 million pre-tax gain ($15 million after taxes) from the sale of real estate in Japan. Net pre-tax gains on sales of investment securities transactions were $20 million, compared with $6 million for the fourth quarter of 1984.

Other operating expenses for the fourth quarter of 1985 were $744 million, up $114 million, or 18%, compared with $630 million for the fourth quarter of 1984. Approximately $11 million of the fourth quarter increase related to acquisitions consummated in the latter half of 1985.

Summary of Significant Accounting Policies

The Chase Manhattan Corporation and Subsidiaries

Introduction

The following summary of the significant accounting policies of The Chase Manhattan Corporation (the Company) and its subsidiaries, including its principal subsidiary, The Chase Manhattan Bank, N.A., and its subsidiaries (the Bank), is presented to assist the reader in understanding the financial statements, notes thereto and other data contained in this report. Throughout this report, the term "Corporation" refers to The Chase Manhattan Corporation and its subsidiaries.

General Accounting Policies

The Corporation follows generally accepted accounting principles and, where applicable, the accounting and reporting guidelines prescribed by the Securities and Exchange Commission and bank regulatory authorities. The Corporation carries its assets and liabilities principally on the historical cost basis and follows the accrual method of accounting.

Assets held by commercial banking subsidiaries and by trust and investment advisory subsidiaries in an agency or fiduciary capacity are not assets of the Corporation and, accordingly, are not included in the accompanying financial statements.

Prior years' financial statements have been reclassified to conform with the current financial statement presentations.

Consolidation Policies

The consolidated financial statements include the accounts of the Company and its subsidiaries, principally the Bank, after elimination of material intercompany transactions.

Investments in associated companies (20%-50% ownership interest) are carried on the equity method of accounting and reported in Other Assets. The Corporation's equity interest in the earnings of these associated companies and gains and losses realized on dispositions of investments in associated companies are reported in Other Income.

Investments in companies which are less than 20% owned are carried at cost and are reported in Federal Reserve Bank and Other Stock Investments. Cash dividends received on these investments are reported in Dividends on Federal Reserve Bank and Other Stock Investments. Gains and losses realized on the disposition of these investments are reported in Investment Securities Gains (Losses).

Translation of Foreign Currency Financial Statements

Assets and liabilities of overseas entities are translated into U.S. dollars at the respective year-end exchange rates. Income and expenses are translated monthly at prevailing rates of exchange.

Foreign exchange translation gains and losses resulting from the Corporation's investments in overseas entities, except for those located in highly inflationary economies, net of related hedging transactions and income tax effects, are credited or charged directly to the stockholders' equity account, Foreign Exchange Translation Adjustments. Foreign exchange translation gains and losses pertaining to entities located in highly inflationary economies are recorded in Other Income. For these entities, premises and equipment and the related depreciation and amortization thereof are translated at exchange rates prevailing at dates of acquisition.

Trading Account Assets

Trading account assets are valued at estimated current market prices. Obligations to deliver securities sold but not yet purchased are included in Accounts Payable, Accrued Expenses and Other Liabilities. Gains and losses realized from trading account activities and unrealized valuation adjustments are reported in Trading Account Profits.

Investment Securities

Investment securities are carried at cost, adjusted for amortization of premium and accretion of discount. Premiums and discounts on investment securities are amortized or accreted, respectively, to interest income on investment securities using the straight-line method over the period to maturity (call dates, if earlier, with respect to premiums) of the related securities.

Interest and dividends on investment securities are reported in Interest Income. Gains and losses realized on sales of investment securities are generally determined on the specific identification method and are reported in Investment Securities Gains (Losses).

Interest Rate Swap Contracts

The Corporation generally enters into interest rate swap contracts to increase net interest income and to generate fee income. All yield-related payments or receipts associated with interest rate swap contracts are accrued over the life of the contracts. Arrangement fees are recognized in current income.

Interest Rate Futures

The Corporation uses interest rate futures contracts to manage its overall interest rate risk exposure. Gains and losses on futures contracts used for asset/liability management purposes are deferred and amortized over the life of the hedged assets or liabilities and are included as adjustments to interest income or interest expense as appropriate.

Gains and losses on futures contracts used in connection with Trading Account activities are recognized in current income by using the mark-to-market method of accounting.

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Loans

Loans are reported at their principal amount outstanding, net of unearned discount, if any. Interest income on loans not made on a discount basis is credited to income based on loan principal amounts outstanding at appropriate interest rates. Unearned discount on loans made on a discount basis is credited to income on a basis which results in approximately level rates of return over the terms of the loans.

Included in loans are lease financings which consist of direct financing and leveraged leases. Interest income on lease financings includes the amount of investment tax credits on direct financing and leveraged leases amortized during the year.

Loans on which the accrual of interest has been discontinued are designated as nonaccrual loans. Loans, other than consumer loans, are placed on nonaccrual status if reasonable doubt exists as to timely collectibility, or if payment of principal or interest is contractually past due ninety days or more and the loan is not well secured and in the process of collection. Any accrued but unpaid interest previously recorded on such loans is reversed against current period interest income. Interest income on nonaccrual loans is recognized subsequently only in the period realized. Loans are returned to an accrual status when the collectibility of both principal and interest on a timely basis are reasonably assured and all delinquent principal and interest is brought current, or the loan becomes well secured and in the process of collection.

Consumer loans are charged off against the reserve for possible loan losses according to an established delinquency schedule.

Loans which have been renegotiated for economic or other reasons related to debtors' financial difficulties to rates below those which the Corporation would be willing to accept for new loans with comparable risk are designated as reduced rate loans. Interest on such loans is accrued at the renegotiated rates. If reasonable doubt exists with respect to collectibility of interest at the renegotiated rates, such loans are transferred to nonaccrual status. Where arrangements call for additional interest to be paid on a contingent basis, such interest is not recognized until deemed realizable.

Reserve for Possible Loan Losses

The Reserve for Possible Loan Losses is increased by provisions charged to expenses and decreased by charge-offs, net of recoveries.

The Provision for Possible Loan Losses is based on Management's evaluation of the adequacy of the Reserve for Possible Loan Losses, which evaluation encompasses consideration of past loss experience and other factors, including changes in the composition and volume of the portfolio, the relationship of the reserve to the portfolio and worldwide economic conditions.

Real Estate Properties Acquired In Satisfaction of Loans

Real estate properties acquired in satisfaction of loans, which are reported in Other Assets, are recorded at the lower of cost or estimated fair market value on their acquisition dates and at the lower of such initial amount or current net realizable value thereafter.

Operating expenses of such properties, net of related income, and gains and losses on their disposition are reported in Other Expenses.

Premises and Equipment

Premises and equipment, excluding land, are reported at original cost less accumulated depreciation and amortization. Land is reported at original cost. Depreciation is charged to operating expenses over the estimated useful lives of the related assets. Leasehold improvements are amortized over the terms of the respective leases or the estimated useful lives of the improvements, whichever are shorter. Depreciation and amortization are generally computed on the straight-line method.

Maintenance, repairs and minor improvements are charged to operating expenses as incurred. Major improvements are capitalized.

Foreign Exchange Trading Income

The Corporation follows the general practice of valuing monthly its foreign exchange trading positions, including spot and forward exchange contracts, at estimated current market rates and reporting the resultant profits or losses in Foreign Exchange Trading Income.

Pension Plans

The Corporation has trusteed, noncontributory pension plans covering substantially all full-time [illegible] employees. Costs of the plans, based on actuarial computations of current and future benefits for employees, are charged to operating expenses and are generally funded as accrued. Prior service costs arising from amendments to the plans are amortized over the average future service lives of participants.

Income Taxes

The Company and [illegible] subsidiaries file consolidated Federal, New York State and [illegible] tax returns. Other subsidiaries file separate domestic and foreign tax returns as required. Applicable taxes of the individual companies are generally determined on the basis of filing separate returns. Amounts to be paid or credited with respect to current taxes determined for subsidiaries included in consolidated tax returns are paid to or received from the Company.

Provision is made for deferred taxes on transactions which are reported for financial statement purposes in different years than for tax purposes. Items of income or expense creating deferred tax provisions include depreciation and amortization of premises and equipment and lease financing equipment, undistributed earnings of overseas subsidiaries and associated companies, provision for possible loan losses, and interest on nonaccrual loans.

Investment tax credits on equipment owned, other than lease financing equipment, are deferred and amortized to income as reductions of tax expense.

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Consolidated Statement of Condition

The Chase Manhattan Corporation and Subsidiaries

$ in thousands	December 31, 1985	1984
Assets		
Cash and Due from Banks	$ 5,574,055	$ 4,197,301
Interest-Bearing Deposits Placed with Banks	4,471,048	[illegible]
Federal Funds Sold and Securities Purchased Under Resale Agreements	1,174,371	3,205
Trading Account Assets	1,344,495	1,354,571
Investment Securities:		
U.S. Treasury Securities	1,839,207	1,734,862
Federal Agency Securities	330,259	192,963
State and Political Subdivision Securities	2,410,373	2,102,785
Other Bonds, Notes and Debentures	1,408,541	1,070,934
Federal Reserve Bank and Other Stock Investments	134,012	144,262
Total Investment Securities (Market Value of $6,098,000 and $5,020,000, Respectively)	6,122,392	5,245,806
Loans	61,930,527	62,003,386
Less: Reserve for Possible Loan Losses	907,672	761,439
Loans, Net	61,022,855	61,241,947
Customers' Liability on Acceptances	2,820,471	3,250,437
Accrued Interest Receivable	1,028,986	1,191,949
Premises and Equipment	913,580	790,[illegible]
Other Assets	3,013,189	1,959,365
Total Assets	$87,685,442	$86,683,[illegible]
Liabilities and Stockholders' Equity		
Deposits:		
Domestic Offices:		
Noninterest-Bearing	$13,499,638	$11,149,045
Interest-Bearing	19,130,323	17,733,994
Overseas Offices:		
Noninterest-Bearing	1,939,120	1,423,674
Interest-Bearing	26,783,968	29,373,298
Total Deposits	61,353,049	59,680,011
Federal Funds Purchased and Securities Sold Under Repurchase Agreements	4,131,793	4,480,290
Commercial Paper	3,483,501	4,408,865
Other Borrowed Money	4,671,994	3,236,446
Acceptances Outstanding	2,828,696	3,362,900
Accrued Interest Payable	668,961	803,730
Accounts Payable, Accrued Expenses and Other Liabilities	3,282,175	2,567,995
	80,420,169	80,[illegible]10,138
Long-Term Notes and Debentures	2,806,499	2,320,198
Total Liabilities	83,226,668	82,860,336
Commitments and Contingent Liabilities (Notes 5, 23 and 24)		
Preferred Stock (Without Par Value—[illegible],000 Shares Authorized):		
Redeemable Preferred Stock:		
616,379 Shares Outstanding	61,638	61,638
Nonredeemable Preferred Stock:		
12,039,737 Shares Outstanding	601,987	601,987
Common Stockholders' Equity:		
Common Stock (Par Value $12.50 Per Share):		
1985 / 1984		
Authorized Shares 125,000,000 / 125,000,000		
Outstanding Shares 77,157,724 / 36,659,653	964,472	458,246
Surplus	276,288	678,342
Foreign Exchange Translation Adjustments	(22,265)	(18,730)
Retained Earnings	2,576,654	2,241,199
Total Common Stockholders' Equity	3,795,149	3,359,057
Total Liabilities and Stockholders' Equity	$87,685,442	$86,[illegible]33,018

The accompanying notes are an integral part of the financial statements.

Consolidated Statement of Income

The Chase Manhattan Corporation and Subsidiaries

(In thousands, except per common share data)	Year Ended December 31, 1985	1984	1983
Interest Income			
Interest and Fees on Loans	$7,173,915	$7,657,578	$6,420,374
Interest on Bank Deposit Placings	480,230	769,072	729,985
Interest and Dividends on Investment Securities:			
Interest on—U.S. Treasury Securities	191,447	170,556	198,397
Federal Agency Securities	25,371	21,226	15,571
State and Political Subdivision Securities Exempt from Federal Income Taxes	150,102	115,162	78,340
Other Bonds, Notes and Debentures	197,865	89,075	105,076
Dividends on Federal Reserve Bank and Other Stock Investments	10,241	5,438	7,610
	575,026	401,457	404,994
Interest on Federal Funds Sold and Securities Purchased Under Resale Agreements	105,417	77,589	56,437
Interest on Trading Account Assets	76,917	45,982	47,144
Total Interest Income	8,417,505	8,951,678	7,658,834
Interest Expense			
Deposits	4,275,695	4,997,270	4,087,741
Federal Funds Purchased and Securities Sold Under Repurchase Agreements	461,796	547,672	554,878
Commercial Paper	265,596	408,002	344,434
Other Borrowed Money	425,644	496,338	394,981
Long-Term Notes and Debentures	240,044	193,905	107,745
Total Interest Expense	5,668,775	6,643,187	5,489,779
Net Interest Income	2,748,730	2,308,491	2,169,055
Provision for Possible Loan Losses	435,000	365,000	285,000
Net Interest Income After Provision for Possible Loan Losses	2,313,730	1,943,491	1,884,055
Other Operating Income			
Fees and Commissions	908,805	715,886	600,844
Foreign Exchange Trading Income	173,385	119,462	116,742
Trading Account Profits	31,415	29,364	24,301
Investment Securities Gains (Losses)	98,106	16,704	24,793
Other Income	104,020	48,168	97,531
Total Other Operating Income	1,315,731	929,584	864,211
Other Operating Expenses			
Salaries and Employee Benefits:			
Salaries	1,103,521	918,464	822,794
Profit Sharing	82,368	60,725	72,884
Other Employee Benefits	264,663	239,639	226,693
	1,450,552	1,218,828	1,122,371
Net Occupancy	283,703	244,765	212,558
Equipment Rentals, Depreciation and Maintenance	203,194	170,894	138,670
Other Expenses	794,429	658,598	571,962
Recovery of Payments on, and Liquidation of, Assumed U.S. Government Securities Positions	—	(48,557)	—
Total Other Operating Expenses	2,731,878	2,244,526	2,045,561
Income Before Taxes	897,583	628,549	702,705
Applicable Income Taxes	332,765	222,731	273,098
Net Income	$ 564,818	$ 405,818	$ 429,607
Net Income Applicable to Common Stock	$ 480,573	$ 320,700	$ 376,656
Average Shares Outstanding	75,240,464	71,152,544	68,748,158
Earnings Per Common Share:			
Primary, Based on Average Shares Outstanding	$ 6.39	$ 4.51	$ 5.48
Assuming Full Dilution	6.15	4.32	5.22
Cash Dividends Declared Per Common Share	$ 1.90	$ 1.82½	$ 1.75

The accompanying notes are an integral part of the financial statements.

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Statement of Changes in Common Stockholders' Equity

The Chase Manhattan Corporation and Subsidiaries and The Chase Manhattan Corporation (Company Only)

(In thousands)	Year Ended December 31, 1985	1984	1983
Common Stock			
Balance at Beginning of Year (36,659,653 Shares, 34,740,931 Shares and 33,916,049 Shares, Respectively)	$ 458,246	$ 434,262	$ 423,951
Conversion of Capital Notes and Debentures (465,501 Shares, 144,727 Shares and 258,667 Shares Issued, Respectively)	5,819	1,809	3,233
Exercise of Stock Options (100,823 Shares, 5,229 Shares and 13,427 Shares Issued, Respectively)	1,260	65	168
Shares Issued Pursuant to Dividend Reinvestment Plan (716,812 Shares, 770,241 Shares and 552,788 Shares, Respectively)	8,960	9,628	6,910
Shares Issued Pursuant to 1984 Acquisition (484,663 Shares)	—	6,058	—
Shares Issued Pursuant to Floating Rate Subordinated Notes Due 1996 (636,073 Shares and 513,862 Shares, Respectively)	7,951	6,424	—
Shares Issued Pursuant to Two-For-One Stock Split Declared January 15, 1986 (38,578,862 Shares)	482,236	—	—
Balance at End of Year (77,157,724 Shares, 36,659,653 Shares and 34,740,931 Shares, Respectively)	964,472	458,246	434,262
Surplus			
Balance at Beginning of Year	678,342	594,195	563,266
Conversion of Capital Notes and Debentures	20,788	6,140	11,487
Exercise of Stock Options	3,151	161	469
Shares Issued Pursuant to Dividend Reinvestment Plan	29,627	23,672	18,973
Shares Issued Pursuant to Acquisition	—	12,791	—
Shares Issued Pursuant to Floating Rate Subordinated Notes Due 1996	26,616	13,221	—
Shares Issued Pursuant to Two-For-One Stock Split Declared January 15, 1986	(482,236)	—	—
Gain on Retirement of Redeemable Preferred Stock	—	28,162	—
Balance at End of Year	276,288	678,342	594,195
Foreign Exchange Translation Adjustments			
Balance at Beginning of Year	(18,730)	(22,341)	(13,921)
Aggregate Translation Gain (Loss) After Applicable Income Taxes (Benefits) of $(32,154), $29,281 and $18,433, Respectively	(5,445)	8,187	(8,994)
Amount Transferred to Net Income After Applicable Income Taxes (Benefits) of $(1,476), $360 and $423, Respectively	1,910	(4,576)	574
Balance at End of Year	(22,265)	(18,730)	(22,341)
Retained Earnings			
Balance at Beginning of Year	2,241,199	2,044,709	1,788,117
Net Income	564,818	405,818	429,607
Cash Dividends Declared:			
Redeemable Preferred Stock	(4,432)	(6,038)	(10,856)
Nonredeemable Preferred Stock	(82,659)	(74,122)	(42,095)
Common Stock	(142,272)	(129,168)	(120,064)
Balance at End of Year	2,576,654	2,241,199	2,044,709
Total Common Stockholders' Equity	$3,795,149	$3,359,057	$3,050,825

The accompanying notes are an integral part of the financial statements.

Consolidated Statement of Changes in Financial Position

The Chase Manhattan Corporation and Subsidiaries

(In thousands)	Year Ended December 31, 1985	1984	1983
Funds Provided			
Net Income	$ 564,818	$ 405,818	$ 429,607
Add (Deduct) Noncash Items Included in Net Income:			
Depreciation and Amortization of Premises and Equipment	138,440	108,010	81,252
Provision for Possible Loan Losses	435,000	365,000	285,000
Amortization of Discount on Long-Term Notes and Other Borrowed Money	9,782	8,478	7,099
Deferred Income Taxes (Benefits)	69,239	104,165	168,279
Funds Provided from Operations	1,217,279	991,471	971,237
Issuance of:			
Common Stock	104,172	79,969	41,240
Nonredeemable Preferred Stock, Floating Rate Series F	—	226,987	—
Gain on Retirement of Redeemable Preferred Stock	—	28,162	—
Foreign Exchange Translation Adjustments	—	3,611	—
Increases in:			
Deposits	1,673,038	3,380,454	—
Federal Funds Purchased and Securities Sold Under Repurchase Agreements	—	739,597	—
Commercial Paper	—	122,408	969,541
Other Borrowed Money	1,435,377	—	—
Accrued Interest Payable	—	127,817	—
Accounts Payable, Accrued Expenses and Other Liabilities	644,941	673,962	—
Long-Term Notes and Debentures	512,983	955,304	348,015
Decreases in:			
Cash and Due from Banks	—	242,407	77,706
Interest-Bearing Deposits Placed with Banks	—	4,303,454	—
Federal Funds Sold and Securities Purchased Under Resale Agreements	118,834	—	188,367
Trading Account Assets	10,076	—	922,948
Investment Securities	—	—	711,762
Accrued Interest Receivable	162,963	—	157,597
Other Assets	—	—	795,754
Other—Net	15,446	140,427	59,046
Total Funds Provided	$5,895,109	$12,016,030	$5,243,213
Funds Used			
Cash Dividends Declared:			
Redeemable Preferred Stock	$ 4,432	$ 6,038	$ 10,856
Nonredeemable Preferred Stock	82,659	74,122	42,095
Common Stock	142,272	129,168	120,064
Conversion of Convertible Capital Notes and Subordinated Debentures into Common Stock	26,615	7,952	14,726
Retirement of Redeemable Preferred Stock	—	88,362	—
Foreign Exchange Translation Adjustments	3,535	—	8,420
Increases in:			
Cash and Due from Banks	1,376,254	—	—
Interest-Bearing Deposits Placed with Banks	315,857	—	767,877
Federal Funds Sold and Securities Purchased Under Resale Agreements	—	1,118,082	—
Trading Account Assets	—	1,075,023	—
Investment Securities	876,586	1,827,697	—
Loans, Before Charge-Offs	344,970	6,388,392	691,138
Premises and Equipment	258,474	356,814	111,867
Accrued Interest Receivable	—	118,979	—
Other Assets	1,054,824	527,095	—
Decreases in:			
Deposits	—	—	558,290
Federal Funds Purchased and Securities Sold Under Repurchase Agreements	348,497	—	1,315,151
Commercial Paper	925,365	—	—
Other Borrowed Money	—	298,306	831,572
Accrued Interest Payable	134,769	—	109,890
Accounts Payable, Accrued Expenses and Other Liabilities	—	—	661,267
Total Funds Used	$5,895,109	$12,016,030	$5,243,213

The accompanying notes are an integral part of the financial statements.

Balance Sheet

The Chase Manhattan Corporation (Company Only)

($ in thousands)	December 31, 1985	1984
Assets		
Cash in Banks—Demand Deposits:		
The Chase Manhattan Bank, N.A.	$ 6,013	$ 14,076
Other Banks	4,778	6,646
Short-Term Money Market Instruments:		
Time Deposits with Banks:		
The Chase Manhattan Bank, N.A.	2,748,369	3,651,136
Other Banks	66,216	4,077
U.S. Treasury Securities	—	49,066
Total Short-Term Money Market Instruments	2,814,585	3,704,279
Notes Receivable from Nonbanking Subsidiaries	1,849,793	1,377,012
Accounts Receivable from The Chase Manhattan Bank, N.A.	51,937	50,711
Other Stock Investments	41,360	55,330
Subordinated Debenture Receivable from The Chase Manhattan Bank, N.A.	400,000	400,000
Investments in Subsidiaries (at Equity in Net Assets):		
Banking Subsidiaries:		
The Chase Manhattan Bank, N.A.	4,454,725	4,228,746
Other Banking Subsidiaries	705,971	467,205
Nonbanking Subsidiaries	343,571	286,838
Accrued Interest Receivable:		
Banking Subsidiaries	26,865	33,218
Nonbanking Subsidiaries	21,643	17,496
Other	1,822	30
Other Assets	94,149	88,026
Total Assets	$10,817,212	$10,730,213
Liabilities and Stockholders' Equity		
Securities Sold Under Repurchase Agreements	$ —	$ 48,983
Commercial Paper	3,351,750	4,341,035
Other Borrowed Money	573,648	325,647
Accounts Payable, Accrued Expenses and Other Liabilities	290,683	257,511
	4,216,087	4,973,176
Long-Term Notes and Debentures	2,142,351	1,734,355
Total Liabilities	6,358,438	6,707,531
Commitments and Contingent Liabilities (Notes 23 and 24)		
Preferred Stock (Without Par Value—20,000,000 Shares Authorized):		
Redeemable Preferred Stock:		
616,379 Shares Outstanding	61,638	61,638
Nonredeemable Preferred Stock:		
12,039,737 Shares Outstanding	601,987	601,987
Common Stockholders' Equity:		
Common Stock (Par Value $12.50 Per Share):		
Authorized Shares: 1985 125,000,000; 1984 125,000,000		
Outstanding Shares: 1985 77,157,724; 1984 36,659,653	964,472	458,246
Surplus	276,288	678,342
Foreign Exchange Translation Adjustments	(22,265)	(18,730)
Retained Earnings	2,576,654	2,241,199
Total Common Stockholders' Equity	3,795,149	3,359,057
Total Liabilities and Stockholders' Equity	$10,817,212	$10,730,213

The accompanying notes are an integral part of the financial statements.

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Statement of Income

The Chase Manhattan Corporation (Company Only)

(In thousands)	Year Ended December 31, 1985	1984	1983
Income			
Dividends Received:			
The Chase Manhattan Bank, N.A.	$300,000	$300,000	$300,000
Nonbanking Subsidiaries	—	2,500	3,079
Other Stock Investments	4,549	344	3,869
Interest Income:			
Time Deposits with Banks:			
The Chase Manhattan Bank, N.A.	215,755	358,380	284,071
Other Banking Subsidiaries	172	504	5,023
Other Banks	6,010	6,196	14,019
U.S. Treasury Securities	322	295	760
Bankers' Acceptances	—	108	277
Notes Receivable from Nonbanking Subsidiaries	150,688	146,802	111,726
Subordinated Debenture Receivable from The Chase Manhattan Bank, N.A.	36,137	11,308	—
Other Income	7,291	1,748	107
Total Income	720,924	828,185	722,931
Expenses			
Interest Expense:			
Securities Sold Under Repurchase Agreements	36	54	90
Commercial Paper	259,168	400,268	336,874
Other Borrowed Money	39,949	35,152	6,103
Long-Term Notes and Debentures	183,389	143,588	70,050
Fees Paid to—The Chase Manhattan Bank, N.A.	2,778	3,232	3,616
Nonbanking Subsidiaries	26,469	25,654	21,040
Other Expenses	10,203	9,519	4,032
Total Expenses	521,992	617,467	441,805
Income Before Income Tax Benefits and Equity in Undistributed Income (Losses) of Subsidiaries	198,932	210,718	281,126
Applicable Income Tax Benefits:			
Federal	(42,895)	(31,096)	(8,787)
State and Local	(9,830)	(20,414)	(4,620)
Total Applicable Income Tax Benefits	(52,725)	(51,510)	(13,407)
Income Before Equity in Undistributed Income (Losses) of Subsidiaries	251,657	262,228	294,526
Equity in Undistributed Income (Losses) of Subsidiaries:			
Banking Subsidiaries:			
The Chase Manhattan Bank, N.A.	192,798	83,493	120,421
Other Banking Subsidiaries	79,385	49,127	7,749
Nonbanking Subsidiaries	40,978	10,970	6,911
Net Income	$564,818	$405,818	$429,607

The accompanying notes are an integral part of the financial statements.

Statement of Changes in Financial Position

The Chase Manhattan Corporation (Company Only)

($ in thousands)	Year Ended December 31. 1985	1984	1983
Funds Provided			
Net Income	$ 564,818	$ 405,818	$ 429,607
Add (Deduct) Noncash Items Included in Net Income:			
Equity in Undistributed Losses (Income) of Banking Subsidiaries:			
The Chase Manhattan Bank, N.A.	(192,798)	(83,493)	(120,421)
Other Banking Subsidiaries	(79,385)	(49,127)	(7,749)
Equity in Undistributed Losses (Income) of Nonbanking Subsidiaries	(40,978)	(10,970)	(6,911)
Amortization of Discount on Long-Term Notes and Other Borrowed Money	9,782	8,478	7,099
Deferred Income Taxes (Benefits)	1,120	2,503	10,860
Funds Provided from Operations	262,559	273,209	312,485
Issuance of:			
Common Stock	104,172	79,969	41,240
Nonredeemable Preferred Stock, Floating Rate Series F	—	226,987	—
Gain on Retirement of Redeemable Preferred Stock	—	28,162	—
Other Stock Investments	13,970	—	—
Foreign Exchange Translation Adjustments	—	3,611	—
Increases in:			
Securities Sold Under Repurchase Agreements	—	48,983	—
Commercial Paper	—	184,168	835,659
Other Borrowed Money	247,830	—	296,802
Accounts Payable, Accrued Expenses and Other Liabilities	32,052	4,320	118,734
Long-Term Notes and Debentures	425,000	779,035	348,600
Decreases in:			
Cash in Banks—Demand Deposits	10,531	—	—
Time Deposits with Banks	840,628	233,443	—
U.S. Treasury Securities	49,066	—	46,493
Bankers' Acceptances	—	9,827	15,119
Accounts Receivable from The Chase Manhattan Bank, N.A.	—	—	13,153
Accrued Interest Receivable	414	4,184	4,823
Total Funds Provided	$1,986,222	$1,875,898	$2,033,108
Funds Used:			
Cash Dividends Declared:			
Redeemable Preferred Stock	$ 4,432	$ 6,038	$ 10,856
Nonredeemable Preferred Stock	82,659	74,122	42,095
Common Stock	142,272	129,168	120,064
Other Stock Investments	—	5,330	—
Investments in Subsidiaries:			
The Chase Manhattan Bank, N.A.	33,181	482,683	293,709
Other Banking Subsidiaries	159,381	310,042	51,050
Nonbanking Subsidiaries	15,755	16,815	59,953
Conversion of Convertible Capital Notes and Subordinated Debentures into Common Stock	26,615	7,952	14,726
Retirement of Redeemable Preferred Stock	—	88,362	—
Foreign Exchange Translation Adjustments	3,535	—	8,420
Increases in:			
Cash in Banks—Demand Deposits	—	10,361	6,329
Time Deposits with Banks	—	—	1,084,424
U.S. Treasury Securities	—	3,690	—
Subordinated Debenture Receivable from The Chase Manhattan Bank, N.A.	—	400,000	—
Notes Receivable from Nonbanking Subsidiaries	472,781	284,055	207,459
Accounts Receivable from The Chase Manhattan Bank, N.A.	1,226	40,753	—
Decreases in:			
Securities Sold Under Repurchase Agreements	48,983	—	91,436
Commercial Paper	989,279	—	—
Other Borrowed Money	—	3,900	—
Other—Net	6,123	12,627	42,587
Total Funds Used	$1,986,222	$1,875,898	$2,033,108

The accompanying notes are an integral part of the financial statements.

Consolidated Statement of Condition

The Chase Manhattan Bank, N.A. and Subsidiaries

In thousands	December 31, 1985	1984
Assets		
Cash and Due from Banks	$ 5,208,200	$ 3,903,069
Interest-Bearing Deposits Placed with Banks	4,566,219	4,371,576
Federal Funds Sold and Securities Purchased Under Resale Agreements	2,458,090	1,254,335
Trading Account Assets	1,331,638	1,342,061
Investment Securities:		
U.S. Treasury Securities	1,721,697	1,617,311
Federal Agency Securities	290,391	81,829
State and Political Subdivision Securities	2,185,798	1,833,812
Other Bonds, Notes and Debentures	1,357,862	990,829
Federal Reserve Bank and Other Stock Investments	82,509	81,934
Total Investment Securities (Market Value of $5,596,000 and $4,356,000, Respectively)	5,638,257	4,606,215
Loans	52,176,137	56,248,996
Less: Reserve for Possible Loan Losses	699,054	660,763
Loans, Net	51,477,083	55,588,233
Customers' Liability on Acceptances	2,810,159	5,217,219
Accrued Interest Receivable	1,002,649	1,150,414
Premises and Equipment	753,834	662,935
Other Assets	2,474,067	1,630,566
Total Assets	$77,720,196	$79,726,623
Liabilities and Stockholder's Equity		
Deposits:		
Domestic Offices:		
Noninterest-Bearing	$12,677,180	$10,425,631
Interest-Bearing	14,629,437	14,533,189
Overseas Offices:		
Noninterest-Bearing	1,939,120	1,423,674
Interest-Bearing	29,500,685	33,017,195
Total Deposits	58,746,422	59,399,689
Federal Funds Purchased and Securities Sold Under Repurchase Agreements	3,972,397	4,434,382
Other Borrowed Funds	3,160,191	2,359,911
Acceptances Outstanding	2,818,384	5,329,392
Accrued Interest Payable	611,150	767,264
Accounts Payable, Accrued Expenses and Other Liabilities	2,925,095	2,254,082
	72,233,639	74,544,710
Long-Term Notes and Debentures	1,031,832	953,167
Total Liabilities	73,265,471	75,497,877
Commitments and Contingent Liabilities (Notes 5, 23 and 24)		
Stockholder's Equity:		
Capital Stock (Par Value $15.00 Per Share):		
Authorized Shares: 1985 61,744,445; 1984 61,744,445		
Outstanding Shares: 1985 50,009,247; 1984 49,333,684	750,139	740,005
Surplus	1,772,407	1,745,409
Foreign Exchange Translation Adjustments	(22,345)	(18,394)
Undivided Profits	1,954,524	1,761,726
Total Stockholder's Equity	4,454,725	4,228,746
Total Liabilities and Stockholder's Equity	$77,720,196	$79,726,623

The accompanying notes are an integral part of the financial statements.

Member Federal Deposit Insurance Corporation

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Consolidated Statement of Income

The Chase Manhattan Bank, N.A. and Subsidiaries

In thousands	Year Ended December 31 1985	1984	1983
Interest Income			
Interest and Fees on Loans	$6,092,577	$7,035,418	$6,165,367
Interest on Bank Deposit Placings	483,682	762,096	719,567
Interest and Dividends on Investment Securities:			
Interest on—U.S. Treasury Securities	180,933	163,605	197,310
Federal Agency Securities	18,019	13,910	15,565
State and Political Subdivision Securities Exempt from Federal Income Taxes	132,157	106,055	78,230
Other Bonds, Notes and Debentures	189,252	85,647	105,062
Dividends on Federal Reserve Bank and Other Stock Investments	5,228	4,750	3,613
	525,589	373,968	399,780
Interest on Federal Funds Sold and Securities Purchased Under Resale Agreements	96,571	78,384	57,487
Interest on Trading Account Assets	75,893	45,270	47,144
Total Interest Income	7,274,312	8,295,136	7,389,345
Interest Expense			
Deposits	4,129,669	5,205,575	4,365,309
Federal Funds Purchased and Securities Sold Under Repurchase Agreements	446,031	528,729	552,240
Other Borrowed Funds	334,192	416,541	383,610
Long-Term Notes and Debentures	90,334	60,386	37,695
Total Interest Expense	5,000,226	6,211,231	5,338,854
Net Interest Income	2,274,086	2,083,905	2,050,491
Provision for Possible Loan Losses	218,663	293,228	245,696
Net Interest Income After Provision for Possible Loan Losses	2,055,423	1,790,677	1,804,795
Other Operating Income			
Fees and Commissions	687,984	589,757	541,207
Foreign Exchange Trading Income	172,865	119,016	116,742
Trading Account Profits	28,774	28,328	24,301
Investment Securities Gains (Losses)	76,290	16,149	24,793
Other Income	66,794	41,781	96,316
Total Other Operating Income	1,032,707	795,031	803,359
Other Operating Expenses			
Salaries and Employee Benefits:			
Salaries	954,697	827,924	780,501
Profit Sharing	74,745	56,553	69,844
Other Employee Benefits	245,039	227,118	219,946
	1,274,481	1,111,595	1,070,291
Net Occupancy	255,888	227,337	206,507
Equipment Rentals, Depreciation and Maintenance	184,434	160,241	135,477
Other Expenses	588,041	530,001	506,968
Recovery of Payments on, and Liquidation of, Assumed U.S. Government Securities Positions	—	(48,559)	—
Total Other Operating Expenses	2,302,844	1,980,615	1,919,243
Income Before Taxes	785,286	605,093	688,911
Applicable Income Taxes	292,488	221,600	268,490
Net Income	$ 492,798	$ 383,493	$ 420,421

The accompanying notes are an integral part of the financial statements.

Member Federal Deposit Insurance Corporation

Consolidated Statement of Changes in Stockholder's Equity

The Chase Manhattan Bank, N.A. and Subsidiaries

	Year Ended December 31,		
In thousands	1985	1984	1983
Capital Stock			
Balance at Beginning of Year	$ 740,005	$ 738,591	$ 738,591
Shares Issued Pursuant to Floating Rate Subordinated Debenture Due 1996 (675,563 Shares and 94,296 Shares, Respectively)	10,134	1,414	—
Balance at End of Year	750,139	740,005	738,591
Surplus			
Balance at Beginning of Year	1,745,409	1,268,012	967,585
Shares Issued Pursuant to Floating Rate Subordinated Debenture Due 1996	24,433	2,175	—
Capital Contributions by The Chase Manhattan Corporation	2,372	475,195	300,375
Tax Benefit Resulting from the Exercise of Stock Options	193	27	52
Balance at End of Year	1,772,407	1,745,409	1,268,012
Foreign Exchange Translation Adjustments			
Balance at Beginning of Year	(18,394)	(22,266)	(13,784)
Aggregate Translation Gain (Loss) After Applicable Income Taxes (Benefits) of $(32,289), $29,385 and $18,401, Respectively	(5,797)	8,448	(9,056)
Amount Transferred to Net Income After Applicable Income Taxes (Benefits) of $(1,514), $360 and $423, Respectively	1,846	(4,576)	574
Balance at End of Year	(22,345)	(18,394)	(22,266)
Undivided Profits			
Balance at Beginning of Year	1,761,726	1,678,233	1,556,048
Net Income	492,798	383,493	420,421
Cash Dividends Paid	(300,000)	(300,000)	(300,000)
Sale of Shares of Subsidiary	—	—	1,764
Balance at End of Year	1,954,524	1,761,726	1,678,233
Total Stockholder's Equity	$4,454,725	$4,228,746	$3,662,570

The accompanying notes are an integral part of the financial statements.

Member Federal Deposit Insurance Corporation

Consolidated Statement of Changes in Financial Position

The Chase Manhattan Bank, N.A. and Subsidiaries

$ in thousands	Year Ended December 31, 1985	1984	1983
Funds Provided			
Net Income	$ 492,798	$ 383,493	$ 420,421
Add: Deduct: Noncash Items Included in Net Income:			
Depreciation and Amortization of Premises and Equipment	124,808	101,180	79,921
Provision for Possible Loan Losses	218,663	293,228	238,502
Deferred Income Taxes (Benefit)	34,830	93,775	150,979
Funds Provided from Operations	871,099	871,676	889,823
Issuance of Capital Stock Pursuant to Floating Rate Subordinated Debenture Due 1996	34,567	3,589	—
Capital Contributions by The Chase Manhattan Corporation	2,372	475,195	300,375
Increases in:			
Deposits	—	—	507,801
Federal Funds Purchased and Securities Sold Under Repurchase Agreements	—	718,689	—
Other Borrowed Funds	800,280	—	—
Long-Term Notes and Debentures	87,984	543,593	—
Decreases in:			
Cash and Due from Banks	—	515,580	86,653
Interest-Bearing Deposits Placed with Banks	—	4,366,207	—
Trading Account Assets	10,423	—	922,948
Investment Securities	—	—	667,910
Loans, Before Charge-Offs	3,806,557	—	264,897
Other—Net	—	434,723	313,145
Total Funds Provided	$5,613,282	$7,929,252	$3,953,552
Funds Used			
Cash Dividends Paid	$ 300,000	$ 300,000	$ 300,000
Increases in:			
Cash and Due from Banks	1,305,131	—	—
Interest-Bearing Deposits Placed with Banks	194,643	—	1,026,748
Federal Funds Sold and Securities Purchased Under Resale Agreements	1,203,755	1,055,214	—
Trading Account Assets	—	1,062,513	—
Investment Securities	1,032,042	1,290,430	—
Loans, Before Charge-Offs	—	2,867,244	—
Premises and Equipment	215,707	228,253	107,283
Decreases in:			
Deposits	653,267	424,909	—
Federal Funds Purchased and Securities Sold Under Repurchase Agreements	461,985	—	1,248,716
Other Borrowed Funds	—	700,689	1,270,805
Other—Net	246,752	—	—
Total Funds Used	$5,613,282	$7,929,252	$3,953,552

The accompanying notes are an integral part of the financial statements.

Member Federal Deposit Insurance Corporation

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Note 1. General

The accounting policies followed by The Chase Manhattan Corporation (the Company) and its subsidiaries, including its principal subsidiary, The Chase Manhattan Bank, N.A. and its subsidiaries (the Bank), are disclosed in the accompanying Summary of Significant Accounting Policies on pages 42 and 43. This summary is an integral part of the financial statements and should be read in conjunction with these notes. Throughout the notes, the term "Corporation" refers to The Chase Manhattan Corporation and its subsidiaries. The term "Nonbanking Subsidiaries" used in the financial statements and notes thereto refers to subsidiaries of the Company not chartered as commercial banks. Such subsidiaries are engaged in mortgage banking, discount brokerage, commercial and consumer financing, investment advisory and other financial services.

Note 2. Common Stock Split

On January 15, 1986, the Board of Directors declared a two-for-one stock split in the form of a 100 per cent stock dividend on the Company's common stock. The shares issued to effect the stock split were distributed on February 13, 1986 to stockholders of record on January 31, 1986. Accordingly, the Consolidated Statement of Condition, the Balance Sheet (Company Only), and the Statement of Changes in Common Stockholders' Equity reflect the stock split as of December 31, 1985. The par value of the additional shares of common stock issued in connection with the stock split was credited to common stock and a like amount charged to surplus. References to common share amounts and average common shares outstanding in the consolidated financial statements are presented after giving effect to the split.

The earnings per common share, cash dividends per common share and average common shares outstanding amounts prior to the split for the respective years ended December 31 were as follows:

	1985	1984	1983
Earnings Per Common Share			
Primary	$12.77	$9.01	$10.96
Fully Diluted	$12.30	$8.65	$10.44
Cash Dividends Per Common Share	$3.80	$3.65	$3.50
Average Common Shares Outstanding	37,620,232	35,576,272	34,374,079
Average Common Shares Outstanding Fully Diluted Basis	39,276,548	37,417,381	36,323,212

Note 3. Acquisitions

On April 4, 1984, Chase Manhattan Overseas Banking Corporation ("CMOBC"), a wholly owned subsidiary of the Bank, acquired for cash substantially all of the outstanding shares not already held by CMOBC, or approximately 68.5%, of Nederlandse Credietbank N.V. ("NCB"), a Dutch bank with headquarters in Amsterdam, The Netherlands. The acquisition of the additional interest cost CMOBC $45 million and resulted in CMOBC owning 99.6% of the shares of NCB. The asset and liability accounts of NCB were consolidated into the Corporation's Consolidated Statement of Condition at June 30, 1984.

On July 1, 1984, Chase Manhattan National Corporation ("CMNC"), a wholly owned subsidiary of the Company, acquired Lincoln First Bank, N.A. (renamed Chase Lincoln First Bank, N.A.), a commercial bank based in Rochester, New York, through the merger of its parent company, Lincoln First Banks Inc. ("Lincoln"), into CMNC. The acquisition cost included $51 million in cash, $18 million of common stock (969,326 shares—restated for the two-for-one stock split declared January 15, 1986) of the Company, $227 million (stated value) of Preferred Stock, Floating Rate Series F (Series F Preferred), of the Company and $10 million of open market purchases of Lincoln shares in the first quarter of 1984.

Both acquisitions were accounted for as purchases and, as such, the assets and liabilities of Lincoln and NCB were recorded at their estimated fair values as of the dates of acquisition. Goodwill and an identified core deposit intangible amounted to approximately $170 million and are being amortized against income over periods not exceeding 20 years. The financial results of both NCB and CMNC commenced to be fully consolidated into the Corporation's financial statements in the third quarter of 1984.

Pro forma combined net income for the years ended December 31, 1984 and 1983 of $418 million and $457 million, respectively, gives effect to the Lincoln and NCB acquisitions as if they had been consummated on January 1, 1983, and is not necessarily indicative of the results that would have actually occurred had the acquisitions taken place at that date.

In the second quarter of 1985, the Company acquired six Ohio savings and loan institutions, with total assets of approximately $450 million and converted them into a commercial bank, named Chase Bank of Ohio. In the fourth quarter of 1985, the Company acquired three Maryland savings and loan institutions with total assets of approximately $700 million and converted them into a commercial bank named, Chase Bank of Maryland. The new commercial banks are both wholly owned subsidiaries of the Company.

The Ohio and Maryland acquisitions were also accounted for as purchases and assets and liabilities were recorded at their estimated fair values as of the dates of acquisition. The total acquisition cost of $45 million included $70 million of goodwill to be amortized against income over periods not exceeding 20 years. The Corporation's net income for the years ended December 31, 1985 and December 31, 1984 would not have been substantially changed had the combined acquisitions of the Ohio and Maryland savings and loan institutions been reflected on a pro forma basis as of January 1, 1984.

During the year the Company made other acquisitions including Banco de Finanzas, of Madrid, Spain with total assets of approximately $265 million.

Note 4. Investment Securities

Shown below are the carrying and estimated market values of Investment Securities at December 31, 1985 and 1984

	1985		1984	
($ in millions)	Carrying Value	Estimated Market Value	Carrying Value	Estimated Market Value
U.S. Treasury Securities	$1,339	$1,307	$1,735	$1,728
Federal Agency Securities	330	328	193	192
State and Political Subdivision Securities	2,410	2,292	2,103	1,963
Other Bonds, Notes and Debentures	1,409	1,403	1,071	1,057
Federal Reserve Bank and Other Stock Investments	134	158	144	159
Total Investment Securities*	$6,122	$5,598	$5,246	$5,099

*The market values of securities are estimated utilizing independent pricing services and are based on over-the-counter market bids, which often reflect transactions of relatively small size and are not necessarily indicative of the prices at which large amounts of particular issues could be sold.

Note 5. Loans

Loans at December 31, 1985 and 1984 are summarized below:

($ in thousands)	1985	1984
Domestic Offices:		
Real Estate Loans:		
Construction and Land Development	$ 2,427,453	$ 2,009,101
Secured by 1-4 Family Residential Properties	2,668,866	1,722,189
Other Real Estate Loans	1,243,639	1,051,504
Loans to Financial Institutions	1,683,152	1,801,380
Loans to Purchase or Carry Securities, Principally to Brokers and Dealers	502,967	543,303
Commercial and Industrial Loans	8,754,752	10,034,945
Loans to Individuals for Personal Expenditures	7,407,269	5,313,237
Lease Financings	1,464,327	1,013,010
Tax-Exempt Loans	1,692,590	1,177,453
Other Loans	654,856	502,009
Total Domestic Offices, Gross	28,499,871	25,168,131
Less: Unearned Discount	580,536	460,058
Total Domestic Offices	27,919,335	24,708,073
Overseas Offices:		
Real Estate Loans	2,818,483	2,278,600
Commercial and Industrial Loans	21,932,966	24,663,203
Lease Financings	336,800	236,981
Other Loans	9,138,392	10,325,862
Total Overseas Offices, Gross	34,226,641	37,504,646
Less: Unearned Discount	215,449	209,333
Total Overseas Offices	34,011,192	37,295,313
Total Loans	$61,930,527	$62,003,386

The following table sets forth the distribution of loans at December 31, 1985 and 1984, based on the domiciles of the obligors:

($ in thousands)	1985	1984
Loans to Domestic Obligors:		
Domestic Offices	$27,515,276	$24,286,564
Overseas Offices	5,007,323	5,751,815
Total	32,522,599	30,038,379
Loans to International Obligors:		
Domestic Offices	404,059	421,509
Overseas Offices	29,003,869	31,543,498
Total	29,407,928	31,965,007
Total Loans	$61,930,527	$62,003,386

Lease financings at December 31, 1985 and 1984 consisted of the following:

($ in thousands)	1985	1984
Direct Financing Leases	$1,500,882	$ 974,536
Less: Unearned Discount	222,064	131,145
Total Direct Financing Leases	1,278,818	843,391
Leveraged Leases	300,245	275,455
Less: Unearned Discount	52,092	34,457
Total Leveraged Leases*	248,153	240,998
Total Lease Financings	$1,526,971	$1,084,389

*Related deferred income taxes totaled $167,030 thousand and $159,411 thousand, respectively.

Loans made by the Corporation during 1985 and 1984 to directors, executive officers, or principal holders of equity securities of the Company and/or the Bank, or to any associate of such persons, as defined by the Securities and Exchange Commission, at no time exceeded 5% of the total of Preferred Stock and Common Stockholders' Equity.

Nonaccrual and reduced rate loans at December 31, 1985, 1984 and 1983 totaled $2,035 million, $2,167 million and $1,870 million, respectively. Interest income realized and foregone on these loans for the respective years ended December 31 was as follows:

($ in millions)	1985	1984	1983
Interest Income Which Would Have Been Recorded Under Original Terms	$224	$278	$210
Interest Income Actually Realized	105	122	65
Reduction in Interest Income:			
Before Applicable Taxes	$119	$156	$145
After Applicable Taxes	58	76	70

At December 31, 1985, 1984 and 1983, unused, conditional commitments to lend to borrowers whose loans were in nonaccrual or reduced rate status aggregated $9 million, $12 million and $5 million, respectively.

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Note 6. Reserve for Possible Loan Losses

Changes in the Reserve for Possible Loan Losses for the three years ended December 31, 1985, 1984 and 1983, respectively, are shown below:

($ in thousands)	1985	1984	1983
Balance at Beginning of Year	$761,439	$564,110	$558,277
Additions:			
Provision Charged to Expenses	435,000	365,000	285,000
Reserves of Acquired Subsidiaries	24,120	64,932	—
Deductions:			
Charge-Offs	417,829	278,534	329,151
Less: Recoveries	97,475	63,172	74,642
Net Charge-Offs	320,354	215,362	254,509
Foreign Exchange Translation Adjustments	7,467	(17,241)	(24,658)
Balance at End of Year	$907,672	$761,439	$564,110

Note 7. Premises and Equipment

A summary of Premises and Equipment at December 31, 1985 and 1984 follows:

($ in thousands)	1985	1984
Domestic Offices:		
Land	$ 43,859	$ 47,110
Buildings	340,137	310,520
Leasehold Improvements	232,173	201,193
Equipment	450,984	372,375
Total Domestic Offices	1,067,153	931,198
Overseas Offices:		
Land	66,561	54,958
Buildings	172,324	140,099
Leasehold Improvements	88,520	69,322
Equipment	205,895	148,741
Total Overseas Offices	533,300	413,120
Total Premises and Equipment, Gross	1,600,453	1,344,318
Less: Accumulated Depreciation and Amortization	686,873	550,772
Total Premises and Equipment	$ 913,580	$ 793,546

Premises and equipment includes capitalized leases, principally those related to buildings which amounted to $33 million at December 31, 1985.

Depreciation and amortization of premises and equipment for the years 1985, 1984 and 1983 amounted to $138,440,000, $108,010,000 and $81,252,000, respectively.

Note 8. Other Assets

A summary of Other Assets at December 31, 1985 and 1984 follows:

($ in thousands)	1985	1984
Accounts Receivable	$1,138,100	$ 722,094
Due for Securities Sold	601,435	246,900
Real Estate Properties Acquired in Satisfaction of Loans	100,480	89,711
Investments in Associated Companies	116,974	72,062
Other	1,056,200	827,598
Total Other Assets	$3,013,189	$1,958,365

Note 9. Deposits

A summary of Deposits at December 31, 1985 and 1984 follows:

($ in thousands)	1985	1984
Domestic Offices:		
Noninterest-Bearing Deposits	$13,499,628	$11,149,045
Savings Deposits	1,187,141	1,204,702
Negotiable Order of Withdrawal Deposits	762,771	679,268
Savings Certificates and Nest Egg Account Deposits	399,773	554,349
Money Market Deposits	9,562,379	6,237,154
Negotiable Certificates of Deposit	937,233	1,054,289
Other Time Deposits	7,280,526	8,004,232
Total Domestic Offices	32,629,961	28,883,039
Overseas Offices:		
Noninterest-Bearing Deposits	1,939,120	1,423,674
Savings Deposits	918,317	829,550
Savings Certificates and Nest Egg Account Deposits	140,604	127,457
Money Market Deposits	218,687	158,064
Negotiable Certificates of Deposit	1,451,378	2,346,327
Other Time Deposits	24,054,952	25,911,900
Total Overseas Offices	28,723,058	30,796,972
Total Deposits	$61,353,049	$59,680,011

Deposits by foreign depositors in domestic offices at December 31, 1985, 1984 and 1983 were $3,977,000,000, $3,684,000,000 and $3,272,000,000, respectively.

Note 10. Other Borrowed Money

A summary of Other Borrowed Money at December 31, 1985 and 1984 follows:

($ in thousands)	1985	1984
Maturing Within One Year:		
Bank:		
Domestic Offices:		
Term Federal Funds	$ 333,113	$ 358,712
Notes Issued to U.S. Treasury Department	900,000	456,347
Student Loan Marketing Association	125,000	225,000
Other Borrowings	18,248	25,035
Overseas Offices:		
Rediscounted Notes	237,111	227,116
Other Borrowings	1,152,675	525,887
Banking Subsidiaries of Company:		
Student Loan Marketing Association	611,250	391,000
Other Borrowings	293,543	87,574
Nonbanking Subsidiaries of Company	100,678	61,849
Maturing After One Year:		
Company:		
Floating Rate Extendable Notes (Due 1992)	299,784	299,672
Floating Rate Extendable Notes (Due 1997)	249,746	—
Floating Rate Notes (Due 1999)	24,118	25,975
Bank:		
Domestic Offices:		
Student Loan Marketing Association	—	125,000
Other Borrowings	866	8,798
Overseas Offices	344,168	329,404
Banking Subsidiaries of Company:		
Student Loan Marketing Association	38,750	45,000
Other Borrowings	42,944	44,067
Total Other Borrowed Money	$4,972,194	$3,236,146

Interest rates on the borrowings from the Student Loan Marketing Association, which are secured by student loans held in the Bank's portfolio, and on the Floating Rate Extendable Notes (Due 1992) and the Floating Rate Notes (Due 1999) are determined by formulas based on the yield of three-month U.S. Treasury bills. The interest rate on the Floating Rate Extendable Notes (Due 1997) has been fixed at 9.00% through June 14, 1987 and will thereafter be adjusted on each June 15, starting in 1987, to a rate, or to a rate to be determined pursuant to a formula, established by the Company. The interest rates in effect on these borrowings at December 31, 1985 and 1984 follow:

Interest Rates	1985	1984
Student Loan Marketing Association	8.70%	9.69%
Floating Rate Extendable Notes (Due 1992)	7.82%	8.68%
Floating Rate Extendable Notes (Due 1997)	9.00%	—
Floating Rate Notes (Due 1999)	8.35%	10.20%

The Company has two Eurodollar Revolving Credit Agreements with groups of banking institutions, one for $200 million expiring June 1, 1986, and one for $300 million expiring February 28, 1989. Under the terms of each agreement, the Company may borrow, renew, repay and reborrow, from time to time, $10 million or a multiple thereof, with repayments due in three or six months, as the Company elects. Borrowings under each agreement bear interest at the greater of London interbank offered rates (LIBOR) plus ⅛ of 1% per annum, or 7% for the $200 million facility and at the greater of LIBOR plus ⅛ of 1% per annum, or 6⅞% for the $300 million facility. Each agreement requires payment of commitment fees of ⅛ of 1%. Such fees are reported as interest expense. There were no borrowings under these or similar agreements during 1985, 1984 or 1983.

Note 11. Long-Term Notes and Debentures

A summary of Long-Term Notes and Debentures outstanding at December 31, 1985 and 1984 and certain applicable terms follows:

($ in thousands)	Maturity Date	Interest Rate (1)	Amount Outstanding 1985	Amount Outstanding 1984	Other Data (2)
Bank:					
The Chase Manhattan Bank, N.A.:					
Capital Notes	1986	8¾%	$ 200,000	$ 200,000	S
Capital Notes	1990	4.60%	3,833	4,288	S
Floating Rate Subordinated Debenture	1996	8⅛(10¹⁵⁄₁₆)%	400,000	400,000	S,P
Chase Manhattan Overseas Banking Corporation:					
Floating Rate Notes	1993	8⅛(12¾)%	150,000	150,000	G
Deutsche Mark Bearer Bonds	1993	6%	32,300	28,976	G,F
Swiss Franc Bonds	1993	4%	30,288	25,839	G,F
Chase Manhattan S.A.:					
French Franc Floating Rate Bonds	1992	9.88(11.53)%	97,485	78,411	S,G
French Franc Floating Rate Bonds	1993	10.30%	45,493	—	S,G
Nederlandse Credietbank N.V.:					
NCB Notes and Debentures	1986-2002	7¾-12½%	72,433	65,653	S
Total			1,031,832	953,167	
Chase Manhattan National Corporation:					
Capital Notes	1986-1989	4.70%	3,976	4,326	F
Debentures	1992	6¼%	7,250	7,250	F
Debentures	1996	8½%	21,090	21,090	G,F
Total			32,316	32,676	
Company:					
Zero Coupon Notes	1992	14¼%	72,964	63,602	
Notes Issued with Detachable Equity Contracts	1992	15½%	150,000	150,000	P
Convertible Capital Notes	1993	4⅞%	7,245	9,989	S
Floating Rate Subordinated Notes	1995	8¾(9¾)%	348,843	348,726	S,P
Floating Rate Subordinated Notes	1996	8⅛(10¹⁵⁄₁₆)%	398,632	398,499	S,P
Convertible Subordinated Debentures	1996	6½%	57,282	81,154	S
Floating Rate Subordinated Notes	1997	8¾%	175,000	—	S
Floating Rate Subordinated Notes	2000	8¼%	250,000	—	S
Floating Rate Subordinated Notes	2009	8¼(9¹⁵⁄₁₆)%	400,000	400,000	S
Floating Rate Notes	2009	8.20(11.30)%	282,385	282,385	F
Total			2,142,351	1,734,355	
Less: Investment by the Company in Floating Rate Subordinated Debenture of the Bank			400,000	400,000	
Total Long-Term Notes and Debentures			$2,906,499	$2,320,198	

(1) The interest rates shown for floating rate issues are those in effect at December 31, 1985 and, in parentheses, at December 31, 1984. Such interest rates are determined by formulas, subject to certain minimum rates. The rate shown for the Zero Coupon Notes, which do not bear interest, represents a level yield to maturity on their carrying value, which increases as the discount on the Notes is amortized to interest expense. The principal amount of the Zero Coupon Notes is $175 million.

(2) Issues indicated by
"S" — Subordinated in right of payment to claims of depositors and/or certain other creditors, as applicable.
"P" — Considered primary capital for United States bank regulatory purposes.
"G" — Guaranteed as to payment by the Company.
"F" — Subject to sinking fund requirements.

Except for the Notes of the Company issued with detachable Equity Contracts, the CMNC 4.70% Capital Notes and the NCB Notes and Debentures, all of the Long-Term Notes and Debentures are redeemable in whole, or in part, at the option of the Corporation, prior to maturity.

The principal amounts of maturities and sinking fund requirements for Long-Term Notes and Debentures during each of the five years commencing January 1, 1986 follow:

($ in thousands)	Capital Notes 8¾% Due 1986	Capital Notes 14.60% Due 1990	Deutsche Mark Bearer Bonds 6% Due 1993	Swiss Franc Bonds 5¼% Due 1993	Aggregate of NCB Notes and Debentures	Aggregate of CMNC Notes and Debentures	Total
1986	$200,000	—	$ 2,844	$1,683	$ 4,310	$ 361	$209,198
1987	—	—	4,063	1,683	4,310	361	10,417
1988	—	—	4,063	1,683	4,310	361	10,417
1989	—	—	4,063	1,683	5,968	2,893	14,607
1990	—	$3,833	4,063	1,683	4,642	—	14,221
Five-Year Total	$200,000	$3,833	$19,096	$8,415	$23,540	$3,976	$258,860

The per share price at which the Convertible Capital Notes are convertible into common stock of the Company was adjusted in 1984 from $27.50 to $27.1665. The conversion price of the Convertible Subordinated Debentures is $28.75 per share. (Per share amounts restated to reflect the two-for-one stock split declared January 15, 1986).

During 1985, foreign exchange translation adjustments pertaining to the Deutsche Mark Bearer Bonds and the Swiss Franc Bonds were $6,884 thousand and $5,898 thousand, respectively. In addition, $3,561 thousand principal amount of the Deutsche Mark Bearer Bonds and $1,449 thousand principal amount of the Swiss Franc Bonds were repurchased during 1985.

Purchases of certain Long-Term Notes and Debentures, at a discount, resulted in gains of $187 thousand, $2,971 thousand and $294 thousand, before applicable income taxes, in 1985, 1984 and 1983, respectively. These gains are reported in Other Income.

The principal of the Floating Rate Subordinated Notes due 1995 is to be repaid with the net proceeds from the issue of shares of common stock or nonredeemable preferred stock of the Company which have been deposited in a "Note Fund" created pursuant to the indenture under which the Notes were issued. The Note Fund is expected to provide a source of funds for the payment of the Notes, but does not constitute security for the Notes.

Note 12. Redeemable Preferred Stock

A summary of Redeemable Preferred Stock of the Company (stated value $100 per share) outstanding at December 31, 1985, 1984 and 1983 is as follows:

Stated Value ($ in thousands)	1985	1984	1983
6¾% Series B (297,583 Shares, 297,583 Shares and 640,000 Shares, Respectively)	$29,758	$29,758	$ 64,000
7.60% Series C (318,796 Shares, 318,796 Shares and 860,000 Shares, Respectively)	31,880	31,880	86,000
Total Redeemable Preferred Stock (616,379 Shares, 616,379 Shares and 1,500,000 Shares, Respectively)	$61,638	$61,638	$150,000

Dividends on shares of Series B and C are payable quarterly and are cumulative. Shares of Series B and C have liquidation preferences of $100 per share, plus accrued and unpaid dividends. Holders of shares of Series B and C generally have only contingent voting rights. There are no redemption requirements for either series of preferred stock during the next five years.

Both the Series B and the Series C shares may be redeemed, as a whole or in part, at any time, at the option of the Company at $100 per share plus accrued and unpaid dividends. Beginning on April 15, 1999, and on each April 15 thereafter, the Company is to redeem, through an annual sinking fund, 5% of the maximum number of shares of Series B and Series C, until all such shares are redeemed. During 1984, the Corporation retired through a cash tender offer 342,417 shares of Series B and 541,204 shares of Series C ($88 million stated value), resulting in a $28 million gain that was credited to Surplus.

Note 13. Nonredeemable Preferred Stock

A summary of Nonredeemable Preferred Stock of the Company (stated value $50 per share) outstanding at December 31, 1985, 1984 and 1983 is as follows:

($ in thousands)				
Stated Value $50 Per Share, Shares Outstanding at:	10¼% Series D 2,500,000 Shares	Floating Rate Series E[1] 5,000,000 Shares	Floating Rate Series F[1] 4,539,737 Shares	Total Non-redeemable Preferred Stock
December 31, 1985	$125,000	$250,000	$226,987	$601,987
December 31, 1984	125,000	250,000	226,987	601,987
December 31, 1983	125,000	250,000	—	375,000
Adjustable Dividend Rates:				
Minimum Rate	—	7½%	6%	
Maximum Rate	—	16½%	15%	
Dividend Rate Per Annum at Year-End:				
December 31, 1985	10 5/8	11.30%	9.75%	
December 31, 1984	10.5%	13.15%	—	
December 31, 1983	10 5/8	12.40%	—	

[1] Rates based on certain money market rates, except the initial dividends on Series F for each of the first four dividend periods ending August 31, 1984, November 30, 1984, February 28, 1985 and May 31, 1985 were at the rate of $3.10 per share.

Dividends on shares of Series D, E and F are payable quarterly and are cumulative. Shares of Series D, E and F have liquidation preferences of $50 per share, plus accrued and unpaid dividends. Holders of shares of Series D, E and F generally have only contingent voting rights.

Series D: The shares of Series D may be redeemed, as a whole or in part, at any time, at the option of the Company, at $50 per share plus a premium of $3.95 per share until July 1, 1986, declining thereafter, and without premium on and after July 1, 2000, plus accrued and unpaid dividends. Prior to July 1, 1990, the shares of Series D may not be redeemed by using the proceeds of certain refinancing operations if the effective cost of money to the Company is less than the dividend rate on shares of Series D.

Series E: The shares of Series E are not redeemable until June 1, 1987, when they will be redeemable, as a whole or in part, at the option of the Company, at $51.50 per share until June 1, 1992, and thereafter at $50 per share, in each case plus accrued and unpaid dividends.

Series F: In connection with the merger of Lincoln into CMNC, 4,539,737 shares of Series F were issued in July 1984. The shares of Series F are not redeemable until July 1, 1989, when they will be redeemable, as a whole or in part, at the option of the Company, at $50 per share, plus accrued and unpaid dividends.

The shares of Series D, E and F are not subject to any sinking fund or other repurchase or retirement obligation of the Company.

Note 14. Common Stockholders' Equity

A summary of shares of common stock reserved for issuance as of December 31, 1985 follows:

	Shares Reserved*
4¼% Convertible Capital Notes	325,990
6½% Convertible Subordinated Debentures	1,992,846
Equity Contracts issued with the 15½% Notes Due 1992	3,599,712
Floating Rate Subordinated Notes Due 1996	13,700,130
Dividend Reinvestment and Stock Purchase Plan	7,787,330
1978 Non-Qualified Stock Option Plan	473,178
1982 Long-Term Incentive Plan	1,763,222
Lincoln First 1982 Incentive Stock Plan	73,952
Total	29,716,360

*Restated for two-for-one stock split declared January 15, 1986.

The Equity Contracts, which were sold with the 15½% Notes due 1992 as units (each consisting of $1,000 principal amount of such Notes and a $1,000 Equity Contract), are detachable from the 15½% Notes and obligate the registered owners to purchase on May 1, 1992, shares of the Company's common stock at a price of $48.78 per share or the then current market price per share, but not less than $41.67 per share (per share amounts restated for two-for-one stock split declared January 15, 1986). Such purchase obligations are subject to adjustment in certain events and may be paid, in whole or in part, by surrender to the Company of specified obligations.

Interest on the Floating Rate Subordinated Notes due 1996 on each interest payment date is payable in shares of common stock of the Company to the extent that such interest is payable at the rate of 8⅞% per annum.

Under the Dividend Reinvestment and Stock Purchase Plan, domestic stockholders of record, without payment of service charges or brokerage commissions, may reinvest all or part of their quarterly common stock dividends in shares of common stock at prices 5% below current average market prices and may purchase up to $3,000 per quarter in additional common shares at current average market prices.

Unless full cumulative dividends have been paid on all of the outstanding shares of Nonredeemable and Redeemable Preferred Stock of the Company and the Company is not in default or in arrears with respect to any sinking fund or redemption requirement, no cash dividends may be paid on or any payments made to purchase or redeem any shares of common stock of the Company.

Note 15. Stock Option and Incentive Plans

A summary of changes in shares of common stock under option for the years 1985 and 1984 is shown below:*

	Stock Options	Stock Options with Appreciation Rights	Option Price Per Share	Option Price Aggregate ($ in thousands)	Market Value Per Share	Market Value Aggregate ($ in thousands)
Outstanding at December 31, 1983	559,890	430,642	$16½-26⅛	$22,524	$22⅛	$22,473
Granted during 1984	174,596	117,504	19⅛	5,684	19⅛	5,684
Lincoln First Plan Assumed	152,582	13,958	6.617-19.45	2,818	23⅞	3,981
Exercised during 1984	(9,752)	(32,286)	16½-23⅛	(759)	23⅞-25⅞	(1,008)
Canceled during 1984	(36,802)	(26,950)	16½-26⅛	(1,408)	21⅝-24⅝	(1,403)
Outstanding at December 31, 1984	840,814	502,868	6.617-26⅛	28,859	23⅞	32,122
Granted during 1985	201,566	228,234	31½	13,391	31½	13,391
Exercised during 1985	(189,660)	(88,156)	6.617-26⅛	(5,243)	25.125-34½	(8,185)
Canceled during 1985	(9,808)	(6,392)	19⅞-31½	(396)	24⅝-36⅜	(488)
Outstanding at December 31, 1985	842,912	626,554	$6.617-31½	$36,611	$36⅜	$53,816
Exercisable at December 31, 1984	555,840	371,406	$6.617-26⅛	$20,763	$23⅞	$22,167
Exercisable at December 31, 1985	644,554	411,112	$6.617-26⅛	$23,407	$36⅜	$38,400

*Amounts restated to reflect two-for-one stock split declared January 15, 1986.

The Chase Manhattan 1982 Long-Term Incentive Plan (the 1982 Plan) provides for the granting of three types of awards to key personnel: options to purchase shares of common stock with or without related stock appreciation rights, restricted stock units and performance share units.

Pursuant to the Lincoln acquisition, options with or without related stock appreciation rights outstanding under the Lincoln 1982 Incentive Stock Plan were assumed by the Company and restricted shares of common stock of Lincoln were converted into restricted shares of common stock of the Company.

Under the 1982 Plan, options to purchase stock are granted at prices not less than the market price per share on the date of grant and are exercisable not less than one year nor more than ten years from the date of grant. Stock appreciation rights permit their holders to surrender related exercisable options, or any portion thereof, in exchange for cash or stock in an amount equal to the excess of the market price of the common stock on the date the right is exercised over the related option price.

Restricted stock units and restricted stock into which units may be converted entitle their holders to receive common stock after a certain period of continued employment. The holders of restricted stock units are entitled to receive cash payments equivalent to the dividends which would have been received if the units were common stock.

Performance share units entitle their holders to receive cash, shares of common stock or a combination of cash and common stock at the end of the performance period upon the satisfactory attainment of specified financial goals and departmental objectives.

The total number of shares of common stock which may be issued with respect to awards under the 1982 Plan and the total number of performance share units which may be granted under the 1982 Plan may not exceed 1,809,030 shares and 536,400 units, respectively (shares and units restated for two-for-one stock split declared January 15, 1986). At December 31, 1985 and December 31, 1984, respectively, 494,200 and 1,019,400 shares of common stock (share amounts restated for two-for-one stock split declared January 15, 1986) were available for issuance with respect to future grants or awards under the 1982 Plan.

During 1985 and 1984, 127,900 and 73,500 restricted stock units and 91,000 and 96,500 performance share units (units restated for two-for-one stock split declared January 15, 1986) were granted, respectively. Compensation expense is recorded over the service period based on the fair market value of the common stock of the Company at the end of each reported period. The fair market value (market value restated for two-for-one stock split declared January 15, 1986) of the common stock at December 31, 1985 and 1984 was $36⅜ and $23⅞, respectively.

Compensation expense for stock appreciation rights associated with non-qualified stock options granted under the 1982 Plan or the 1978 Non-Qualified Stock Option Plan is recorded based upon the amount by which the market price of the common stock at the end of each reported period exceeds the option price.

For 1985, 1984 and 1983, compensation expense of $12,914,000, $3,612,000 and $1,812,000, respectively, was recognized in connection with stock appreciation rights, restricted stock units and performance share units.

Note 16. Regulatory Limitations

National banks are subject to legal limitations on the amount of dividends that can be paid to their shareholders. The approval of the Comptroller of the Currency is required if the total of all dividends declared by a national bank in any calendar year exceeds such bank's net profits (as defined) for that year, combined with its retained net profits for the preceding two calendar years, less any required transfers to surplus. Under this limitation, the Bank, Chase Lincoln First Bank, N.A. and The Chase Manhattan Bank (USA), N.A. could declare dividends in 1986, without approval of the Comptroller of the Currency, of approximately $352,000,000, $74,000,000 and $118,000,000, respectively, plus an additional amount equal to each bank's retained net profits for 1986 up to the date of any dividend declaration.

The Federal Reserve Act imposes various legal limitations on the extent to which banks which are members of the Federal Reserve System can finance or otherwise supply funds to certain of their affiliates. In particular, each bank is subject to certain restrictions on any extensions of credit to, or other covered transactions, such as certain purchases of assets, with the Company or such affiliates. Such restrictions prevent each bank from lending to the Company and such affiliates unless such extensions of credit are secured by U.S. Treasury or other specified collateral. Further, such secured extensions of credit by each bank are limited in amount as to the Company or any such affiliate to 10 per cent of each bank's capital and surplus and as to the Company and all such affiliates in the aggregate to 20 per cent of each bank's capital and surplus.

Note 17. Recovery of Payments on, and Liquidation of, Assumed U.S. Government Securities Positions

In 1984, the Corporation recovered $49 million ($20 million after taxes) as a result of its settlements with certain defendants in the action it brought against Drysdale Securities Corporation, Drysdale Government Securities, Inc. and others to recover a special loss incurred by the Corporation in 1982, related to the liquidation of securities positions assumed from Drysdale Government Securities, Inc. and performance by the Bank of obligations related to those positions) and of the net recovery realized by the Corporation on certain other transactions relating to the Drysdale situation.

Note 18. International Activities

International activities include the business conducted by overseas offices, as well as international business conducted from domestic offices, principally the Head Office in New York. Because of the close integration of the Corporation's foreign and domestic activities, it is difficult to estimate the amount of assets, liabilities, income and expenses attributable to international activities. Such amounts are based on internal allocations and allowances, which are necessarily subjective. Such allocations of assets, income and expenses to geographic areas are based on the domiciles of obligors. The principal internal allocations and allowances used to estimate the assets, income and expenses related to international activities are as follows:

—Allocation of the cost of funds based substantially on a computed marginal cost of funds concept.

—Allocation of expenses incurred by one geographic area on behalf of another, including general and administrative costs.

—Provision for Possible Loan Losses based on charge-off experience and risk characteristics of the portfolio, including an allocation of the total Reserve for Possible Loan Losses to international activities.

—Allowance for the differences between foreign and United States tax rates.

The following table sets forth estimated Total Assets at December 31, 1985, 1984 and 1983, respectively, and Gross Income, Gross Expenses, Income Before Taxes and Net Income for the respective years then ended:

	1985				
($ in millions)	Total Assets	Gross Income	Gross Expenses	Income Before Taxes	Net Income
Domestic	$46,360	$4,709	$4,170	$539	$371
International:					
Asia	9,070	925	842	83	50
Europe	15,550	1,645	1,570	75	41
Middle East and Africa	2,080	197	208	(11)	(6)
Western Hemisphere	14,130	2,257	2,045	212	109
Total International	40,830	5,024	4,665	359	194
Total	$87,690	$9,733	$8,835	$898	$565

	1984				
($ in millions)	Total Assets	Gross Income	Gross Expenses	Income Before Taxes	Net Income
Domestic	$44,140	$4,409	$3,914	$495	$299
International:					
Asia	10,910	1,055	1,025	30	21
Europe	14,800	1,664	1,654	10	16
Middle East and Africa	2,690	266	264	2	4
Western Hemisphere	14,340	2,487	2,395	92	66
Total International	42,740	5,472	5,338	134	107
Total	$86,880	$9,881	$9,252	$629	$406

	1983				
($ in millions)	Total Assets	Gross Income	Gross Expenses	Income Before Taxes	Net Income
Domestic	$35,570	$3,580	$3,145	$435	$249
International:					
Asia	12,400	958	885	250	49
Europe	16,150	1,514	1,473	41	33
Middle East and Africa	3,540	288	255	33	24
Western Hemisphere	14,260	2,183	2,062	121	75
Total International	46,350	4,943	4,675	268	181
Total	$81,920	$8,523	$7,820	$703	$430

The following is an analysis of certain asset and liability accounts related to international activities at December 31, 1985 and 1984:

($ in millions)	1985	1984
Cash and Noninterest-Bearing Deposits	$ 590	$ 551
Interest-Bearing Deposits Placed with Banks	3,342	3,111
Loans (Based on Domicile Outside the United States):		
Increase in Loans—Domestic Offices	$ 404	$ 421
Increase in Loans—Overseas Offices	29,219	31,753
Total Loans, Gross	29,623	32,174
Less: Unearned Discount	215	209
Total Loans	$29,408	$31,965
A Summary of Loans by Type:		
Real Estate	$ 1,919	$ 1,814
Government and Official Institutions	3,786	3,781
Banks and Other Financial Institutions	3,277	4,796
Commercial and Industrial	18,253	19,870
Other	2,388	1,913
Total Loans, Gross	29,623	32,174
Less: Unearned Discount	215	209
Total Loans	$29,408	$31,965
Deposits:		
Foreign Banks	$ 7,345	$ 8,570
Foreign Governments and Official Institutions	2,635	3,438
Other Foreign Demand Deposits	4,524	3,429
Other Foreign Time and Savings Deposits	18,196	19,043
Total Deposits	$32,700	$34,480
Funds Borrowed:		
Other Borrowed Money	$ 1,829	$ 1,139
Commercial Paper of Bank Subsidiaries	146	75
Long-Term Notes and Debentures	428	349
Total Funds Borrowed	$ 2,403	$ 1,563

The table below shows cross-border outstandings for the countries to which such outstandings totaled more than one per cent of Total Assets at December 31, 1985 and 1984:

($ in millions)	Total	Percentage of Total Assets
Outstandings at December 31, 1985:		
Japan	$3,020	3.4%
Brazil	2,820	3.2
United Kingdom	2,740	3.1
Mexico	1,680	1.9
West Germany	1,420	1.6
Venezuela	1,250	1.4
France	930	1.1
Argentina	920	1.1
Outstandings at December 31, 1984:		
Japan	$2,980	3.4%
United Kingdom	2,840	3.3
Brazil	2,830	3.3
Mexico	1,750	2.0
West Germany	1,690	1.9
France	1,380	1.6
Venezuela	1,280	1.5
Korea	1,230	1.4

Income after applicable income taxes of overseas offices not included in consolidated net income because of restrictions on the remittance of income, net of prior years' remittances, was $(3.1) million, $.4 million and $(3.2) million for the years ended December 31, 1985, 1984 and 1983, respectively. At December 31, 1985, the cumulative amount of such income not included was $1.3 million.

In the years 1985, 1984 and 1983, net foreign exchange transaction losses on investments in overseas branches, subsidiaries and associated companies, included in income, amounted to approximately $9.1 million, $15.2 million and $27.3 million, respectively, after applicable income taxes.

Note 19. Pension Plans

The Corporation has a number of pension plans covering substantially all employees. The cost of the plans charged to operating expenses in 1985, 1984 and 1983 was $41,203,000, $45,265,000 and $47,363,000, respectively, including $18,968,000, $17,085,000 and $33,387,000 respectively, for the Corporation's major defined benefit plan. Past service costs were fully funded in prior years.

The calculation of the cost of the Corporation's major plan in 1985 and 1984 is based on an interest rate assumption which was revised in 1984 from 8.0% to 8.85% to better reflect recent experience and future expectations. Had the current assumption been used in 1983, pension costs for 1983 would have been $14 million lower than reported.

The actuarial present value of accumulated plan benefits and plan net assets at their estimated market value for all defined benefit plans and for the Corporation's major defined benefit plan at December 31, 1985 and 1984 follow:

	All Plans		Major Plan	
($ in millions)	1985	1984	1985	1984
Actuarial Present Value of Accumulated Plan Benefits:				
Vested	$451	$395	$347	$320
Nonvested	53	47	44	40
Total	$504	$442	$391	$360
Net Assets Available for Benefits	$958	$753	$750	$606

In determining the present value of accumulated plan benefits for the Corporation's major defined benefit plan and other plans, a rate of return approximating 8.85% was assumed. In addition to providing pension benefits, the Corporation provides certain health care and life insurance benefits for retired employees. The Corporation recognizes the cost of providing these benefits by expensing them in the year incurred. The 1985 expense for post retirement health care and life insurance benefits was immaterial.

Note 20. Income Taxes

The following table sets forth the income before taxes from domestic and foreign operations for the years ended December 31, 1985, 1984 and 1983, respectively. As specifically defined by the Securities and Exchange Commission for this purpose, the determination of the income of foreign operations is based on the fact that such operations are located outside the United States.

($ in thousands)	1985	1984	1983
Domestic Locations	$615,535	$439,454	$376,199
Foreign Locations	282,048	189,095	326,516
Total	$897,583	$628,549	$702,705

Investment securities gains (losses) included in income before taxes and the applicable taxes for the years ended December 31, 1985, 1984 and 1983, respectively, were as follows:

($ in thousands)	1985	1984	1983
Investment Securities Gains (Losses)	$98,106	$16,704	$24,793
Applicable Income Taxes (Benefits)	49,182	8,839	13,341
Investment Securities Gains (Losses) After Applicable Income Taxes	$48,924	$ 7,865	$11,452

The current and deferred tax provisions for the years ended December 31, 1985, 1984 and 1983, respectively, were as follows:

$ in thousands	1985	1984	1983
Current:			
Federal	$ 27,102	$ 31,125	$ 12,102
State and Local	43,792	14,329	10,343
Foreign	158,392	102,753	100,930
Total Current	229,286	148,207	123,375
Deferred:			
Federal	95,086	80,442	140,347
State and Local	(14,017)	48,374	41,706
Foreign	(11,830)	(24,651)	(13,774)
Total Deferred	69,239	104,165	168,279
Total Provision for Income Taxes	$299,125	$252,372	$291,954

Although not affecting the total tax provision, current tax payments may differ from the amounts treated above as current pending the final determinations as to the timing of certain income, deductions and credits. The effects, if any, of these determinations are reflected in the following year.

The principal items which caused the timing differences resulting in deferred taxes in the years ended December 31, 1985, 1984 and 1983, respectively, and the tax effect of each follow:

$ in thousands	1985	1984	1983
Loan Loss Deduction for Income Tax Purposes Under/Over Provision for Possible Loan Losses Charged to Expenses	$40,968	$ 26,725	$ 55,537
Unadjusted Earnings of Overseas Subsidiaries and Associated Companies	15,818	9,181	4,515
Lease Financing Transactions and Premises and Equipment	80,990	75,179	33,224
Interest on Nonaccrual Loans	(2,066)	(22,288)	39,555
Loan Interest Subject to Refund (CAP Loan Interest)	(250)	18,206	2,311
Other—Net	(16,315)	50,612	33,137
Total Provision for Deferred Taxes	$ 69,239	$104,165	$168,279

Taxes, other than taxes on income, amounted to $151 million, $132 million and $118 million for the years 1985, 1984 and 1983, respectively.

The provisions for income taxes for each of the years ended December 31, 1985, 1984 and 1983, respectively, vary from the amounts computed by applying the applicable U.S. Federal income tax rate to income before taxes. The principal reasons for these differences, which result in a lower effective tax rate, follow:

	1985		1984		1983	
($ in thousands)	Amount	Percent of Income Before Taxes	Amount	Percent of Income Before Taxes	Amount	Percent of Income Before Taxes
Provision Applicable to Net Income at U.S. Federal Income Tax Rate	$412,888	46.00%	$289,133	46.00%	$323,244	46.00%
Increase (Decrease) in:						
Tax-Exempt Interest on Investments in State and Political Subdivision Securities	(64,191)	(7.15)	(52,715)	(8.39)	(38,006)	(5.41)
Tax-Exempt Interest—Loans	(50,371)	(5.61)	(44,837)	(7.13)	(34,335)	(4.89)
State and Local Income Taxes, Net of Federal Income Tax Benefits	21,858	2.44	23,714	3.77	21,730	3.09
Other—Net	12,581	1.39	7,436	1.19	465	.07
Provision Applicable to Net Income	332,765	37.07	222,731	35.44	273,098	38.86
Provision Applicable to Foreign Exchange Translation Adjustments Included in Stockholders' Equity	(33,640)	(2.30)	29,641	2.69	18,856	2.08
Total Provision for Income Taxes	$299,125	34.77%	$252,372	38.13%	$291,954	40.94%

Note 21. Earnings per Common Share

Primary earnings per common share amounts are computed by dividing Net Income after deduction of preferred stock dividends by the average number of common shares outstanding during the period. Per common share amounts assuming full dilution give effect to the assumed conversion of all outstanding convertible capital notes and debentures and the assumed exercise of outstanding dilutive stock options and conversion of restricted stock units. Average common shares on a fully diluted basis for the years 1985, 1984 and 1983 were 78,553,000, 74,835,000 and 72,646,000, respectively, (restated for two-for-one stock split declared January 15, 1986).

Note 22. Pledged Assets and Required Reserves

Pledged assets consisted of certain investment and trading account securities and other assets aggregating approximately $6.1 billion at December 31, 1985. Of these, approximately $1.3 billion were pledged to secure repurchase agreements and approximately $4.8 billion were pledged to secure public and trust deposits and for other purposes.

In addition, the Bank and certain banking subsidiaries of the Company are required to maintain average reserves on deposit with Federal Reserve Banks against outstanding domestic deposit liabilities. The reserves, which are included in Cash and Due from Banks, were $383 million and $390 million at December 31, 1985 and 1984, respectively. Average required reserves during 1985 and 1984 were $746 million and $595 million, respectively.

Note 23. Commitments and Contingent Liabilities

In the normal course of business, the Corporation makes various commitments and incurs certain contingent liabilities which are not reflected in the accompanying financial statements. A summary of certain of these commitments and contingent liabilities at December 31, 1985 follows:

	($ in thousands)
Commitments to Extend Credit	27,900,000
Standby Letters of Credit and Foreign Office Guarantees	11,500,000
Other Letters of Credit	2,600,000
Foreign Exchange Contracts—Purchases	80,900,000
Futures and Forward Contracts:	
Commitments to Purchase	2,200,000
Commitments to Sell	1,400,000
Acceptance Participations Sold	950,000

Standby Letters of Credit and Foreign Office Guarantees

Total standby letters of credit and foreign office guarantees (SBLCs) have been reduced by approximately $2.1 billion for SBLCs participated to other financial institutions or collateralized by cash or marketable securities. Fees from issuing SBLCs are recognized principally over the period to maturity. Losses, if any, are charged to the Reserve for Possible Loan Losses. These SBLCs have an average risk profile comparable to investment grade obligations.

SBICs have been issued in support of the following obligations:

	Approximate Percentage	Approximate Remaining Average Maturities (Months)
Private debt	15%	30
Public debt	5	60
Purchase of products and services	45	10
Other	35	10

Interest-Rate Swaps

Notional principal on outstanding interest-rate swap transactions in which Chase acts as principal approximated $10 billion at December 31, 1985. The hypothetical risk associated with these contracts calculated on a present value basis using current market rates approximated $270 million at December 31, 1985. Because this analysis is based on current market rates, this amount will increase or decrease during the life of the contracts primarily as a function of maturity and market interest rates.

Guarantees

The Company, in the normal course of business, may guarantee the obligations of its subsidiaries. A summary of certain of these guarantees at December 31, 1985 follows:

—The Chase Manhattan Bank of Canada—up to Canadian $500 million or its equivalent in other currencies for commercial paper, acceptances and certain other obligations.
—The Chase Manhattan Bank (USA), N.A.—$350 million in borrowings from the Student Loan Marketing Association secured by student loans held in the Bank's portfolio.
—Chase Manhattan Overseas Banking Corporation—$150,000,000 (principal amount) of unsecured Floating Rate Notes due 1993, $32,300,000 (Deutsche Mark 79,500,000) (principal amount) of unsecured 6% Deutsche Mark Bearer Bonds due 1993 and $30,288,000 (Swiss Franc 63,000,000) (principal amount) of unsecured 4% Swiss Franc Bonds due 1993.
—Chase Manhattan, S.A.—$97,485,000 (French Franc 750,000,000) (principal amount) of unsecured Floating Rate Bonds due 1992 and $45,493,000 (French Franc 350,000,000) (principal amount) of unsecured Floating Rate Bonds due 1993.
—Chase Manhattan National Corporation—$21,090,000 (principal amount) of unsecured 8¼% Debentures due 1996.

These guarantees rank on a parity with all other unsecured and unsubordinated indebtedness of the Company.

Lease Commitments

The Corporation leases many properties under standard real estate leases which include renewal options and escalation clauses. Equipment is rented under both long-term and month-to-month leases. Certain of these leases are cancelable in the normal course of business without substantial penalty. Rental expense charged to operating expenses in 1985, 1984 and 1983 was approximately $187,502,000, $165,735,000 and $152,949,000, respectively.

Minimum future rentals under long-term noncancelable operating leases at December 31, 1985 are shown below:

Years	($ in thousands)
1986	$ 131,320
1987	116,040
1988	106,525
1989	100,661
1990	92,315
1991 and Thereafter (Aggregate)	805,651
Total Minimum Future Rentals	$1,352,412

Note 24. Litigation

Various actions and proceedings are pending against the Company, the Bank and certain of their subsidiaries, in which claims for substantial money damages are asserted. Management, after consultation with legal counsel, is of the opinion that the ultimate effect on the Corporation of all such pending actions and proceedings would not be material in relation to its financial position.

Note 25. Fees and Commissions

Fees and Commissions included trust and fiduciary investment fees of $193,334,000, $154,056,000 and $119,589,000 for the years 1985, 1984 and 1983, respectively.

Note 26. Notes Receivable From Nonbanking Subsidiaries (Company Only Financial Statements)

Notes Receivable from Nonbanking Subsidiaries of the Company are evidenced by promissory notes. The average interest rates earned on these notes were 9.20%, 11.73% and 11.60% for the years 1985, 1984 and 1983, respectively. These notes represent funding of the nonbanking subsidiaries.

Note 27. Summarized Financial Information of Chase Manhattan National Corporation

On July 1, 1984, Lincoln merged into CMNC as further discussed in Note 3 of the Notes to Financial Statements. The following summarized financial data of CMNC, are being reported because a class of Lincoln's debt securities are publicly held. In connection with the merger CMNC assumed, and subsequently the Company guaranteed, Lincoln's 8¼% Debentures due 1996. Set forth below is summarized financial information for CMNC and Lincoln for the periods indicated. Information for periods prior to July 1, 1984 is on Lincoln's historical cost basis. Subsequent information gives effect to the purchase method of accounting.

Statement of Income Information

($ in millions)	Year Ended December 31, 1985	1984
Net Interest Income After Provision For Possible Loan Losses	$144	$157
Net Income	43	31

Statement of Condition Information

($ in millions)	December 31, 1985	1984
Loans	$2,986	$2,621
Total Assets	4,164	4,227
Deposits	3,319	3,206
Total Liabilities	3,792	3,898
Stockholder's Equity	372	329
Total Liabilities and Stockholder's Equity	4,164	4,227

Independent Accountants' Report

The Chase Manhattan Corporation and Subsidiaries

Price Waterhouse

153 East 53rd Street
New York, New York 10022

To the Board of Directors and Stockholders of
The Chase Manhattan Corporation

In our opinion, the accompanying consolidated statement of condition of The Chase Manhattan Corporation and Subsidiaries, the balance sheet of The Chase Manhattan Corporation (Company Only) and the consolidated statement of condition of The Chase Manhattan Bank, N.A. and Subsidiaries and the related statements of income, changes in stockholders' equity and changes in financial position present fairly the financial position of The Chase Manhattan Corporation and Subsidiaries, The Chase Manhattan Corporation (Company Only) and The Chase Manhattan Bank, N.A. and Subsidiaries at December 31, 1985 and 1984, and the results of their operations and the changes in their financial position for each of the three years in the period ended December 31, 1985, in conformity with generally accepted accounting principles consistently applied. Our examinations of these statements were made in accordance with generally accepted auditing standards and accordingly included such tests of the accounting records and such other auditing procedures as we considered necessary in the circumstances.

Price Waterhouse

January 15, 1986

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Report of Management

The Chase Manhattan Corporation and Subsidiaries

To the Stockholders

Management is responsible for the content of the financial statements included in this annual report and the information contained in other sections of this annual report, which information is believed to be consistent with the content of the financial statements. Management believes that the financial statements have been prepared in conformity with generally accepted accounting principles appropriate in the circumstances to reflect, in all material respects, the substance of events and transactions that should be included. The financial statements of necessity reflect Management's judgments and estimates as to the effects of events and transactions that are accounted for or disclosed.

Management has long recognized the importance of the Corporation maintaining and reinforcing the highest possible standards of conduct in all of its actions, including the preparation and dissemination of statements fairly presenting the financial condition of the Corporation. In this regard, it has developed a system of internal accounting control which plays an important role in assisting Management in fulfilling its responsibilities in preparing the Corporation's financial statements. The Corporation's system of internal accounting control is designed to provide reasonable assurance that assets are safeguarded and that transactions are executed in accordance with Management's authorizations and recorded properly to permit the preparation of financial statements in accordance with generally accepted accounting principles. This system is augmented by written policies and procedures and by an independent worldwide internal audit staff, which reports to the Audit Committee of the Board of Directors. Management recognizes that because of cost-benefit considerations and other inherent limitations on the effectiveness of any internal accounting control system, some errors and irregularities may occur. However, Management believes that the Corporation's internal accounting control system provides reasonable assurance that errors or irregularities that could be material to the financial statements are prevented or would be detected on a timely basis and corrected in the normal course of business.

The Audit Committee of the Board of Directors, composed entirely of outside Directors, has responsibility for recommending the independent public accountants for the Corporation who are appointed by the Board of Directors. The Audit Committee reviews with the independent public accountants the scope of their audit and audit reports and meets with them on a scheduled basis to review their findings and any action to be taken thereon. In addition, the Committee meets separately with the internal auditors and with Management to review the scope of the internal audit program and the performance and findings of the internal audit staff and any action to be taken by Management. The independent public accountants and the internal auditors have free access to the Committee without Management being present, as the Committee deems necessary.

The independent public accountants are engaged in their annual audit function to express an opinion on the Corporation's financial statements, which opinion is based on their performance of generally accepted auditing procedures believed by them to be sufficient to provide reasonable assurance that the financial statements included in this annual report are not materially misleading and do not contain material errors.

J C Butcher

Chairman and Chief Executive Officer

Michael C. Laforest Jr.

Executive Vice President and Controller

January 15, 1986

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Consolidated Summary of Assets, Liabilities and Stockholders' Equity

The Chase Manhattan Corporation and Subsidiaries

In millions	December 31				
	'85	'84	'83	'82	'81
Assets					
Cash and Due from Banks	$ 5,574,055	$ 4,497,301	$ 4,440,105	$ 4,517,214	$ 3,263,010
Interest-Bearing Deposits Placed with Banks	4,957,648	4,355,191	3,858,645	7,390,748	10,233,566
Federal Funds Sold and Securities Purchased under Resale Agreements	1,174,371	1,093,205	175,123	263,490	592,956
Trading Account Assets	1,344,465	1,354,571	279,548	1,202,496	1,113,697
Investment Securities					
U.S. Treasury Securities	1,839,207	1,734,862	984,795	1,996,559	1,253,279
Federal Agency Securities	330,259	192,963	153,428	213,249	500,274
State and Political Subdivision Securities	2,410,373	2,102,785	1,582,976	1,163,651	1,356,517
Other Bonds, Notes and Debentures	1,408,541	1,070,934	587,021	644,480	645,742
Federal Reserve Bank and Other Stock Investments	134,012	144,262	109,879	112,132	95,067
Total Investment Securities	6,122,392	5,245,806	3,418,109	4,129,871	3,850,879
Loans	61,930,527	62,003,336	55,893,528	55,531,541	51,331,191
Less: Reserve for Possible Loan Losses	907,672	761,439	564,110	558,277	541,082
Loans, Net	61,022,855	61,241,947	55,329,418	54,973,264	50,790,109
Customers' Liability on Acceptances	2,820,471	5,250,637	6,571,416	3,813,382	3,552,229
Accrued Interest Receivable	1,028,983	1,191,949	1,072,970	1,220,567	1,479,525
Premises and Equipment	913,580	793,546	544,742	514,127	431,068
Other Assets	3,013,139	1,958,365	1,431,270	2,227,024	1,865,399
Total Assets	$87,885,442	$86,893,015	$81,921,449	$80,262,903	$77,839,338
Liabilities and Stockholders' Equity					
Deposits:					
Domestic Offices					
Noninterest-Bearing	$13,490,638	$11,149,045	$ 9,938,372	$10,191,118	$ 9,706,147
Interest-Bearing	19,130,323	17,733,964	13,370,594	11,746,385	14,012,492
Overseas Offices					
Noninterest-Bearing	1,939,120	1,423,674	1,393,139	1,449,775	1,617,831
Interest-Bearing	26,783,968	29,373,298	31,597,452	33,470,569	29,903,199
Total Deposits	61,353,049	59,680,011	56,299,557	56,857,847	55,239,670
Federal Funds Purchased and Securities Sold under Repurchase Agreements	4,131,793	4,440,290	3,740,693	5,055,844	4,854,867
Commercial Paper	3,483,501	4,408,866	4,286,458	3,316,917	4,296,208
Other Borrowed Money	4,671,994	3,235,446	3,534,634	4,366,202	1,860,146
Acceptances Outstanding	2,828,696	5,362,300	6,642,711	3,865,261	3,603,432
Accrued Interest Payable	668,981	803,730	675,913	785,803	1,057,144
Accounts Payable, Accrued Expenses and Other Liabilities	3,282,175	2,567,905	1,789,866	2,282,856	2,919,714
	80,420,189	80,340,133	76,969,834	76,530,750	73,827,331
Long-Term Notes and Debentures	2,806,499	2,520,198	1,375,790	1,045,740	944,408
Total Liabilities	83,226,668	82,860,336	78,345,624	77,576,490	74,841,739
Redeemable Preferred Stock	61,638	61,638	150,000	150,000	250,000
Nonredeemable Preferred Stock	601,987	601,987	375,000	375,000	125,000
Common Stockholders' Equity					
Common Stock	964,472	458,246	434,262	423,951	413,613
Surplus	276,288	678,342	564,195	563,266	526,080
Foreign Exchange Translation Adjustments	22,265	(18,730)	(22,341)	(13,921)	--
Retained Earnings	2,576,654	2,241,199	2,044,709	1,788,117	1,662,906
Total Common Stockholders' Equity	3,795,149	3,359,057	3,050,825	2,761,413	2,602,599
Total Liabilities and Stockholders' Equity	$87,885,442	$86,893,018	$81,921,449	$80,262,903	$77,839,338

Average Balances, Interest and Average Rates—Taxable Equivalent

The Chase Manhattan Corporation and Subsidiaries

(In millions, based on daily averages)	1985 Average Balance	Interest	Average Rate
Assets			
Interest-Earning Assets:			
Interest-Bearing Deposits Placed with Banks	$ 5,127	$ 486	9.48%
Federal Funds Sold and Securities Purchased Under Resale Agreements	2,236	244	8.65
Trading Account Assets	764	82	10.79
Investment Securities:			
Domestic Offices:			
U.S. Treasury Securities	1,826	191	10.43
Federal Agency Securities	240	25	10.54
State and Political Subdivision Securities	1,985	262	13.11
Other Securities	259	27	10.41
Total Domestic Offices	4,310	505	11.67
Overseas Offices	1,217	202	16.57
Total Investment Securities	5,527	707	12.74
Loans:			
Domestic Offices	25,202	3,064	12.16
Overseas Offices	36,334	4,219	11.61
Total Loans	61,536	7,283	11.83
Less: Reserve for Possible Loan Losses*	533	—	—
Loans, Net	60,703	7,283	11.83
Total Interest-Earning Assets,* Net	73,365	8,663	11.68
Summary—Gross Interest-Earning Assets:			
Domestic Offices	31,247	3,714	11.88
Overseas Offices	42,951	4,949	11.52
Total Gross Interest-Earning Assets	74,198	8,663	11.68
Noninterest-Earning Assets:			
Cash and Due from Banks	4,448		
Customers' Liability on Acceptances	4,025		
Other Assets	4,453		
Total Noninterest-Earning Assets	12,926		
Total Assets	$86,291		
Liabilities and Stockholders' Equity			
Interest-Bearing Liabilities:			
Interest-Bearing Deposits:			
Domestic Offices:			
Savings and Negotiable Order of Withdrawal Deposits	$ 1,901	$ 98	5.16%
Savings Certificates and Nest Egg Account Deposits	393	35	8.84
Money Market Deposits	7,693	561	7.29
Negotiable Certificates of Deposit	903	76	8.35
Other Time Deposits	7,348	677	9.21
Total Domestic Offices	18,243	1,447	7.93
Overseas Offices	30,705	2,829	9.21
Total Interest-Bearing Deposits	48,948	4,276	8.74
Federal Funds Purchased and Securities Sold Under Repurchase Agreements	4,804	462	9.61
Other Borrowed Money:			
Domestic Offices	5,369	476	8.86
Overseas Offices	1,224	215	17.59
Total Other Borrowed Money	6,593	691	10.48
Long-Term Notes and Debentures	2,525	240	9.51
Total Interest-Bearing Liabilities	62,870	5,669	9.02
Summary—Interest-Bearing Liabilities:			
Domestic Offices	22,240	1,800	8.10
Overseas Offices	40,630	3,869	9.52
Noninterest-Bearing Liabilities:			
Deposits in Domestic Offices	9,822		
Deposits in Overseas Offices	1,438		
Acceptances Outstanding	4,068		
Accounts Payable, Accrued Expenses and Other Liabilities	3,906		
Total Noninterest-Bearing Liabilities	19,234		
Total Liabilities	82,104		
Redeemable Preferred Stock	162		
Nonredeemable Preferred Stock	602		
Common Stockholders' Equity	3,423		
Total Liabilities and Stockholders' Equity	$86,291		
Taxable Equivalent Net Interest Income and Average Interest Rate Spread		$2,994	2.66%
Net Interest Income as a Percentage of Gross Interest-Earning Assets			4.03%

*Reserve for possible loan losses is excluded from calculations of average balances and average rates, as appropriate.
Note: Loan amounts include nonaccrual and restructured loans, as appropriate.

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	1984			1983			3rd Qtr 1985			3rd Qtr 1984		
	Average Balance	Interest	Average Rate	Average Balance	Interest	Average Rate	Average Balance	Interest	Average Rate	Average Balance	Interest	Average Rate
	$ 7,015	$ 774	11.03%	$ 7,792	$ 732	9.40%	$ 5,042	$ 121	9.56%	$ 4,960	$ 138	11.28%
	772	77	10.05	619	57	9.12	1,408	39	10.12	807	24	9.40
	425	54	12.67	521	52	10.06	977	24	11.02	586	17	11.61
	1,484	171	11.46	1,682	198	11.78	1,743	44	9.98	1,556	45	11.28
	201	21	10.48	163	16	9.55	311	7	9.36	237	7	11.34
	1,595	222	13.92	1,196	157	13.14	2,040	67	12.87	2,008	73	14.42
	213	13	6.24	161	16	10.16	243	6	9.63	270	4	7.37
	3,498	427	12.21	3,202	387	12.10	4,337	124	11.28	4,071	129	12.61
	841	94	11.18	612	109	17.71	1,418	59	16.43	1,059	35	13.32
	4,339	521	12.01	3,814	496	13.00	5,755	183	12.55	5,130	164	12.76
	22,969	3,012	13.11	19,513	2,367	12.13	26,435	808	12.13	24,958	821	13.08
	36,741	4,742	12.91	34,074	4,133	12.13	35,048	1,025	11.60	37,535	1,248	13.23
	59,710	7,754	12.99	53,587	6,500	12.13	61,483	1,833	11.83	62,493	2,069	13.17
	659	—	—	569	—	—	902	—	—	757	—	—
	59,051	7,754	12.99	53,018	6,500	12.13	60,581	1,833	12.01	61,736	2,069	13.17
	71,602	9,180	12.70	65,764	7,837	11.81	73,663	2,197	11.69	73,409	2,412	12.94
	27,667	3,568	12.90	23,952	2,871	11.98	32,528	967	11.80	30,525	988	12.89
	44,594	5,612	12.58	42,381	4,966	11.72	42,037	1,230	11.61	43,641	1,424	12.98
	72,261	9,180	12.70	66,333	7,837	11.81	74,565	2,197	11.69	74,166	2,412	12.94
	4,354			4,551			4,905			4,472		
	5,743			5,737			3,184			4,727		
	3,642			3,019			4,797			4,230		
	13,739			13,307			12,886			13,429		
	$85,341			$79,071			$86,549			$86,838		
	$ 1,611	$ 82	5.09%	$ 1,440	$ 73	5.03%	$ 1,909	$ 25	5.12%	$ 1,853	$ 24	5.14%
	382	36	9.48	1,293	118	9.10	359	9	9.24	416	9	8.84
	4,994	469	9.39	3,742	333	8.91	8,368	147	6.99	5,968	135	9.03
	1,364	143	10.50	2,665	247	9.28	911	18	7.93	1,154	31	10.62
	7,067	793	11.23	3,111	336	10.80	7,340	162	8.76	8,303	245	11.71
	15,418	1,523	9.88	12,251	1,107	9.03	18,887	361	7.58	17,694	444	9.98
	33,057	3,473	10.51	31,268	2,981	9.53	29,929	645	8.56	33,158	859	10.30
	48,475	4,996	10.31	43,519	4,088	9.39	48,816	1,006	8.18	50,852	1,303	10.19
	5,204	548	10.52	6,116	555	9.07	4,823	125	10.32	5,268	135	10.20
	6,164	653	10.59	5,835	542	9.28	5,061	113	8.90	5,277	136	10.29
	1,237	252	20.35	1,028	197	19.22	1,484	92	24.53	1,191	58	19.43
	7,401	905	12.22	6,863	739	10.77	6,545	205	12.44	6,468	194	11.97
	1,795	194	10.81	1,083	108	9.95	2,690	62	9.10	2,051	56	10.87
	62,875	6,643	10.57	57,581	5,490	9.53	62,974	1,398	8.92	64,639	1,688	10.39
	19,592	1,957	9.99	16,540	1,494	9.03	23,209	454	7.77	22,161	556	9.99
	43,293	4,686	10.83	41,041	3,996	9.74	39,665	944	9.44	42,478	1,132	10.60
	8,843			8,731			10,562			9,308		
	1,250			1,223			1,614			1,251		
	5,866			5,795			3,220			4,061		
	2,755			2,342			3,925			2,844		
	18,714			18,091			19,321			18,264		
	81,589			75,672			82,195			82,903		
	95			150			62			62		
	489			375			602			602		
	3,168			2,874			3,690			3,271		
	$85,341			$79,071			$86,549			$86,838		
		$6,337	8.13%		$2,347	3.04%		$ 789	3.87%		$ 724	3.55%
			3.51%			3.54%			4.35%			3.88%

Summary Quarterly Statement of Income for 1985

The Chase Manhattan Corporation and Subsidiaries

	Quarter Ended			
[$ in thousands, except per common share data]	Dec. 31, 1985	Sept. 30, 1985	June 30, 1985	March 31, 1985
Interest Income	$2,131,271	$2,068,141	$2,103,316	$2,114,477
Interest Expense	1,398,239	1,369,271	1,442,726	1,468,678
Net Interest Income	733,032	698,870	660,590	645,799
Provision for Possible Loan Losses	125,000	110,000	105,000	95,000
Net Interest Income After Provision for Possible Loan Losses	608,032	588,870	555,590	550,799
Other Operating Income	381,309	321,231	329,742	283,356
Other Operating Expenses	744,216	688,377	667,058	622,227
Income Before Taxes	245,125	221,974	218,514	211,970
Applicable Income Taxes	94,445	72,550	87,699	78,071
Net Income	$ 150,680	$ 149,424	$ 130,815	$ 133,899
Net Income Applicable to Common Stock	$ 133,484	$ 132,143	$ 107,135	$ 107,311
Average Shares Outstanding*	76,789,784	75,898,388	74,497,664	73,735,222
Earnings Per Common Share:*				
Primary, Based on Average Shares Outstanding	$ 1.74	$ 1.74	$ 1.44	$ 1.46
Assuming Full Dilution	1.68	1.68	1.38	1.41
Cash Dividends Declared Per Common Share*	$ .47½	$ .47½	$ .47½	$ .47½

Summary Quarterly Statement of Income for 1984

	Quarter Ended			
[$ in thousands, except per common share data]	Dec. 31, 1984	Sept. 30, 1984	June 30, 1984	March 31, 1984
Interest Income	$2,343,060	$2,468,612	$2,108,875	$2,031,131
Interest Expense	1,688,709	1,879,533	1,575,564	1,499,381
Net Interest Income	654,351	589,079	533,311	531,750
Provision for Possible Loan Losses	90,000	125,000	75,000	75,000
Net Interest Income After Provision for Possible Loan Losses	564,351	464,079	458,311	456,750
Other Operating Income	264,804	237,771	220,513	206,490
Other Operating Expenses	630,073	564,842	536,832	512,779
Income Before Taxes	199,082	137,008	141,992	150,461
Applicable Income Taxes	78,973	43,998	51,787	47,973
Net Income	$ 120,109	$ 93,010	$ 90,205	$ 102,494
Net Income Applicable to Common Stock	$ 93,427	$ 61,137	$ 77,483	$ 88,654
Average Shares Outstanding*	72,928,852	71,952,776	70,039,596	69,660,640
Earnings Per Common Share:*				
Primary, Based on Average Shares Outstanding	$ 1.28	$ .85	$ 1.11	$ 1.27
Assuming Full Dilution	1.23	.82	1.06	1.22
Cash Dividends Declared Per Common Share*	$ .45½	$ .45½	$ .45½	$ .45½

Summary Quarterly Statement of Income for 1983

	Quarter Ended			
[$ in thousands, except per common share data]	Dec. 31, 1983	Sept. 30, 1983	June 30, 1983	March 31, 1983
Interest Income	$1,998,963	$1,930,490	$1,824,424	$1,898,958
Interest Expense	1,454,044	1,375,127	1,313,295	1,347,314
Net Interest Income	544,919	561,363	511,129	551,644
Provision for Possible Loan Losses	75,000	70,000	70,000	70,000
Net Interest Income After Provision for Possible Loan Losses	469,919	491,363	441,129	481,644
Other Operating Income	222,854	203,697	228,582	199,077
Other Operating Expenses	508,296	515,090	512,552	509,622
Income Before Taxes	184,477	179,970	157,159	171,099
Applicable Income Taxes	74,343	71,750	62,016	64,989
Net Income	$ 110,134	$ 108,220	$ 95,143	$ 106,110
Net Income Applicable to Common Stock	$ 86,339	$ 85,205	$ 72,352	$ 83,210
Average Shares Outstanding*	69,290,536	68,935,694	68,574,132	68,177,990
Earnings Per Common Share:*				
Primary, Based on Average Shares Outstanding	$ 1.39	$ 1.38	$ 1.34	$ 1.37
Assuming Full Dilution	1.33	1.31	1.28	1.30
Cash Dividends Declared Per Common Share*	$ .43¾	$ .43¾	$ .43¾	$ .43¾

*Amounts restated to reflect two-for-one stock split declared January 15, 1986.

Consolidated Analysis of Loan Loss Experience

The Chase Manhattan Corporation and Subsidiaries

	Year Ended December 31,				
	1985	1984	1983	1982	1981
Loans ($ in millions)					
—Outstanding Balance of Loans	$ 61,931	$ 62,003	$ 55,894	$ 55,532	$ 51,331
—Average Balance of Loans	61,536	59,710	53,537	52,057	47,434
Reserve for Possible Loan Losses at Beginning of Year ($ in thousands)	$761,439	$564,110	$558,277	$541,082	$467,807
Charge-Offs:					
Domestic Loans:					
Commercial and Industrial Loans	125,909	127,929	164,437	145,520	78,862
Loans to Financial Institutions	11,000	—	2,592	4,000	5,303
Loans for Purchasing or Carrying Securities	—	700	—	2,690	1,918
Real Estate Loans	14,551	2,596	1,070	2,802	11,296
Loans to Individuals for Personal Expenditures	149,974	73,755	47,671	44,570	37,998
Lease Financings	1,175	816	37	4,102	—
Other Loans	1,204	1,075	—	529	457
Total Domestic Loans	303,813	206,871	215,807	204,213	135,914
International Loans:					
Commercial and Industrial Loans	67,317	52,893	82,106	62,332	21,799
Real Estate Loans	1,404	8,293	17,007	24,331	2,372
Loans to Individuals for Personal Expenditures	13,947	4,830	12,700	4,700	4,997
Loans to Foreign Governments and Official Institutions	30,672	5,581	1,531	17,100	—
Other Loans	676	66	—	5,241	567
Total International Loans	114,016	71,663	113,344	113,704	29,735
Total Charge-Offs	417,829	278,534	329,151	317,917	165,649
Recoveries:					
Domestic Loans:					
Commercial and Industrial Loans	33,069	18,077	28,238	24,293	7,571
Loans to Financial Institutions	10,721	7,909	11,947	13,401	11,297
Loans for Purchasing or Carrying Securities	3	43	20	1,713	612
Real Estate Loans	6,300	3,471	6,231	3,101	1,571
Loans to Individuals for Personal Expenditures	18,496	14,959	13,156	10,340	6,174
Lease Financings	177	30	10	2	—
Other Loans	746	382	742	772	499
Total Domestic Loans	69,512	44,871	60,344	53,622	27,724
International Loans:					
Commercial and Industrial Loans	19,060	12,619	7,967	28,403	6,558
Real Estate Loans	1,263	721	2,921	3,776	717
Loans to Individuals for Personal Expenditures	6,335	3,117	3,335	1,961	3,540
Loans to Foreign Governments and Official Institutions	645	261	—	1	27
Other Loans	660	1,583	75	179	1,182
Total International Loans	27,963	18,301	14,298	34,319	12,024
Total Recoveries	97,475	63,172	74,642	87,941	39,748
Net Charge-Offs	320,354	215,362	254,509	229,976	125,901
Provision Charged to Expenses	435,000	365,000	285,000	263,000	211,000
Reserves of Acquired Subsidiaries	24,120	64,932	—	—	—
Foreign Exchange Translation Adjustments	7,467	(17,241)	(24,658)	(15,829)	(11,824)
Reserve for Possible Loan Losses at End of Year	$907,672	$761,439	$564,110	$558,277	$541,082
Ratios:					
Total Recoveries to Total Charge-Offs	23.3%	22.7%	22.7%	27.7%	24.0%
Net Charge-Offs to:					
Outstanding Balance of Loans	.52	.35	.46	.41	.25
Average Balance of Loans	.52	.36	.47	.44	.26
Reserve for Possible Loan Losses	35.3	28.3	45.1	41.2	23.3
Provision for Possible Loan Losses	73.6	59.0	89.3	87.4	59.7
Reserve for Possible Loan Losses to:					
Outstanding Balance of Loans	1.47	1.23	1.01	1.01	1.05
Average Balance of Loans	1.48	1.28	1.05	1.07	1.14
Summary of Net Charge-Offs:					
Domestic Loans	$234,301	$162,000	$155,463	$150,591	$108,190
International Loans	86,053	53,362	99,046	79,385	17,711
Total Net Charge-Offs	$320,354	$215,362	$254,509	$229,976	$125,901

Selected Loan Maturities and Sensitivity to Changes in Interest Rates

The Chase Manhattan Corporation and Subsidiaries

($ in millions)	Within 1 Year	After 1 but Within 5 Years	After 5 Years	Total
Remaining Maturities of Selected Loans as of December 31, 1985:				
Domestic Offices:				
Real Estate Loans:				
Construction and Land Development	$ 1,230	$ 1,165	$ 32	$ 2,427
Other Real Estate Loans (Excluding Loans Secured by 1–4 Family Residential Properties)	331	533	380	1,244
Loans to Financial Institutions:				
Mortgage Companies	232	36	12	280
Domestic Commercial Banks	141	1	—	142
Banks in Foreign Countries	325	2	—	327
Other Depositary Institutions	6	—	—	6
Other Financial Institutions	448	413	67	928
Loans for Purchasing or Carrying Securities	482	21	—	503
Commercial and Industrial Loans	4,785	3,353	617	8,755
Tax-Exempt Loans	414	523	756	1,693
Other Loans (Excluding Loans to Individuals for Personal Expenditures and Lease Financings)	564	73	18	655
Total Domestic Offices	8,958	6,120	1,882	16,960
Overseas Offices	18,969	10,369	4,889	34,227
Total Selected Loans	$27,927	$16,489	$ 6,771	$51,187
Interest Rate Sensitivity of Selected Loans:*				
Domestic Offices: —Fixed Rate		$ 2,262	$ 890	
—Variable Rate		3,858	992	
—Total		6,120	1,882	
Overseas Offices: —Fixed Rate		3,002	1,168	
—Variable Rate		7,367	3,721	
—Total		10,369	4,889	
Consolidated: —Fixed Rate		5,264	2,058	
—Variable Rate		11,225	4,713	
—Total		$16,489	$ 6,771	

*Excludes loans in domestic offices secured by 1–4 family residential properties, loans to individuals for personal expenditures and lease financings.

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Consolidated Loan Balances by Type and Percentage Distribution

The Chase Manhattan Corporation and Subsidiaries

	December 31,									
($ in millions)	1985		1984		1983		1982		1981	
Domestic Offices:										
Real Estate Loans:										
Construction and Land Development	$ 2,427	3.9%	$ 2,009	3.2%	$ 1,552	2.8%	$ 1,566	2.8%	$ 1,197	2.3%
Secured by 1-4 Family Residential Properties	2,669	4.3	1,722	2.7	1,307	2.3	1,237	2.2	1,280	2.5
Other Real Estate Loans	1,244	2.0	1,052	1.7	821	1.5	826	1.5	785	1.5
Loans to Financial Institutions:										
Mortgage Companies	280	0.4	208	0.3	132	0.2	132	0.2	118	0.2
Domestic Commercial Banks	142	0.2	70	0.1	84	0.1	91	0.2	89	0.2
Banks in Foreign Countries	327	0.5	353	0.6	339	0.6	356	0.6	418	0.8
Other Depository Institutions	6	—	7	—	2	—	9	—	7	—
Other Financial Institutions	928	1.5	1,163	1.9	1,126	2.0	1,261	2.2	1,083	2.1
Loans for Purchasing or Carrying Securities	503	0.8	543	0.9	718	1.3	1,209	2.2	607	1.2
Commercial and Industrial Loans	8,755	14.0	10,035	16.0	9,736	17.3	9,838	17.6	10,422	20.1
Loans to Individuals for Personal Expenditures	7,407	11.8	5,313	8.5	3,605	6.4	3,085	5.5	2,726	5.3
Lease Financings	1,464	2.3	1,013	1.6	398	0.7	394	0.7	385	0.7
Tax-Exempt Loans	1,693	2.7	1,178	1.9	687	1.2	752	1.4	884	1.7
Other Loans	655	1.0	502	0.8	815	1.4	854	1.5	784	1.5
Total Domestic Offices, Gross	28,500	45.4	25,168	40.2	21,322	37.8	21,610	38.6	20,785	40.1
Less: Unearned Discount	580		460		354		397		372	
Total Domestic Offices	27,920		24,708		20,968		21,213		20,413	
Overseas Offices:										
Real Estate Loans	2,818	4.5	2,279	3.6	1,294	2.3	1,395	2.5	1,578	3.0
Loans to Banks	2,462	3.9	3,743	5.9	3,801	6.7	4,251	7.6	3,547	6.9
Loans to Other Financial Institutions	804	1.3	972	1.6	855	1.5	1,065	1.9	1,136	2.2
Loans to Governments and Official Institutions	3,491	5.6	3,780	6.0	2,735	4.8	2,559	4.6	2,749	5.3
Commercial and Industrial Loans	21,933	35.0	24,663	39.3	24,516	43.5	23,673	42.2	20,552	39.7
Loans to Individuals for Personal Expenditures	1,265	2.0	1,038	1.7	575	1.0	575	1.0	637	1.2
Lease Financings	337	0.5	237	0.4	149	0.3	85	0.1	50	0.1
Other Loans	1,117	1.8	793	1.3	1,147	2.1	843	1.5	791	1.5
Total Overseas Offices, Gross	34,227	54.6	37,505	59.8	35,072	62.2	34,446	61.4	31,040	59.9
Less: Unearned Discount	216		210		146		127		122	
Total Overseas Offices	34,011		37,295		34,926		34,319		30,918	
Total Loans	$61,931		$62,003		$55,894		$55,532		$51,331	

Consolidated Average Loan Balances

	Year Ended December 31,				
($ in millions, based on daily averages)	1985	1984	1983	1982	1981
Domestic Offices:					
Real Estate Loans	$ 5,157	$ 4,263	$ 3,908	$ 3,841	$ 3,623
Loans to Mortgage Companies	300	160	149	100	103
Loans to Other Financial Institutions	1,614	1,982	1,971	2,106	2,244
Loans for Purchasing or Carrying Securities	582	591	633	493	329
Commercial and Industrial Loans	8,990	10,444	8,791	9,633	9,946
Loans to Individuals for Personal Expenditures	6,270	4,285	3,181	2,918	2,364
Lease Financings	1,105	585	370	382	362
Tax-Exempt Loans	1,182	775	626	783	793
Other Loans	468	259	235	274	378
Total Domestic Offices, Gross	25,668	23,344	19,864	20,530	20,142
Less: Unearned Discount	466	375	351	392	302
Total Domestic Offices	25,202	22,969	19,513	20,138	19,840
Overseas Offices	36,527	36,892	34,208	32,033	27,911
Less: Unearned Discount	193	151	134	114	117
Total Overseas Offices	36,334	36,741	34,074	31,919	27,794
Total Average Loans	$61,536	$59,710	$53,587	$52,057	$47,634

Financial Ratios

The Chase Manhattan Corporation and Subsidiaries

	1985	1984	1983	1982	1981
Earnings Ratios					
Net Income as a Percentage of:					
Average Total Interest-Earning Assets	.77%	.57%	.65%	.47%	.67%
Average Total Assets	.65	.48	.54	.40	.55
Average Common Stockholders' Equity*	13.64	10.12	13.11	9.79	15.87
Average Common Stockholders' Equity and Nonredeemable Preferred Stock*	13.58	10.92	12.59	10.01	15.61
Average Common Stockholders' Equity and Total Preferred Stock	13.49	10.82	12.64	9.84	14.78
Net Interest Income (Taxable Equivalent Basis) as a Percentage of:					
Average Total Interest-Earning Assets	4.08%	3.54%	3.57%	3.40%	3.28%
Average Total Assets	3.47	2.97	2.97	2.90	2.67
Cash Dividends Paid on Common Stock as a Percentage of Net Income Applicable to Common Stock	29.60%	40.28%	31.88%	43.92%	26.81%
Total Cash Dividends Paid as a Percentage of Net Income	40.61	51.98	40.27	52.81	32.80
Leverage Ratios—Averages					
Common Stockholders' Equity as a Percentage of:					
Loans, Net	5.80%	5.36%	5.42%	5.15%	5.06%
Total Interest-Earning Assets	4.80	4.42	4.37	4.02	3.90
Total Assets	4.08	3.71	3.63	3.43	3.18
Common Stockholders' Equity, Total Preferred Stock and Long-Term Notes and Debentures	52.50	57.12	64.12	63.39	63.54
Common Stockholders' Equity and Nonredeemable Preferred Stock as a Percentage of:					
Loans, Net	6.80%	6.19%	6.13%	5.67%	5.32%
Total Interest-Earning Assets	5.62	5.11	4.94	4.43	4.11
Total Assets	4.78	4.29	4.11	3.78	3.34
Common Stockholders' Equity and Total Preferred Stock as a Percentage of:					
Loans, Net	6.90%	6.35%	6.41%	6.07%	5.92%
Total Interest-Earning Assets	5.71	5.24	5.17	4.74	4.57
Total Assets	4.85	4.40	4.30	4.05	3.72
Leverage Ratios—at December 31,					
Common Stockholders' Equity as a Percentage of:					
Loans, Net	6.22%	5.48%	5.51%	5.02%	5.10%
Total Interest-Earning Assets	5.11	4.57	4.50	4.03	3.90
Total Assets	4.33	3.87	3.72	3.41	3.33
Common Stockholders' Equity, Total Preferred Stock and Long-Term Notes and Debentures	52.24	52.96	61.61	63.74	65.77
Common Stockholders' Equity and Nonredeemable Preferred Stock as a Percentage of:					
Loans, Net	7.21%	6.47%	6.19%	5.71%	5.35%
Total Interest-Earning Assets	5.92	5.39	5.05	4.57	4.08
Total Assets	5.01	4.56	4.18	3.88	3.49
Common Stockholders' Equity and Total Preferred Stock as a Percentage of:					
Loans, Net	7.31%	6.57%	6.46%	5.98%	5.90%
Total Interest-Earning Assets	6.00	5.47	5.27	4.79	4.50
Total Assets	5.08	4.63	4.36	4.06	3.85
Capital Ratios—at December 31,					
Primary Capital** as a Percentage of Total Gross Assets	6.87%	6.37%	5.44%	4.73%	4.17%
Total Capital** as a Percentage of Total Gross Assets	9.23	8.11	6.69	6.01	5.73

*Based on Net Income, Adjusted as Applicable.

**Based on Federal Reserve Board definition. See page 30 for discussion of Capital.

The Chase Manhattan Bank, N.A. and Subsidiaries					
Capital Ratios—at December 31,					
Primary Capital*** as a Percentage of Total Gross Assets	7.05%	6.57%	5.26%	4.75%	4.83%
Total Capital*** as a Percentage of Total Gross Assets	7.46	6.90	5.52	5.01	5.18

***Based on Office of the Comptroller of the Currency definition.

Stockholder Data

The Chase Manhattan Corporation and Subsidiaries

$ in thousands except per common share data	Common Stock Total Paid	Common Stock Per Common Share***	Preferred Stock 6¾% Series B	Preferred Stock 7.60% Series C	Preferred Stock 10½% Series D	Preferred Stock Floating Rate Series E	Preferred Stock Floating Rate Series F	Preferred Stock Total Paid
Quarterly Cash Dividends								
1985								
1st Quarter	$ 34,838	$ .47½	$ 502	$ 606	$ 3,281	$ 7,626	$14,073	$26,088
2nd Quarter	35,194	.47½	502	606	3,281	7,375	14,073	26,337
3rd Quarter	35,924	.47½	502	606	3,281	6,875	6,101	17,365
4th Quarter	36,316	.47½	502	606	3,281	7,065	5,847	17,301
Total	$142,272	$ 1.90	$2,008	$2,424	$13,124	$29,441	$40,094	$87,091
1984								
1st Quarter	$ 31,710	$ .45¾	$1,080	$1,634	$ 3,281	$ 7,845	$ —	$13,840
2nd Quarter	31,865	.45¾	1,080	1,634	3,281	8,065	—	14,060
3rd Quarter	32,546	.45¾	502	606	3,281	8,721	14,073	27,183
4th Quarter	33,047	.45¾	502	606	3,281	8,221	14,073	26,683
Total	$129,168	$ 1.82½	$3,164	$4,480	$13,124	$32,852	$28,146	$81,766

Quarterly Comparison of Market Prices**

Common Stock***	1985 High	1985 Low	1985 Close	1984 High	1984 Low	1984 Close	1983 High	1983 Low	1983 Close	1982 High	1982 Low	1982 Close	1981 High	1981 Low	1981 Close
1st Quarter	27⅛	23¼	25⅜	26¾	22⅛	24⅛	27⅛	23⅛	26⅛	30⅛	26¼	27⅞	24⅛	20⅛	22¼
2nd Quarter	30⅞	25⅛	30⅛	26	18⅜	19⅛	31⅛	25⅛	26⅛	29⅜	19⅜	20⅛	29¼	22¼	26⅞
3rd Quarter	31⅛	24⅛	24⅛	23⅛	17⅛	21⅞	26⅞	23	24	21⅜	15⅜	21⅛	27⅞	24⅛	25⅛
4th Quarter	36⅛	24⅛	36⅛	24	19⅛	23⅞	24⅛	20⅝	22⅜	28⅛	20⅜	24⅛	29⅛	24⅛	26⅛

Preferred Stock	6¾% Series B High	6¾% Series B Low	6¾% Series B Close	7.60% Series C High	7.60% Series C Low	7.60% Series C Close	10½% Series D High	10½% Series D Low	10½% Series D Close	Floating Rate Series E High	Floating Rate Series E Low	Floating Rate Series E Close	Floating Rate Series F High	Floating Rate Series F Low	Floating Rate Series F Close
1985															
1st Quarter	59	55	57⅜*	68	60½	64*	46	40¼	42¼	56	52¼	53¼	55⅞	52	53¼
2nd Quarter	62	58	61⅛*	74	64	73½*	48½	42⅛	47½	56⅛	52¼	54	55	51¾	52¾
3rd Quarter	65	59	65*	73¾	72½	72½*	48½	45½	46⅜	56¼	53½	54½*	56¼	52	52½
4th Quarter	69	63½	68½	75	72½	72½	50¼	45⅞	49¼	56¼	52	53⅛	54⅛	50½	51¼
1984															
1st Quarter	57	53½	55	64	61¾	61¾*	44	39¼	39⅞	57½	54⅜	55¾*	—	—	—
2nd Quarter	63	53½	56*	70⅝	61	68*	43¾	37¼	37½	58	48	48½	—	—	—
3rd Quarter	56	54	52¾*	67½	63½	62*	41¼	36¾	39¼	56	48	51¾	57⅞	52⅛	53
4th Quarter	56¾	52¼	54½	64	60½	60¾*	43	39¼	40¼	55⅛	50¾	53*	56⅛	51	52¼

*No sales. Based on the average of bid and asked prices.

**The high, low and closing sales prices for transactions reported on the composite tape.

***Amounts restated to reflect two-for-one stock split declared January 15, 1986.

Number of Common Stockholders, Preferred Stockholders and Convertible Security Holders

The following table sets forth the approximate number of holders of record of each class of equity and securities convertible into equity securities of the Corporation at the end of the years indicated:

	1985	1984	1983	1982	1981
Common Stock, Par Value $12.50	49,000	53,800	48,700	53,000	57,000
Common Stock Equity Contracts	82	83	82	72	—
Preferred Stock, 6¾% Series B	600	600	2,300	2,500	2,700
Preferred Stock, 7.60% Series C	100	100	500	500	600
Preferred Stock, 10½% Series D	2,100	2,100	2,000	2,000	2,000
Preferred Stock, Floating Rate Series E	100	100	100	100	—
Preferred Stock, Floating Rate Series F	6,700	6,800	—	—	—
Convertible Capital Notes (4¾% Due 1993)	2,900	3,200	3,400	3,800	4,300
Convertible Subordinated Debentures (6½% Due 1996)	1,000	1,200	1,300	1,700	2,100

Note: The principal market in which the Company's Common Stock is traded is the New York Stock Exchange.

Combined Balance Sheet

The Chase Manhattan Corporation Nonbanking Subsidiaries of the Company

	December 31				
$ in thousands	1985	1984	1983	1982	1981
Assets					
Cash in Banks:					
The Chase Manhattan Bank, N.A.	$ 5,754	$ 11,254	$ 9,281	$ 6,287	$ 7,080
Other Banks	4,895	13,199	4,792	3,965	5,861
Time Deposits Placed with Banks	29,384	15,016	14,640	12,205	11,650
Federal Funds Sold and Securities Purchased Under Resale Agreements	38,181	30,719	11,303	—	—
Investment in U.S. Treasury Securities	2,516	4,923	2,927	1,209	—
Due from the Company and Affiliated Companies:					
Commercial Paper of the Company	13,775	7,100	6,945	21,997	4,570
Securities Purchased Under Resale Agreements	—	—	—	—	1,165
Loans:					
Residential Property Loans	491,092	296,735	263,173	169,730	42,929
Other Real Estate Loans	27,428	29,427	28,966	48,813	58,028
Commercial	934,803	936,378	790,923	684,015	561,618
Consumer Loans	430,035	192,951	62,533	21,115	1,935
Loans for Purchasing or Carrying Securities	54,942	40,369	45,848	—	—
Lease Financings	286,580	183,025	169,761	149,414	123,797
Loans to Affiliates of The Chase Manhattan Bank, N.A.	3,490	3,681	20,399	20,132	—
	2,228,370	1,682,565	1,381,603	1,093,219	788,307
Less: Reserve for Possible Loan Losses	26,113	20,909	15,061	13,218	11,615
Loans, Net	2,202,257	1,661,657	1,366,542	1,080,001	776,692
Real Estate Properties Acquired in Satisfaction of Loans	4,252	2,737	2,517	1,992	8,255
Investments in Associated Companies (at Equity in Net Assets)	—	4,981	4,708	4,391	2,466
Other Assets	66,628	52,649	38,798	21,793	17,647
Total Assets	$2,387,642	$1,804,235	$1,462,253	$1,159,040	$935,416
Liabilities and Stockholder's Equity					
Due to the Company and Affiliated Companies:					
Notes Payable	$1,849,793	$1,377,012	$1,092,957	$ 885,498	$654,014
Accounts Payable—Taxes, Net	37,339	28,350	15,017	13,495	1,979
Accrued Interest Payable	21,643	17,496	11,455	27,879	10,854
Accounts Payable, Accrued Expenses and Other Liabilities	6,247	89	7,916	3,324	129
Savings Accounts and Time Certificates	1,449	1,122	3,333	1,242	99
Other Borrowed Money	100,678	61,849	51,540	14,911	11,823
Accounts Payable, Accrued Expenses and Other Liabilities	26,922	31,479	20,982	20,502	15,725
Total Liabilities	2,044,071	1,517,397	1,203,200	966,851	694,623
Stockholder's Equity:					
Common Stock	1,057	1,056	1,105	1,504	1,504
Additional Paid-In Capital	369,478	354,140	336,232	275,932	230,989
Foreign Exchange Translation Adjustments	80	(336)	(75)	(137)	—
Retained Earnings (Deficit)	(27,044)	(68,022)	(78,209)	(85,110)	(91,700)
Total Stockholder's Equity	343,571	286,838	259,053	192,189	140,793
Total Liabilities and Stockholder's Equity	$2,387,642	$1,804,235	$1,462,253	$1,159,040	$835,416

Combined Statement of Income

The Chase Manhattan Corporation Nonconsolidating Subsidiaries of the Company

$ in millions	Year Ended December 31				
	'85	'84	'83	'82	'81
Income					
Interest and fees on loans	$251,713	$219,347	$175,803	$156,075	$ [illegible]
Interest on time Deposits Placed with Banks	2,583	1,723	1,021	1,511	[illegible]
Interest on Federal Funds Sold and Securities Purchased under Resale Agreements	3,492	2,079	666	—	—
Interest on Investment U.S. Treasury Securities	291	299	210	48	—
Interest on Commercial Paper of the Company	811	868	591	2,609	349
Fees and Commissions	62,334	51,306	36,464	18,837	15,038
Equity in Earnings (losses) of Associated Companies	—	654	317	328	29
Gain on Sale of Associated Companies	20,595	—	—	—	—
Fees from Affiliated Companies	61,513	48,136	35,568	30,356	18,602
Other Income	2,182	3,509	1,018	2,951	1,136
Total Income	405,984	327,936	251,918	212,715	130,070
Expenses					
Interest on Notes Payable to the Company	150,688	146,802	111,726	107,926	80,221
Interest on Savings Accounts and Time Certificates	70	242	238	50	—
Interest on Other Borrowed Money	5,207	4,395	11,893	1,167	671
Provision for Possible Loan Losses	18,677	12,702	14,617	10,647	6,781
Salaries and Employee Benefits	75,428	59,859	46,793	35,285	22,873
Fees Charged by Affiliated Companies	11,176	6,194	5,852	8,343	5,770
Expense of Real Estate Properties Acquired, Net of Related Income	(760)	(2,424)	918	853	6,757
Other Expenses	74,740	69,531	48,917	50,812	17,328
Total Expenses	335,228	297,301	230,954	195,083	140,401
Income (Loss) Before Taxes (Benefits)	70,756	30,635	21,004	17,632	(10,331)
Applicable Income Taxes (Benefits)					
Current	5,869	9,940	497	11,699	(4,456)
Deferred	23,909	7,225	10,517	(2,657)	(64)
Total Applicable Income Taxes (Benefits)	29,778	17,165	11,014	9,042	(3,857)
Net Income (Loss)	$ 40,978	$ 13,470	$ 9,990	$ [illegible]	$ [illegible]

Statements of Condition of Chase Lincoln First Bank, N.A., The Chase Manhattan Bank (USA), N.A., Chase Bank of Maryland and Chase Bank of Ohio

The Chase Manhattan Corporation and Subsidiaries

$ in millions	Chase Lincoln First Bank, N.A.		The Chase Manhattan Bank (USA), N.A.[2]		Chase Bank of Maryland[3]	Chase Bank of Ohio[4]
	Dec. 31, 1985	Dec. 31, 1984	Dec. 31, 1985	Dec. 31, 1984	Dec. 31, 1985	Dec. 31, 1985
Assets						
Cash and Due from Banks	$ 330	$ 249	$ 27	$ 16	$ 17	$ 7
Interest-Bearing Deposits Placed with Banks	17	20	—	—	4	5
Federal Funds Sold and Securities Purchased Under Resale Agreements	120	419	—	—	4	73
Trading Account Assets	6	13	—	—	—	—
Investment Securities	408	537	3	3	24	15
Loans	3,006	2,655	4,577	1,960	347	274
Less: Reserve for Possible Loan Losses	41	37	128	43	7	7
Loans, Net	2,965	2,618	4,449	1,917	340	267
Customers' Liability on Acceptances	10	29	—	—	—	—
Other Assets	208	241	41	21	225	45
Total Assets	$4,064	$4,146	$4,520	$1,957	$619	$412
Liabilities and Stockholder's Equity						
Deposits						
Noninterest-Bearing	$ 735	$ 733	$ 100	$ 33	$ 2	$ 3
Interest-Bearing	2,598	2,578	1,193	676	422	255
Federal Funds Purchased and Securities Sold Under Repurchase Agreements	211	269	1,394	143	95	—
Other Borrowed Money	165	196	1,493	878	—	—
Acceptances Outstanding	10	29	—	—	—	—
Accounts Payable, Accrued Expenses and Other Liabilities	41	48	149	91	8	5
Long-Term Notes and Debentures	4	4	—	—	—	—
Total Liabilities	3,764	3,857	4,329	1,821	527	363
Capital Stock	64	64	24	24	2	—
Surplus	64	64	89	74	93	50
Undivided Profits Retained	172	161	78	38	(3)	(1)
Total Stockholder's Equity	300	289	191	136	92	49
Total Liabilities and Stockholder's Equity	$4,064	$4,146	$4,520	$1,957	$619	$412

(1) Headquarters in Rochester, New York, with over 100 branches in New York State.
(2) Headquarters in Wilmington, Delaware.
(3) Acquired in 1985. Headquarters in Bethesda, Maryland, with 13 branches in Maryland.
(4) Acquired in 1985. Headquarters in Columbus, Ohio, with 23 branches in Ohio.

Members Federal Deposit Insurance Corporation

Financial Reporting and Analysis of the Effects of Changing Prices

The Chase Manhattan Corporation and Subsidiaries

Financial statements presented in accordance with generally accepted accounting principles have traditionally reported amounts in historical dollars without taking into account the effects of inflation. Statement of Financial Accounting Standards No. 33 entitled "Financial Reporting and Changing Prices" is an effort to report the effects of changing prices (inflation). The schedule below is a five-year comparison of certain historical dollar financial data and certain supplementary data adjusted for the effects of changing prices. These inflation-adjusted data are referred to as constant dollar amounts and were computed by adjusting the historical dollar data by the U.S. Consumer Price Index for All Urban Consumers (CPI) to reflect changes in general purchasing power. It should be noted, however, that the use of the CPI may not be appropriate in that it does not necessarily bear any direct relationship to all of the assets, liabilities, stockholders' equity, income or expenses of financial institutions.

(In thousands, except per share data)	Year Ended December 31, 1985	1984	1983	1982	1981
Net Interest Income					
Historical Dollars	$2,748,730	$2,308,491	$2,169,055	$2,023,582	$1,771,937
Constant Dollars (1)	2,748,730	2,390,858	2,342,057	2,255,605	2,095,884
Net Income					
Historical Dollars	564,818	405,818	429,607	367,483	412,150
Constant Dollars (2)	534,940	392,833	437,225	312,695	460,570
Earnings Per Common Share*					
Historical Dollars	6.39	4.51	5.48	3.86½	5.78
Constant Dollars (2)	5.99	4.29	5.53	3.86	6.43
Cash Dividends Declared Per Common Share*					
Historical Dollars	1.90	1.82½	1.75	1.70	1.55
Constant Dollars	1.99	1.89	1.89	1.89½	1.83½
Market Price Per Common Share at End of Year*					
Historical Dollars	36.31¼	23.87½	22.75	24.50	26.93¾
Constant Dollars	35.73¼	24.38¼	24.15¼	26.99¾	30.83¼
Net Assets at End of Year					
Historical Dollars	4,397,136	3,961,044	3,425,825	3,136,415	2,717,699
Constant Dollars	4,663,008	4,420,212	3,930,570	3,768,298	3,474,511
Average Monetary Assets					
Historical Dollars	84,023,000	87,801,000	77,637,000	75,893,000	73,934,000
Constant Dollars	84,023,000	86,791,000	83,829,000	84,582,000	87,451,000
Decline in Net Monetary Assets (3)	49,159	77,862	64,001	37,014	88,634
Average Consumer Price Index	322.2	311.1	298.4	289.1	272.4

(1) Because the Corporation does not have significant amounts of property, plant and equipment, Constant Dollar data has been substituted for Current Cost information.

(2) The Constant Dollar amounts include an adjustment to Depreciation and Amortization Expense due to the restatement of the underlying assets for the effect of changing prices. For the year ended December 31, 1985, this adjustment amounted to approximately $30 million.

(3) The Decline in Net Monetary Assets (purchasing power loss) represents the effect on the Corporation of restating its Net Monetary Assets (total assets less nonmonetary assets, all liabilities and redeemable preferred stock). The Corporation's major nonmonetary assets include Trading Account Assets, Premises and Equipment, Investments in Associated Companies and Real Estate Properties Acquired in Satisfaction of Loans.

*Amounts restated to reflect two-for-one stock split declared January 15, 1986.

On the Historical Dollar basis, Net Interest Income increased 55% from 1981 to 1985. For the same five-year period, however, Net Interest Income in Constant Dollars increased by 31%.

Net Income showed the same general trend in both Historical Dollars and Constant Dollars. For the five-year period, Net Income in Constant Dollars increased by approximately 17%. Earnings Per Common Share fluctuated during the period from 1981 to 1985 and the Constant Dollar amounts reflect this pattern.

Cash Dividends Declared on the Historical Dollar basis have increased from $1.55 per common share in 1981 to $1.90 in 1985. On the Constant Dollar basis, dividends declared ranged from $1.83½ in 1981 to $1.90 in 1985, indicating that the increase in dividends declared has been slightly greater than the increase in the CPI.

The actual market price of the Corporation's common stock fluctuated during the period from 1981 to 1985 and the Constant Dollar amounts reflect this pattern.

On the Historical Dollar basis, Net Assets at End of Year increased by 62% over the five-year period. On the Constant Dollar basis, Net Assets at End of Year increased by approximately 34% over the period.

Average Monetary Assets on the Historical Dollar basis increased over the five-year period. On the Constant Dollar basis, Average Monetary Assets decreased by 4% between 1981 and 1985, indicating that the overall change in the CPI has been greater than the growth in Average Monetary Assets.

The Decline in Net Monetary Assets in Constant Dollars reflects the fact that, as in most banking institutions, the Corporation's monetary assets exceed its monetary liabilities. That is, the erosion of the purchasing power of monetary assets exceeded the benefit attached to the lesser "real" burden of monetary liabilities.

The Art Collection of The Chase Manhattan Bank, N.A.

The Chase Manhattan Corporation and Subsidiaries

The Chase art collection includes 10,732 works of art exhibited in Chase offices worldwide, including 193 locations in New York State, 57 domestic offices outside New York State and 101 overseas locations. The collection is appraised by category on a rotating basis so that each work of art is reappraised at least once every five years by experts in the field. At the close of 1985, the estimated current market value of the collection, based on the above-mentioned appraisals, was in excess of $17.2 million (cost—$10,273,611).

During 1985, 852 items were purchased at a cost of $1,321,511. During the year, 2 items with an original cost of $1,514 were given as gifts to other institutions and 44 items with an original cost of $24 were deleted from the collection for other reasons (sale, loss, destruction, normal deterioration).

The Chase Art Committee, which is composed of both Chase executives and outside art experts, develops general art policy for Chase, approves major additions to the collection and advises the program director. The committee last met formally on September 23, 1985; informal meetings with various members are held periodically.

Further information about the collection and programs is available in the annual acquisitions brochure, a separate publication which stockholders may obtain from The Chase Manhattan Bank Art Program, 410 Park Avenue, New York, New York 10022.

Statement of Assets Held in Art Collection

	December 31	
	1985	1984
Art Medium:		
Paintings	$ 4,402,588	$3,316,175
Prints	1,277,507	942,411
Sculpture	927,595	792,464
Drawings	1,495,642	1,294,408
Fabrics	412,281	381,431
Photographs	828,042	744,870
Constructions	385,243	362,363
Other	744,513	638,016
Total	$10,273,611	$8,972,138

Note: The amounts above represent the purchase cost of the works of art, excluding sales taxes and the cost of framing, both of which are charged to expense. Works of art received as gifts from outside sources are included in the above statement at nominal cost.

Statement of Changes in Assets Held in Art Collection

	Year Ended December 31,	
	1985	1984
Balance at Beginning of Year	$ 8,972,138	$7,112,085
Add: Purchases	1,321,511	1,862,489
Less: Donations and Gifts	1,514	225
Other Deletions	18,524	2,211
Balance at End of Year	$10,273,611	$8,972,138

International Advisory Committee

David Rockefeller
Chairman

Dr. Henry A. Kissinger
Counsellor

Australia
Sir Arvi H. Parbo
Chairman and Managing Director
Western Mining Corporation Limited

Brazil
Paulo D. Vilares
Chairman of the Board
Vilares Group

Canada
The Hon. Ian D. Sinclair, Q.C., Q.C., Senator
Retired Chairman
Canadian Pacific Enterprises Limited

France
Jean-Paul Peravre
Chief Executive Officer
Dumez S.A.

Germany
Hans L. Merkle
Chairman of the Supervisory Board
Robert Bosch GmbH

Hong Kong
Sir Yue-Kong Pao
Chairman and Chief Executive
World-Wide Shipping Agency Limited

India
J.R.D. Tata
Chairman
Tata Sons Limited

Italy
Dr. Giovanni Agnelli
Chairman
FIAT S.p.A.

Japan
Isamu Yamashita
Chairman
Mitsui Engineering & Shipbuilding Co., Ltd.

Mexico
Lic. Ernesto Fernandez Hurtado
Director General
Bancomer, S.N.C.

The Netherlands
G.A. Wagner
Chairman of the Supervisory Board
Royal Dutch Petroleum Company

Saudi Arabia
Sheikh Ahmed Juffali
Managing Director
E.A. Juffali & Bros.

Sweden
Pehr G. Gyllenhammar
Chairman and Chief Executive Officer
AB Volvo

Switzerland
Fritz Gerber
Chairman of the Board of Directors
F. Hoffmann-La Roche & Co. Ltd.

United Kingdom
Kenneth Durham
Chairman
Unilever PLC

United States
John B. Fery
Chairman of the Board and Chief Executive Officer
Boise Cascade Corporation

Richard M. Furlaud
Chairman and Chief Executive Officer
Squibb Corporation

Pierre Gousseland
Chairman of the Board
AMAX Inc.

Edson W. Spencer
Chairman and Chief Executive Officer
Honeywell, Inc.

Venezuela
Gustavo A. Cisneros
President and Chief Executive Officer
Organizacion Diego Cisneros

Ex-Officio Members
(The Chase Manhattan Bank, N.A.)
Willard C. Butcher
Thomas G. Labrecque
Robert R. Douglass
Arthur F. Ryan
Anthony P. Terracciano
Donald L. Beurskens
Francis A. Stanzione

Board of Directors

Board of Directors

Willard C. Butcher
Chairman and Chief Executive Officer of The Chase Manhattan Corporation and The Chase Manhattan Bank, N.A.

Thomas G. Labrecque
President and Chief Operating Officer of The Chase Manhattan Corporation and The Chase Manhattan Bank, N.A.

Robert R. Douglass
Vice Chairman of The Chase Manhattan Corporation and The Chase Manhattan Bank, N.A.

Arthur F. Ryan
Vice Chairman of The Chase Manhattan Corporation and The Chase Manhattan Bank, N.A.

Anthony P. Terracciano
Vice Chairman of The Chase Manhattan Corporation and The Chase Manhattan Bank, N.A.

Alexander D. Hargrave
Chairman of Chase Lincoln First Bank, N.A.

William T. Coleman, Jr.
Senior Partner in the law firm of O'Melveny & Myers

Joan Ganz Cooney
President of Children's Television Workshop

James L. Ferguson
Chairman and Chief Executive of General Foods Corporation and Vice Chairman and Director of Philip Morris Companies Inc.

Edward S. Finkelstein
Chairman and Chief Executive Officer of R.H. Macy & Co., Inc.

Robert E. Flowerree
Retired Chairman of the Board of Georgia-Pacific Corporation

H. Laurance Fuller
President of Amoco Corporation

Howard C. Kauffmann
Retired President of Exxon Corporation

David T. Kearns
Chairman and Chief Executive Officer of Xerox Corporation

Richard W. Lyman
President of The Rockefeller Foundation

John D. Macomber
Chairman and Chief Executive Officer of Celanese Corporation

John H. McArthur
Dean of the Harvard Graduate School of Business Administration

David T. McLaughlin
President of Dartmouth College

James E. Olson
President and Chief Operating Officer of American Telephone and Telegraph Company

Edmund T. Pratt, Jr.
Chairman and Chief Executive Officer of Pfizer Inc.

Henry B. Schacht
Chairman and Chief Executive Officer of Cummins Engine Company, Inc.

Richard R. Shinn
Former Chairman and Chief Executive Officer of Metropolitan Life Insurance Company

Donald H. Trautlein
Chairman and Chief Executive Officer of Bethlehem Steel Corp.

Ralph E. Ward
Chairman and Chief Executive Officer of Chesebrough-Pond's Inc.

Kay R. Whitmore
President of Eastman Kodak Company

Committees of the Board

Executive Committee
Mr. Butcher, *chairman*
Mrs. Cooney
Mr. Finkelstein
Mr. Kauffmann
Dr. Lyman
Mr. Olson
Mr. Pratt
Mr. Shinn
Mr. Ward, *regular members*
Mr. Labrecque
Mr. Douglass
Mr. [illegible]
Mr. Terracciano
Mr. [illegible]rove,
alternate members
Mr. Butcher, *member ex-officio*
Mr. Coleman
Mr. Ferguson
Mr. Macomber, *alternate members*

This committee is entitled to exercise, to the extent permitted by law, all the powers of the Board of Directors when the Board is not in session.

Compensation Committee
Mr. Kauffmann, *chairman*
Mr. Ferguson
Mr. Kearns
Mr. Macomber
Mr. McArthur
Mr. Olson

This committee reviews and makes recommendations to the Board concerning major compensation policies and compensation of officer-directors.

Audit Committee
Mr. Macomber, *chairman*
Mr. Ferguson
Mr. Finkelstein
Mr. Kearns
Mr. McLaughlin
Mr. Shinn
Mr. Trautlein

This committee is responsible for reviewing the financial condition of the Corporation, its internal controls and audit program, the performance and findings of the internal audit staff, and any action to be taken thereon by Management. It reviews audit and examination reports of governmental agencies and of the independent auditors. The committee selects the independent auditors for appointment by the Board.

Employee Benefits Review Committee
Mr. Pratt, *chairman*
Mr. Coleman
Mr. Flowerree
Mr. McLaughlin
Mr. Schacht
Mr. Trautlein

This committee reviews reports of the Bank's employee benefit plans made by the named fiduciaries appointed pursuant to the Employee Retirement Income Security Act of 1974.

Investment Committee
Mr. Coleman, *chairman*
Mrs. Cooney
Mr. Flowerree
Mr. Fuller
Dr. Lyman
Mr. McArthur, *regular members*
Mr. Butcher
Mr. Labrecque
Mr. Douglass
Mr. Ryan
Mr. Terracciano, *members ex-officio*

This committee is responsible for reviewing the general conduct of the business of Chase Investors Management Corporation New York, a wholly owned subsidiary of the Corporation with investment management and advisory functions.

Nominating Committee
Mr. Shinn, *chairman*
Mr. Ferguson
Mr. Kauffmann
Mr. Macomber
Mr. Olson
Mr. Pratt, *regular members*
Mr. Butcher, *member ex-officio*

This committee is responsible for considering and making recommendations to the Board regarding nominees for election to the Board, Board committee assignments, and succession in the offices of Chairman of the Board, President, and Vice Chairmen of the Board.

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Policy and Planning Committee

The Policy and Planning Committee is a forum broadly representative of businesses and corporate functions for the chief executive officer to obtain inputs periodically, explore implications, and build a common perspective concerning key bank-wide management issues. Such issues include:

—Periodic review of broad strategies in light of anticipated external conditions.

—Significant changes in corporate-wide policies.

—Assessment and corporate response to major external developments.

—Approaches to emerging constraints on corporate performance.

—Planning guidance and areas of bank-wide performance emphasis.

Willard C. Butcher
is chairman and chief executive officer. He began his career at Chase in 1947 and in 1960 was named senior vice president and head of retail and corporate business for the New York midtown area. He was named executive vice president in charge of the International Department in 1969, president and chief operating officer in 1972, and was elected chairman in 1981.

Thomas G. Labrecque
is president and chief operating officer. He joined Chase in 1964. In 1974 he became executive vice president and Treasury Department executive. Prior to assuming the presidency in 1981, Mr. Labrecque was vice chairman with overall responsibility for Commercial Banking, Institutional Banking, Retail Banking, Trust and Fiduciary Investment as well as Corporate Operations and Systems.

Robert R. Douglass
is vice chairman in charge of National Banking. Before joining Chase in 1976 as executive vice president and General Counsel, he was a partner in Mabank, Tweed, Hadley and McCloy and served as Counsel and then Secretary to the Governor of New York State. He became head of National Banking in 1984 and was elected to the Board in 1985.

Arthur F. Ryan
is vice chairman in charge of Consumer Banking. He joined Chase in 1972 in the data processing division. He was named group executive for the owner securities handling division in 1976. In 1982 he became head of Corporate Operations and Systems. He was named Consumer Banking executive in 1984 and was elected to the Board in 1985.

Anthony P. Terracciano
is vice chairman in charge of Global Banking, including Corporate Industries, International Banking, and Chase Manhattan Capital Markets. He joined Chase in 1964, was named treasurer in 1976, and became chief financial officer in 1983. He became head of Global Banking in 1984 and was elected to the Board in 1985.

A. Edward Allinson
is executive vice president in charge of the Institutional, Trust, Investment and Information Services Sector. Prior to joining Chase in 1977, he was executive vice president of the State Street Bank and Trust Company of Boston. Previously, he spent 14 years with IBM, including a year as a Sloan fellow at Massachusetts Institute of Technology.

William Balderston III
is president and chief executive officer of Chase Lincoln First Bank, N.A. He was elected president of Lincoln First Bank, N.A., the forerunner of Chase Lincoln First, in 1980 and was named chief executive officer in 1984.

Elaine R. Bond
is senior vice president and director of Corporate Systems. She joined Chase in 1981 after 23 years with IBM, where she served in many executive capacities, lastly as a group director of information systems of IBM's data processing complex in White Plains.

Donald L. Boudreau
is executive vice president in charge of International Banking. He joined Chase in 1961, was promoted to senior vice president in 1975 and, in 1980, became area executive for Chase's Middle East business. In 1982 he was appointed International Institutional Banking executive. He assumed his present position in 1984.

Richard J. Boyle
is executive vice president in charge of the Corporate Industries Sector. Since joining Chase in 1965, Mr. Boyle has headed Real Estate Finance, U.S. National Industries and, most recently, the Commercial Sector.

A. Wright Elliott
is executive vice president for Corporate Communications. Prior to joining the Bank in 1974, Mr. Elliott was executive vice president and chief administrative officer of the National Association of Manufacturers.

Michael P. Esposito, Jr.
is executive vice president and controller. He joined the Bank in 1961 and was appointed head of the accounting and reports division in 1970. He was named controller in 1974.

Joseph J. Harkins
is executive vice president in charge of the Commercial Sector, a position he assumed in 1985. Mr. Harkins joined Chase in 1954 and served in the branch system. Subsequently, he became senior banking executive in Corporate Banking and was thereafter executive in charge of International and Domestic Institutional Banking.

Robert M. Lichten
is executive vice president and president of Chase Manhattan Capital Markets and executive for Capital Planning. He joined Chase in 1966 and is a member of the Asset Liability Management Committee.

O.J. McGill
is senior vice president and general auditor. Prior to joining Chase in 1984, he was vice president and general auditor of Gulf Oil Corporation. A certified public accountant, he was a senior audit manager at Price Waterhouse before joining Gulf.

Wolfgang Schoellkopf
is executive vice president in charge of the new Trading and Securities Sector with responsibility for global activities in foreign exchange, securities and bullion trading, municipal finance, and broker/dealer banking. He joined Chase in 1963.

L. Edward Shaw, Jr.
is executive vice president and General Counsel. Prior to joining Chase in 1983, Mr. Shaw was a partner in Mabank, Tweed, Hadley and McCloy where he was a member of the Executive Committee.

Francis X. Stankard
is executive vice president and chairman of Chase Manhattan Capital Markets. Mr. Stankard joined Chase in 1955, served as area executive of Asia, the Middle East, and Europe and, prior to assuming his present position in 1984, was head of International Banking.

Michael Urkowitz
is executive vice president in charge of Corporate Operations and Systems. He joined Chase in 1974 and was promoted to senior vice president in 1980. Prior to assuming his present position in 1984, he was responsible for Chase's Global Product and Production Risk Management program.

Paul T. Walker
is executive vice president and credit policy officer. He is also chairman of the Bank's Credit Risk Management Committee. Mr. Walker joined Chase in 1957, assumed responsibility for the Lending Services Group in 1976, and was named senior vice president for Credit Policy in 1979.

Gerald Weiss
is senior vice president for Corporate Planning and Development. He joined Chase in 1975 after 24 years with the General Electric Company. He is past chairman of the board of trustees of the Strategic Planning Institute.

J. Richard Zecher
is senior vice president, Treasury executive, and treasurer of the Corporation. He joined Chase in 1981 and was chief economist prior to assuming his current position in January 1986. Mr. Zecher serves as a public director of the Chicago Board Options Exchange.

Domestic Locations

The Chase Manhattan Corporation and The Chase Manhattan Bank, N.A.

Commercial Banking Subsidiaries

The Chase Manhattan Bank, N.A.
New York, N.Y. (212) 552-2222
222 Branch Offices in New York State

The Chase Manhattan Bank (USA), N.A.
Wilmington, Del. (302) 651-7500

Chase Lincoln First Bank, N.A.
Rochester, N.Y. (716) 258-5000
109 Branch Offices in New York State

Chase Bank of Ohio
Columbus, Ohio (614) 463-1700
23 Branch Offices in Ohio

Chase Bank of Maryland
Bethesda, Md. (301) 652-6800
13 Branch Offices in Maryland

Other Subsidiaries

Chase Bank International
Newark, Del. (302) 366-1165
Type of Business:
Edge Act Banking Company
Offices:
Los Angeles, San Francisco, Calif.; Miami, Fla.; Atlanta, Ga.; Chicago, Ill.; Houston, Texas

Chase Commercial Corp.
Englewood Cliffs, N.J.
(201) 894-4400
Type of Business:
Equipment Leasing
Offices:
Irvine, Los Angeles, San Carlos, San Francisco, Calif.; Stamford, Conn.; Lakeland, Miami, Fla.; Atlanta, Ga.; Chicago, Ill.; Boston, Canton, Mass.; West Bloomfield, Mich.; Paramus, N.J.; Cleveland, Ohio; Dallas, Texas

Interactive Data Corp.
Waltham, Mass. (617) 890-1234
Type of Business:
Time Sharing, Securities Information, Investment Analysis and Securities Pricing Services
Offices:
Los Angeles, San Francisco, Calif.; Hartford, Stamford, Conn.; Atlanta, Ga.; Chicago, Ill.; Boston, Cambridge, Woburn, Mass.; Detroit, Mich.; Minneapolis, Minn.; West Orange, N.J.; New York, N.Y.; Cleveland, Ohio; Philadelphia, Pittsburgh, Penn.; Houston, Texas; Washington, D.C.

Chase Manhattan Industrial Bank
Denver, Col. (303) 759-1411
Type of Business:
Consumer Financial Services

Chase Home Mortgage Corp.
Montvale, N.J. (201) 573-5000
Type of Business:
Mortgage Banking
Offices:
Brandon, Jacksonville, Miami, Orange Park, Orlando, Tampa, West Palm Beach, Winter Park, Fla.; Annapolis, Baltimore, Rockville, Md.; Waltham, Mass.; Salem, N.H.; Marmon, Morristown, N.J.; Buffalo, New York, Rochester, Wantagh, White Plains, N.Y.; Lancaster, Wayne, Penn.; Clear Lake, Dallas, Grand Prairie, Houston, Texas; Annandale, Va.

Chase Investors Management Corp. New York
New York, N.Y. (212) 730-2967
Type of Business:
Investment Advice and Asset Management

Chase Manhattan Capital Markets Corp.
New York, N.Y. (212) 552-4372
Type of Business:
Investment Banking
Offices:
Los Angeles, San Francisco, Calif.; Miami, Fla.; Chicago, Ill.; Boston, Mass.; White Plains, N.Y.; Philadelphia, Penn.; Houston, Texas; Hato Rey, San Juan, P.R.

Chase Manhattan Financial Services, Inc.
New York, N.Y. (212) 432-4602
Type of Business:
Consumer Financial Services
Offices:
Phoenix, Tucson, Ariz.; Beverly Hills, La Jolla, Newport Beach, Palo Alto, Walnut Creek, Calif.; Greenwich, Conn.; Boca Raton, Coral Gables, Jacksonville, Maitland, Tampa, Fla.; Atlanta, Ga.; Rockville, Md.; Tulsa, Okla.; Austin, Dallas, Fort Worth, Houston, San Antonio, Texas

Chase Manhattan Government Securities, Inc.
New York, N.Y. (212) 552-3842
Type of Business:
U.S. Government Securities Trading

Chase Manhattan of California Thrift
Newport Beach, Calif.
(714) 760-2671
Type of Business:
Consumer Financial Services

Chase Manhattan of Utah
Salt Lake City, Utah (801) 363-0750
Type of Business:
Consumer Financial Services

Chase Manhattan Overseas Banking Corp.
Newark, Del. (302) 366-0390
Type of Business:
Edge Act Company

Chase Manhattan Service Corp.
New York, N.Y. (212) 223-7009
Type of Business:
Equipment Leasing

Chase Manhattan Treasury Corp.
New York, N.Y. (212) 552-5395
Type of Business:
Regional Distribution of Treasury Products
Offices:
Los Angeles, San Francisco, Calif.; Miami, Fla.; Chicago, Ill.; Boston, Mass.; Philadelphia, Penn.; Houston, Texas

Chase National Corporate Services, Inc.
New York, N.Y. (212) 907-6455
Type of Business:
Regional Marketing Offices
Offices:
Los Angeles, San Francisco, Calif.; Stamford, Conn.; Boca Raton, Fla.; Atlanta, Ga.; Boston, Mass.; Hasbrouck Heights, N.J.; Dallas, Houston, Texas

Chase Trade, Inc.
New York, N.Y. (212) 432-8075
Type of Business:
International Financial Services
Office:
St. Croix, U.S. Virgin Islands

Chase T/C Service Corp.
New York, N.Y. (212) 676-2904
Type of Business:
Marketing, Distribution and Servicing of VISA Travelers Checks Issued by Chase

Chase Econometrics, Inc.
Bala Cynwyd, Penn.
(215) 667-6000
Type of Business:
Economic Forecasting and Consulting Services
Offices:
San Francisco, Calif.; Chicago, Ill.; New York, N.Y.; Cleveland, Ohio; Washington, D.C.

Chase Access Services Corp.
Waltham, Mass. (617) 890-1234
Type of Business:
Cash Management Services
Offices:
San Francisco, Calif.; New York, N.Y.; Cleveland, Ohio; Dallas, Texas

Computer Power, Inc.
Jacksonville, Fla. (904) 350-1400
Type of Business:
Mortgage Servicing, Software and Computer Services for Real Estate-Related Applications

Chase Trans-Info, Inc.
New York, N.Y. (212) 676-5817
Type of Business:
Automated Freight Bill Payment, Information and Decision Support Services for Shippers
Office:
San Francisco, Calif.

Rose & Company Investment Brokers, Inc.
Chicago, Ill. (312) 663-8300
Type of Business:
Discount Securities Broker
Offices:
Los Angeles, San Francisco, Calif.; Boston, Mass.; New York, N.Y.; Pittsburgh, Penn.; Houston, Texas; Washington, D.C.

Chase Auto Leasing Corp.
Manhasset, N.Y. (516) 574-0343
Type of Business:
Auto Leasing

Chase Manhattan Financial Center, Inc.
Minneapolis, Minn. (612) 831-0006
Type of Business:
Consumer Financial Services

Chase Manhattan Futures Corp.
New York, N.Y. (212) 552-3610
Type of Business:
Futures Commission Merchant

The Chase Manhattan Trust Company of California, N.A.
San Francisco, Calif.
(415) 433-8430
Type of Business:
Trust Services

The Chase Manhattan Trust Company of Florida, N.A.
Palm Beach, Fla. (305) 659-6704
Type of Business:
Trust Services
Offices:
Boca Raton, Naples, Fla.

Chase Automated Clearing House, Inc.
New York, N.Y. (212) 676-4207
Type of Business:
Automated Clearing House

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Overseas Locations

The Chase Manhattan Corporation and The Chase Manhattan Bank, N.A.

Europe

Branches

Belgium, Channel Islands, Denmark, England, France, Germany, Greece, Italy, Monaco, Portugal, Spain, Switzerland, Turkey

Representative Offices

Norway, Sweden, Switzerland, U.S.S.R.

Subsidiary and Associate Banks

Austria:
Chase Manhattan Bank (Austria) A.G.

Belgium:
Chase Banque de Commerce, S.A.

Channel Islands:
Chase Bank and Trust Co. (C.I.) Ltd.

Finland:
Chase Manhattan Bank, OY

France:
Chase Manhattan, S.A.

Germany:
Chase Bank, A.G.

Luxembourg:
Chase Manhattan Bank Luxembourg, S.A.

The Netherlands:
Nederlandse Credietbank N.V.

Norway:
Chase Manhattan Bank (Norway) A.S.

Republic of Ireland:
Chase Bank (Ireland) Ltd.

Spain:
Banco de Finanzas
Chase Asesoramiento Financiero S.A.

Switzerland:
Chase Manhattan Bank (Switzerland)

United Kingdom:
Chase Manhattan Capital Markets (U.K.) Ltd.
Chase Manhattan Limited
Libra Bank Limited

Subsidiary and Associate Companies

France:
Financiere d'Investissements et de Construction Immobiliere (F.I.C.I.)

Germany:
Interactive Data GmbH

Italy:
Chase-in-Chase Finanziaria, S.p.A.

Spain:
Chase Leasing S.A.E.

United Kingdom:
Chase Trade Finance, Ltd.

Middle East and Africa

Branches

Bahrain, Ivory Coast, Lebanon, Liberia

Representative Offices

Egypt, Nigeria, South Africa

Subsidiary and Associate Banks

Cameroon:
Chase Bank Cameroon, S.A.

Egypt:
The Chase National Bank (Egypt) S.A.E.

Nigeria:
Continental Merchant Bank Nigeria Limited

Saudi Arabia:
The Saudi Investment Bank

Asia and Australasia

Branches

Guam, Hong Kong, Indonesia, Japan, Korea, Malaysia, Pakistan, The Philippines, Singapore, Taiwan, Thailand

Representative Offices

Australia, China, India

Subsidiary and Associate Banks

Australia:
Chase AMP Bank Limited

Hong Kong:
Chase Manhattan Asia Limited
Chase Manhattan Financial Services (Hong Kong) Ltd.
Chase Manhattan Investment Services (Hong Kong) Ltd.
Chase Manhattan Trust Company (Hong Kong) Ltd.

Japan:
Chase Manhattan Trust and Banking Company (Japan) Ltd.

Malaysia:
Amanah Chase Merchant Bank Berhad

Singapore:
Chase Capital Markets Limited

Subsidiary and Associate Companies

Indonesia:
P.T. Chase Leasing Indonesia

Japan:
Chase Leasing (Japan) Ltd.

Western Hemisphere

Branches

Argentina, The Bahamas, Cayman Islands, Chile, Dominican Republic, Guadeloupe, Martinique, Panama, Paraguay, Peru, Puerto Rico, St. Maarten, U.S. and British Virgin Islands

Representative Offices

Brazil, Colombia, Ecuador, Mexico, Uruguay, Venezuela

Subsidiary and Associate Banks

Argentina:
Chase Manhattan Trading S.A.

The Bahamas:
The Chase Manhattan Trust Corporation Limited

Brazil:
Banco de Investimentos Lar Brasileiro, S.A.
Banco Lar Brasileiro, S.A.

Canada:
The Chase Manhattan Bank of Canada

Cayman Islands:
Chase Manhattan Trust Cayman Ltd.

Chile:
Chase Manhattan Capital Markets International Limitada

Colombia:
Banco del Comercio

Panama:
Banco del Comercio (Panama), S.A.

Puerto Rico:
Chase Manhattan Capital Markets Corporation of Puerto Rico

Subsidiary and Associate Companies

Brazil:
Financeira Lar Brasileiro, S.A.

Canada:
Chase Manhattan Leasing Canada, Ltd.

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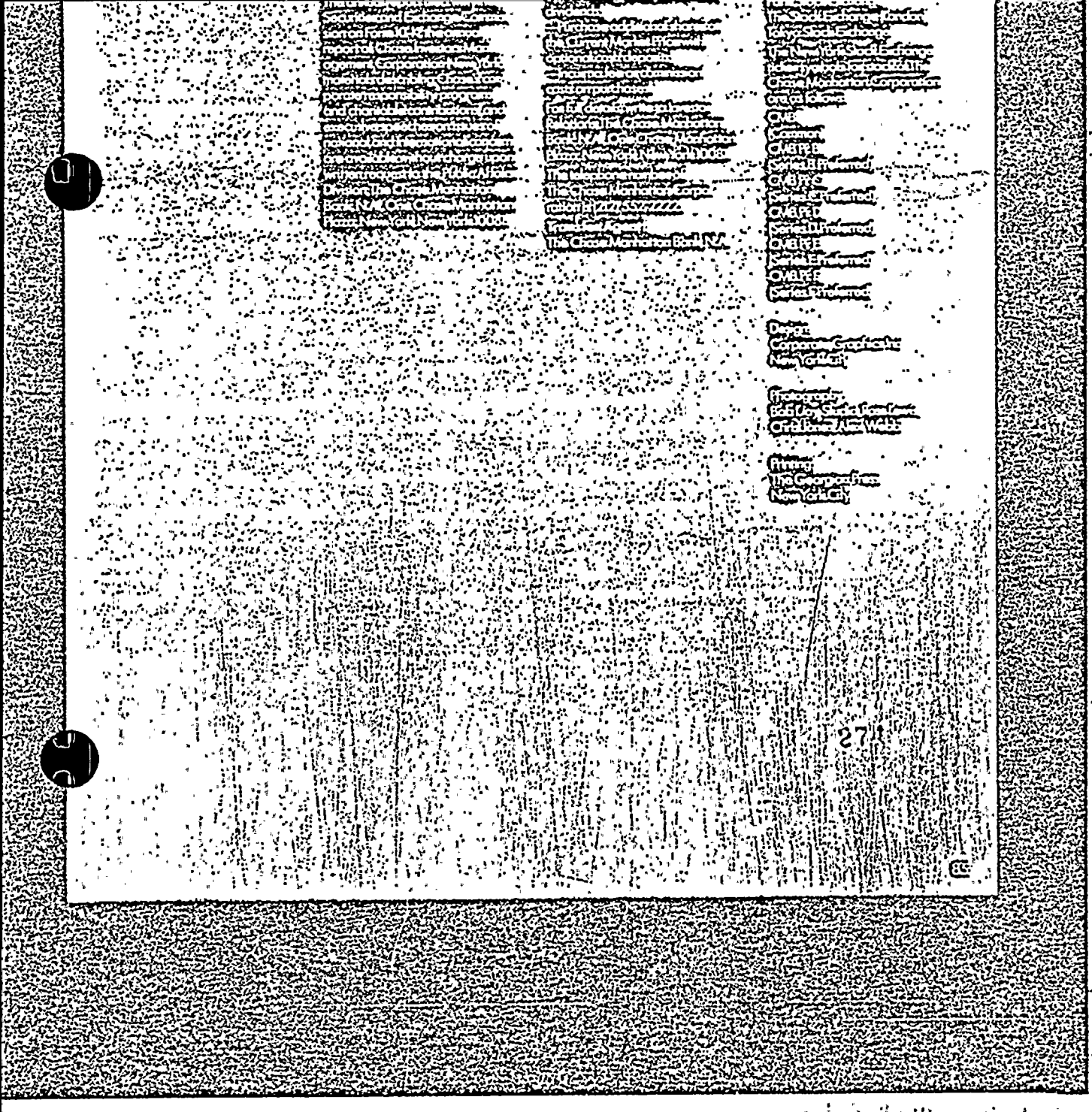

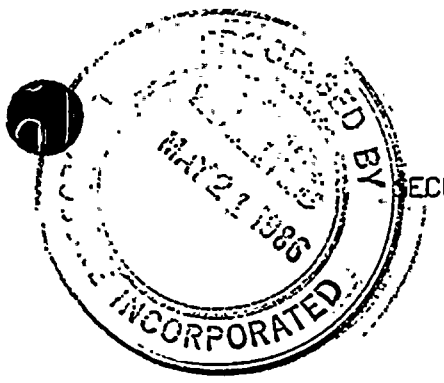

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SECURITIES AND EXCHANGE COMMISSION
WASHINGTON, D.C. 20549

FORM 10-Q

QUARTERLY REPORT UNDER SECTION 13 or 15(d)
OF THE SECURITIES EXCHANGE ACT OF 1934

For Quarter Ended: March 31, 1986

Commission file number: 1-5945

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The Chase Manhattan Corporation
(Exact name of registrant as specified in its charter)

Delaware (State or other jurisdiction of incorporation or organization)	13-2633613 (I.R.S. Employer Identification No.)
1 Chase Manhattan Plaza, New York, New York (Address of principal executive offices)	10081 (Zip Code)

212-552-2222
(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 X No

The number of shares outstanding of the registrant's common stock (par value $12.50 per share) was 78,903,826 at March 31, 1986.

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PART I - FINANCIAL INFORMATION

Item 1. Financial Statements

The Consolidated Statement of Condition of The Chase Manhattan Corporation and its subsidiaries (the "Corporation") as of March 31, 1986, December 31, 1985 and March 31, 1985, the Consolidated Statement of Income for the quarters ended March 31, 1986 and 1985, the Statement of Changes in Common Stockholders' Equity for the quarters ended March 31, 1986 and 1985, and the Consolidated Statement of Changes in Financial Position for the quarters ended March 31, 1986 and 1985, are set forth on the following pages.

The interim consolidated financial statements are unaudited. However, in the opinion of Management, all adjustments, consisting only of normal recurring accruals, necessary for the fair presentation of the financial position, results of operations and changes in financial position for such periods have been made.

Prior periods' financial statements have been reclassified to conform with the current financial statement presentations.

The Chase Manhattan Corporation and Subsidiaries

CONSOLIDATED STATEMENT OF CONDITION

($ in thousands)	March 31, 1986	December 31, 1985	March 31, 1985
Assets			
Cash and Due from Banks	$ 4,996,637	$ 5,574,055	$ 4,39[redacted]
Interest-Bearing Deposits Placed with Banks	5,081,633	4,671,048	5,183,958
Federal Funds Sold and Securities Purchased Under Resale Agreements	1,008,969	1,174,371	1,131,931
Trading Account Assets	1,375,368	1,344,495	1,098,028
Investment Securities:			
U.S. Treasury Securities	1,825,899	1,839,207	1,959,539
Federal Agency Securities	294,931	330,259	134,537
State and Political Subdivision Securities	2,360,051	2,410,373	1,821,659
Other Bonds, Notes and Debentures	1,470,232	1,408,541	1,079,786
Federal Reserve Bank and Other Stock Investments	143,208	134,012	145,568
Total Investment Securities (Estimated Market Value of $6,257,000, $6,098,000 and $4,902,000, Respectively)	6,094,321	6,122,392	5,141,089
Loans	61,948,918	61,930,527	60,524,568
Less: Reserve for Possible Loan Losses	934,835	907,672	779,362
Loans, Net	61,014,083	61,022,855	59,745,206
Customers' Liability on Acceptances	3,275,663	2,820,471	4,706,956
Accrued Interest Receivable	1,010,528	1,028,986	1,104,087
Premises and Equipment	959,225	913,580	808,788
Other Assets	3,436,515	3,013,189	3,114,062
Total Assets	$88,252,942	$87,685,442	$86,429,814
Liabilities and Stockholders' Equity			
Deposits:			
Domestic Offices:			
Noninterest-Bearing	$12,165,834	$13,499,638	$ 9,7[redacted]
Interest-Bearing	19,455,555	19,130,323	17,686,167
Overseas Offices:			
Noninterest-Bearing	2,046,010	1,939,120	1,460,489
Interest-Bearing	27,795,731	26,783,968	30,081,280
Total Deposits	61,463,130	61,353,049	58,948,609
Federal Funds Purchased and Securities Sold Under Repurchase Agreements	3,982,785	4,131,793	4,275,580
Commercial Paper	3,242,501	3,483,501	4,156,609
Other Borrowed Money	4,136,116	4,671,994	3,265,622
Acceptances Outstanding	3,283,083	2,828,696	4,718,652
Accrued Interest Payable	686,949	668,961	792,028
Accounts Payable, Accrued Expenses and Other Liabilities	3,813,329	3,282,175	3,844,325
	80,607,893	80,420,169	80,001,425
Long-Term Notes and Debentures	3,047,072	2,806,499	2,315,925
Total Liabilities	83,654,965	83,226,668	82,317,350
Preferred Stock (Without Par Value-20,000,000 Shares Authorized):			
Redeemable Preferred Stock:			
616,379 Shares Outstanding	61,638	61,638	61,638
Nonredeemable Preferred Stock:			
12,039,737 Shares Outstanding	601,987	601,987	601,987
Common Stockholders' Equity:			
Common Stock (Par Value $12.50 Per Share):			
Authorized Shares (3/31/86: 125,000,000; 12/31/85: 125,000,000; 3/31/85: 125,000,000)			
Outstanding Shares (3/31/86: 78,903,826; 12/31/85: 77,157,724; 3/31/85: 37,033,691)	986,298	964,472	46[redacted]
Surplus	307,946	276,288	6[redacted]
Foreign Exchange Translation Adjustments	(23,921)	(22,265)	(21,149)
Retained Earnings	2,664,029	2,576,654	2,314,172
Total Common Stockholders' Equity	3,934,352	3,795,149	3,448,839
Total Liabilities and Stockholders' Equity	$88,252,942	$87,685,442	$86,429,814

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e Chase Manhattan Corporation and Subsidiaries

NSOLIDATED STATEMENT OF INCOME

in [illegible]sands, except per common share data)	Quarter Ended March 31, 1986	1985
terest Income		
terest and Fees on Loans	$1,808,867	$1,812,209
terest on Bank Deposit Placings	115,318	115,880
terest and Dividends on Investment Securities:		
Interest on-U.S. Treasury Securities	40,072	47,557
Federal Agency Securities	9,050	5,554
State and Political Subdivision Securities Exempt from Federal Income Taxes	43,232	36,730
Other Bonds, Notes and Debentures	70,742	51,687
Dividends on Federal Reserve Bank and Other Stock Investments	2,416	1,557
	165,512	143,085
terest on Federal Funds Sold and Securities Purchased Under esale Agreements	49,236	24,226
terest on Trading Account Assets	28,171	20,664
otal Interest Income	2,167,104	2,116,064
erest Expense		
posits	959,723	1,124,151
eral Funds Purchased and Securities Sold Under Repurchase reements	161,119	115,594
mercial Paper	56,844	72,378
er Borrowed Money	177,545	99,776
g-Term Notes and Debentures	63,421	58,367
otal Interest Expense	1,418,652	1,470,266
Int[illegible]t Income	748,452	645,798
visi[illegible]or Possible Loan Losses	130,000	95,000
Interest Income After Provision for Possible Loan Losses	618,452	550,798
er Operating Income		
s and Commissions	241,580	199,610
eign Exchange Trading Income	60,277	35,543
ding Account Profits (Losses)	22,173	(5,415)
estment Securities Gains (Losses)	40,204	20,165
er Income	9,085	33,496
otal Other Operating Income	373,319	283,399
er Operating Expenses		
aries and Employee Benefits:		
alaries	319,065	254,451
rofit Sharing	20,502	16,484
ther Employee Benefits	84,863	70,452
	424,430	341,387
Occupancy	71,182	56,145
ipment Rentals, Depreciation and Maintenance	67,867	54,581
er Expenses	209,978	170,114
otal Other Operating Expenses	773,457	622,227
me Before Taxes	218,314	211,970
licable Income Taxes	74,624	78,071
Income	$ 143,690	$ 133,899
Income Applicable to Common Stock	$ 127,408	$ 107,811
rage Shares Outstanding	78,156,253	73,735,222
nings Per Common Share:		
ima[illegible]ased on Average Shares Outstanding	$ 1.63	$ 1.46
sumi[illegible]ull Dilution	$ 1.59	$ 1.41
Dividends Declared Per Common Share	$ .51 1/4	$ .47 1/2

The Chase Manhattan Corporation and Subsidiaries and
The Chase Manhattan Corporation (Company Only)

STATEMENT OF CHANGES IN COMMON STOCKHOLDERS' EQUITY

($ in thousands)	Quarter Ended March 31, 1986	1985
Common Stock		
Balance at Beginning of Period (77,157,724 Shares and 36,659,653 Shares, Respectively)	$ 964,472	$ 458,246
Conversion of Capital Notes and Debentures (1,110,621 Shares and 29,051 Shares, Respectively)	13,883	363
Exercise of Stock Options (88,591 Shares and 4,026 Shares, Respectively)	1,107	50
Shares Issued Pursuant to Dividend Reinvestment Plan (305,064 Shares and 169,076 Shares, Respectively)	3,813	2,113
Shares Issued Pursuant to Floating Rate Subordinated Notes Due 1996 (241,826 and 171,885 Shares, Respectively)	3,023	2,149
Balance at End of Period (78,903,826 Shares and 37,033,691 Shares, Respectively)	986,298	462,921
Surplus		
Balance at Beginning of Period	276,288	678,342
Conversion of Capital Notes and Debentures	18,019	1,244
Exercise of Stock Options	1,029	92
Shares Issued Pursuant to Dividend Reinvestment Plan	6,944	6
Shares Issued Pursuant to Floating Rate Subordinated Notes Due 1996	5,666	6,540
Balance at End of Period	307,946	692,895
Foreign Exchange Translation Adjustments		
Balance at Beginning of Period	(22,265)	(18,730)
Aggregate Translation Gain (Loss) After Applicable Income Taxes (Benefit) of ($10,474) and $2,626, Respectively	(1,656)	(2,419)
Balance at End of Period	(23,921)	(21,149)
Retained Earnings		
Balance at Beginning of Period	2,576,654	2,241,199
Net Income	143,690	133,899
Cash Dividends Declared:		
Redeemable Preferred Stock	(1,108)	(1,108)
Nonredeemable Preferred Stock	(15,345)	(24,980)
Common Stock	(39,862)	(34,838)
Balance at End of Period	2,664,029	2,314,172
Total Common Stockholders' Equity	$3,934,352	$3,448,839

e Chase Manhattan Corporation and Subsidiaries

NSOLIDATED STATEMENT OF CHANGES IN FINANCIAL POSITION

in thousands)	Quarter Ended March 31, 1986	1985
nds Provided		
t Income	$ 143,690	$ 133,899
d (Deduct) Noncash Items Included in Net Income:		
Depreciation and Amortization of Premises and Equipment	39,390	31,337
Provision for Possible Loan Losses	130,000	95,000
Amortization of Discount on Long-Term Notes and Other Borrowed Money	2,680	2,310
Deferred Income Taxes	19,472	5,217
Funds Provided from Operations	335,232	267,763
suance of:		
Common Stock	53,484	19,228
8 1/2% Notes Due 1996	248,998	-
creases in:		
Deposits	110,081	-
Other Borrowed Money	-	29,148
Accrued Interest Payable	17,988	-
Accounts Payable, Accrued Expenses and Other Liabilities	511,682	1,271,113
creases in:		
Cash and Due from Banks	577,418	-
Federal Funds Sold and Securities Purchased Under Resale Agreements	165,402	161,274
Trading Account Assets	-	256,543
Investment Securities	28,071	104,717
Loans, Before Charge-Offs	-	1,386,221
Accrued Interest Receivable	18,458	87,862
her-Net	59,262	-
tal Funds Provided	$2,126,076	$3,583,869
nds Used		
sh Dividends Declared:		
Redeemable Preferred Stock	$ 1,108	$ 1,108
Nonredeemable Preferred Stock	15,345	24,980
Common Stock	39,862	34,838
nversion of Capital Notes and Subordinated Debentures nto Common Stock	31,907	1,609
reign Exchange Translation Adjustments	1,656	2,419
creases in:		
Cash and Due from Banks	-	197,908
Interest-Bearing Deposits Placed With Banks	410,585	828,767
Trading Account Assets	30,873	-
Loans, Before Charge-Offs	160,434	-
Premises and Equipment	85,035	46,579
Other Assets	423,326	1,155,697
creases in:		
Deposits	-	731,402
Federal Funds Purchased and Securities Sold Under Repurchase Agreements	149,008	204,710
Commercial Paper	241,000	252,257
Other Borrowed Money	535,937	-
crued Interest Payable	-	11,702
her-Net	-	89,893
tal Funds Used	$2,126,076	$3,583,869

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

Consolidated net income for the first quarter of 1986 was $143.7 million, or $1.63 per common share, compared with consolidated net income of $133.9 million, or $1.46 per common share, for the first quarter of 1985. The net income per common share amount for the first quarter of 1986 reflects the impact of a lower level of preferred stock dividend requirements, partially offset by an increased number of common shares outstanding.

Earnings Summary

($ in millions)	First Quarter 1986	1985
Net Interest Income	$748	$646
Provision for Possible Loan Losses	130	95
Other Operating Income:		
Fee-Based	242	200
Nonfee-Based	131	83
Other Operating Expenses	773	622
Income Before Taxes	218	212
Applicable Income Taxes	74	78
Net Income	$144	$134

Profitability ratios based on net income and the period-end book value per common share for the first quarters of 1986 and 1985 were as follows:

	First Quarter 1986	1985
Profitability Ratios		
Return on Average Assets	.67%	.63%
Return on Average Common Stockholders' Equity	13.5%	13.0%
Book Value		
Common Stockholders' Equity per Common Share	$49.86	$46.56

Net Interest Income - Taxable Equivalent Basis*

Net interest income on a taxable equivalent basis for the first quarter of 1986 was $827 million, up 17% compared with $705 million for the first quarter of last year.

*Net interest income on a taxable equivalent basis was higher by $79 million and $59 million for the first quarter of 1986 and the first quarter of 1985, respectively, than comparable net interest income amounts reported on a financial statement basis. These taxable equivalent amounts have been adjusted (by applying a combined U.S. federal, state and local income tax rate of approximately 51% for both 1986 and 1985) to recognize the differential between interest income that is exempt from income taxes and interest income that is fully taxable.

On a taxable equivalent basis, the spread between the average rate earned on interest-earning assets and the average rate paid to fund such assets, including the effect of noninterest-bearing sources, was 4.49% for the first quarter of 1986, compared with 3.88% for the first quarter of 1985.

Domestic net interest income on a taxable equivalent basis for the first quarter of 1986 was $535 million, up 20% compared with $446 million for the first quarter of last year. The increase in domestic net interest income was attributable to a higher volume of interest-earning assets and to generally lower rates paid on interest-bearing liabilities. First quarter 1986 domestic gross interest-earning assets increased approximately $3.2 billion over the $30.4 billion reported for the first quarter of 1985.

First quarter 1986 overseas net interest income on a taxable equivalent basis was $292 million, up 13% compared with $259 million for the first quarter of last year. Overseas net interest income increased due to a wider net interest rate spread partially offset by a decline of $2.1 billion in interest earning assets.

Average loans recorded in domestic offices increased approximately $3.4 billion, or 14%, over the first quarter of 1985. Average loans recorded in overseas offices included approximately $5.1 billion and $5.6 billion of loans to U.S. commercial borrowers for the first quarters of 1986 and 1985, respectively.

Net Interest Income and Interest Rate Spreads - Taxable Equivalent Basis

($ in millions)	First Quarter 1986	1985
Domestic Offices		
Interest Earned	$ 990	$ 917
Interest Paid(1)	455	471
Net Interest Income	$ 535	$ 446
--as a % of Gross Interest-Earning Assets	6.45%	6.13%
Overseas Offices		
Interest Earned	$1,256	$1,258
Interest Paid(1)	964	999
Net Interest Income	$ 292	$ 259
--as a % of Gross Interest-Earning Assets	2.88%	2.41%
Corporation Consolidated		
Interest Earned	$2,246	$2,175
Interest Paid	1,419	1,470
Net Interest Income	$ 827	$ 705
--as a % of Gross Interest-Earning Assets	4.49%	3.88%

(1) Includes appropriate allocations for the cost of time deposits received by overseas offices for domestic use and the cost of domestic monies raised for use in overseas offices.

Capital and Liquidity Management

Discussions regarding both capital management and liquidity management are set forth on pages 30, 31 and 32 of The Chase Manhattan Corporation Annual Report 1985 filed as Exhibit 13 to the registrant's Report on Form 10-K for the year ended December 31, 1985, portions of which were incorporated by reference in said Report on Form 10-K (the "1985 Annual Report").

During the first three months of 1986, there were no material changes from the capital and liquidity positions disclosed in the 1985 Annual Report.

In March of 1986, the Corporation issued $250 million of 8 1/2% Notes Due 1996. These notes come within the guidelines of the bank regulatory authorities for secondary capital.

Primary and Secondary Capital*

($ in millions)	March 31, 1986	1985
Primary Capital:		
Common Stockholders' Equity	$3,934	$3,449
Minority Interest in Consolidated Subsidiaries	3	3
Mandatory Convertible Securities (Net of Note Fund)	765	839
Reserve for Possible Loan Losses	935	779
Nonredeemable Preferred Stock	602	602
Total Primary Capital	6,239	5,672
Secondary Capital:		
Redeemable Preferred Stock	62	62
Long-Term Notes and Debentures	2,282	1,477
Total Secondary Capital	2,344	1,539
Total Capital	$8,583	$7,211
End of Period Capital as % of Gross Assets:		
Primary Capital	7.00%	6.50%
Total Capital	9.62%	8.27%

*Based on Federal Reserve Board definition.
Gross assets consist of Total Assets and the Reserve for Possible Loan Losses.

Provision and Reserve for Possible Loan Losses

The provision for possible loan losses for the first quarter of 1986 was $130 million, up $35 million from $95 million for the first quarter of 1985. The increase in the provision was made principally in recognition of continuing uncertain conditions in certain developing countries and in anticipation of higher levels of domestic consumer loan charge-offs due to the rapid growth of the domestic consumer loan portfolio. First quarter 1986 net loan charge-offs totaled $114 million, compared with $74 million for the first quarter a year ago. Domestic net loan charge-offs for the first quarter of 1986 increased $23 million over the first quarter of 1985, to $76 million. This increase was the result of domestic consumer net loan charge-offs which increased $41 million over the first quarter of 1985, partially offset by a decrease in commercial and other net charge-offs of $18 million from first quarter 1985. In March 1986, the Corporation recorded an $11.9 million net recovery in respect of the previously disclosed settlement of a derivative action, in the Court of Chancery of the State of Delaware in and for New Castle County, relating to the previously reported Drysdale and Penn Square matters. The terms of the settlement included a payment of $32.5 million to the Corporation by certain former officers of the Corporation and The Chase Manhattan Bank, N.A. (the "Bank") funded by officers and directors' liability insurance. As previously reported, the amount of the recovery was substantially offset by expenses associated with the settlement.

First quarter 1986 international net loan charge-offs were $38 million, an increase of $17 million over the first quarter of last year.

Analysis of Loan Loss Experience

($ in millions)	First Quarter 1986	1985
Loan Charge-Offs	$142	$ 93
Less: Loan Recoveries	28	19
Net Loan Charge-Offs	$114	$ 74
Provision for Possible Loan Losses	$130	$ 95

Reserve for Possible Loan Losses

($ in millions)		
At End of Period	$935	$779
As a % of Total Loans	1.51%	1.29%

Net Loan Charge-Offs and Loan Loss Experience Ratios

($ in millions)	First Quarter 1986	1985
Net Loan Charge-Offs		
Domestic - Consumer (2)	$ 64	$ 23
- Commercial and Other	12	30
Total Domestic	76	53
International	38	21
Total	$114	$ 74
Loan Loss Experience Ratios (Annualized) (3)		
Domestic - Consumer (2)	2.56%	1.32%
- Commercial and Other	.22	.53
Total Domestic	.94	.72
International	.53	.26
Total	.75%	.49%

(2) Loans to Individuals for Personal Expenditures and 1-4 family residential properties.

(3) Net Loan Charge-offs as a percentage of average loans.

Nonaccrual, Reduced Rate and Past Due Loans

Nonaccrual and reduced rate loans were approximately $2.1 billion at March 31, 1986, compared with approximately $2.0 billion at year-end 1985 and approximately $2.4 billion at March 31, 1985. Nonaccrual and reduced rate loans equaled 3.4% of total loans at March 31, 1986. At December 31, 1985 and March 31, 1985, the comparable ratios were 3.3% and 3.9%, respectively.

Included in March 31, 1986 nonaccrual loan balances were cross-border loans to Argentine and Brazilian borrowers of approximately $62 million and $18 million, respectively. Nonaccrual loan balances at March 31, 1986 also included approximately $208 million and $98 million of cross-border private sector loans to Venezuelan and Mexican borrowers, respectively.

Accruing loans past due 90 days or more were $331 million at March 31, 1986, compared with $211 million and $179 million at year-end 1985 and March 31, 1985, respectively. The increase since year end 1985 is principally due to real estate loans which are both well secured or guaranteed by financially responsible third parties and are in the process of collection.

The negative impact on first quarter 1986 earnings from nonaccrual and reduced rate loans was approximately $20 million after taxes, compared with $27 million after taxes for the first quarter of 1985.

Nonaccrual and Reduced Rate Loans

($ in millions)	Mar. 31, 1986	Dec. 31, 1985	Mar. 31, 1985
Nonaccrual Loans:			
Real Estate Loans	$ 319	$ 250	$ 233
Loans to Banks and Other Financial Institutions	134	111	104
Commercial and Industrial Loans	1,490	1,500	1,814
Other Loans	139	144	205
Total Nonaccrual Loans	2,082	2,005	2,356
Reduced Rate Loans:			
Real Estate Loans	4	4	12
Loans to Banks and Other Financial Institutions	6	7	1
Commercial and Industrial Loans	16	19	8
Total Reduced Rate Loans	26	30	21
Total Nonaccrual and Reduced Rate Loans	$2,108	$2,035	$2,377
Distribution of Nonaccrual and Reduced Rate Loans:			
Domestic Loans	$ 890	$ 804	$ 791
International Loans	1,218	1,231	1,586
Total Nonaccrual and Reduced Rate Loans	$2,108	$2,035	$2,377

Real estate properties acquired in satisfaction of loans totaled $92 million at March 31, 1986, compared with $100 million and $98 million at year-end 1985 and March 31, 1985, respectively.

Country Risk

During the first quarter of 1986, progress was made on debt restructuring programs of certain Latin American countries in which Chase has large cross-border outstandings. Chase continues to cooperate with the international financial community in addressing issues relating to the debt obligations of these countries as well as others in Latin America and elsewhere which are experiencing liquidity problems

In light of the difficulties affecting borrowers in these countries, it is possible that the amount of Chase's cross-border outstandings in nonaccrual status may increase in the future.

The approximate amounts of Chase's extensions of credit outstanding at March 31, 1986 to public and private sector borrowers included in cross-border outstandings and the approximate principal amounts of nonaccrual loans included in such extensions of credit at March 31, 1986 are shown in the table below for the principal rescheduling countries in which Chase has cross-border outstandings exceeding 1% of its total assets.

($ in millions)	Total Cross-Border Outstandings	Extensions of Credit		Nonaccrual Loans
		Public Sector	Private Sector	
Brazil	2,760	1,710	930	18
Mexico	1,640	1,250	370	98
Venezuela	1,230	860	350	208
Argentina	920	670	220	62

At March 31, 1986, the Corporation had cross-border outstandings in Chile aggregating approximately $695 million or .79% of Total Assets. These included extensions of credit to public sector borrowers of $420 million. At March 31, 1986, the corporation had approximately $2 million of cross-border nonaccrual loans to Chilean borrowers.

Brazil

In March 1986, the Bank Advisory Committee and the Government of Brazil reached agreement on the terms of a 1985-1986 Financing Plan which has been sent to the international banking community. The 1985 maturities of cross-border medium term debt (Chase share: $250 million) deposited in the Central Bank of Brazil in accordance with the interim measures for 1985 described in the 1985 Annual Report will be available for re-lending at interest rates of London Interbank Offered Rate (LIBOR) plus 1 1/8% for the public sector and LIBOR plus 1 1/4% for the private sector. Interim measures have been put in place for 1986 maturities which are to be deposited in the Central Bank with no re-lending. The interest rate on the deposits will be LIBOR plus 1 1/8% retroactive to January 18, 1986. It is intended that these deposits will be included in a multi-year rescheduling agreement to be negotiated later this year.

The $9.8 billion (Chase share: $371 million) facility for trade finance and the $5.4 billion (Chase share: $118 million) of interbank deposits, formally extended to January 17, 1986, are continuing on an informal basis until the Financing Plan is signed at which time it is anticipated that they will be extended to March 31, 1987.

In the first quarter of 1986, Chase reported total income on cross-border outstandings to public and private sector borrowers in Brazil of $84 million and approximately $86 million in interest payments were received in cash. No material principal payments were received other than approximately $87 million with respect to 1986 maturities pursuant to the interim deposit arrangements. The impact of Chase's nonaccrual cross-border loans to Brazilian borrowers on Chase's net income for the first quarter of 1986 was not material.

In light of the difficulties affecting borrowers in Brazil, it is possible that the amount of Chase's cross-border outstandings in nonaccrual status may increase in the future.

Mexico

The Multi-Year Debt Restructuring Agreements described in the 1985 Annual Report became effective in the first quarter of 1986. Payment of the remaining $950 million (Chase share: $24 million) balance of the $1.2 billion principal (Chase share: $30 million) due in 1985 under the amendment of the 1983 $5.0 billion new money credit agreement with Mexico was further postponed to October 1986.

Under the terms of the restructuring, interest rates were adjusted retroactive to January 1, 1985. Approximately $665 million of Chase's approximately $930 million share (after the estimated remaining payment of approximately $24 million) in the Multi-Year Debt Restructuring carried a weighted average rate of 9/16% over the prevailing prime rate and approximately $265 million carried a weighted average rate of approximately 11/16% over LIBOR. Following the restructuring, the estimated weighted average rate on Chase's $930 million share is 15/16% over LIBOR. Under the terms of the restructuring this estimated weighted average rate is scheduled to increase over time to 1 1/4% over LIBOR in 1992 through 1998.

At March 31, 1986, Chase's cross-border outstandings to public sector borrowers in Mexico were substantially current as to payment of principal and interest. Chase reported approximately $33 million as income on such outstandings in the first quarter of 1986 and approximately $34 million in interest was received in cash. During the first quarter of 1986, Chase received minimal principal repayments on cross-border outstandings to Mexican public sector borrowers. At March 31, 1986, $98 million of Chase's cross-border outstandings to Mexican private sector borrowers were in nonaccrual status. The negative impact of these loans to private sector borrowers on Chase's net income for the first quarter of 1986 was approximately $1 million after taxes.

In light of continuing uncertainties regarding the Mexican economy and conditions currently prevailing in world petroleum markets, it is possible that additional amounts of Chase's cross-border outstandings to borrowers in Mexico could be placed in nonaccrual status.

Venezuela

In the first quarter of 1986, agreements covering a substantial portion of the proposed restructuring of $21.2 billion (Chase share: approximately $800 million) of Venezuelan public sector debt described in the 1985 Annual Report were signed but are not yet effective to restructure such debt. However, Venezuela has requested that the international banking community renegotiate the terms of the restructuring. The restructured principal (after the prepayment of approximately $26 million) will be repriced on the effective date of the restructuring and the effect on Chase will be approximately as follows:

Before Restructuring		After Restructuring	
Principal $ in Millions	Average Interest Rate (a)	Principal $ in Millions	Interest Rate
$600	Prime	$400	Domestic reference rate (b) plus 1.125%
$200	LIBOR plus 1.39%	$400	LIBOR plus 1.125%

(a) At March 31, 1986, weighted by principal outstanding.
(b) As defined in the agreements.

The following table compares the amount of interest income reported in the first quarter of 1986 related to the principal to be restructured with that which would have been reported on a pro forma basis had that principal been restructured as of January 1, 1986:

($ in Millions)

Principal to be Restructured	Actual Interest Income Reported	Pro Forma Interest Income-Accrual Basis After Restructuring
$800	$19	$18

At March 31, 1986, Chase's cross-border outstanding to Venezuela public sector borrowers were current as to payment of principal and interest.

Chase reported approximately $26 million as income on all cross-border outstandings in the first quarter of 1986 and approximately $24 million in interest was received in cash. Minimal principal payments were received.

The negative impact of these loans to Venezuelan private sector borrowers on Chase's net income for the first quarter of 1986 was immaterial.

In light of continuing uncertainties regarding Venezuela, including conditions currently prevailing in the world petroleum markets, it is possible that additional amounts of Chase's cross-border outstandings to borrowers in Venezuela could be placed in nonaccrual status.

Argentina

During the first quarter of 1986, Chase received minimal principal payments on cross-border outstandings to Argentine public and private sector borrowers. On April 18, 1986, $600 million (Chase share: $21 million) of the $3.7 billion (Chase share: $129 million) new ten-year term credit facility which was part of the Argentine Republic 1984-1985 Refinancing Plan described in the 1985 Annual Report was disbursed.

At March 31, 1986, Chase's cross-border Argentine public sector loans were substantially current as to payment of principal and interest although delays are being experienced in the payment of interest on some loans. In the first quarter of 1986, Chase reported total income on cross-border outstandings to public and private sector borrowers in Argentina of $39 million. Interest payments of $39 million were received in cash on such cross-border outstandings during the first quarter of 1986.

The amount of Chase's cross-border nonaccrual loans to Argentine private sector borrowers was approximately $62 million at March 31, 1986. The negative impact of such nonaccrual loans on Chase's net income for the first quarter of 1986 was immaterial.

In light of continuing uncertainties regarding Argentina, it is possible that additional amounts of Chase's cross-border outstandings to borrowers in Argentina could be placed in nonaccrual status.

Other Operating Income

First quarter 1986 other operating income totaled $373 million, compared with $283 million for the first quarter of 1985. Fee-based income in the first quarter of 1986 was up 21% to $242 million and included increases in investment banking fee income, up 88%; consumer banking fee income, up 9%; trust and fiduciary fee income, up 30% and, commercial banking fee income, up 30%. Foreign exchange trading income was $60 million, up $25 million from the first quarter of 1985. Dealer trading account profits were $22 million, compared with a net loss of $5 million for the first quarter of 1985. Included in first quarter 1985 other income was a gain of $22 million from the sale of nearly all of Chase's minority equity interest in a leasing company in Japan. Net foreign exchange translation losses on Chase's investments in overseas branches, subsidiaries and associated companies for the first quarter of 1986 were approximately $3 million, compared with gains of approximately $5 million for the first quarter of 1985. On an after-tax basis, net foreign exchange translation losses in the first quarter of 1986 were approximately $2 million compared with $1 million in the first quarter of 1985. Net gains, before applicable income taxes, from investment securities transactions were $40 million for the first quarter of 1986 compared with $20 million for the first quarter of 1985. Income taxes applicable to investment securities gains were $20 million compared with $11 million for the first quarter of 1985.

Other Operating Income

($ in millions)	First Quarter 1986	1985
Fee-Based Income:		
International Business Fees	$ 43	$ 41
Trust and Fiduciary Investment Fees	58	45
Consumer Banking Fees	52	47
Other Fee-Based Income	89	67
Total Fee-Based Income	242	200
Nonfee-Based Income:		
Foreign Exchange Trading Income	60	35
Trading Account Profits (Losses)	22	(5)
Investment Securities Gains (Losses)	40	20
Other Nonfee-Based Income	9	33
Total Nonfee-Based Income	131	83
Total Other Operating Income	$373	$283

Other Operating Expenses

Total other operating expenses for the first quarter of 1986 were $773 million, compared with $622 million for the first quarter of 1985.

The quarter-to-quarter increase in operating expenses is mainly the result of substantial incremental expenses related to strategic areas of emphasis such as nationwide expansion, investment banking and domestic and international consumer activities. Also included in the increase, was approximately $20 million applicable to new acquisitions, and performance-related compensation expenses and approximately $21 million due to the impact of exchange rates on expenses of overseas offices.

Other Operating Expenses (4)

($ in millions)	First Quarter 1986	1985
Salaries and Employee Benefits	$424	$341
Net Occupancy	71	56
Equipment Rentals, Depreciation and Maintenance	68	55
Other Expenses	210	170
Total Other Operating Expenses	$773	$622

(4) First Quarter 1985 restated for comparability with current period classifications.

Provision for Income Taxes

The provision for income taxes was $74 million for the first quarter of 1986, compared with $78 million for the first quarter of 1985. The decrease is primarily due to an increase in income which is exempt from federal income taxes, partially offset by a higher level of pre-tax income.

The Chase Manhattan Corporation and Subsidiaries

Stockholder Data

($ in thousands, except per common share data)	1986 1st Qtr.	1985 4th Qtr.	1985 3rd Qtr.	1985 2nd Qtr.	1985 1st Qtr.
Quarterly Cash Dividends					
Common Stock:					
Per Share	$.51 1/4	$.47 1/2	$.47 1/2	$.47 1/2	$.47 1/2
Aggregate	$ 39,862	$ 36,316	$ 35,924	$ 35,194	$ 34,838
Preferred Stock:					
6 3/4% Series B	502	502	502	502	502
7.60% Series C	606	606	606	606	606
10 1/2% Series D	3,281	3,281	3,281	3,281	3,281
Floating Rate Series E	6,530	7,065	6,875	7,875	7,626
Floating Rate Series F	5,534	5,847	6,101	14,073	14,073
Total Preferred Stock	16,453	17,301	17,365	26,337	26,088
Total Cash Dividends	$ 56,315	$ 53,617	$ 53,289	$ 61,531	$ 60,926
Cash Dividends Paid on Common Stock as a Percentage of Net Income Applicable to Common Stock	31.29%	27.21%	27.19%	32.85%	32.31%
Total Cash Dividends Paid as a Percentage of Net Income	39.19	35.58	35.66	47.04	45.50
Earnings Ratios					
Net Income as a Percentage of:					
Average Total Interest-Earning Assets, Net	.79%	.81%	.80%	.72%	.75%
Average Total Assets	.67	.69	.68	.61	.63
Average Common Stockholders' Equity(1)	13.51	14.35	14.65	12.44	12.98
Average Common Stockholders' Equity and Nonredeemable Preferred Stock(1)	13.06	13.83	14.08	12.83	13.57
Average Common Stockholders' Equity and Total Preferred Stock	12.98	13.73	13.98	12.74	13.47
Leverage Ratios-Averages					
Common Stockholders' Equity as a Percentage of:					
Loans, Net	6.29%	6.09%	5.87%	5.70%	5.56%
Total Interest-Earning Assets, Net	5.18	5.01	4.83	4.74	4.62
Total Assets	4.42	4.26	4.12	4.02	3.93
Common Stockholders' Equity, Total Preferred Stock and Long-Term Notes and Debentures	52.01	52.39	52.26	52.30	53.09
Common Stockholders' Equity and Nonredeemable Preferred Stock as a Percentage of:					
Loans, Net	7.28%	7.08%	6.86%	6.69%	6.55%
Total Interest-Earning Assets, Net	6.00	5.83	5.65	5.56	5.45
Total Assets	5.11	4.96	4.81	4.72	4.63
Common Stockholders' Equity and Total Preferred Stock as a Percentage of:					
Loans, Net	7.38%	7.19%	6.96%	6.79%	6.65%
Total Interest-Earning Assets, Net	6.08	5.91	5.73	5.65	5.54
Total Assets	5.18	5.03	4.88	4.79	4.70
Common Stockholders' Equity Per Common Share	$ 49.86	$ 49.19	$ 48.10	$ 47.24	$ 46.56
Capital Ratios - at Quarter End					
Primary Capital(2) as a Percentage of Total Gross Assets	7.00%	6.87%	6.71%	6.64%	6.50%
Total Capital(2) as a Percentage of Total Gross Assets	9.62	9.23	8.82	8.75	8.27
The Chase Manhattan Bank, N.A. and Subsidiaries					
Primary Capital(3) as a Percentage of Total Gross Assets	7.21	7.05	6.88	6.80	6.73
Total Capital(3) as a Percentage of Total Gross Assets	7.64	7.46	7.25	7.17	7.08
Market Prices of Preferred and Common Stock**					
Preferred Stock, 6 3/4% Series B					
High	$ 93	$ 69	$ 65	$ 62	$ 59
Low	64	63 1/2	59	58	55
Close	75	68 1/2	65 •	61 1/8	57 3/4
Preferred Stock, 7.60% Series C					
High	100	75	73 3/4	74	68
Low	69	72 1/2	72 1/2	64	60 1/2
Close	80	72 1/2	72 1/8 •	73 1/2 •	64 •
Preferred Stock, 10 1/2% Series D					
High	56 1/2	50 3/8	48 1/2	48 1/2	46
Low	49 1/4	45 7/8	45 1/2	42 1/8	40 3/4
Close	54	49 1/4	46 3/8	47 1/2	42 1/4
Preferred Stock, Floating Rate Series E					
High	55 1/4	56 3/8	56 1/4	56 1/4	56
Low	52 3/8	52	53 1/2	52 1/4	52 3/8
Close	53 1/2	53 1/8	54 1/5 •	54	53 3/4
Preferred Stock, Floating Rate Series F					
High	54 1/2	54 1/8	56 5/8	55	55 7/8
Low	51	50 1/2	52	51 3/4	52
Close	52 1/2 •	51 3/4	52 1/2	52 3/4	53 1/8
Common Stock					
High	48	36 5/8	31 15/16	30 1/2	27 5/8
Low	34	24 1/2	24 1/2	25 5/8	23 1/4
Close	46 3/4	36 5/16	24 9/16	30 3/16	25 3/4

*No sales, based on average of bid and asked prices.
**The high, low and closing sales prices for transactions reported on the composite tape.
(2)Based on Federal Reserve Board definition
(3)Based on Office of the Comptroller of the Currency definition.

The Chase Manhattan Corporation (Company Only)

BALANCE SHEET

($ in thousands)	March 31, 1986	December 31, 1985	March 31, 1[illegible]
Assets			
Cash in Banks-Demand Deposits:			
The Chase Manhattan Bank, N.A.	$ 8,664	$ 6,013	$ 4,641
Other Banks	2,730	4,778	5,420
Short-Term Money Market Instruments:			
Time Deposits with Banks:			
The Chase Manhattan Bank, N.A.	2,483,313	2,748,369	3,339,193
Other Banks	136,506	66,216	61,487
U.S. Treasury Securities		-	-
Total Short-Term Money Market Instruments	2,619,819	2,814,585	3,400,680
Notes Receivable from Nonbanking Subsidiaries	1,997,609	1,849,793	1,450,189
Accounts Receivable from The Chase Manhattan Bank, N.A.	66,650	51,937	67,427
Other Stock Investments	48,390	41,360	55,330
Subordinated Debenture Receivable from The Chase Manhattan Bank, N.A	400,000	400,000	400,000
Investments in Subsidiaries (at Equity in Net Assets):			
Banking Subsidiaries:			
The Chase Manhattan Bank, N.A.	4,518,594	4,454,725	4,267,689
Other Banking Subsidiaries	828,084	705,971	486,624
Nonbanking Subsidiaries	354,150	343,571	309,652
Accrued Interest Receivable:			
Time Deposits with Banking Subsidiaries	20,694	26,865	26,462
Notes Receivable from Nonbanking Subsidiaries	16,997	21,643	16,564
Other Interest Receivable	1,426	1,822	2,197
Other Assets	84,980	94,149	[illegible]3
Total Assets	$10,968,787	$10,817,212	$10,[illegible]8
Liabilities and Stockholders' Equity			
Commercial Paper	$ 3,127,040	$ 3,351,756	$ 4,114,863
Other Borrowed Money	573,706	573,648	325,675
Accounts Payable, Accrued Expenses and Other Liabilities	308,000	290,683	286,718
	4,008,746	4,216,087	4,727,256
Long-Term Notes and Debentures	2,362,064	2,142,351	1,735,028
Total Liabilities	6,370,810	6,358,438	6,462,284
Preferred Stock (Without Par Value-20,000,000 Shares Authorized):			
Redeemable Preferred Stock:			
616,379, Shares Outstanding	61,638	61,638	61,638
Nonredeemable Preferred Stock:			
12,039,737, Shares Outstanding	601,987	601,987	601,987
Common Stockholders' Equity:			
Common Stock (Par Value $12.50 Per Share):			
3/31/86 / 12/31/85 / 3/31/85			
Authorized Shares 125,000,000 / 125,000,000 / 125,000,000			
Outstanding Shares 78,903,826 / 77,157,724 / 37,033,691	986,298	964,472	462,921
Surplus	307,946	276,288	692,895
Foreign Exchange Translation Adjustments	(23,921)	(22,265)	(21,149)
Retained Earnings	2,664,029	2,576,654	2,314,172
Total Common Stockholders' Equity	3,934,352	3,795,149	3,448,839
Total Liabilities and Stockholders' Equity	$10,968,787	$10,817,212	$10,574,748

The Chase Manhattan Bank, N.A. and Subsidiaries

CONSOLIDATED STATEMENT OF CONDITION

($ in thousands)	March 31, 1986	December 31, 1985	March 31, 1985
Assets			
Cash and Due from Banks	$ 4,648,573	$ 5,208,200	$ 4,094,109
Interest-Bearing Deposits Placed with Banks	4,885,461	4,566,219	5,114,789
Federal Funds Sold and Securities Purchased Under Resale Agreements	2,253,935	2,458,090	1,076,262
Trading Account Assets	1,360,058	1,331,638	1,091,839
Investment Securities:			
U.S. Treasury Securities	1,622,231	1,721,697	1,883,272
Federal Agency Securities	253,302	290,391	81,267
State and Political Subdivision Securities	2,122,708	2,185,798	1,570,897
Other Bonds, Notes and Debentures	1,436,841	1,357,862	1,000,941
Federal Reserve Bank and Other Stock Investments	83,022	82,509	82,212
Total Investment Securities (Estimated Market Value of $5,657,000, $5,596,000 and $4,357,000, Respectively)	5,518,104	5,638,257	4,618,589
Loans	51,798,680	52,176,137	54,323,014
Less: Reserve for Possible Loan Losses	710,903	699,054	667,250
Loans, Net	51,087,777	51,477,083	53,655,764
Customers' Liability on Acceptances	3,265,245	2,810,159	4,691,142
Accrued Interest Receivable	942,279	1,002,649	1,053,527
Premises and Equipment	780,273	753,834	674,787
Other Assets	2,797,987	2,474,067	2,812,906
Total Assets	$77,539,692	$77,720,196	$78,883,714
Liabilities and Stockholder's Equity			
Deposits:			
Domestic Offices:			
Noninterest-Bearing	$11,302,401	$12,677,180	$ 9,102,738
Interest-Bearing	14,497,851	14,629,437	14,297,892
Overseas Offices:			
Noninterest-Bearing	2,046,010	1,939,120	1,460,490
Interest-Bearing	30,262,955	29,500,685	33,390,350
Total Deposits	58,109,217	58,746,422	58,251,470
Federal Funds Purchased and Securities Sold Under Repurchase Agreements	4,148,092	3,972,397	4,122,760
Other Borrowed Funds	2,377,134	3,160,191	2,362,890
Acceptances Outstanding	3,272,665	2,818,384	4,702,837
Accrued Interest Payable	573,199	611,150	732,048
Accounts Payable, Accrued Expenses and Other Liabilities	3,488,097	2,925,095	3,495,799
	71,968,404	72,233,639	73,667,804
Long-Term Notes and Debentures	1,052,694	1,031,832	948,221
Total Liabilities	73,021,098	73,265,471	74,616,025
Stockholder's Equity:			
Capital Stock (Par Value $15.00 Per Share):			
	3/31/86 / 12/31/85 / 3/31/85		
Authorized Shares	61,744,445 / 61,744,445 / 61,744,445		
Outstanding Shares	50,145,351 / 50,009,247 / 49,511,444	752,180	750,139	742,672
Surplus		1,780,235	1,772,407	1,751,482
Foreign Exchange Translation Adjustments		(24,065)	(22,345)	(21,047)
Undivided Profits		2,010,244	1,954,524	1,794,582
Total Stockholder's Equity		4,518,594	4,454,725	4,267,689
Total Liabilities and Stockholder's Equity		$77,539,692	$77,720,196	$78,883,714

Member Federal Deposit Insurance Corporation

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The Chase Manhattan Corporation and Subsidiaries

Average Balances, Interest and Average Rates-Taxable Equivalent

($ in millions)	First Quarter 1986 Average Balance	Interest	Average Rate	Fourth Quarter 1985 Average Balance	Interest	Average Rate	Third Quarter 1985 Average Balance	Interest	Average Rate
Assets									
Interest-Earning Assets:									
Interest-Bearing Deposits Placed with Banks	$ 4,897	$ 115	9.55%	$ 5,042	$ 121	9.56%	$ 5,445	$ 130	9.45%
Federal Funds Sold and Securities Purchased Under Resale Agreements	899	49	22.21 **	1,406	36	10.12	1,051	21	8.04
Trading Account Assets	1,186	30	10.68	877	24	11.02	791	20	9.95
Investment Securities:									
Domestic Offices:									
U.S. Treasury Securities	1,694	40	9.59	1,743	44	9.98	1,950	49	9.98
Federal Agency Securities	340	9	10.79	311	7	9.36	285	7	10.19
State and Political Subdivision Securities	2,161	71	13.32	2,040	67	12.87	1,999	66	12.99
Other Securities	226	6	9.38	243	6	9.63	249	8	13.00
Total Domestic Offices	4,419	126	11.50	4,337	124	11.28	4,483	130	11.50
Overseas Offices	1,644	78	19.10	1,418	59	16.43	1,263	46	14.61
Total Investment Securities	6,063	203	13.66	5,755	183	12.55	5,746	176	12.19
Loans:									
Domestic Offices	27,760	835	12.19	26,435	808	12.13	26,351	743	11.62
Overseas Offices	33,944	1,014	12.11	35,048	1,025	11.60	34,467	1,036	11.27
Total Loans	61,704	1,849	12.14	61,483	1,833	11.83	61,818	1,779	11.42
Less: Reserve for Possible Loan Losses*	927	-	-	902	-	-	847	-	-
Loans, Net	60,779	1,849	12.14	60,581	1,833	12.01	60,971	1,779	11.42
Total Interest-Earning Assets,* Net	73,793	2,246	12.19	73,663	2,197	11.69	74,024	2,126	11.27
Summary-Gross Interest-Earning Assets									
Domestic Offices	33,627	990	11.93	32,528	967	11.80	31,464	904	11.43
Overseas Offices	41,094	1,256	12.39	42,037	1,230	11.61	43,417	1,220	11.15
Total Gross Interest-Earning Assets	74,721	2,246	12.19	74,565	2,197	11.69	74,871	2,126	11.27
Noninterest-Earning Assets:									
Cash and Due from Banks	4,787			4,905			4,307		
Customers' Liability on Acceptances	2,703			3,384			3,952		
Other Assets	5,322			4,797			4,594		
Total Noninterest-Earning Assets	12,812			12,656			12,853		
Total Assets	$86,605			$86,649			$86,877		
Liabilities and Stockholders' Equity									
Interest-Bearing Liabilities:									
Interest-Bearing Deposits:									
Domestic Offices:									
Savings and Negotiable Order of Withdrawal Deposits	$ 1,926	$ 25	5.17%	$ 1,909	$ 25	5.12%	$ 1,922	$ 26	5.26%
Savings Certificates and Nest Egg Account Deposits	381	8	8.75	359	9	9.24	384	9	9.10
Money Market Deposits	8,739	147	6.85	8,368	147	6.99	7,889	136	6.83
Negotiable Certificates of Deposit	672	13	7.63	911	18	7.93	874	17	7.89
Other Time Deposits	7,367	140	8.79	7,340	162	8.76	7,312	153	8.31
Total Domestic Offices	19,085	333	7.49	18,887	361	7.58	18,383	341	7.35
Overseas Offices	28,787	607	8.56	29,929	645	8.56	30,286	691	9.06
Total Interest-Bearing Deposits	47,872	940	8.13	48,816	1,006	8.18	48,669	1,032	8.41
Federal Funds Purchased and Securities Sold Under Repurchase Agreements	4,659	161	14.03 **	4,823	125	10.32	5,059	116	9.13
Other Borrowed Money:									
Domestic Offices	5,655	120	8.62	5,041	113	8.90	5,479	115	8.30
Overseas Offices	1,707	116	27.09 **	1,484	92	24.53	1,205	35	11.64
Total Other Borrowed Money	7,362	236	12.91	6,525	205	12.44	6,684	150	8.90
Long-Term Notes and Debentures	2,864	66	8.98	2,690	62	9.10	2,605	61	9.20
Total Interest-Bearing Liabilities	62,757	1,619	9.17	62,874	1,398	8.82	63,017	1,359	8.56
Summary-Interest-Bearing Liabilities									
Domestic Offices	23,870	455	7.73	23,209	454	7.77	22,204	421	7.52
Overseas Offices	38,887	964	10.06	39,665	944	9.44	40,813	938	9.12
Total Interest-Bearing Liabilities	62,757	1,619	9.17	62,874	1,398	8.82	63,017	1,359	8.56
Noninterest-Bearing Liabilities:									
Deposits in Domestic Offices	10,696			10,662			9,850		
Deposits in Overseas Offices	1,765			1,614			1,470		
Acceptances Outstanding	2,714			3,220			3,960		
Accounts Payable, Accrued Expenses and Other Liabilities	4,185			3,925			4,338		
Total Noninterest-Bearing Liabilities	19,360			19,321			19,618		
Total Liabilities	82,117			82,195			82,635		
Redeemable Preferred Stock	62			62			62		
Nonredeemable Preferred Stock	602			602			602		
Common Stockholders' Equity	3,824			3,690			3,578		
Total Liabilities and Stockholders' Equity	$86,606			$86,549			$86,877		
Taxable Equivalent Net Interest Income and Average Interest Rate Spread		$ 627	3.02%		$ 799	2.87%		$ 767	2.71%
Net Interest Income as a Percentage of Gross Interest-Earning Assets			4.49%			4.28%			4.07%

* Reserve for possible loan losses is excluded from calculations of average balances and average rates, as appropriate.

** Reflects the extraordinarily high level of local interest rates prevailing in certain South American countries.

NOTE: Loan amounts include nonaccrual and reduced rate loans, as applicable.

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The Chase Manhattan Corporation and Subsidiaries

Average Balances, Interest and Average Rates-Taxable Equivalent

($ in millions)	Second Quarter 1985 Average Balance	Interest	Average Rate	First Quarter 1985 Average Balance	Interest	Average Rate
Assets						
Interest-Earning Assets:						
Interest-Bearing Deposits Placed with Banks	$ 5,010	$ 119	9.51%	$ 4,987	$ 116	9.42%
Federal Funds Sold and Securities Purchased Under Resale Agreements	1,266	24	7.60	1,210	24	8.12
Trading Account Assets	557	16	11.74	829	22	10.87
Investment Securities:						
Domestic Offices:						
U.S. Treasury Securities	1,903	50	10.54	1,746	48	11.05
Federal Agency Securities	171	6	14.07	192	5	11.67
State and Political Subdivision Securities	1,954	65	13.34	1,945	64	13.34
Other Securities	273	8	11.75	270	5	7.51
Total Domestic Offices	4,301	129	12.03	4,153	122	11.91
Overseas Offices	1,145	44	15.54	1,038	52	20.23
Total Investment Securities	5,446	173	12.74	5,191	174	13.59
Loans:						
Domestic Offices	24,641	760	12.37	24,357	754	12.55
Overseas Offices	36,820	1,072	11.68	37,022	1,085	11.89
Total Loans	61,461	1,832	11.96	61,379	1,839	12.15
Less: Reserve for Possible Loan Losses*	804	-	-	777	-	-
Loans, Net	60,657	1,832	11.96	60,602	1,839	12.15
Total Interest-Earning Assets,* Net	72,936	2,164	11.96	72,819	2,175	11.99
Summary-Gross Interest-Earning Assets						
Domestic Offices	30,601	923	12.10	30,379	917	12.24
Overseas Offices	43,139	1,241	11.54	43,217	1,258	11.81
Total Gross Interest-Earning Assets	73,740	2,164	11.77	73,596	2,175	11.99
Noninterest-Earning Assets:						
Cash and Due from Banks	4,295			4,280		
Customers' Liability on Acceptances	4,432			4,548		
Other Assets	4,310			4,103		
Total Noninterest-Earning Assets	13,037			12,931		
Total Assets	$85,973			$85,750		
Liabilities and Stockholders' Equity						
Interest-Bearing Liabilities:						
Interest-Bearing Deposits:						
Domestic Offices:						
Savings and Negotiable Order of Withdrawal Deposits	$ 1,917	$ 25	5.22%	$ 1,854	$ 23	5.10%
Savings Certificates and Nest Egg Account Deposits	404	8	7.94	423	10	9.11
Money Market Deposits	7,427	139	7.52	7,074	138	7.95
Negotiable Certificates of Deposit	972	20	8.53	876	20	9.05
Other Time Deposits	7,286	174	9.56	7,456	188	10.22
Total Domestic Offices	18,006	366	8.17	17,683	379	8.69
Overseas Offices	31,246	747	9.59	31,378	745	9.63
Total Interest-Bearing Deposits	49,252	1,113	9.07	49,061	1,124	9.29
Federal Funds Purchased and Securities Sold Under Repurchase Agreements	4,266	105	9.81	5,068	116	9.25
Other Borrowed Money:						
Domestic Offices	5,572	124	8.94	5,369	124	9.34
Overseas Offices	1,103	40	14.44	1,098	48	17.90
Total Other Borrowed Money	6,675	164	9.85	6,467	172	10.79
Long-Term Notes and Debentures	2,487	60	9.61	2,311	58	10.24
Total Interest-Bearing Liabilities	62,680	1,442	9.22	62,907	1,470	9.48
Summary-Interest-Bearing Liabilities						
Domestic Offices	21,912	454	8.32	21,616	471	8.83
Overseas Offices	40,768	988	9.71	41,291	999	9.82
Total Interest-Bearing Liabilities	62,680	1,442	9.22	62,907	1,470	9.48
Noninterest-Bearing Liabilities:						
Deposits in Domestic Offices	9,478			9,384		
Deposits in Overseas Offices	1,390			1,272		
Acceptances Outstanding	4,467			4,642		
Accounts Payable, Accrued Expenses and Other Liabilities	3,840			3,514		
Total Noninterest-Bearing Liabilities	19,175			18,812		
Total Liabilities	81,855			81,719		
Redeemable Preferred Stock	62			62		
Nonredeemable Preferred Stock	602			602		
Common Stockholders' Equity	3,454			3,367		
Total Liabilities and Stockholders' Equity	$85,973			$85,750		
Taxable Equivalent Net Interest Income and Average Interest Rate Spread		$ 722	2.55%		$ 705	2.51%
Net Interest Income as a Percentage of Gross Interest-Earning Assets			3.93%			3.88%

* Reserve for possible loan losses is excluded from calculations of average balances and average rates, as appropriate.

NOTE: Loan amounts include nonaccrual and reduced rate loans, as applicable.

The Chase Manhattan Corporation and Subsidiaries

Consolidated Average Loan Balances**

($ in millions)	1986 1st Qtr.	1985 4th Qtr.	3rd Qtr.	2nd Qtr.	1st Qtr
Domestic Offices:					
Real Estate Loans:					
Secured by 1-4 Family Residential Properties	$ 2,717	$ 2,649	$ 2,218	$ 1,875	$ 1,72
Other Real Estate Loans	4,065	3,362	2,974	2,873	2,93
Loans to Mortgage Companies	337	347	300	295	25
Loans to Other Financial Institutions	1,317	1,430	1,548	1,808	1,67
Loans for Purchasing or Carrying Securities	579	600	608	614	50
Commercial and Industrial Loans	8,208	8,584	8,799	8,961	9,63
Loans to Individuals for Personal Expenditures	7,417	7,012	6,548	6,046	5,45
Lease Financings	1,313	1,277	1,167	984	98
Tax-Exempt Loans	1,659	1,277	1,189	1,113	1,14
Other Loans	562	402	504	474	48
Total Domestic Offices, Gross	28,174	26,940	25,855	25,043	24,80
Less: Unearned Discount	414	505	504	402	45
Total Domestic Offices	27,760	26,435	25,351	24,641	24,35
Overseas Offices*	34,160	35,238	36,661	37,003	37,22
Less: Unearned Discount	214	190	194	183	20
Total Overseas Offices	33,946	35,048	36,467	36,820	37,02
Total Average Loans	$ 61,706	$ 61,483	$ 61,818	$ 61,461	$ 61,37
*Loans in overseas offices includes loans to U.S. commercial borrowers	$ 5,050	$ 5,262	$ 5,777	$ 5,57	6,64

**Prior period amounts have been reclassified for comparative purposes.

Consolidated Analysis of Loan Loss Experience

($ in thousands)	1986 1st Qtr.	1985 4th Qtr.	3rd Qtr.	2nd Qtr.	1st Qtr
Reserve for Possible Loan Losses at Beginning of Period	$907,672	$872,399	$820,690	$779,362	$761,43
Net Loan Charge-Offs:					
Domestic Loans:					
Commercial and Industrial Loans	5,640	20,639	24,236	18,219	29,74
Loans to Financial Institutions	(75)	456	(67)	659	(76
Loans for Purchasing or Carrying Securities	(81)	-	-	(3)	
Real Estate Loans	6,166	8,739	(542)	(622)	67
Loans to Individuals for Personal Expenditures	63,940	48,768	33,881	25,518	23,31
Lease Financings	733	931	103	(32)	(
Other Loans	(9)	650	(314)	(16)	13
Total Domestic Net Loan Charge-Offs	76,314	80,183	57,297	43,723	53,09
International Loans:					
Commercial and Industrial Loans	25,055	22,195	11,385	2,733	11,94
Real Estate Loans	140	(221)	(529)	205	68
Loans to Individuals for Personal Expenditures	2,923	2,241	2,992	1,887	49
Loans to Foreign Governments and Official Institutions	9,631	79	1,309	21,385	7,25
Other Loans	122	(13)	538	(631)	12
Total International Net Loan Charge-Offs	37,871	24,281	15,695	25,57	0,49
Total Net Loan Charge-Offs	114,185	104,464	72,992	69,30	3,59
Provision Charged to Expenses	130,000	125,000	110,000	105,000	95,00
Reserves of Acquired Subsidiaries	5,489	7,337	9,923	6,860	
Foreign Exchange Translation Adjustments	5,859	7,400	4,778	(1,230)	(3,48
Reserve for Possible Loan Losses at End of Period	$934,835	$907,672	$872,399	$820,690	$779,36

he Chase Manhattan Corporation and Subsidiaries

unds Borrowed

($ in thousands)	1986 March 31,	1985 Dec. 31,	1985 Sept. 30,	1985 June 30,	1985 March 31,
ederal Funds Purchased	$ 2,662,949	$ 2,585,402	$ 1,863,036	$ 2,029,211	$ 2,042,552
ecurities Sold Under Repurchase Agreements	1,319,836	1,546,391	2,280,031	1,491,029	2,233,028
Total	3,982,785	4,131,793	4,143,067	3,520,240	4,275,580
ommercial Paper:					
Company	3,116,410	3,337,981	3,567,949	4,081,902	4,098,316
Subsidiaries of Bank	126,091	145,520	120,346	85,492	58,293
Total	3,242,501	3,483,501	3,688,295	4,167,394	4,156,609
ther Borrowed Money:					
Maturing Within One Year:					
Banking Subsidiaries of Company	1,086,008	904,793	504,017	549,983	478,122
Nonbanking Subsidiaries of Company	113,489	100,678	83,329	78,847	72,268
Bank:					
Domestic Offices	548,966	1,276,361	1,129,833	1,442,555	1,049,099
Overseas Offices	1,268,296	1,389,786	1,013,239	612,635	750,535
Mat[illegible] After One Year:					
[illegible]y:					
Floating Rate Extendable Notes (Due 1992)	299,813	299,784	299,756	299,728	299,700
Floating Rate Extendable Notes (Due 1997)	249,775	249,746	249,717	249,694	-
Floating Rate Notes (Due 1999)	24,118	24,118	25,147	25,147	25,975
Banking Subsidiaries of Company	109,790	81,694	88,107	88,007	91,391
Nonbanking Subsidiary of Company	7,269	-	-	-	-
Bank:					
Domestic Offices	869	866	2,654	128,485	125,883
Overseas Offices	427,723	344,168	398,863	377,631	372,649
Total	4,136,116	4,671,994	3,794,662	3,852,712	3,265,622
Total Funds Borrowed	$11,361,402	$12,287,288	$11,626,024	$11,540,346	$11,697,811

The Chase Manhattan Corporation and Subsidiaries

Long-Term Notes and Debentures

($ in thousands)	1986 March 31,	1985 Dec. 31,	Sept. 30,	June 30,	March 31,
Company:					
Convertible Capital Notes (4 7/8% Due 1993)	$ 6,759	$ 7,245	$ 7,626	$ 8,207	$ 8,907
Convertible Subordinated Debentures (6 1/2% Due 1996)	25,862	57,282	57,374	79,522	80,627
Notes (15 1/2% Due 1992) Issued with Detachable Equity Contracts	150,000	150,000	150,000	150,000	150,000
Notes (8 1/2% Due 1996)	249,006	-	-	-	-
Zero Coupon Notes (Due 1992)	75,515	72,964	70,499	68,119	65,821
Floating Rate Notes (Due 2009)	282,385	282,385	282,385	282,385	282,385
Floating Rate Subordinated Notes (Due 1995)	348,872	348,843	348,814	348,785	348,756
Floating Rate Subordinated Notes (Due 1996)	398,665	398,632	398,598	398,565	398,532
Floating Rate Subordinated Notes (Due 1997)	175,000	175,000	-	-	-
Floating Rate Subordinated Notes (Due 2000)	250,000	250,000	250,000	250,000	-
Floating Rate Subordinated Notes (Due 2009)	400,000	400,000	400,000	400,000	400,000
Total	2,362,064	2,142,351	1,965,296	1,985,583	1,735,028
Chase Manhattan National Corporation:					
Debentures (6 1/4% Due 1992)	7,250	7,250	7,250	7,250	7,250
Debentures (8 1/2% Due 1996)*	21,090	21,090	21,090	21,090	21,090
Chase Lincoln First Bank N.A. Capital Notes (4.70% Due 1989)	3,974	3,976	3,975	3,975	4,336
Total	32,314	32,316	32,315	32,315	32,676
Bank:					
Capital Notes (8 3/4% Due 1986)	200,000	200,000	200,000	200,000	200,000
Capital Notes (4.60% Due 1990)	3,768	3,833	3,886	4,153	4,183
Floating Rate Notes (Due 1993)**	150,000	150,000	150,000	150,000	150,000
Deutsche Mark Bearer Bonds (6% Due 1993)**	31,284	32,300	29,297	25,863	27,896
French Franc Floating Rate Bonds (Due 1992)***	105,152	97,485	90,744	80,057	74,069
French Franc Floating Rate Bonds (Due 1993)***	49,071	45,493	42,347	37,359	-
Swiss Franc Bonds (4% Due 1993)**	31,594	30,288	28,750	25,839	24
Long-Term Notes and Debentures of NCB (1) (Various Maturities)	81,825	72,433	65,998	63,987	65,839
Floating Rate Subordinated Debenture (Due 1996)	400,000	400,000	400,000	400,000	400,000
Total	1,052,694	1,031,832	1,011,022	987,258	948,221
Less: Investment by the Company in Floating Rate Subordinated Debenture of the Bank (Due 1996)	400,000	400,000	400,000	400,000	400,000
Total Long-Term Notes and Debentures	$2,047,072	$2,806,499	$2,608,633	$2,605,156	$2,315,925

*Guaranteed by the Company.

**Issued by the Chase Manhattan Overseas Banking Corporation, a wholly owned subsidiary of the Bank, and guaranteed by the Company.

***Issued by Chase Manhattan S.A., a wholly owned subsidiary of the Bank, and guaranteed by the Company.

(1) Nederlandse Credietbank N.V.

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Manhattan Corporation and Subsidiaries

Consolidated Statement of Income

($ in thousands, except per common share data)	1986 1st Qtr.	1985 4th Qtr.	1985 3rd Qtr.	1985 2nd Qtr.	1985 1st Qtr.
Interest Income					
Interest and Fees on Loans	$1,808,867	$1,802,486	$1,755,003	$1,804,216	$1,812,209
Interest on Bank Deposit Placings	115,318	121,013	130,551	118,786	115,880
Interest and Dividends on Investment Securities:					
Interest on U.S. Treasury Securities	40,072	43,857	49,044	50,988	47,557
Federal Agency Securities	9,050	7,356	7,310	5,151	5,554
State and Political Subdivision Securities Exempt from Federal Income Taxes	43,232	38,509	37,876	36,987	36,730
Other Bonds, Notes and Debentures	70,742	57,054	45,153	43,972	51,687
Dividends on Federal Reserve Bank and Other Stock Investments	2,416	2,373	3,293	3,018	1,557
	165,512	149,149	142,676	140,116	143,085
Interest on Federal Funds Sold and Securities Purchased Under Resale Agreements	49,236	35,919	21,300	25,559	24,226
Interest on Trading Account Assets	28,171	22,704	18,611	14,939	20,664
Total Interest Income	2,167,104	2,131,271	2,068,141	2,103,616	2,116,064
Interest Expense					
Deposits	959,723	1,006,231	1,031,908	1,113,405	1,124,151
Federal Funds Purchased and Securities Sold Under Repurchase Agreements	161,119	125,090	116,825	105,873	115,594
Commercial Paper	56,844	60,547	63,346	69,326	72,378
Other Borrowed Money	177,545	144,668	86,585	94,615	99,776
Long-Term Notes and Debentures	63,421	61,703	60,407	59,567	58,367
Total Interest Expense	1,418,652	1,398,239	1,359,071	1,442,786	1,470,266
Net Interest Income	748,452	733,032	709,070	660,830	645,798
Provision for Possible Loan Losses	130,000	125,000	110,000	105,000	95,000
Net Interest Income After Provision for Possible Loan Losses	618,452	608,032	599,070	555,830	550,798
Other Operating Income					
Fiduciary Commissions	241,580	262,220	228,404	218,571	199,610
Foreign Exchange Trading Income	60,277	46,470	48,231	43,141	35,543
Trading Account Profits (Losses)	22,173	11,460	3,022	22,349	(5,415
Investment Securities Gains (Losses)	40,204	20,021	28,776	29,143	20,165
Other Income	9,085	41,138	12,848	16,538	33,496
Total Other Operating Income	373,319	381,309	321,281	329,742	283,399
Other Operating Expenses					
Salaries and Employee Benefits:					
Salaries	319,065	311,613	280,038	267,219	254,451
Profit Sharing	20,502	22,489	22,351	22,108	16,484
Other Employee Benefits	84,863	63,641	72,336	66,485	70,452
	424,430	397,743	374,725	355,812	341,387
Net Occupancy	71,182	68,055	67,869	64,536	56,145
Equipment Rentals, Depreciation and Maintenance	67,867	54,700	59,456	57,031	54,581
Other Expenses	209,978	223,718	196,327	189,679	170,114
Total Other Operating Expenses	773,457	744,216	698,377	667,058	622,227
Income Before Taxes	218,314	245,125	221,974	218,514	211,970
Applicable Income Taxes	74,624	94,445	72,550	87,699	78,071
Net Income	$ 143,690	$ 150,680	$ 149,424	$ 130,815	$ 133,899
Net Income Applicable to Common Stock	$ 127,408	$ 133,484	$ 132,143	$ 107,135	$ 107,811
Average Shares Outstanding	78,156,253	76,789,784	75,898,388	74,497,664	73,735,222
Earnings Per Common Share:					
Primary, Based on Average Shares Outstanding	$ 1.63	$ 1.74	$ 1.74	$ 1.44	$ 1.46
Assuming Full Dilution	$ 1.59	$ 1.68	$ 1.68	$ 1.38	$ 1.41
Cash Dividends Declared Per Common Share	$ .51 1/4	$ .47 1/2	$ .47 1/2	$ .47 1/2	$ .47 1/2

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PART II - OTHER INFORMATION

Item 6. Exhibits and Reports on Form 8-K

(a) Exhibits

	Page
Exhibit 11 Statement re: Computation of Earnings Per Common Share for the quarters ended March 31, 1986 and 1985	30
Exhibit 28 Summarized Financial Information - Chase Manhattan National Corporation	31

(b) Reports on Form 8-K

The registrant filed the following Reports on Form 8-K during the quarter ended March 31, 1986.

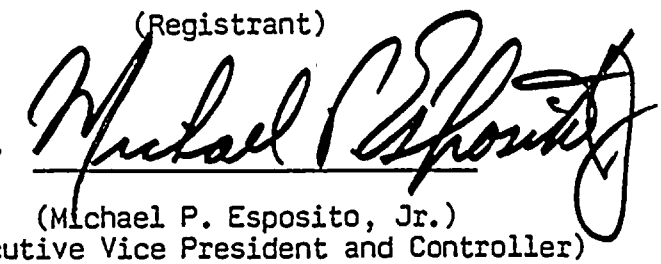
Date of Report	Items Reported
1/13/86	- News release announcing the Corporation's earnings for the full year and the quarter ended December 31, 1985.
	- On January 15, 1986, The Chase Manhattan Corporation issued a news release announcing a 2-for-1 split of its common stock in the form of a 100% stock dividend.
3/3/86	- On March 3, 1986 The Chase Manhattan Corporation entered into an underwriting agreement covering the issue and sale of $250,000,000 aggregate principal amount of 8 1/2% Notes Due 1996.

SIGNATURE

Pursuant to the requirements of the Securities Exchange Act of 1934, the registrant has duly caused this report to be signed on its behalf by the undersigned thereunto duly authorized.

THE CHASE MANHATTAN CORPORATION

(Registrant)

By 

(Michael P. Esposito, Jr.)
(Executive Vice President and Controller)

May 14, 1986

EXHIBIT 1

The Chase Manhattan Corporation and Subsidiaries
Computation of Earnings Per Common Share

($ in thousands, except per share amounts)	Quarter Ended March 31, 1986	1985
Primary		
Net Income	$ 143,690	$ 133,899
Less: Preferred Stock Dividend Requirements	16,282	26,088
Net Income Applicable to Common Stock	$ 127,408	$ 107,811
Average Common Shares Outstanding	78,156,253	73,735,222
Primary Earnings Per Common Share	$ 1.63	$ 1.46
Assuming Full Dilution		
Net Income Applicable to Common Stock - as adjusted*	$ 127,651	$ 108,620
Shares of Common Stock Outstanding During the Period, retroactively adjusted for conversions of capital notes and subordinated debentures and exercises of stock options	78,654,444	73,764,472
Add: Shares Issuable upon Conversion of Convertible Capital Notes and Debentures	1,148,338	3,132,290
Shares Issuable upon Exercise of Stock Options and Conversion of Restricted Stock Units	630,446	384,424
Shares of Common Stock Outstanding - as adjusted	80,433,228	77,281,186
Earnings Per Common Share Assuming Full Dilution	$ 1.59	$ 1.41

*Adjusted for interest expense on convertible notes and debentures after applicable income taxes.

EXHIBIT 28

Summarized Financial Information - Chase Manhattan National Corporation

In connection with the merger of Lincoln First Banks Inc. ("Lincoln") into Chase Manhattan National Corporation ("CMNC") on July 1, 1984, CMNC assumed, and subsequently the Company guaranteed, Lincoln's 8 1/2% Debentures Due 1996. Set forth below is summarized consolidated financial information for CMNC for the periods indicated.

Statement of Income Information

($ in millions)	Three Months Ended March 31, 1986	1985
Net Interest Income After Provision For Possible Loan Losses	$39	$38
Net Income	8	12

Statement of Condition Information

($ in millions)	March 31, 1986	December 31, 1985	March 31, 1985
Loans	$2,995	$2,986	$2,725
Total Assets	4,122	4,164	4,010
Deposits	3,290	3,319	3,176
Total Liabilities	3,742	3,792	3,669
Stockholder's Equity	380	372	341
Total Liabilities and Stockholder's Equity	4,122	4,164	4,010

END

(ANNUAL REPORT) TO THE SECURITIES AND EXCHANGE COMMISSION 1985

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FINANCIAL HIGHLIGHTS

IN MILLIONS OF DOLLARS EXCEPT PER SHARE AMOUNTS

RESULTS **In 1985, fully diluted earnings per share and net income rose 12% from 1984.**	1985	1984
Earnings Per Share (Fully Diluted)	**$ 7.11**	$ 6.36
Net Income	**998**	890
Return on Common Stockholders' Equity	**15.1%**	15.0%

SECTOR EARNINGS	1985	1984
Earnings of Three Core Businesses (Not including items retained at the corporate level)	**$1,157**	$1,019

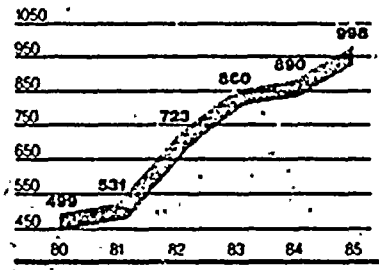
COMMON DIVIDENDS **Dividends rose $.20 per share, or 10%, in 1985.**	1985	1984
Cash Dividends Declared	**$ 290**	$ 259
Cash Dividends Declared Per Share	**2.26**	2.06

TOTAL CAPITAL **Total capital increased 35% from a year ago.**	1985	1984
Total Capital	**$ 15,948**	$ 11,805
Percentage of Total Assets	**9.12%**	7.79%

YEAR-END BALANCES **Total assets rose 15% from 1984, primarily reflecting growth in the consumer loan portfolio.**	1985	1984
Total Assets	**$173,597**	$150,586
Commercial Loans, Net of Unearned Discount	**58,172**	58,799
Consumer Loans, Net of Unearned Discount	**55,518**	42,661
Total Deposits	**104,959**	90,349
Total Stockholders' Equity	**7,765**	6,426
Common Stockholders' Equity Per Share	**50.63**	45.82

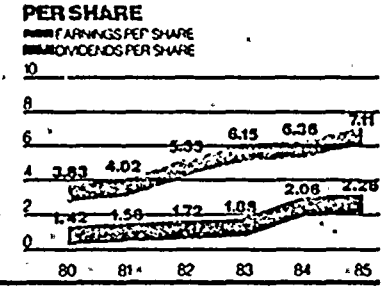
NET INCOME

IN MILLIONS OF DOLLARS



EARNINGS AND DIVIDENDS PER SHARE

EARNINGS PER SHARE
DIVIDENDS PER SHARE



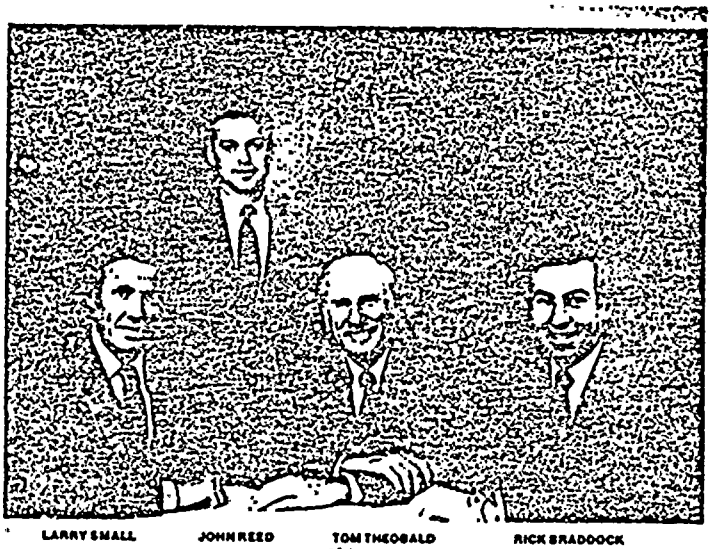
TO CITICORP INVESTORS

In many ways, 1985 was a year of important accomplishment for Citicorp and, also, it was a year that reflected the continued tensions associated with a changing global economy.

- During 1985, the Corporation earned $7.11 (fully diluted) per share, an increase of 12%, or $.73, over 1984. Over the last five years, the compound growth rate of EPS was 13.2%.
- As of December 31, the Corporation's total capital was $15.9 billion, an increase of 35%, or $4.1 billion, since the same time in 1984.
- The rate of return earned on your equity was 15.1%, essentially the same as last year.
- During the year, Citicorp common stock sold in a range of $36⅞ to $51¾, closing the year at $49⅜, and approaching our book value of $50.63. Your dividend was increased 10% to $2.26 per share during the year.

We remain committed to the long-term goal of building value for shareholders, customers, and staff by developing a truly unique global financial services business which will record superior performance. Our work during the year 1985 continues to suggest that this goal is realistic and achievable. The markets in which we work are large and full of new opportunities. The legal and regulatory restrictions which have historically limited your Company's activities are visibly eroding.

As was announced in 1985, we reorganized our three core businesses. We moved our money market and foreign exchange trading activities into the Investment Bank, improving the interaction between the Institutional Banking officers and their Investment Banking colleagues and creating a truly global force to serve our customers. We also structured our Individual Bank



LARRY SMALL JOHN REED TOM THEOBALD RICK BRADDOCK

to integrate our U.S. branching and card products activities within common units and formed a global Private Banking business which we believe will be of future importance. Even at this early date it appears that this reorganization, which puts Messrs. Theobald, Braddock, and Small in charge of the three core businesses of the Corporation, has opened up new opportunities, brought new strengths to our customers, and will be of important longer term significance in the evolution of Citicorp.

More immediately, the Corporation is pursuing parallel goals. On the one hand, we are making good progress building each of the three core businesses, and on the other, strengthening the Corporation's balance sheet. Each one of the Sector Executives makes his report on the following pages. We feel that the core business efforts are strong and promising. Within each, we continue to balance the opportunities to invest and build against the need to pace our growth. We are enthusiastic about our progress.

We continue to manage the balance sheet conservatively. Our capital is strengthening relative to our overall activities. We also have continued to manage our interest rate exposure on a conservative basis. We have seen considerable progress in the percentage of total deposits which come from customer sources, having developed deposit businesses in important markets within the United States and around the world. We manage our liquidity and funding in such a way as to insure access to the world's money markets and to insure important long-term stability for your Company. We have grown our loan loss reserves more rapidly. We expect

YOUR MANAGEMENT DIRECTORS

PAUL J. COLLINS

to continue to build these reserves beyond the level normally required by the day-to-day economics of the business, a strengthening which seems appropriate given the nature of the risks in the global system and the world's business environment.

Nineteen eighty-five was a year of progress in terms of the global debt situation. A specific report on this is found on page 18 in this report. From a purely financial point of view, the impact of restructuring countries on this year's results was small and we have seen reductions of cash basis loans. Many countries have made impressive progress both in managing their external accounts and in resuming growth. However, the country debt problem continues to be an important one, and it is quite predictable that in the years ahead we will see both good and bad news. The absolute level of indebtedness of these developing nations is still very high compared to the activity of the global economy. As reflected later in this report there are any number of cross currents which make the role of your Corporation in these matters both important and challenging.

As shown in our financial results, our loan write-offs during 1985 were high. This is a trend that has been with the banking industry for a number of years and is likely to continue. The global financial system is the conduit through which much economic change and volatility are transmitted. Any number of our customers around the world have experienced and continue to experience difficulty in managing the economics of their businesses in this changing environment. We feel strongly that one of our responsibilities is to provide our good customers time to make appropriate business adjustments. In doing so, we reflect some of the underlying economic risk on our own balance sheet. While, as indicated, these write-offs are substantial,

JAMES D. FARLEY JOHN S. REED

they are well within the risk-taking capacity of your Company, as evidenced by the 1985 performance which reported increased earnings and write-offs, and the buildup of reserves. We are quite proud of the professional lending officers in all of our business sectors and of the processes that we have in place to manage our many risks in a way that insures the soundness of your business enterprise while still providing appropriate support for our customers.

During the year, your Corporation lost the services of Mr. Peter Grace and Mr. Irving Shapiro, who retired as Directors after having served on your Board for many years. Mr. Grace is an outstanding American and outstanding business leader. He joined the Board in 1946. Like his father before him, he served the National City Bank and more recently Citicorp with vigor, wisdom, and enthusiasm. We will miss his contributions. Mr. Shapiro is also a unique businessman and public person who brought his many skills to bear on your Company's problems and opportunities with dedication and insight. We wish both of them well. In parallel with their new responsibilities Messrs. Braddock, Small, and Collins were elected to the Board.

As we look to 1986 and beyond, we anticipate continuing hard work and consistent accomplishment in building superior value for stockholders, customers, and staff. We recognize that our optimism with respect to our plans and aspirations simply reflects the dedication and capability of your Board and the unique professionalism and energy of the 81,000 Citicorpers who work for your Company around the world.

JOHN S. REED

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CORE BUSINESS RESULTS

Citicorp continues to be organized into the three core business sectors of Individual, Institutional, and Investment Banking. The breakdown of the earnings of these sectors has been disclosed since 1983 to present a better understanding of Citicorp's core businesses. In line with this objective, we have made three changes in our presentation of sector results for 1985. These changes reflect the recent reorganization, the treatment of the allowance for possible credit losses, and the treatment of income taxes.

The first change reflects the reorganization that was made in late 1985, in which the treasury function was transferred from the Institutional Bank to the Investment Bank and the International Private Banking activities were moved from the Investment Bank to the Individual Bank.

The second change that has been made is to the allocation of the total credit loss allowance to reflect management's philosophy of how its businesses should be charged with the credit losses which may be expected over a protracted period of time. Citicorp now charges its sectors with a credit loss provision that maintains an allowance at a level that provides a measurement of costs against revenue generation consistent with the manner in which Citicorp manages its businesses and makes incremental business decisions. In any time period, the total allowance required to present the total loan portfolio in accordance with generally accepted accounting principles may be more than that allocated to the businesses. The additional amount along with its related provision is recorded at the corporate level.

The total allowance for possible credit losses was $1,235 million, or 1.06% of total loans and lease financing outstanding at December 31, 1985. Of the total, $278 million has now been allocated to the Individual Bank, representing .50% of the consumer loan portfolio. The Institutional Bank has been allocated $349 million of the allowance, or .60% of commercial loans. The remaining $608 million has been reported at the corporate level.

The third change concerns certain tax expenses, which had previously been held at the corporate level. The allocation of these taxes to the businesses more appropriately reflects sector performance and is necessitated by the increasing impact of these taxes on the Corporation.

As a result of the above changes, the amounts held at the corporate level will contain:

- The credit loss provision that represents the build-up of the credit allowance beyond that charged to the businesses.
- Unallocated corporate staff costs.
- Other corporate items including certain start-up activities.

The sectors are not charged for these items which reflect corporate level decisions and which, if allocated, would detract from an understanding of how the core businesses are performing.

The following two tables reflect the changes to core business reporting. The remaining tables in this section show Citicorp's management of its businesses along the two major dimensions of customer relationships and geographic earnings. The third major dimension of management, by product, is discussed by the sector executives, beginning on page 10. Each sector executive also discusses customer relationships. A discussion of the geographic distribution of earnings can be found on page 46.

REVISED CORE BUSINESS REPORTING NET INCOME—FULL YEAR

IN MILLIONS OF DOLLARS	INDIVIDUAL BANKING		INSTITUTIONAL RELATIONSHIPS		INVESTMENT BANKING		OTHER		TOTAL CITICORP	
	1985	1984	1985	1984	1985	1984	1985	1984	1985	1984
Previous Basis	$298	$212	$733	$742	$160	$153	$(191)	$(217)	$998	$890
Effect of:										
Business Reorganization	38	36	(345)	(265)	307	229	—	—	—	—
Credit Loss Provision Reallocation	42	6	61	30	—	—	(103)	(36)	—	—
Tax Expense Reallocation	(30)	(27)	(44)	(41)	(42)	(39)	116	107	—	—
Other	(6)	(5)	(13)	(12)	—	—	19	17	—	—
REVISED CORE BUSINESS NET INCOME (MANAGEMENT BASIS)*	$340	$222	$392	$454	$425	$343	$(159)	$(129)	$998	$890
INVESTMENT BANK NET INCOME ATTRIBUTABLE TO INSTITUTIONAL RELATIONSHIPS**			$363	$289						
TOTAL INSTITUTIONAL RELATIONSHIP NET INCOME			$755	$743						

*If the Corporate allowance for possible credit losses is allocated to reflect core business results in conformity with generally accepted accounting principles, Individual Banking and Institutional Banking would reflect incremental provisions of $85 million and $141 million for 1985, respectively, and $12 million and $40 million for 1984 respectively, bringing the ratio of allowance to loans for these businesses respectively to 85% and 1.37% for 1985 and .75% and 1.01% for 1984.

**The $363 million for 1985 and $289 million for 1984 is that part of the total Investment Banking net income of $425 million for 1985 and $343 million for 1984 which is attributable to products and services which are delivered to Institutional Relationships.

SECTOR EARNINGS AND OTHER ITEMS

IN MILLIONS OF DOLLARS	1985	1984
SECTOR EARNINGS	**$1,157**	$1,019
Corporate Items (after tax)		
Credit Loss Provision	(103)	(36)
Corporate Staff Costs	(67)	(76)
Other Including Start-up Activities	11	(17)
Total Corporate Items	$ (159)	$ (129)
TOTAL CITICORP	$ 998	$ 890
EARNINGS PER SHARE	$ 7.11	$ 6.36

CUSTOMER RELATIONSHIPS

IN MILLIONS OF DOLLARS	1985	1984
Individual Relationships	$340	$222
Institutional Relationships	755	743
Market Trading & Other Activities	62	54
Other Items	(159)	(129)
TOTAL CITICORP	$998	$890

GEOGRAPHIC DISTRIBUTION

IN MILLION OF DOLLARS	1985		1984	
North America	$463	46%	$367	41%
Caribbean, Central & South America	245	25	177	20
Europe, Middle East & Africa	191	19	208	23
Asia/Pacific	99	10	138	16
TOTAL CITICORP	$998	100%	$890	100%

INDIVIDUAL BANK

SECTOR PERFORMANCE

IN MILLIONS OF DOLLARS	1985	1984	VAR.	%
Customer Net Revenue	$4,120	$3,107	$1,013	33
Expenses:				
Credit Cycle Expense	989	586	403	69
Delivery Expense	2,625	2,149	476	22
Total Expenses	$3,614	$2,735	$ 879	32
Other Income (Expense)	102	(12)	114	—
Income Before Taxes	608	360	248	69
NET INCOME	$ 340	$ 222	$ 118	53
Average Assets ($ Billions)[1]	53	44	11	25
Return on Assets (%)	.61	.51	.10	—
Return on Equity (%)	15.3	12.7	2.6	—

(1) Year to date average

The sector performance summary presents Individual Banking results in a format using terms closely related to the Individual Banking business. Customer net revenue embraces all net revenue primarily generated through customer relationships. Credit cycle expense includes credit write-offs, the portion of the provision for possible credit losses allocated to the sector in excess of write-offs, fraud losses, and the expense associated with credit appraisal and the process of collecting past-due or written-off accounts. Delivery expense includes all non-credit related costs of delivering our products and services to the consumer. Other income (expense) primarily includes interest costs of carrying non-customer assets, affiliate earnings, and earnings on allocated equity.

AVERAGE BALANCE SHEET

IN BILLIONS OF DOLLARS	DECEMBER 1985[2]
Assets	
Revolving Loans	$12.3
Shelter Loans	25.7
Student Loans	1.7
Other Loans[3]	15.6
Other Assets	6.2
	$61.5
Liabilities	
Transaction Account Deposits[4]	$ 8.0
Savings Deposits	45.8
Other (Includes Allocated Equity)	7.7
	$61.5

(2) Average balances for the month of December
(3) Principally includes lending to high net worth individuals and auto loans
(4) Includes demand deposits, travelers check and money order outstandings

The Individual Bank is committed to satisfying the broadest range of financial service needs of consumers in the United States and 32 other countries around the world. While the services we can offer are sometimes limited by local regulatory constraints, our intent is that they include banking, insurance, and investment products sold both individually and in convenient, consumer-oriented packages.

During the past year, our strategic direction was enhanced by a reorganization that incorporated our worldwide high net worth banking activities with our other consumer efforts. With the inclusion of these initiatives, we can now pursue activities against the entire worldwide consumer marketplace and offer our customers a range of more sophisticated asset management products.

We recognize that, ultimately, our success will be directly attributable to our ability to offer our consumers worldwide preeminent service for each of their relationships with us. Our view is that by pursuing service excellence across all of our efforts, we enhance our standing with our customers and thereby the likelihood that they will choose us for a growing share of their financial needs.

By the end of 1985, the Individual Bank had total customer assets of $55.3 billion, up 30% versus the prior year, and total deposits of $53.8 billion, up 18% versus the prior year. In the United States, we are the largest issuer of bank credit cards, the largest marketer of student loans (over $1.7 billion), and the largest servicer of mortgages. We do business with 16.6 million households in the United States and another 6.2 million abroad.

From a number of perspectives, 1985 was a noteworthy year for the Individual Bank. We earned $340 million, up $118 million, or 53%, from 1984—an accomplishment made more meaningful by the fact that our effort first became profitable only three years ago. Our earnings growth is directly attributable to our customer revenue momentum, up $1,013 million or 33% versus a year ago. As the table below indicates, this revenue momentum is broadly based across our domestic and international activities and suggests that we are building market share in most of our activities.

Customer Net Revenue Trends

MILLIONS OF DOLLARS	1985	INCREASE/ (DECREASE) 1984	
Domestic			
Net Interest Revenue	$1,980	$ 606	44%
Non Interest Revenue	970	234	32
TOTAL	$2,950	$ 840	40%
International			
Net Interest Revenue	$ 812	$ 116	17%
Non-Interest Revenue	358	57	19
TOTAL	$1,170	$ 173	17%
Individual Bank			
Net Interest Revenue	$2,792	$ 722	35%
Non-Interest Revenue	1,328	291	28
TOTAL	$4,120	$1,013	33%

While our earnings momentum is heartening, we continue to view ourselves as having our major opportunities ahead of us and have therefore directed attention to improving our competitive position across both product and geographic spectrums, even where this

"In the Individual Bank, while our current momentum is encouraging, we continue to view ourselves as a business of the future with our major potential ahead of us."

required substantial investment. As a result, our delivery expenses increased to $2,625 million worldwide, up $476 million, or 22%. Approximately two thirds of this increase is estimated to have been spent supporting the revenue momentum of our basic businesses, while the remainder represents investments in new marketing or infrastructure activities, or in programs that had little revenue impact in 1985 but are judged to be critical in the long term.

Domestically, we continue to pursue our market opportunity in two distinct directions: the expansion of individual products, such as credit cards and mortgages, on a nationwide basis, and the selective building of branch-based distribution systems in attractive markets that will allow the delivery of a full array of services to our customer bases.

The product emphasis was again paced by the steady expansion of our card businesses. By year-end, we had approximately 17.5 million cardmember accounts across the United States, up more than 3 million from 1984. Other dimensions of our card business also increased considerably during the year, including purchase sales, up 45%, and card member outstandings, up 54%. Primarily as a result of this activity, we estimate that we now do business with 16.6 million, or approximately one in five U.S. households, a penetration level that is growing more than 30% per year.

We also are developing into a major factor in the nationwide mortgage business. We sourced $7.5 billion in new mortgage volume during the year and continued to build our mortgage servicing capability, which we believe to be the largest in the industry. To enhance further our product and relationship orientation, we introduced a variety of new options such as the Citi-One packaged account (in New York) and continued to expand and experiment with the Citibank Financial Account, Focus, Direct Access (home banking), and the Equity Source Account.

The other aspect of our domestic business thrust, full-service banking, was again frustrated by inactivity in Washington, D.C. and y[illegible] eral opportunities arose on a state-by-state basis. We announced an agreement to acquire Great Western Bank & Trust in Arizona, giving us a 36-branch presence in the second fastest-growing state in the country. We received full banking privileges in Maryland, and bought an S&L in Nevada. We made steady progress managing the S&L's we own in California, Illinois, and Florida and had a banner year in terms of our New York branch system, where we again built share and achieved record profits that had a material impact on our overall results. At year-end, we were evaluating opportunities in several other states across the country.

Given our substantial business growth in the United States, we have taken steps to improve the operations infrastructure supporting our customers. As our card businesses, particularly bankcards, continued to expand, we completed our second processing center and broke ground for our third. The former is located in The Lakes, Nevada, where we now employ over 500 people; the latter is under construction in Hagerstown, Maryland. Employment at our Sioux Falls, South Dakota premises has exceeded 2,000. Each of these facilities is a state-of-the-art center where we believe we deliver considerable efficiencies vis-a-vis the industry and highly effective service for our customers. We have also entered into an agreement allowing our customers access to shared ATM distribution networks nationwide—

approximately 15,000 terminals by year-end, probably the largest domestic shared network capability of any financial services company.

Internationally we expanded our presence in a number of marketplaces during 1985 while maintaining returns well in excess of corporate standards. During the year, we completed significant acquisitions in Italy (Banca Centro Sud), Belgium (Banque Sud Belge), and Chile (Corporacion Financiera Atlas) and also entered the consumer business in Colombia, Guam, and India, bringing our total presence to 32 countries. In addition, we continued product introductions in many of our local marketplaces, including such new entries as mutual funds (Citinvest) in Brazil, indirect auto financing in Spain, and a new mortgage program and life insurance in Germany, while expanding Citifunds, a multi-product money management account, to several markets. We view our opportunities in the international marketplace as substantial, not only because our share tends to be relatively small in most places, but also because we have the opportunity to apply lessons learned from market to market and to expand attractive and proven product packages like those mentioned above.

Our results for the year are not without some disappointments. Our businesses were under heavy credit pressure during 1985 and, in fact, our loan losses more than doubled from 1984. While the uneven economic recovery had some impact on these results, a large portion was due to our aggressive bankcard solicitations, which attracted over 3 million new accounts for the second year in a row, but exposed us to added pressures because new accounts have credit losses approximately three times the ongoing average. In our view, this is a cost of expansion that is justifiable in terms of the business we are building. We also note that our returns to the shareholder on several of our domestic businesses, while progressing, remain below corporate hurdles and, as a result, our overall domestic returns are below those standards despite the fact that many of our initiatives, most importantly bankcards and the New York branch system, are now performing above them.

As mentioned earlier, despite the growing profitability of our efforts, we still perceive we are building a business that will be a growing contributor to the Corporation over time. We evaluate our progress against this objective strategically both in terms of such indicators as household penetration, relationship depth, and revenue momentum, and also in terms of the potential of the various business thrusts we are pursuing. While we have already proven we can generate substantial profits from bankcards and the New York branch system, we see a variety of initiatives that have the potential for greatly enhanced contribution over time. These include our domestic mortgage activities, various insurance related activities generally as a result of the cross sell of insurance products to our customer bases, continued progress in turning our S&L's into important local competitors, our high net worth banking activities both domestically and worldwide, and our amalgam of individual business activities in each of our three international regions.

By the end of 1985, our Individual Banking activities included more than 54,000 dedicated people worldwide. With a broad base of activities and a commitment to progress against both market segments and geographic opportunities, we have begun to fulfill the Corporation's commitment to becoming the preeminent consumer financial services corporation in the world. We believe we have the strategic direction, the marketplace momentum, the people, and the resources to continue to develop this position in future years.

Richard B. Bradbock

RICHARD B. BRADDOCK

INSTITUTIONAL RELATIONSHIPS

SECTOR PERFORMANCE

IN MILLIONS OF DOLLARS	1985	1984	VAR	%
Total Revenue	$3,771	$3,291	$480	15
Provision for Possible Credit Losses	374	213	161	76
Operating Expenses	2,016	1,705	311	18
Income Before Taxes	1,381	1,373	8	1
NET INCOME	$ 755	$ 743	$ 12	2
Average Assets ($ Billions)[1]	91	88	3	3
Return on Assets (%)	0.83	0.85	(0.02)	—
Return on Equity (%)	20.9	21.2	(0.3)	—

(1) Year to Date average

NET INCOME BY PRODUCT

IN MILLIONS OF DOLLARS	1985
Core Lending	$205
Debt Products/Money Market Services	172
Foreign Exchange Services	112
Specialized Finance	101
Liquidity Insurance, Financial Guarantees & Asset Intermediation	66
Advisory, Trade, Transaction Processing & Other	99
TOTAL INSTITUTIONAL RELATIONSHIPS	$755

AVERAGE BALANCE SHEET

IN BILLIONS OF DOLLARS — DECEMBER 1985[1]

Assets		Liabilities	
Loans & Leases	$59.2	Interest Bearing Deposits	$37.9
Deposits at Interest with Banks	11.3	Non-Interest Bearing Deposits	8.4
Acceptances	8.0	Other Borrowed Money	18.6
Other	12.9	Acceptances	8.0
		Other (primarily interco)[2]	18.3
	$91.4		$91.4

(1) Average balances for month of December
(2) Includes allocated equity

INSTITUTIONAL RELATIONSHIP PRODUCTS

Core Lending. Net income in this product family reflects our more traditional lending activities, e.g. working capital loans, long-term financing and syndicated lending to corporations, governments and financial institutions.

Debt Products/Money Market Services. Citicorp assists corporations and financial institutions in raising short-term funds through note issuance facilities, commercial paper and interbank money market instruments. We also provide a variety of risk management products such as interest rate swaps, futures, forwards, and options that protect customers against interest rate volatility. Citicorp also may take positions within pre-approved limits that result in a mismatch of interest rate maturities.

Foreign Exchange Services. Citicorp is the world's largest foreign exchange dealer. We obtain currency for our customers whose business, investment or fund raising activities reach beyond national boundaries. We also help customers hedge their currency exposure through swaps, FX options and forward rate contracts. Citicorp may also take positions within pre-approved guidelines in anticipation of changes in currency markets.

Specialized Finance. Specialized Finance is the generic term for our non-traditional lending, for example, Asset-Based Lending, Corporate Asset Funding and Equipment Finance. Activities include the wholesale purchase of all or part of a company's portfolio of financial asset[illegible]quipment related secured lending and lease options to end users; leveraged leasing, tax leasing and vendor finance to assist the manufacturers or sellers of capital equipment.

Liquidity Insurance, Financial Guarantees and Asset Intermediation. Included in this category are fees generated on loan commitments outstanding, earnings from guaranteeing performance by another party; and income from asset intermediation activities such as asset sales, brokering and direct placements.

Advisory, Trade, Transaction Processing, and Other. Citicorp is a leading manager in the US of pension funds for corporations, state and local governments, and non profit organizations. We have merger and acquisition specialists in 15 countries to assist companies in finding buyers or sellers, and in structuring these complex transactions. Trade includes direct financing of trade related transactions; countertrade and transaction processing such as documentary collections. Also included in this category are our Cash Management, Information businesses, and earnings on allocated equity.

In 1985, Citicorp's relationships with corporations, financial institutions, and governments continued to produce bottom-line results exceeding our corporate target for return on equity. Earnings growth, however, did not take place. Institutional Relationships' after-tax profits were $755 million, up just 2% from last year.

Growth is the primary challenge of Institutional Banking. Earnings have been essentially in the $725-750 million range for four years in a row. While much has been done to lay the foundation for future earnings, the investments made have not yet produced enough in the way of results to offset the challenges of today's difficult credit-quality environment. In 1985, for example, Institutional Banking had net loan write-offs of $377 million. Because of the size of these amounts, even the 15% increase in revenue was unable to bring about significant earnings growth over 1984.

Nevertheless, we are very optimistic the flat earnings profile is going to change substantially over the coming year and in the ones to follow. Our belief is founded on a fairly straightforward premise. We offer the best and broadest range of institutional banking services in the world, we are in every significant market; and yet, we have very small market shares. In essence, we have no situation where we even approach market saturation.

Close to 60% of our earnings come from the United States, Canada, Europe, and Japan. In the US and Canada alone, our earnings have grown at an annual average rate of 15% over the last five years, and we continue to see enormous opportunities ahead of us. Growth in this market has come from a wide variety of new sources, so much so that traditional lending now accounts for less than half of our profits. Furthermore, we have become a clear market leader. In virtually all surveys of North American-based businesses, Citicorp leads both in market share and measurements of customer satisfaction. Nevertheless, because of the huge size of the North American market, we still have only a small share of the total business. For example, there are approximately 3,000 companies in the US. with sales in the $250 million plus range. These companies represent about half of the total corporate banking business in the country. Yet, although Citicorp is the biggest corporate bank in the nation, we only do business with approximately one half of the 3,000 companies. Hence, we believe we have lots of room to grow in what is the world's biggest and most stable business market.

A similar situation exists in many other economies around the world. It is not unusual for Citicorp to be the largest international bank in a given location. Yet, our share of most of the institutional banking markets around the world is extremely small. Accordingly, we have significant growth potential virtually everywhere we choose to place the resources to achieve it.

Growth will come from many sources. In 1985, for example, many illustrative initiatives were implemented:

- We opened additional offices in the United Kingdom, Germany, Italy, Portugal, the People's Republic of China, Sweden, and several other countries.
- We received a full banking license in Australia.
- We became a "clearing bank" in the United Kingdom.
- We increased the contribution of "local currency" activities to earnings in Latin America to a point where more than a third of profits now comes from non-US. dollar business.

Interestingly, growth is coming not only from increasing the number of clients with whom we do business, but also from what we do for

"While the world economy has clearly not solved all its problems, we believe we are close to getting Institutional Banking growing again."

them. Our mix of business activity is now much more diverse than it was years ago. For example:

- Earnings from Investment Banking services used by Institutional Banking customers now represent one of our most significant areas of growth. This was simply not the case five to ten years ago. Today, Citicorp's Investment Banking activities place us not only on top of the lists of the world's most important foreign exchange traders, but also, we figure very prominently in the rankings of those who provide interest rate and currency swaps, options, merger and acquisition services, financial restructurings, and lease syndications.
- We have come to be regarded as the worldwide leader in electronically delivered banking services to the institutional market. We have more than 10,000 customers using these services. In the U.S. alone, we established a single division just to do this type of business.
- We started a joint venture with McGraw-Hill to provide the first integrated global electronic trading, information, and financial services marketplace for petroleum, petroleum products, and petrochemicals.
- We expanded our aircraft leasing services by acquiring an aviation spare parts business.
- We established presences of Citicorp International Trading Company in 15 locations around the world.

As is the case with the potential for growth in the number of customers, there is significant potential in the growth of service usage by existing and future customers. In the vast majority of cases, customers use only a small percentage of the services we offer. If each customer simply used one more of our services in 1986, we might well produce the largest rate of growth in Citicorp's 174 years of participation in the institutional banking market. In essence, even if we didn't add new customers, we would have substantial growth possibilities from gaining broader service usage by existing customers.

For just that reason, a major step taken in 1985 was the re-establishment of Citicorp's World Corporation Group. Back in 1973, Citicorp pioneered the concept of managing the corporate banking relationships of large multinational customers on a closely coordinated global basis. The approach was extremely successful. After seven years, however, new priorities prevailed, and the World Corporation Group was absorbed by other organizational entities. The management system applied to multinational relationships was kept in place, but the organization was decentralized. In retrospect, we probably shouldn't have decentralized this aspect of our business as much as we did. Our experience over the last five years has shown that the complexity of meeting the sophisticated requirements of the world's largest global corporations does, in fact, require very close-in relationship management. Fortunately, we have remained on the top of all the competitive market surveys in the multinational segment. Our commitment to growth, however, convinced us our original approach was better than the existing one, so we went back to what worked best. We are quite certain this change will bring about very positive results in a reasonably short period of time.

In the end, however, the crucial variable in Institutional Banking is the quality of the loan portfolio. Revenues are sizable—$3.8 billion.

But even with revenue growth rates well in excess of inflation, and reasonable control of operating costs, nothing is more important than making sure Citicorp's $58 billion commercial loan portfolio is managed with the highest degree of professionalism. We believe we are doing quite well in that regard...not as well as we would like to, but quite well. No other financial institution in the world earns as much from institutional banking as Citicorp, and no other financial institution has as broadly diversified a portfolio of corporate, government, and financial institution financings as Citicorp. As a result, even with the challenges faced by market segments such as energy, high technology, and shipping, we have still been able to produce significant returns. However, conservative management of our loan portfolio has caused us to take enough in the way of credit write-offs so as to inhibit earnings growth.

We believe this will change due to a number of measures taken over the last few years to improve upon the already strong processes for credit quality control which have existed in Citicorp for a long time. The Institutional Bank now has a proportionately larger number of experienced lending officers than ever before in its history. The degree of intensity applied to the scrutiny of our internal audit program results is greater than ever before. And the number of highly skilled market segment specialists is at record levels. The improvements have already produced results. As an example, in 1985, earnings from our domestic energy, asset-based finance, and real estate departments, in spite of significant difficulties in those particular marketplaces, more than met our corporate rate of return targets. In the case of domestic asset-based finance and real estate, 1985 was a record year.

Finally, one cannot talk about Institutional Banking without mentioning the challenges implicit in the process of working with countries that are restructuring their foreign currency debts. This activity is so significant, we devote an entire segment of this report to it. (See page 18) It's clear very meaningful progress has been made, but a great deal of hard work still lies ahead. What has been shown is that as long as representatives of the affected countries and financial institutions work together in a cooperative fashion, as has been the case, the probability of continued and steady improvement will be high.

Institutional Banking is Citicorp's oldest business. From the time of our founding back in 1812, we have been regarded as a key player in the financial picture of major institutions around the world. In view of our significant size, it is quite improbable that we could have escaped reflecting some of the stresses and strains the world's business community has felt over the last few years. Our results have shown that Institutional Banking remains quite profitable even while passing through such periods. Nevertheless, the strains have resulted in flat earnings. While the world economy has clearly not solved all its problems, we believe we are close to getting Institutional Banking growing again. First and foremost, we have been conservative in our handling of customer credit and the recognition of write-offs. Second, we have plenty of room to grow, both in customers and in the products and services we deliver to them. Third, hundreds of millions of dollars have been invested in technology, human resource development, product innovation, and business expansion over the last five years. These investments are now starting to yield substantial results.

LAWRENCE M. SMALL

Since the international debt crisis began in August 1982, we have seen gradual improvement, overall, in the situation year by year. Nineteen eighty-five was no exception.

The first year or two were characterized by emergency rescue packages, negotiated by the debtor countries and their commercial banks under considerable pressure. These packages consisted of the rescheduling of loans maturing in the immediate future and some new bank lending to tide the countries over as they began to adjust their economies.

During that phase, all creditor banks were expected to contribute their share of the new loans in proportion to their existing exposure, in a process referred to, somewhat inaccurately, as involuntary lending.

In 1985 we began a second phase, that of multiyear restructuring packages for those countries that had made progress in their economic adjustment programs. These restructuring packages, which cover three or more years of maturities, postpone principal repayments until the countries' economies are growing again to the point where their debt is manageable.

By year-end, Ecuador, Mexico, and Yugoslavia had signed multiyear restructuring agreements, with several more to follow in early 1986 including Venezuela, the Dominican Republic, and Uruguay, and with others reaching the negotiating stage.

Such progress has been possible because some of the countries are making economic recoveries.

For example, of the three largest, Brazil, despite continuing problems with inflation, had a trade surplus in 1985 of $12.5 billion, one of the world's largest and close to the 1984 record of $13.1 billion. Foreign cash reserves now exceed $9 billion, compared to $7.5 billion at year-end 1984 and negative reserves at year-end 1983. In 1985, the Brazilian economy grew by close to 8%, again one of the highest rates in the world.

On the other hand, Mexico, which began an initially successful adjustment program in late 1982, had a disappointing economic performance in 1985, exacerbated by the devastation of earthquakes. The sharp drop in oil prices, if sustained over time, will reduce foreign currency earnings for Mexico. Of even greater concern is the need for the country to improve the internal investment environment in order to reverse capital flows. After announcing an ambitious austerity budget for 1986, Mexico initiated discussions with the International Monetary Fund for a new standby agreement.

Argentina has made considerable progress since introducing its Austral economic program last June. Inflation, which was 31% in June, has ranged from 1.9% to 3.2% in recent months. In November, the government completely eliminated all public-sector interest arrearages for the first time in over three years.

Overall, countries with debt-servicing problems recently were growing at about 3% a year. Their current-account deficits were down to under 2% of gross domestic product, which is better than many countries whose creditworthiness has remained unquestioned. Furthermore, many of the debtor countries, including all the major ones, by year-end were current in public-sector interest payments to creditor banks.

As a result, in late 1985, we saw the first signs of a third phase in the effort—the gradual return of some countries to the voluntary credit markets, which is the goal we have been working toward. In the years ahead it will enable these countries to roll over their external debt in the markets, as they did before the crisis began, while raising the additional capital they will need to continue their economic development.

Last September, Uruguay and its Bank Advisory Committee reached agreement on a multiyear restructuring transaction and, parallel to it, on the first voluntary loan by commercial banks to any Latin America country since the crisis began. This loan is a $45 mil-

lion co-financing with the World Bank for an energy project. The voluntary nature of this loan is illustrated by the participation by banks that had made no previous loans to Uruguay.

The special case of Colombia gives us another preview of phase three. Although Colombia never missed an interest or principal payment, it nevertheless encountered the same reluctance in the marketplace as nations that had. Last year, with a unique monitoring arrangement with the International Monetary Fund, Colombia completed a $1 billion syndication, mainly for export-related oil and coal projects. Such lending is designed to support the structural adjustment of a country's economy.

Last October, U.S. Treasury Secretary James A. Baker III announced the Baker Initiative, a proposal that builds on the accomplishments to date. Under the proposal, the developing countries would commit to greater structural adjustment than in the past, the multilateral development banks would lend $20 billion net over the next three years, and the commercial banks would provide approximately $20 billion in net new loans over the same period. The lending would be on a case-by-case basis, tied to each country's progress in attaining non-inflationary growth.

Implicit in the Baker Initiative is a commitment by the industrialized nations to policies similar to those asked of the developing countries. The goals of these policies include lower inflation, which should lead to lower interest rates, and sustained growth, which along with continued access to world export markets would enable debtor countries to further build their foreign-exchange resources.

We at Citibank endorse the Baker Initiative as an important step toward the free flow of investment funds, and the international banking community generally has expressed similar support. As we move ahead in our cooperative efforts, we expect to see more countries re-enter the markets for project finance; co-financing by the commercial banks with the World Bank and regional development banks; bond issues, increasingly in currencies other than the U.S. dollar; and more trade finance. Some existing debt will be converted to equity.

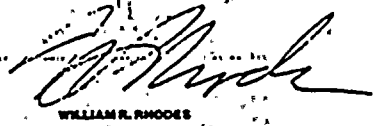
To attract the capital they need, the developing countries must adopt policies to remove structural inefficiencies and reduce capital flight, so that domestic savings become a far greater source of their development funds. They must encourage more private direct investment from both domestic and foreign sources, which would stimulate growth and reduce dependence on foreign borrowings. Both points are part of the Baker Initiative, and some countries already are taking steps in this direction.

As before, there are many potential problems as we move ahead. The direction of interest rates, oil prices, commodity prices, and exchange rates are all important factors, as is the threat of protectionism.

One crucial question is whether the industrialized world can maintain the steady, non-inflationary growth it has enjoyed over the past few years. Citibank's economists predict that growth in the industrialized nations will average over 3% in 1986, which would maintain demand for developing-country exports.

A second crucial question is whether the developing countries have the political will to continue the steps necessary to return their economies to health. In Latin America, many countries are undertaking economic adjustment during one of the region's most significant political transformations in generations, with widespread movement from military government to democracy. Argentina is an example of a newly elected government taking strong measures to resolve its economic problems.

Although there are bound to be setbacks ahead, as there have been in the past, we believe that a number of countries have made, and will continue to make, real progress toward regaining their creditworthiness.



WILLIAM R. RHODES

INTERNATIONAL FINANCING ACTIVITIES

Like all of Citicorp's activities, international financing involves the management of risk. Whenever Citicorp lends, places, or invests funds across a national border or in a currency that is "foreign" to the borrower, it incurs a transfer and/or convertibility risk, commonly referred to as "country" risk. This risk arises because a country may impose exchange controls that may prevent Citicorp's customer, at least temporarily, from obtaining and/or transferring the foreign exchange needed to service its obligation to Citicorp in full and/or on time, even though the customer remains at all times creditworthy in terms of local currency. If this situation persists for more than 90 days, Citicorp must place the affected assets on a cash basis, and this has an adverse impact on earnings. Interest previously accrued must be deducted from current earnings, and current earnings are further reduced by the cost of carrying the cash basis loans, net of interest actually received in cash.

Citicorp manages country risk by evaluating the economic climate and prospects for individual countries and by imposing limits on total cross-border and foreign currency amounts that may be lent within each country. At the end of 1985 approximately $48 billion of Citicorp's assets were cross-border and foreign currency outstandings and therefore exposed to country risk. This figure represents a slight decline from the level prevailing at the end of 1984. However, relative to assets and capital, Citicorp's total cross-border exposure has fallen sharply.

Total cross-border exposure at year-end 1985 was divided among industrial countries ($24.3 billion), non-oil developing countries ($18.5 billion), oil exporting developing countries ($3.3 billion), and offshore banking centers ($2 billion). In no single country did cross-border and foreign currency outstandings account for more than 5% of Citicorp's total assets. Citicorp's largest exposure ($5.8 billion, or 3%, of total assets) was to Japan, which is, after the United States, the largest economy in the world. Citicorp's exposure to other countries was lower. There are seven countries in which outstandings were between 1% and 3% of total assets and three countries where outstandings were between 0.75% and 1% of total assets.

Since 1982 a number of countries have found it necessary to refinance their external debt. Citicorp has cross-border and foreign currency outstandings to 31 such refinancing countries, amounting to $15.0 billion at the end of 1985. This level is slightly higher than at year-end 1984 and significantly lower relative to Citicorp's total assets and capital. Cash basis loans in the refinancing countries declined to $1.1 billion from $1.6 billion at year-end 1984. Consequently, the earnings drag of $62 million caused by cash basis loans in the refinancing countries in 1984 turned into an earnings benefit of $30 million in 1985, when Argentina, Venezuela, and other countries paid both previously due and currently due interest on cash basis loans. A summary of developments in the major refinancing countries follows.

While no absolute assurance can be given, Citicorp management believes that these developments will not ultimately have a material adverse effect on Citicorp's financial condition.

CROSS-BORDER AND FOREIGN CURRENCY OUTSTANDINGS
Adjusted For Net Local Currency Outstandings, External Guarantees and Collateral[1]

IN BILLIONS OF DOLLARS AT YEAR-END	1985	1984	1983
Industrial Countries	$24.3	$25.4	$24.3
Centrally Planned Economies of Eastern Europe	.2	.2	.2
Oil Exporting Developing Countries	3.3	3.7	3.9
Non-Oil Developing Countries	18.5	19.0	19.3
Offshore Banking Centers	2.0	1.9	2.5
TOTAL	$48.3	$50.2	$50.1

(1) Outstandings are presented on a regulatory basis and include all loans, deposits at interest with banks, acceptances, other interest-bearing investments, and other monetary assets. Adjustments are made to include the excess of local currency outstandings over local currency liabilities, if any, for each country included in a category and to allow for external guarantees and collateral.

MEXICO

The government of Mexico and the participating international banks have signed agreements to implement the previously reported restructuring of medium-term maturities. Through these agreements, which affect $48.7 billion of Mexican public-sector debt, certain amounts that would have matured through 1990 have been rescheduled through 1998. All of these agreements should become effective by the end of the first quarter of 1986.

Citicorp's share of the restructuring is approximately $1.4 billion, none of which is accounted for on a cash basis or reported as renegotiated loans. The weighted-average rate margins for Citicorp's share of these loans are as follows:

WEIGHTED AVERAGE RATE MARGIN

IN MILLIONS OF DOLLARS	BEFORE RESTRUCTURING	AFTER RESTRUCTURING
$ 199	2.125% over prime	1.125% over prime
497	0.772% over various reference rates, including prime and LIBOR	Initially 0.875% over LIBOR or a comparable domestic reference rate[1][2]
673	1.75% over prime	Initially 0.875% over LIBOR or a comparable domestic reference rate[1][2]
$1,369		

(1) Rate margins are 0.875% as shown for the period 1985-1986, 1.125% for the period 1987-1991 and 1.250% for the period 1992-1998.
(2) At December 31, 1985, prime exceeded LIBOR by approximately 1.5%.

In addition, the 13-member Bank Advisory Group, of which Citibank, N.A. is a member, has endorsed a Mexican request to defer, for 180 days, $950 million of principal payments that had been due in the fourth quarter of 1985 under a previous financing.

Mexico is reassessing its 1986 financial plan in the context of the recent oil price decline. Mexico has indicated that its discussions with the IMF and World Bank continue in order to obtain the support of these institutions for its 1986 program.

During 1985, Citicorp's additional cross-border advances to Mexican public-sector borrowers were approximately $43 million, and approximately $28 million of principal was repaid. Interest on Mexican public-sector outstandings included in income for the

year amounted to $166 million, and such interest received in cash amounted to $190 million.

BRAZIL

Discussions with Brazilian officials to reschedule and extend 1985 and 1986 maturities of public and private-sector debt, including maintenance of trade and interbank facilities, continue.

During 1985, cross-border outstandings in Brazil were affected by additions of approximately $69 million and reductions of approximately $213 million, primarily composed of principal payments of $160 million. Approximately $597 million of gross interest revenue was earned on cross-border and foreign currency outstandings, and approximately $657 million was collected in cash.

ARGENTINA

Based on IMF support for Argentina's new economic program, the participating international banks have executed agreements with Argentina providing for the following:

- A new $3.7 billion, 10-year term credit, with principal payments beginning after three years and interest at LIBOR plus 1⅞% or prime plus 1¼%.
- A new $500 million, four-year trade credit and deposit facility at LIBOR plus 1⅜% or prime plus 1%.

Banks have also agreed to commit for one year to a trade credit maintenance facility and a money market facility. In addition, substantial progress has been made in the execution and implementation of agreements for refinancing $9.9 billion of public-sector maturities and $3.5 billion of private sector debt. The public-sector refinancing matures from 1982 to 1985 and provides for tenors of up to 12 years. The private-sector refinancing covers 1984 and 1985 maturities plus certain 1982 and 1983 maturities not previously covered and provides for tenors of 10 years.

Citicorp is participating in the new lending in an amount approximating $226 million, and its share of the public and private-sector refinancing, detailed in the accompanying table, amounts to $387 million. Citicorp's commitments under the trade credit maintenance facility and money market facility are $95 million and $156 million, respectively.

Argentina received the first disbursement of new money in the amount of $2.2 billion on September 30, 1985. At that time, Argentina paid approximately $800 million of interest to creditor banks, bringing public-sector interest current through September 1, 1985, and repaid the remaining principal balance of $750 million on the 1982 bridge loan outstanding to commercial banks. The second disbursement of new money, amounting to $800 million, was made on November 26, 1985, at which time all public-sector interest was brought current. During the fourth quarter, approximately $266 million of Citicorp's Argentine debt was returned to full accrual status, of which $159 million related to the public sector. In January 1986, a scheduled drawdown under the IMF standby was not made, pending completion of discussions and the reaching of an agreement between the IMF and Argentina with respect to Argentine compliance with certain IMF performance criteria. Final disbursements by the banks will be delayed until IMF drawdowns resume.

The government of Argentina has advised the international banking community that it intends to begin discussions with the Argentine bank advisory committee in March with respect to a 1986 financing program. Pending completion of those discussions, the government has requested that banks roll over all principal maturities of Argentine public sector and private sector indebtedness falling due during the period, January 1, 1986 through April 30, 1986 for 90-day and 180-day periods, respectively.

During 1985, Citicorp's cross-border advances to Argentina were increased by additions of $335 million. Approximately $126 million in principal was repaid. Interest on cross-border outstandings in Argentina included in income was $221 million, and $211 million of interest on such outstandings was received in cash. Of the cash received, $65 million represented interest on cash basis loans for years prior to 1985.

VENEZUELA

An agreement in principle has been reached for the restructuring of $21.2 billion of Venezuelan public-sector debt. The restructuring covers principal payments maturing through 1983 and provides for the rescheduling of these maturities over 12 years with quarterly payments ending in 1997. A $750 million principal payment will be made upon the effective date. Discussions regarding the availability of foreign exchange for private-sector debt servicing are nearing completion.

As detailed in the accompanying table, Citicorp's share of the public-sector restructuring is $709 million, none of which is accounted for on a cash basis or reported as renegotiated loans. No Venezuelan

DATA ON ARGENTINA AND VENEZUELA AGREEMENTS IN PRINCIPLE

		Weighted average rate margin		Interest revenue for 1985 — pro forma as if on accrual basis of accounting		
In millions of dollars	Amount	Before restructuring	After restructuring	As reported	Based on rates before restructuring	Based on rates after restructuring
Argentina						
Public sector	$122	1.759% over LIBOR	1.375% over LIBOR	$20	$16	$15
Private sector	265	2.431% over LIBOR	1.375% over LIBOR	52	34	31
TOTAL	$387			$72	$50	$46
Venezuela						
Public sector	$709	2.27% over reference rates including LIBOR and prime	1.125% over LIBOR or other domestic reference rate	$76	$76	$69

public-sector outstandings were removed from the cash basis of accounting as a result of the restructuring negotiations.

During 1985, no cross-border advances to Venezuelan public-sector borrowers were made, and approximately $17 million of principal was repaid. Interest on Venezuelan public-sector outstandings included in income for the year amounted to $83 million, and $88 million of interest on such outstandings was received in cash. Of the cash received, less than $1 million represented interest on cash basis loans for years prior to 1985.

PHILIPPINES

In the Philippines, Citibank and other banks have signed an agreement that provides for a new $925 million, 9-year term loan and have committed to maintain approximately $2.9 billion of short-term trade credit facilities through 1986. In addition, the Philippine government and the 12-member Bank Advisory Committee for the Philippines have agreed in principle to reschedule approximately $5.8 billion of existing bank debt, and the IMF has agreed to provide a standby credit. The availability of funds under the standby credit is subject to compliance with IMF targets and conditionalities.

Citicorp's share of the new term loan is approximately $126 million, and its commitment under the trade credit facilities is approximately $751 million. The rescheduling of existing bank debt will involve approximately $3.1 billion of Citicorp's Philippine outstandings.

CROSS-BORDER AND FOREIGN CURRENCY OUTSTANDINGS
In Countries With Outstandings Exceeding ¾% of Total Assets Adjusted For Net Local Currency Outstandings, External Guarantees, and Collateral

	1985						1984	1983
	CROSS-BORDER AND FOREIGN CURRENCY OUTSTANDINGS[1]							
In billions of dollars at year end	Banks	Public sector	Private sector	Total	Adjustments[2]	Total adjusted outstandings[3]	Total adjusted outstandings	Total adjusted outstandings
Japan	$2.7	$ .1	$1.6	$4.4	$1.4	$5.8	$7.6	$6.8
Brazil	.6	2.7	1.1	4.4	.3	4.7	4.9	4.7
United Kingdom	1.1	—	1.5	2.6	1.0	3.6	3.4	3.8
Canada	.8	—	1.0	1.8	1.0	2.8	2.9	2.1
Mexico	.4	1.7	.8	2.9	(.1)	2.8	2.9	2.9
Federal Republic of Germany	.6	—	.7	1.3	1.1	2.4	1.7	2.3
Australia	—	—	.3	1.3	.5	1.8	1.6	1.6
Philippines	.1	1.0	.4	1.5	.3	1.8	1.6	1.6
France	.9	.1	.3	1.3	.2	1.5	2.0	1.7
Argentina	.4	.5	.6	1.5	(.1)	1.4	1.2	1.2
Korea	.3	.1	.7	1.1	.3	1.4	1.4	1.8
Venezuela[4]	.3	.5	.5	1.3	(.1)	1.2	1.3	1.5
Greece[4]	.1	.1	.9	1.1	—	1.1	1.1	1.2
Hong Kong[4]	.2	—	.4	.6	(.1)	.5	.7	1.1

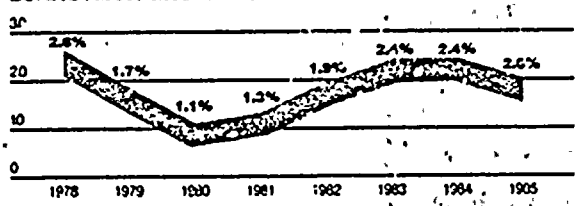
(1) Outstandings are presented on a regulatory basis and include all loans, deposits at interest with banks, acceptances, other interest-bearing investments, and other monetary assets.
(2) Amounts primarily represent excess of local currency outstandings over local currency liabilities, if any. Additional adjustments are made to assign ultimately guaranteed outstandings and outstandings for which tangible liquid collateral is held outside of the borrower's country to the country of the guarantor and the country in which the collateral is held, respectively.
(3) Legally binding cross-border and foreign currency commitments, including irrevocable letters of credit and commitments to extend credit, after adjustments to assign ultimately guaranteed commitments to the country of the guarantor amounted to $5 billion in Australia, $6 billion in Canada, $5 billion in the Federal Republic of Germany, $13 billion in France, $6 billion in Japan, $5 billion in Korea, and $16 billion in the United Kingdom at December 31, 1985. Commitments were not material in relation to adjusted outstandings in any other country in this table.
(4) Less than ¾% of total assets at December 31, 1985.
(5) Less than ¾% of total assets at December 31, 1985 and 1984.

CASH BASIS AND RENEGOTIATED COMMERCIAL LOANS

Cash basis (nonaccrual) loans are those on which, as a result of doubt as to collection, income is recognized only to the extent cash is received. Renegotiated loans are those on which the rate of interest has been reduced as a result of the borrower's inability to meet the original terms.

The classification of loans as cash basis and renegotiated is a specialized diagnostic tool used by financial institutions. Citicorp's experience, as well as the experience of others, generally has shown

CASH BASIS AND RENEGOTIATED COMMERCIAL LOANS AS A PERCENTAGE OF TOTAL LOANS



that a substantial percentage of cash basis and renegotiated loans are ultimately collected.

Citicorp's policy of placing loans on cash basis status embraces all loans on which principal or interest is 90 days past due, or when payment of interest or principal is determined to be doubtful of collection. Even if a cash payment may be anticipated, accrued interest is reversed and the loan is put on cash basis status after a 90-day period has elapsed.

Cash basis and renegotiated commercial loans at year-end 1985 were $2.2 billion, down $170 million from a year ago, compared with a $308 million increase in 1984 over year-end 1983. The 1985 decrease primarily reflects reduced cash basis loans in the domestic real estate and overseas sectors of the loan portfolio. Cash basis and renegotiated loans as a percentage of total loan volume declined from 2.4% in 1984 to 2.0% in 1985. The percentage was 2.4% at December 31, 1983. Cash basis lease financings were $35 million at December 31, 1985 and $64 million at December 31, 1984.

Included in overseas cash basis loans are a number of loans in countries that are currently in the process of refinancing their external debt or that have completed such refinancings. In view of investor interest in this aspect of Citicorp's activities, the accompanying table provides additional details of cross-border and foreign currency outstandings and also local and foreign currency cash basis loans in the affected countries; the third column of the table shows the impact on our earnings, spread among various countries. The amounts include interest reversed when loans are placed on a cash basis, plus the cost of carrying the cash basis loans, reduced by interest received in cash and included in income.

DETAILS OF REFINANCING COUNTRIES

	Adjusted Total Cross Border and Foreign Currency Outstandings	Cash Basis Loans[1]	Estimated Impact of Cash Basis Loans on Earnings
	Billions	Millions	Millions
Argentina	$ 1.4	$ 116	$35
Brazil	4.7	99	(11)
Chile	.5	13	—
Dominican Republic	.1	10	—
Ecuador	.4	14	(1)
Jamaica	.1	—	—
Mexico	2.8	52	(2)
Morocco	.1	10	—
Nigeria	.1	1	—
Panama	.2	2	—
Peru	.1	47	(1)
Philippines	1.8	182	(6)
Poland	.1	101	3
South Africa	.7	4	—
Uruguay	.3	3	—
Venezuela	1.2	295	10
Yugoslavia	.2	—	—
All Other[2]	.2	117	3
TOTAL	$15.0	$1,066	$30

(1) Includes both local and foreign currency loans
(2) 14 countries under $50 million of Cross-Border Outstandings: Bolivia, Costa Rica, Honduras, Ivory Coast, Liberia, Malagasy, Malawi, Mozambique, Nicaragua, Senegal, Sudan, Togo, Zaire, Zambia

CASH BASIS AND RENEGOTIATED COMMERCIAL LOANS

In Millions of Dollars	1985 Cash Basis Loans	1985 Renegotiated Loans	1985 Total	1984	1983	1982	Total 1981
Cash Basis and Renegotiated Loans							
In Domestic Offices							
Real Estate Loans	$ 89	$12	$ 101	$ 233	$ 127	$ 107	$ 111
Other Commercial Loans	384	8	392	302	345	444	350
In Overseas Offices	1,729	26	1,755	1,883	1,638	1,111	575
TOTAL CASH BASIS AND RENEGOTIATED LOANS	$2,202	$46	$2,248	$2,418	$2,110	$1,662	$1,036
Cash Basis and Renegotiated Loans as a % of Commercial Loans			3.9%	4.1%	3.5%	2.7%	1.8%
Cash Basis and Renegotiated Loans as a % of Total Loans			2.0%	2.4%	2.4%	1.9%	1.3%

Real estate acquired in settlement of loans, included in other assets in the financial statements, totaled $250 million at December 31, 1985, up $64 million from $186 million at December 31, 1984. Domestic real estate represented $202 million of the total real estate at year-end, and overseas real estate accounted for $48 million. Approximately $59 million of the $64 million total increase was classified as domestic.

(For further analysis see Commercial Loan Portfolio Risk Analysis on page 31).

INVESTMENT BANK

SECTOR PERFORMANCE

IN MILLIONS OF DOLLARS	1985	1984	VAR	%
Total Revenue	$1,589	$1,241	$348	28
Operating Expenses	803	587	216	37
Income Before Taxes	786	654	132	20
NET INCOME	$ 425	$ 343	$ 82	24
Average Assets ($ Billions)[1]	32	26	6	23
Return on Assets (%)	1.34	1.33	0.01	—
Return on Equity (%)	33.5	33.2	0.3	—

(1) Year-to-Date average

NET INCOME BY PRODUCT

IN MILLIONS OF DOLLARS	1985
Debt Products/Money Market Services	$255
Equity Products	18
Foreign Exchange Services	138
Advisory Products	25
Other	(11)
TOTAL INVESTMENT BANKING	$425

AVERAGE BALANCE SHEET

IN BILLIONS OF DOLLARS — DECEMBER 1985[2]

Assets		Liabilities	
Deposits at Interest with Banks	$11.7	Interest-Bearing Deposits	$19.4
Investment Securities	5.8	Securities Sold Under Agreements to Repurchase	7.5
Trading Account Assets	4.9	Other Borrowed Money	15.6
Securities Purchased Under Agreements to Resell	6.3	Other[3]	4.9
Other (primarily interco)	18.7		
	$47.4		$47.4

(2) Average balances for month of December.
(3) Includes allocated equity.

INVESTMENT BANK PRODUCTS

Debt Products/Money Market Services. Citicorp is one of the top three dealers in U.S. government securities, which is the largest and most liquid debt market in the world. This past year we became a primary dealer in the U.K. government securities market. We also underwrite, trade, and distribute securities for municipal governments in the U.S. and for many sovereign governments.

We assist corporations and financial institutions in raising short-term funds through note issuance facilities, commercial paper, and interbank money market instruments. We arrange long-term financing through private placements, mortgage-backed securities, and bonds issued outside the United States. We are market-makers and distributors of a wide variety of debt instruments worldwide. Citicorp may also take positions within pre-approved limits that result in a mismatch of interest rate maturities.

Equity Products. For new and emerging businesses, Citicorp has established venture capital companies in the U.S., Canada, U.K., Italy, France, Germany, and Australia. We have stock brokerage businesses in Japan, Hong Kong, Singapore, the United Kingdom, and Australia. Our discount brokerage subsidiary, Newbridge Securities, is a member firm of the New York Stock Exchange.

Foreign Exchange Services. Citicorp is the world's largest foreign exchange dealer. We provide foreign exchange services for our customers whose business, investment, or fund raising activities reach beyond national boundaries. We help customers hedge their interest rate and currency exposure through a variety of risk management products—such as interest rate and foreign exchange swaps, futures, forwards, and options.

In the course of market-making activities in foreign exchange markets, we may also take positions within pre-approved guidelines in anticipation of changes in currency markets.

Advisory Products. Citicorp is a leading manager in the U.S. of pension funds for corporations, state and local governments, and non-profit organizations. We also provide global perspective with offices in major markets worldwide and internationally-diversified portfolios managed out of both London and Zurich. We have merger and acquisition specialists in 15 countries who assist companies in finding buyers or sellers, and in structuring these complex transactions.

The Investment Bank also provides investors a broad array of trust, custodial, and portfolio services, including American Depository Receipts which facilitate U.S. investment in overseas securities.

The Investment Bank, at the end of 1985, had become a different organization than it was at the start of the year. In September, Citicorp merged its treasury business, both foreign exchange and money market activities, with the Investment Bank's securities activities. The new organization accounted for $425 million in earnings in 1985.

We are not limiting our aspirations to the historic definitions of investment banking. For one thing, Glass-Steagall restrictions affect us only in corporate debt and equity underwriting in the U.S. In world markets, we are permitted to raise funds for both U.S. and international customers. We are a leading dealer and distributor of United States government securities, and we provide a broad range of securities and securities-related products for our customers everywhere. For us, investment banking is defined only by our customers' needs and our own imagination in finding ways to meet these needs.

Citicorp is doing well in investment banking. Our 1985 earnings place us in the very top tier of investment banks worldwide. As we look to the future, it becomes clear that Citicorp has strengths that few of our competitors can easily match.

OUR STRENGTHS

While we tend to take Citicorp's 93-country global network for granted, it's unique among investment banks. And as customers and potential customers look increasingly beyond their national boundaries to meet their funding and investment needs, this global reach—which has already made us the clear leader in foreign exchange and the dominant force in interest rate and currency swaps—makes us the envy of competitors. We've only begun to apply the leverage of this network.

Citicorp's unparalleled customer base is another unique strength for the Investment Bank. We have long standing, continuing, and close relationships with tens of thousands of the more important corporations, governments, financial institutions, and investors. Increasingly, these customers are looking for securities or securities-related products, and Citicorp, which in the past offered them traditional banking products, is well positioned to provide new investment banking products and services.

We have always taken pride in Citicorp's innovative spirit. While intangible, this strength has held us in good stead over the years. We're given credit for inventing both the swap and the Euronote—two of today's most prominent investment banking products. By creating new ways to meet our customers' needs, we earn better margins and we stay at the leading edge of the rapidly changing investment banking business.

Product innovation depends on technological innovation, and Citicorp has a well-earned reputation for its commitment to technology. This is a springboard for the Investment Bank. In 1985, we spent approximately $50 million on new systems and technology, and we

"At Citicorp, investment banking is defined only by our customers' needs and our own imagination in finding ways to meet these needs."

plan to spend $60 million in 1986. Better technology enables us to fully capitalize on our global presence, brings us into closer contact with our customers, and enables us to act faster and more surely in the worldwide capital markets. We want to be number one in the effective use of technology on a global scale.

OUR STRATEGY

When you have significant strengths—like our global reach and customer base—strategy becomes straightforward: You play from those strengths. This means working more closely with Institutional Bank relationship managers to deliver investment banking products to customers. In essence, the Investment Bank will concentrate on R&D and production, and the Institutional Bank will handle marketing and delivery. Teamwork will be a top priority both within the Investment Bank and throughout Citicorp.

The integration with Treasury will enable us to capitalize on a number of possible synergies, like the close relationship between our foreign exchange business and our interest rate and currency risk management products. And Treasury's funding activities for Citicorp give us an expertise in market and timing that can be put to good use for customers.

Focus on the investor continues to be a critical part of our strategy. Our goal is to become the preeminent distribution network for both global reserve currency and key country capital market paper. Investors are the ultimate customers in investment banking. They buy the securities—or the exchange, interest rate contracts, or whatever. When we serve investors we also serve issuers, because we gain the placing power essential to fulfilling their financial needs. More potential buyers also means more continuous profits in our trading and positioning activities. As in most businesses, the firm with the marketing advantage enjoys the superior margins.

OUR SUCCESSES

The best way to implement strategy is to build on successes. The Investment Bank recorded a number of achievements in 1985:

- We maintained our strong market position as one of the top three dealers in U.S. government securities.
- We were far and away the world's leading foreign exchange dealer. This business contributed approximately $340 million in revenues in 1985.

■ In Tokyo, our affiliate Vickers da Costa Ltd. traded $25 billion in debt securities and expanded significantly its equity brokerage franchise by becoming one of the first six foreign firms to gain a seat on the Tokyo Stock Exchange.

■ In Europe we acquired major stockbroking businesses in the U.K. and Ireland, became a primary dealer in the U.K. government securities market, and started securities businesses in Denmark, Italy and Luxembourg.

■ In the U.S., we launched Newbridge Securities, a discount brokerage and member firm of the New York Stock Exchange. Newbridge provides support to the discount brokerage activities of the Individual Bank and executes orders for other Citicorp units around the world.

■ We acquired AMBAC, an insurance company that is a market leader in the fast-growing area of financial guarantees. AMBAC is a natural extension of our municipal finance business.

■ We increased our market share in municipal securities underwriting, where we were the top lead manager in short-term issues. Fee income from our public finance business increased by 59%.

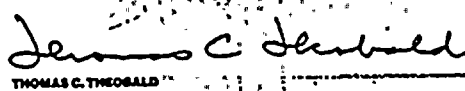
■ Our earnings from merger and acquisition fees increased dramatically. We now have M&A specialists in 15 countries around the world, and the number of transactions in which we played a role would rank us among the top 12 investment banks worldwide.

■ Citicorp Venture Capital Ltd., our venture capital and special transaction vehicle, had a record year, making $90 million in new investments. £100 million was placed in a fund for venture capital and restructuring investments in the U.K. Similar businesses are being started in continental Europe, Latin America, and Asia.

■ In the burgeoning Eurocommercial paper market, we continued to be the market leader in Euronotes.

■ In numerous national markets outside the U.S., we are market makers in government issues, underwriters of corporate securities, and managers and distributors of mutual funds. These activities are well represented in Asia, Latin America, and Europe.

We look for increasing success in investment banking. We are where we are today, and our future is very bright, because of Citicorp's many skilled and resourceful people around the globe. They are our fundamental continuing strength.



THOMAS C. THEOBALD

"In 1985 we expanded our franchises around the world, into new states, new countries, and new businesses; the change will continue steadily in the future."

In 1985 Citicorp continued to expand its business franchises around the world. Our commercial or institutional banking activities having been widely established for many years, recent expansion has taken place mostly in our individual and investment banking businesses.

In the United States, where restrictive legislation and regulation has been a significant limiting factor, expansion has been slower, but nevertheless continual and gratifying. Abroad, where regulation is more liberal (terms like Glass-Steagall and the McFadden Act don't seem to translate well into other languages), expansion is moving apace.

Overseas in 1985, we acquired Banca Centro Sud, based in Naples, Italy. Its 43 branches will constitute a significant expansion of our banking presence in Italy.

In Belgium we acquired the Banque Sud Belge, with a 50-branch network, thus supplementing our already widespread Fambank distribution system in that country.

Australia changed its laws to give banking licenses to foreign banks and by year-end we had undertaken full commercial banking activities in all six major cities on that continent.

In Latin America we acquired a consumer finance company in Chile and took other initiatives consistent with our plan to grow local currency businesses and moderate the growth of our cross-border exposure in those countries.

We obtained a full banking license in Sweden, which now gives us a commercial banking presence in all of the Scandinavian countries.

We opened Citibank Budapest. In recent years such banking as we did with Hungary was handled out of our Vienna office. This new subsidiary will let us move this business closer to its origin.

We initiated steps in 1985 to acquire British National Life Assurance Company, a life insurance underwriter and distributor based in the United Kingdom. The acquisition was completed early in 1986.

Our Investment Bank grew substantially last year in the more liberal overseas regulatory environment.

We strengthened its presence in London, the heart of international financing. It brought our ownership of the Scrimgeour Kemp-Gee brokerage firm up to the legal limit of 29%, and in April 1986, when this limit is dropped, our ownership will become 100%. It linked Scrimgeour with the London activities of Vickers da Costa, a brokerage firm we acquired in 1984, which has a strong presence in the Far East. When British laws allowed, we acquired Seccombe Marshall & Campion PLC, a brokerage specializing in government securities and money market trading, which Britain has designated a Primary Dealer in these securities. These acquisitions, which strengthened our position in sterling and yen trading, when combined with our London Eurodollar activities, round out our already significant U.K. presence.

We also acquired J&E Davy, a large stockbroker in the Republic of Ireland, and together with a local firm set up the Clarke-Vickers brokerage in Australia.

In Japan, we obtained a trust company license enabling us to access that country's vast investment management market, and our Vickers da Costa subsidiary was among the first to be approved for a Japanese stock exchange seat.

All this progress overseas is based largely on the fact that it is usually easier to open or expand a banking presence in another country than it is to open or acquire one in another state in the United States.

In the United States, Congress has substantially slowed its efforts to further banking deregulation. Bringing the nation's 50-year old banking laws up-to-date enjoyed considerable attention and progress for several years, but in 1985 the attention of Congress was seized by issues that it perceived, understandably, as more urgent: the Federal deficit, tax reform legislation, foreign competition, and problems in agriculture and energy. Congress in effect put bank deregulation on the back burner—where, realistically speaking, it is likely to remain during 1986.

That, however, doesn't signal a recess of our efforts. While not giving up on Congress, we turned more to the judicial, regulatory agency, and state legislative avenues.

Our tilt at the Supreme Court windmill dashed our hope for one-stroke national expansion. The Court upheld that, contrary to our position, it is constitutional for states to let banks within a limited region cross state lines, while locking out banks outside that region. At the same time, together with other excluded banks, we were trying to get Congress to pass "trigger" legislation, which would let us enter the protected regions after five years even if the states themselves did not permit us to do so. A bill was reported out by the Banking Committee, but after the Supreme Court decision, the bill did not make it through the Rules Committee.

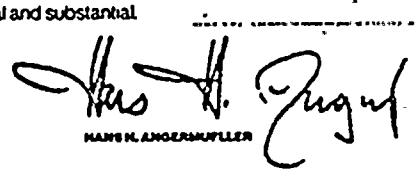
In our state-by-state efforts we were successful in opening a bank in Nevada and persuaded the Maryland legislature to let us open a multi branch full commercial bank there in mid-1986. Arizona passed legislation that permitted us to acquire a bank there in 1986. Michigan, Ohio, and Washington passed bills in 1985 that contain triggers that will permit Citicorp to enter within reasonable periods.

Our regulatory agency efforts also produced important results. They enabled us to acquire more than 80% of AMBAC, the country's oldest credit insurer of municipal bonds, marking a major breakthrough into an exciting new way of conducting our business. We also extended Citicorp insurance brokerage activities into five new countries.

We made our first substantial foray into the information business—another of our strategic goals—through a joint venture with McGraw-Hill. Marrying McGraw Hill's information on commodities with Citicorp's financial communications network, we now can bring together buyers and sellers of commodities and enable them to trade directly with each other, with Citicorp available to provide ancillary financial services to complete the transactions.

These insurance and information beachheads promise to provide the starting point for major lines of business we hope to enter over time.

As we look ahead, we see the era of dramatic expansion, with Congressional hearings on TV and in the news headlines, is evolving into a process of gradual, piece-by-piece, state-by-state, project-by-project expansion, as technology, institutionalization of savings, and development of new financial instruments proceed. The next few years will add up to a change in banking activities that may not be explosive, sudden, or dramatic, but in its own gradual and steady way will be fundamental and substantial.



HANS H. ANGERMUELLER

RISK MANAGEMENT

Risk taking is inherent to the business of a financial institution. Effective management of risk is critical to the success and long-term profitability of any financial institution. At Citicorp, the concept of risk management is embodied in all aspects of our operations and subject to continual review. New risk management techniques continue to evolve in response to changes in environment and the nature of Citicorp's own businesses.

Traditionally, risk management in banking focused on credit, liquidity and operations. However, as the range of Citicorp's activities and geographic diversity have changed, so have the nature and scope of the risks. Today Citicorp is a multinational financial services company that faces a broad range of risks as it delivers competitive services to its customers. Key areas of risk that must be managed are credit, liquidity, interest rate, foreign exchange, sovereign and cross-border, trading, business and environmental, legal and regulatory, and operations. Selected areas are discussed in detail later in this section.

Key to Citicorp's approach in managing risk is clear, sound management policies and their effective communication to all levels of the Corporation. Primary among those policies is diversification. Citicorp's management philosophy has always stressed the importance of assets, liabilities, earnings, and related risks being diversified in terms of geography, currency, customer, product, and tenor. This diversification, referred to as the actuarial base, hedges against the adverse impact to the institution from any one event or set of conditions.

Decentralization is a cornerstone of Citicorp's strategy. Decision-making is placed as close as possible to the marketplaces we serve to ensure that decisions are based on the best available information and on a close understanding of changes that could affect us.

Diversification and decentralization are balanced by strong financial and operating controls. These include highly formalized credit and operating policies and procedures, developed over a long period of time. Appropriate limits are established for liquidity, interest rate gaps, foreign exchange, and trading exposure for all units of the organization and are monitored for adherence. Similarly, sovereign risk and cross-border risks are also subject to a formal review process by senior management. Documented operational procedures that specify levels of approval authority, separation of duties, and other sound practices are required for all businesses.

In addition, Citicorp adheres to conservative accounting policies, particularly to recognize expenses like write-offs at the earliest moment. Aggressive identification of write-offs and well-developed procedures for managing problem credits lead to a higher probability of principal recovery.

In support of its strict controls and procedures, Citicorp has a strong independent review process, with an internal audit staff that exceeds 600. Further examination is provided by continual reviews by external auditors and by regulatory bodies around the world.

These financial and operating controls are supported by a major investment in information systems that supply timely and accurate information to all levels of management. This upward flow of information serves as a key measure for the effectiveness of management policies.

Finally, Citicorp continues to believe that strong and growing earnings, in conjunction with a large capital base, provide the ability to absorb unforeseen risks or losses.

The following sections discuss risk management as it relates to the commercial and consumer loan portfolios, liquidity and interest rate management, and capital management. Elsewhere in this annual report discussions may be found concerning risk management as it relates to sovereign and cross-border exposure (page 18), accounting policies (page 55), and non-funds related financial products (page 66).

COMMERCIAL LOAN PORTFOLIO RISK ANALYSIS

Citicorp's management philosophy has always emphasized the importance of assets and earnings being diversified in terms of geography, currency, customer, tenor and product. This diversification, referred to as the actuarial base, hedges against the adverse impact to the institution from any one event or set of conditions. History has shown that adverse developments affecting individual countries or industries or particular products tend to be cancelled out by favorable developments in other activities in the long run. Citicorp utilizes this strategy of broad diversification in its loan portfolio management in order to better control the amount of unpredictable losses. For example, no single country outside the United States has accounted for more than 8% of the total commercial loan portfolio in the last five years. However, banks are in the business of measured risk-taking, and losses are part of the normal cost of lending money. In commercial lending, the amount of losses as a percentage of outstanding loans can vary widely from period to period, and is particularly sensitive to fluctuations caused by changing economic conditions. The percentage of loan losses to average loans reached a post-war peak of .83% in 1975 due primarily to the 1973-1975 recession in the U.S. which particularly impacted the real estate industry. The loss percentage steadily improved in the 1975-1980 period, paralleling the progress of economic recovery in the wake of the past recession. As the pace of economic growth slowed, the percentage rose to .32% in 1982 and .39% in 1983 and reached .65% in 1985. These percentages are well below the 1975 high. Looking ahead over the next 12 to 18 months we expect our loss experience will remain within the range experienced in the past five years. Citicorp emphasizes a well-diversified and healthy earnings stream as the primary means of absorbing recurring loan losses. Accordingly, Citicorp immediately recognizes as losses all loan amounts judged to be uncollectible. Over time a significant portion of these losses are recovered. Historical experience indicates that certain losses exist in the portfolio at a point in time but have not been specifically identified. In anticipation of these unidentified losses, the allowance for possible credit losses is established by charging current earnings with amounts over and above actual net loan losses. No portion of the resulting allowance is specifically allocated or restricted to any individual loan, or groups of loans or geographic areas, and the entire allowance is available to absorb losses from any and all loans and lease financing receivables. In order to assess the risk characteristics of the loan portfolio at year-end 1985, Citicorp believes it is appropriate to view the portfolio according to the elements shown in the accompanying table.

COMMERCIAL LOAN PORTFOLIO, NET OF UNEARNED DISCOUNT

		1985			1984		
MILLIONS OF DOLLARS	LOANS AT DECEMBER 31, 1985	AVERAGE LOANS	NET LOAN LOSSES (RECOVERIES)	LOSSES TO AVERAGE LOANS	AVERAGE LOANS	NET LOAN LOSSES (RECOVERIES)	LOSSES TO AVERAGE LOANS
Commercial and Industrial Loans[1]							
In Domestic Offices	$13,403	$12,827	$ 59	.5%	$13,766	$ 58	.4%
In Overseas Offices[2]	25,472	27,929	249	.9%	27,671	116	.4%
TOTAL	$38,875	$40,756	$308	.8%	$41,437	$174	.4%
Loans to Financial Institutions[3]							
In Domestic Offices	$ 1,342	$ 604	$ —	—	$ 1,189	$ —	—
In Overseas Offices[2]	5,318	4,733	19	.4%	4,377	9	.2%
TOTAL	$ 6,660	$ 5,337	$ 19	.4%	$ 5,566	$ 9	.2%
Real Estate Loans[1]							
In Domestic Offices	$ 6,114	$ 5,300	$ —	—	$ 4,331	$ (1)	—
In Overseas Offices	2,125	1,995	14	.7%	1,809	(1)	—
TOTAL	$ 8,239	$ 7,295	$ 14	.2%	$ 6,140	$ (2)	—
Loans to Governments and Official Institutions[3][4]	$ 4,398	$ 4,695	$ 36	.8%	$ 4,884	$ 40	.8%
TOTAL COMMERCIAL LOANS	$58,172	$58,083	$377	.7%	$58,027	$221	.4%

(1) Includes loans not otherwise separately categorized.
(2) Loan classifications are based on Comptroller of the Currency definitions.
(3) Substantially all in overseas offices.
(4) Loans to government owned enterprises and banks which are not included in direct loans to governments and official institutions are included in commercial and industrial loans and loans to financial institutions, respectively.

COMMERCIAL AND INDUSTRIAL LOANS

Citicorp's commercial and industrial loan portfolio is broadly diversified in terms of industry, geography and size of customer. None of the major industry segments in Citicorp's commercial and industrial lending portfolio accounts for more than 10% of the total commercial loan portfolio, and 35% of this category is to major multinational corporations. This diversification has proven to be a successful factor in controlling risk. The weakness of the worldwide economy in certain industry sectors contributed to an increase in the net loan loss ratio to .8% in 1985, with higher losses overseas. In the past five years, commercial and industrial loan loss experience has ranged between .2% and .8%. Net losses on commercial lending can vary widely from period to period, particularly within any given narrowly defined sector. While loan losses in commercial and industrial lending cannot be accurately predicted, Citicorp expects that over the next 12 to 18 months its loan losses will remain within the range experienced in the last five years.

LOANS TO FINANCIAL INSTITUTIONS

Loans extended to correspondent banks and other financial institutions in the U.S. and overseas averaged $5.3 billion, or approximately 9% of Citicorp's portfolio.

Borrowers in this category tend to be of better-than-average creditworthiness, reflected by the losses to average loans of 0.4%.

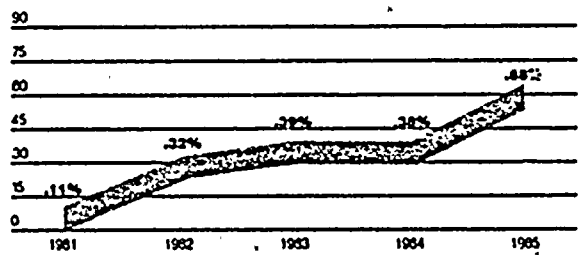
1985 losses recorded in the financial institutions category overseas continue to be affected by foreign currency availability considerations representing a protracted inability of a country to service foreign currency debt and the lack of definitive prospects for the resumption of orderly debt servicing. This is particularly so where foreign currency borrowing by a country is channeled through a financial institution borrower. Citicorp anticipates, however, eventually collecting all or part of these loans, although such write-offs are expected to continue.

Loss experience from the financial institutions borrowers, excluding such write-offs based on foreign currency debt servicing considerations, continues below that for commercial and industrial lending, and this trend is expected to continue over the next 12 to 18 months.

REAL ESTATE LOANS

Despite difficult conditions in the global real estate markets, the real estate portfolio performed well within institutional and industry standards. No significant change is expected over the next 12 to 18 months.

PERCENT OF COMMERCIAL LOAN LOSSES TO AVERAGE LOANS



NET LOAN LOSSES, IN MILLIONS OF DOLLARS

$60	$192	$341	$221	$377

AVERAGE LOANS, NET OF UNEARNED DISCOUNT, IN MILLIONS OF DOLLARS

$54,967	$56,810	$60,581	$62,027	$66,083

LOANS TO GOVERNMENT AND OFFICIAL INSTITUTIONS

International lending to governments and official institutions is a continuing part of Citicorp's worldwide activities. Outstanding loans to governments and official institutions averaged $4.7 billion during 1985 and were approximately 8% of the average commercial loan portfolio.

Losses recorded in this category largely represent certain instances where portions of loans were written off based on a protracted inability to service foreign currency debt and a lack of definitive prospects for the resumption of orderly debt servicing.

During the next 12 to 18 months, Citicorp expects the net loss ratio in this category to remain above that for commercial and industrial loans. However, excluding those instances of write-offs based on foreign currency debt servicing considerations, Citicorp expects any losses to be well below those in commercial and industrial lending.

CONSUMER LOAN PORTFOLIO ANALYSIS

The profit dynamics of consumer lending are such that each product has an expected level of credit loss, which is generally a statistically predictable expense of doing business. For example, loans with low loss experience include home mortgage loans (first and second) and government-guaranteed student loans. Loans with medium loan loss experience are secured products, such as mobile home loans and automobile loans. Included in the category of high loan loss experience are such unsecured products as credit cards, travel and entertainment cards, and other personal revolving credit products. Pricing and marketing policies reflect the loss experience of each particular product.

Citicorp follows a write-off policy that requires that most consumer loans, with the exception of adequately secured consumer mortgages, be written off when payments are delinquent by a predetermined number of days after the contractual payment date. The number of days is set at a level appropriate to loan product and environmental characteristics so as to result in the recognition of losses that makes the likelihood of subsequent recovery of those losses fall between 20% to 30%. Those loans not yet written-off and with principal or interest payment delinquencies of 90 days or more comprised 155% of the total year-end 1985 consumer loan portfolio, a decrease from the comparable 1984 ratio of 159%. The policy for suspending accruals of interest on consumer loans varies depending on the terms, security and loan loss experience characteristics of each product and in consideration of write-off criteria in place. Consumer loans for which accruals of interest had been suspended were $502 million at year-end 1985. Foregone interest revenue resulting from suspension of interest accruals was not material in 1985. Consumer loans with delinquencies of 90 days or more for which interest continued to be accrued were $415 million at year-end 1985.

The worldwide consumer loan portfolio showed strong growth in 1985, with the average loan portfolio increasing by $110 billion, or 30%, to $477 billion. This is principally due to the continuing domestic growth in credit cards and shelter-related mortgage products.

The worldwide revolving credit portfolio, which has a high loan loss experience, grew from 19% to 23% of the total portfolio in 1985. Home mortgage loans (first and second), which have a low loan loss experience, decreased from 45% to 44% of the worldwide portfolio. International consumer loans now account for 15%, down from 17% last year.

Losses as a percentage of average loans were up substantially from .78% in 1984 to 1.23% in 1985, driven primarily by two factors: the increased volume of credit card receivables, which historically have a higher loss experience, and the somewhat higher-than-anticipated loss rates of certain medium and high loss experience loans.

In 1985, Citicorp added approximately 3 million cards to its credit card base. The cost of this successful solicitation includes the relatively higher loss rates that credit cards experience during their early years. The combination of greater volume plus the high early-year loss rates resulted in credit loss expenses that were considerably higher than 1984.

DOMESTIC PORTFOLIO

The average domestic loan portfolio increased by $99 billion to $405 billion. Growth occurred in each category of consumer credit loss expense experience.

	1985 AVERAGE LOANS IN BILLIONS	1985 NET LOSSES IN MILLIONS	1985 LOAN LOSS RATIO	1984 LOAN LOSS RATIO
Credit loss expense experience:				
Higher	$11.3	$430	3.8	2.5
Medium	8.7	91	1.0	0.6
Lower	20.5	10	0.1	0.1
TOTAL	$40.5	$531	1.3	0.8

The relative year-to-year comparisons in the portfolio are shown in the following table:

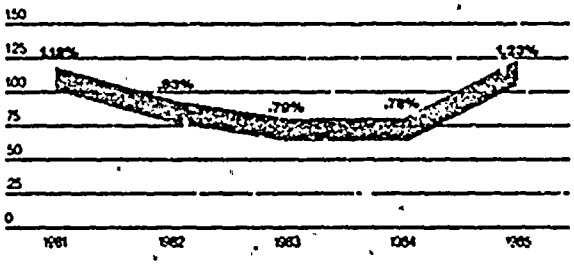
PERCENT OF AVERAGE LOANS	1985	1984	1983
Higher	28	24	25
Medium	22	23	25
Lower	50	53	50
TOTAL	100	100	100

INTERNATIONAL PORTFOLIO

The average international portfolio volume rose from $61 billion to $72 billion, principally due to a combination of new acquisitions and growth of base business. The portfolio remains concentrated in the major industrial nations of Europe and Asia.

	EUROPE		ASIA/ PACIFIC			LATIN AMERICA	
	AVERAGE LOANS IN BILLIONS	%		AVERAGE LOANS IN MILLIONS	%	AVERAGE LOANS IN BILLIONS	%
Germar.,	$2.2	31	Australia	$0.6	8	Puerto Rico $0.6	8
UK.	1.2	17	Hong Kong	0.6	8	Other	0.3	5
Other	1.0	13	Other	0.7	10			
TOTAL	$4.4	61	TOTAL	$1.9	26	TOTAL	$0.9	13

PERCENT OF CONSUMER LOAN LOSSES TO AVERAGE LOANS



NET LOAN LOSSES, IN MILLIONS OF DOLLARS				
$196	$184	$196	$286	$585

AVERAGE LOANS, NET OF UNEARNED DISCOUNT, IN MILLIONS OF DOLLARS				
$16,708	$20,783	$24,923	$36,755	$47,737

CAPITAL ANALYSIS

During 1985, Citicorp significantly increased its total and primary capital through internal equity generation, increases in the allowance for possible credit losses, and the issuance of a new form of perpetual preferred stock. Total capital, as defined by the regulators, was $15.9 billion at December 31, 1985, up $4.1 billion, or 35%, over last year. Primary capital, as defined by the regulators, was $10.9 billion, up $2.0 billion, or 23%, from 1984. Citicorp's total capital ratio at December 31, 1985 was 9.12%, up 1.33% from the prior year's ratio of 7.79%. The comparable primary capital ratio was 6.23%, up from 5.86% in 1984. Both ratios are well above the regulator's minimum requirements of 6.00% for total capital and 5.50% for primary capital. The capital ratios of each of Citicorp's domestic subsidiary banks and savings and loan associations were also above the regulatory minimums.

LIQUIDITY AND INTEREST RATE MANAGEMENT

Citicorp defines adequate liquidity as having the funds available to repay fully and promptly all maturing liabilities or customer deposits in accordance with their terms. The nature of the financial intermediation function performed by banks and bank holding companies is such that they are minimally able to meet their immediate financial obligations with readily marketable assets, assets payable on demand and assets scheduled to mature. The extent of liquidity risk can be measured by the difference in maturity dates of assets and liabilities (including those assets and liabilities payable on demand). There is also a risk to earnings from exposure to interest rate fluctuations. Interest rate risk results from a mismatch of repricing dates between assets and liabilities, and may also be affected by non funds related interest rate products, discussed further on pages 66 and 67. Liquidity and interest rate risk are not identical since repricing and maturity dates frequently differ. However, containing both exposures within acceptable risk limits over the short term is accomplished primarily by liability management. This requires continuous attention to the maturity and repricing structure of assets and liabilities.

For a large multinational financial intermediary, successful liability management is characterized by a broad diversification of funding sources. Extensive diversification of market, currency, lender, maturity, repricing frequency, and liability instrument enhances liquidity. The ability to react quickly to changing market conditions for liability products is essential. Citicorp has continued to develop new funding sources and to maintain acceptable levels of liquidity.

In 1985, Citicorp raised a dollar equivalent total of $5.9 billion of funds with a maturity of one year or longer, including $1.0 billion with final maturities of 20 years or longer.

TERM FUNDS RAISED IN 1985

IN MILLIONS OF DOLLARS	FIXED RATE	FLOATING RATE	TOTAL
US Market	$2,061	$1,233	$3,294
Overseas Markets	998	1,564	2,562
TOTAL	$3,059	$2,797	$5,856

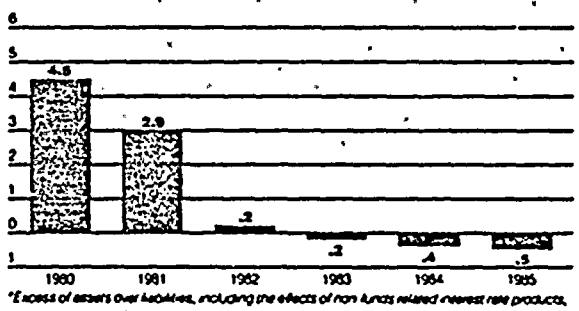
This fund raising program lengthened the average maturity of Citicorp's liability structure and improved liquidity.

In general, the long-term funds raised and preferred stock issued in 1985 had interest rate repricing characteristics closely related to the incremental assets being financed. This reflects Citicorp's active management of risk associated with mismatches in the repricing dates of assets and liabilities. As the accompanying chart shows, Citicorp's long-term U.S. dollar interest rate exposure remained very modest. This is consistent with management's strategy of confining interest rate exposure to the shorter term. Among other actions, Citicorp executed interest rate swap agreements for its own account in a continuing effort to manage institutional interest rate risk. The long-term interest rate exposure in currencies other than U.S. dollars is nominal and closely monitored on a monthly basis.

Recent deregulation within the United States has enabled Citicorp to offer the consumer a growing variety of products. Over the past twelve months, average domestic consumer liabilities have grown from $25.2 billion to $29.9 billion. As a consequence, average U.S. domestic consumer liabilities as a percentage of total average domestic assets now stands at 34%. Concurrent with the increase in the domestic portfolio, overseas average consumer liabilities have grown to 27% of total average overseas assets. Total consumer liabilities as a percent of total average assets has increased to 31%, from 29% a year ago. Continued growth in Citicorp's consumer liabilities has added further stability and depth to the Corporation's funding profile—thereby enhancing liquidity.

LONG-TERM DOMESTIC U.S. DOLLAR INTEREST RATE GAP*

IN BILLIONS OF DOLLARS, AT YEAR END



*Excess of assets over liabilities, including the effects of non-funds related interest rate products, with repricing dates beyond one year

COMPONENTS OF CAPITAL

IN MILLIONS OF DOLLARS	DEC. 31, 1985	DEC. 31, 1984	CHANGE
TOTAL CAPITAL	**$15,948**	$11,805	$4,143
Of which:			
Common Stock and Surplus	**$ 1,250**	$ 1,149	$ 101
Preferred Stock	**1,215**	640	575
Retained Earnings	**5,300**	4,637	663
Allowance for Possible Credit Losses	**1,235**	917	318
Qualifying Subordinated Capital Notes	**1,815**	1,479	336
Minority Interest in Consolidated Subsidiaries	**77**	50	27
PRIMARY CAPITAL	**$10,892**	$ 8,872	$2,020
Remainder of Subordinated Capital Notes	**$ 84**	$ 170	$ (86)
Redeemable Preferred Stock	**40**	40	—
Qualifying Debt	**4,932**	2,723	2,209
SECONDARY CAPITAL	**$ 5,056**	$ 2,933	$2,123

Primary Capital, as defined by the Federal Reserve, includes Stockholders' Equity, Qualifying Subordinated Capital Notes, the Allowance for Possible Credit Losses and minority interest in consolidated subsidiaries.

Total Capital includes Primary Capital, Redeemable Preferred Stock, and gross Qualifying Debt restated in compliance with new regulatory requirements.

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C I T I C O R P I N B R I E F

PEOPLE

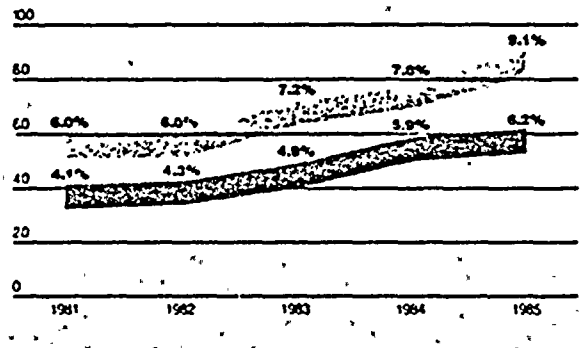
Common Stockholders	51,000
Staff	
Domestic	42,100
Overseas	39,200
TOTAL	81,300

OFFICES

United States (1185 offices in 42 states and the District of Columbia)	
Citibank, N.A., branches	293
Citibank, N.A., subsidiaries	65
Citibank (New York State), N.A., branches	46
Citibank (New York State), N.A., subsidiaries	61
Citicorp Savings	228
Other Citicorp subsidiaries	492
Overseas (1806 offices in 92 countries)	
Citibank branches and representative offices	292
Banking subsidiaries	601
Banking affiliates	109
Other financial affiliates and subsidiaries	804
TOTAL DOMESTIC AND OVERSEAS	2,991

CAPITAL RATIOS

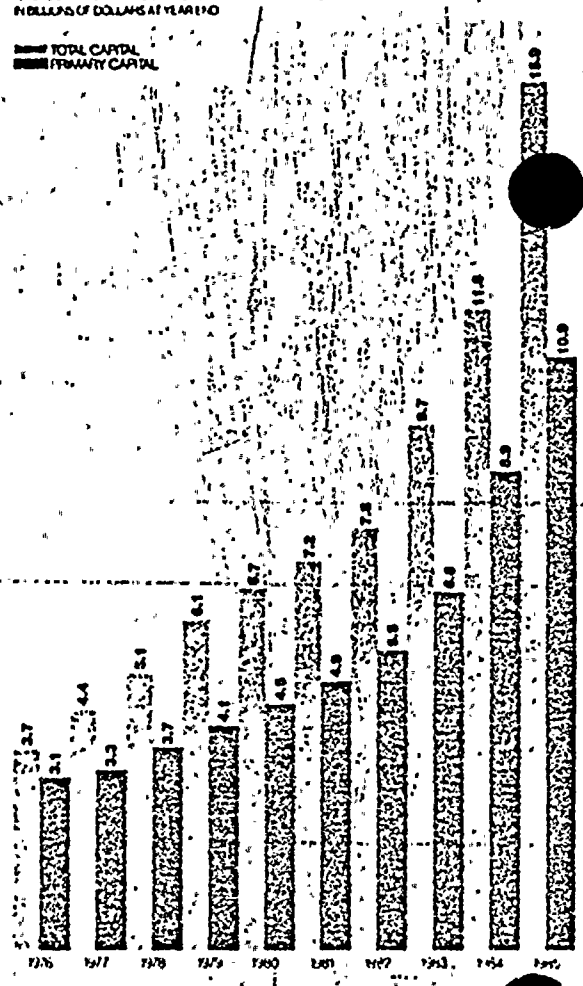
YEAR END TOTAL CAPITAL AS A PERCENTAGE OF TOTAL ASSETS
YEAR END PRIMARY CAPITAL AS A PERCENTAGE OF TOTAL ASSETS



TOTAL CAPITAL AND PRIMARY CAPITAL

IN BILLIONS OF DOLLARS AT YEAR END

TOTAL CAPITAL
PRIMARY CAPITAL



COMMON DIVIDENDS DECLARED AND NET INCOME PER SHARE

DOLLARS

COMMON DIVIDENDS DECLARED

NET INCOME (FULLY DILUTED)

RETURN ON COMMON STOCKHOLDERS' EQUITY* AND AVERAGE ASSETS**

PERCENT

RETURN ON EQUITY

RETURN ON ASSETS

*Net Income Less Preferred Stock Dividends, as a Percentage of Average Common Stockholders' Equity

**Net Income as a Percentage of Average Total Assets

THE BUSINESSES OF CITICORP

Citicorp, a holding company, was incorporated in 1967 under the laws of Delaware and is the sole shareholder of Citibank, N.A.

Today Citicorp, with its subsidiaries and affiliates, is a multinational financial services organization. Its staff of 81,300 people serves the financial needs of individuals, businesses, governments and financial institutions in approximately 3,000 locations, including branch banks, representative offices and subsidiary and affiliate offices in 42 States and the District of Columbia and 92 other countries throughout the world.

Citicorp, Citibank and their subsidiaries and affiliates are subject to intense competition in all aspects of their businesses from both bank and nonbank institutions that provide financial services and, in some of their activities, from governmental agencies.

In order to meet the challenges of today's and tomorrow's marketplace, Citicorp has organized its activities around customer-oriented core businesses. The Individual Bank, which focuses on serving the needs of consumers, and the Institutional Bank and Investment Bank, which work in conjunction to serve corporations, financial institutions, and governments. For further information regarding the three core businesses see the sector discussions below.

SECTOR PERFORMANCES

The following discussion analyzes sector financial performances using the core business format changes outlined on page 7.

INDIVIDUAL BANKING

Individual Bank earnings of $340 million rose $118 million, or 53%, over 1984. This strong performance was built on the continuing revenue momentum generated by the consumer sector's rapidly expanding businesses. As the accompanying table indicates, Customer Net Revenue grew 33%, with each business group making contributions to the increase. The strong revenue growth enabled the sector to absorb the higher credit costs associated with portfolio expansion and increased delivery expense needed to fund new business initiatives. Reflecting the sector's improved profitability, return on equity rose to 15.3% from 12.7% last year. Although short-term interest rates remained relatively stable through most of 1985, efforts continued to reduce the impact of rate fluctuations on earnings performance. Through the purchase of longer term liabilities and the use of interest rate swaps, the net rate spread component of customer revenues was better protected against rate volatility.

Earnings improved on a global basis. Domestically, nationwide mortgage, retail banking and card products businesses all contributed to the growth in profitability. In addition, our international activities in the three geographic regions – Asia/Pacific, Europe and Latin America – all posted strong earnings. Higher loan volumes and fee revenue and lower net credit write-offs paced an improvement in worldwide Private Banking results.

Average customer assets rose 25%, led by the mortgage and credit card activities. Generally lower interest rates helped keep mortgage financing demand firm. Fast mortgage assets rose 27%. The improvement was largely registered in Individual Banking's important domestic markets: the New York branch system, the savings and loans and the nationwide mortgage network. Intensified solicitation programs combined with the continued vitality of consumer spending to broaden the card product base, as total card accounts increased to 17.5 million. Average net card receivables rose 54%.

The sharp increase in average asset volumes and related customer revenues was accompanied by higher consumer loan loss expense. While much of this increase was volume related, the continuing shift in the portfolio toward a higher proportion of credit card receivables was also a significant factor. Credit card portfolios have a historically higher loss experience, particularly in their early years of development. The higher write-offs were reflected in the comparative ratios of net loan losses to average loans: 1.23% versus .78% the previous year. Consistent with the change in the way the Corporation reports sector results, Individual Bank earnings were charged an amount to build the total allowance for possible credit losses equal to 50% of consumer loan growth from 1984 year-end to 1985 year-end. This charge in 1985 was $58 million, up $10 million from 1984.

In contrast to the 33% increase in customer net revenue, delivery expense increased 22% year to year. Of that increase, approximately two-thirds was related to support of the base businesses, particularly in the area of higher processing costs for expanded customer volumes. The remainder was directed toward initiatives aimed at improving our longer-term positioning and the development of new revenue sources, including investment in marketing, technology and product development. The improvement in other income (expense) was driven primarily by the impact of lower domestic interest rates on funding costs of non-customer assets and interest amounts held at the sector level.

SECTOR PERFORMANCE

	1985	1984	[illegible]	[illegible]
Customer Net Revenue	**$4,120**	$3,107	$1,013	33
Expenses				
Credit Cycle Expense	**989**	586	403	69
Delivery Expense	**2,625**	2,149	476	22
Total Expenses	**$3,614**	$2,735	$ 879	32
Other Income (Expense)	**(102)**	(12)	(114)	--
Income Before Taxes	**608**	360	248	69
NET INCOME	**$ 340**	$ 222	$ 118	53
Average Assets ($ Billions)	**55**	44	11	25
Return on Assets (%)	**.61**	.51	.10	--
Return on Equity (%)	**15.3**	12.7	2.6	--

INSTITUTIONAL RELATIONSHIPS

Citicorp's Institutional Bank units provide a complete range of financial services to business and government organizations around the world. Institutional Relationships earnings are derived from products originating in both the Institutional Bank and Investment Bank sectors.

In 1985, Institutional Relationships earned $755 million, representing a 2% increase over the $743 million earned in 1984. As the accompanying table indicates, total revenues of $3,771 million were up 15% over 1984, with both Institutional Bank and Investment Bank products contributing to this growth. Write offs were at a higher level, reflecting the continued weakness in certain industries domestically and overseas, such as shipping and energy, while expenses were 18% higher. Average assets of $91 billion increased by 3% over last year. With a return on equity of 20.9%, Institutional Relationships continues to exceed the corporate target.

Geographically, sharp earnings growth in North America combined with higher cash receipts in Latin America helped to offset declines in Asia/Pacific and Europe, Middle East and Africa, primarily due to higher write offs and increased operating expenses.

The Financial Institutions Group, which operates within all the geographic regions, recorded a modest increase in earnings over last year.

SECTOR PERFORMANCE

Net Income By Product Contribution

	1985	1984	VAR	%
INSTITUTIONAL RELATIONSHIPS	**$755**	$743	$ 12	2
Of which				
Institutional Bank	**392**	454	(62)	(14)
Investment Bank	**363**	289	74	26

Institutional Relationships

	1985	1984	VAR	%
Total Revenue	**$3,771**	$3,291	$480	15
Prov for Possible Credit Losses	**374**	213	161	76
Operating Expenses	**2,016**	1,705	311	18
Income Before Taxes	**1,381**	1,373	8	1
NET INCOME	**$ 755**	$ 743	$ 12	2
Average Assets ($ Billions)*	**91**	88	3	3
Return on Assets (%)	**0.83**	0.85	(0.02)	–
Return on Equity (%)	**20.9**	21.2	(0.3)	–

INSTITUTIONAL BANK

Institutional Banking products earned $392 million in 1985, representing a 14% decrease from the $454 million earned in 1984, primarily due to the $374 million provision for possible credit losses recorded in 1985 as compared with $213 million in 1984. Return on equity was 13.6% compared with 15.9% for the prior year.

Total revenue for 1985, as indicated in the accompanying table, was $2,542 million, representing an 11% growth over the $2,281 million recorded in 1984, benefiting from gains across a wide range of loans based and fee based products, fees and commissions, and other revenue sources—including aircraft lease residual sales and amounts received in a contract settlement.

Operating expenses for 1985 of $1,500 million increased by 18% over last year, reflecting continued investments in improved service delivery and product development, expenses of new acquisitions, consolidation of certain businesses, and adverse foreign exchange impact.

Net commercial loan write offs were $377 million, or 65 basis points of the full year average commercial loan portfolio, an increase of $156 million or 27 basis points, over last year's level. Over the past ten years, net write offs as a percentage of the commercial loan portfolio have averaged 35 basis points. Citicorp continued to maintain its conservative policies in the recognition of both public and private sector write-offs.

Consistent with the change in the way the Corporation reports sector results, the Institutional Bank's allowance for possible credit losses is maintained at 60 basis points of year-end loans. Reflecting the sector's smaller loan portfolio, the credit allowance currently equals $349 million, down $4 million from a year ago.

On a geographic basis, North America's net income was higher than the previous year due to higher fees and commissions, and aircraft lease residual sales. Latin American net income also improved because of increased cash collections and the amounts received in a contract settlement. Higher write offs and increased operating expenses in Asia/Pacific and Europe, Middle East and Africa resulted in lower earnings in these regions compared to last year.

At year end, cash basis loans totaled $2.2 billion, down from $2.4 billion a year ago. The ratio of cash basis loans to total loans decreased from 2.4% in 1984 to 2.0% in 1985. The decrease includes the effect of $266 million of Argentine debt that was returned to full accrual status at the end of the fourth quarter.

Average assets of $72 billion grew 1% compared to 1984, reflecting continuing strict management of asset growth.

Institutional Bank

	1985	1984	VAR	%
Total Revenue	**$2,542**	$2,281	$261	11
Prov for Possible Credit Losses	**374**	213	161	76
Operating Expenses	**1,500**	1,275	225	18
Income Before Taxes	**668**	793	(125)	(16)
NET INCOME	**$ 392**	$ 454	$(62)	(14)
Average Assets ($ Billions)*	**72**	71	1	1
Return on Assets (%)	**0.54**	0.64	(0.10)	–
Return on Equity (%)	**13.6**	15.9	(2.3)	–

AVERAGE BALANCE SHEET

DECEMBER 1985**

Assets		Liabilities	
Loans & Leases	$59.2	Interest Bearing Dep	$23.7
Acceptances	8.0	Non Interest Bearing Dep	8.4
Cash & Due from Banks	3.3	Acceptances	8.0
Other	5.7	Other (primarily intercorp*)	36.1
	$76.2		$76.2

INVESTMENT BANKING

Investment Banking at Citicorp encompasses securities activities, foreign exchange and money market trading, venture capital investment, merchant banking, investment management, insurance, trust and custodial services, and economic information services. For the Investment Bank, 1985 was a year of strong growth in an increasingly complex marketplace. Net earnings of $425 million increased 24% over 1984.

Revenues rose sharply to $1.6 billion, as shown in the accompanying table. This rise was largely the result of increased securities trading, positioning, and distribution activities as well as higher foreign exchange and money market revenues. Revenues from fee based activities also rose, particularly in US Corporate Finance, and Mergers and Acquisitions. Venture Capital reported lower earnings compared with 1984. Revenues in 1985 included AMBAC for the first time.

Operating expenses increased 37% over 1984, in line with the continuing expansion of the global business activity. Approximately $35 million of the increase was related to acquisitions in Asia and Europe, with additional amounts expended for business development, technology and other programs. Average assets grew by 23%, principally stemming from business expansion in North America and Europe. Return on assets and return on equity were above the corporate targets and marginally higher than 1984.

Because of the diverse nature of the Investment Banking business, it is useful to look at the results by functional activity as well as by region. Trading and positioning in foreign exchange, money market and securities instruments accounted for approximately 80% of total Investment Bank earnings. Fund raising for our customers and financial advisory represented approximately 10%, while Venture Capital contributed less than 5% of total earnings.

From a customer perspective, a major portion of Investment Bank earnings in 1985 came from products sold to Institutional Relationship customers. These products include foreign exchange and hedging products, financial advisory services, debt products, investment management, and portfolio services.

Geographically, Europe and North America each contributed approximately one third of total Investment Bank net income, while Latin America and Asia accounted for the other third.

SECTOR PERFORMANCE

(Millions of Dollars)	1985	1984	VAR	%
Total Revenue	$1,589	$1,241	$348	28
Operating Expenses	803	587	216	37
Income Before Taxes	786	654	132	20
NET INCOME	$ 425	$ 343	$ 82	24
Average Assets ($ Billions)*	32	26	6	23
Return on Assets (%)	1.34	1.33	0.01	—
Return on Equity (%)	33.5	33.2	0.3	—

(5 year to date average)

OTHER ITEMS

As a result of the changes described on page 7, charges held at the corporate level contain:

- The credit loss provision that represents the build up of the credit allowance beyond that charged to the businesses
- Unallocated corporate staff costs
- Other corporate items including certain start up activities

The sectors are not charged for these items which reflect corporate level decisions and which, if allocated, would detract from our understanding of how the core businesses are performing.

Other items were lower in 1985 compared to 1984 primarily as a result of the decision to build the credit allowance from 88 basis points to 106 basis points.

Other Items

(Millions of Dollars)	1985	1984	VAR	%
Total Revenue	$ 28	$ (79)	$107	—
Operating Expenses	148	116	32	28
Corporate Credit Loss Provision	226	68	158	—
Income Before Taxes	(346)	(263)	(83)	(32)
NET INCOME	$(159)	$(129)	$ (30)	(23)
Average Assets ($ Billions)*	2	3	(1)	(33)

(5 year to date average)

SUMMARY OF FINANCIAL RESULTS

SELECTED FINANCIAL INFORMATION

CITICORP AND SUBSIDIARIES

(MILLIONS OF DOLLARS EXCEPT PER-SHARE AMOUNTS)	1985 AMOUNT	1985 % CHANGE	1984 AMOUNT	1984 % CHANGE	1983 AMOUNT	1983 % CHANGE	1982 AMOUNT	1982 % CHANGE	1981 AMOUNT	1981 % CHANGE
Net Interest Revenue	$5,446	26	$4,319	7	$4,043	15	$3,526	42	$2,479	(3)
Fees, Commissions and Other Revenue	3,030	32	2,300	25	1,840	15	1,595	1	1,574	36
TOTAL REVENUE	$8,476	28	$6,619	13	$5,883	15	$5,121	26	$4,053	9
Provision for Possible Credit Losses	$1,243	—	$ 619	19	$ 520	10	$ 473	55	$ 305	2
Operating Expense	5,517	24	4,456	19	3,757	11	3,398	16	2,936	14
TOTAL EXPENSE	$6,760	33	$5,075	19	$4,277	10	$3,871	19	$3,241	13
Income Before Taxes	$1,716	11	$1,544	(4)	$1,606	28	$1,250	54	$ 812	(2)
Income Taxes	718	10	654	(12)	746	42	527	88	281	(15)
NET INCOME	$ 998	12	$ 890	3	$ 860	19	$ 723	36	$ 531	6
Per Share										
Net Income[1]										
On Common and Common Equivalent Shares	$7.12	10	$6.45	—	$6.48	16	$5.60	33	$4.20	4
Assuming Full Dilution	$7.11	12	$6.36	3	$6.15	15	$5.33	33	$4.02	5
Dividends Declared Per Common Share	$2.26	10	$2.06	10	$1.88	9	$1.72	10	$1.56	10
TOTAL ASSETS	$173,597	15	$150,586	12	$134,655	4	$129,997	9	$119,232	4
DEBT[2]	$ 18,255	24	$ 14,682	20	$ 12,221	16	$ 10,566	25	$ 8,462	42

(1) On Net Income available for Common Stockholders after deducting total Preferred Stock Dividends of $63 million in 1985, $60 million in 1984, $37 million in 1983, and $4 million in both 1982 and 1981.

(2) Includes Long-Term Debt, Subordinated Capital Notes and Redeemable Preferred Stock.

STATEMENT OF INCOME ANALYSIS

NET INTEREST REVENUE TAXABLE EQUIVALENT BASIS

A significant rise in consumer loan volumes propelled a 25% increase in net interest revenue over 1984. Average interest earning asset volume of $140.6 billion in 1985 was up 13% over the previous year. In 1985, total net interest revenue of $5.6 billion grew $1.1 billion on the year-to-year comparison. The volume increase was accompanied by an increase in the net rate spread—3.98% in 1985 versus 3.61% in 1984—reflecting a general decline in U.S. dollar interest rates which yielded lower funding costs. The improved net rate spread was also affected by the lower drag from cash basis loans. The downward trend in average interest rates evidenced through most of 1983 was reversed in the first three quarters of 1984. Interest rates fell sharply in the last quarter of 1984 and remained relatively stable throughout most of 1985. The net rate spread, up 37 basis points over last year, widened as a 7% rise in interest revenue more than offset a 1% increase in interest expense.

In 1984, a 12% volume increase was led by a significant rise in consumer loans, and partially offset by a narrower net rate spread, to push net interest revenue up over the previous year.

The sharp rise in average consumer loans in 1985 was driven primarily by a $9.9 billion increase in domestic consumer loans which was principally in mortgage and credit card activities. The increase in card receivable volume was fueled by an expanded customer card base combined with continued vigorous consumer spending. Demand remained firm for shelter financing in an environment of generally lower interest rates. Improvement was largely evidenced in the New York branch system, the savings and loans and the nationwide mortgage network.

Internationally, strong money market positioning profits in certain overseas locations, the lower drag from cash basis loans and the positive effect of the decline in the U.S. dollar on local currency earnings contributed to the growth in net interest revenue above the prior year's total.

In 1985, Citicorp continued to manage the interest sensitivity of the portfolio through stringent worldwide rate gap limits on the mismatch of the repricing dates between assets and liabilities, also taking into account the effects of non-funds related interest rate products. New fixed rate lending is being match funded at favorable spreads through Citicorp's program of issuing fixed rate debt. Reflecting management's strategy to confine the institution's interest rate exposure primarily to the short-term, Citicorp's domestic long term gap was modestly positive at year end, while long term rate exposure internationally was also modest and continued to be diverse across many currencies.

NET RATE SPREAD TAXABLE EQUIVALENT BASIS

	1985	1984	1983
In Domestic Offices	4.48	3.79	4.32
In Overseas Offices	3.45	3.44	3.28
TOTAL	3.98	3.61	3.74

CREDIT LOSS EXPENSE AND ALLOWANCE

Citicorp has continued its policy of reflecting all known loan losses in current earnings. In 1985 the total credit loss provision was $1,243 million and included $962 million of net loan losses while adding $281 million to the allowance. In 1984, the total credit loss provision of $619 million covered $507 million of net loan losses while adding $112 million to the allowance, and in 1983 the comparable amounts were $520 million, $437 million, and $83 million, respectively. The credit loss allowance totalled $1,235 million at the end of the year, reflecting 1.06% of total loans and lease financing. In 1984 the amounts were $917 million and 0.88%, and in 1983, $771 million and 0.85%, respectively.

Net commercial loan losses for 1985 amounted to $377 million, compared with $221 million in 1984 and $241 million in 1983. The $156 million increase in 1985 over the previous year reflected the protracted weakness in certain industries, such as shipping and energy, both domestically and overseas. In addition, write-offs related to foreign debt servicing problems continued in certain countries. The ratio of net loan losses as a percentage of average commercial loans was .65% in 1985 compared with .38% in 1984, and .39% in 1983. The ten-year average of this ratio is .35%. Recoveries of $65 million increased by $9 million over the previous year and were derived primarily from commercial and industrial loans; in 1983 recoveries amounted to $51 million. These strong recoveries are an indicator of Citicorp's conservative write-off policy and stringent processes to monitor and assess problem credit situations.

Net consumer loan losses for 1985 amounted to $585 million, reflecting a $299 million increase from 1984; 1983 net losses amounted to $196 million. Net credit losses as a percentage of average consumer loans were 1.23%, up from .78% in 1984 and .79% in 1983. The higher level of net loan losses reflects the shift in the portfolio toward a higher proportion of credit card receivables. Credit card portfolios have a historically higher loss experience, particularly in early years of development. Over 3 million additional credit card accounts were added in 1985.

As Citicorp has consistently maintained, the credit loss allowance is, in essence, an allocation of capital and serves the same purpose as all capital—to absorb any losses not covered by current earnings. The Comptroller of the Currency and Federal Reserve formally recognized this position in their definitions of primary and total capital (see definition on page 36), which are applied in their minimum capital guidelines.

We noted in previous annual reports that consumer loan losses are a predictable cost of participating in the consumer lending business and that it is sound and conservative to charge such predictable losses to earnings as the directly related revenues are recognized. Therefore, we continue to favor a change in present accounting conventions to permit us to charge income for consumer credit loss expense over the life of the loan portfolio instead of recording this expense at the time each loan is booked. This change would better match consumer loan losses against current revenues.

FEES, COMMISSIONS AND OTHER REVENUE

Total fees, commissions and other revenue of $3.0 billion in 1985 increased 32%, or $730 million, over 1984, the total in 1984 was up $460 million, or 25%, over 1983. The improvement in 1985 reflected strong performances in all revenue lines – fees and commissions, securities trading, foreign exchange, investment securities transactions and other revenue.

Fees and commissions increased $437 million, or 26%, to $2.1 billion in 1985 from $1.7 billion in 1984. Individual Banking card product activities – Citibank Visa and Citibank MasterCard – contributed more than one third of this growth. Increased promotional programs, combined with continued strong domestic consumer spending, pushed card membership and merchant discount fees higher as the customer base expanded.

Institutional Banking posted an increase in fees particularly on the strength of letter-of-credit activity. The rise in Investment Banking's fees and commissions was sustained over various business activities, including corporate finance, public finance, financial advisory and merger and acquisition fees.

The $398 million rise in fees and commissions recorded in 1984 over 1983 was primarily attributable to improved credit card fees in Individual Banking, trade related fees in Institutional Banking, and diversified fees in Investment Banking.

Expanded securities trading activities had a strong year in 1985, with revenues of $210 million, an increase of $67 million, or 47%, over 1984. While revenue generated from domestic trading activities declined $13 million to $52 million in 1985, revenues from overseas operations climbed $80 million from year to year reaching $158 million in 1985. Domestic operations are primarily centered on trading in US government and state and municipal debt obligations, similarly, international revenues are largely achieved through the trading of foreign government obligations. In 1984, total trading revenue of $143 million improved $61 million over 1983.

Global foreign exchange revenue, from both customer commercial transactions and trading, continued to be diversified across many trading centers. Foreign exchange revenue of $358 million advanced $100 million over 1984 reflecting the strong gains recorded in Asia and Europe.

Investment securities transactions registered a $59 million net gain in 1985, compared with net gains of $16 million in 1984 and $11 million in 1983. Gains on the sale of investment securities managed by the core businesses in both 1983 and 1984 more than offset moderate losses resulting from sales in the corporate portfolio. In 1985, disposition of securities resulted in net gains realized by both the core businesses and the investment portfolio managed at the corporate level.

Other revenue was $280 million in 1985 compared with $197 in 1984 and $185 million in 1983. The strong improvement in 1985 was principally derived from gains realized on sales of mortgage portfolios and other assets, amounts received in a contract settlement and gains on sales of aircraft and railcar lease residuals. Gains on the sales of venture capital investments amounted to $25 million in 1985. In 1984, other revenue included gains on the sales of venture capital investments of $49 million, a $12 million after tax gain on the sale of an affiliate, a $14 million gain on the buyback of the corporation's convertible notes and gains on sales of real estate, mortgages and other assets. In 1983, the total included a $32 million gain on a sale of Hong Kong real estate, gains on venture capital investments of $31 million and $34 million in gains on sales of securities received in settlement of loans.

Other Revenue

In Millions of Dollars	1985	1984	1983
Affiliate Earnings	$ 68	$ 78	$ 83
Gains on Sale of Residual Value of Leased Equipment	43	14	13
Net Gains on Sale/Disposition of Assets	107	91	97
Other Items	62	14	(8)
TOTAL	$280	$197	$185

OPERATING EXPENSE

Total operating expense in 1985 was $5.5 billion, an increase of $1,061 million, or 24%, over the $4.5 billion recorded in 1984, the 1984 total represented an increase of $699 million, or 19%, over 1983. The year-to-year increase in expenses was spent supporting the revenue momentum of our base businesses, improving service delivery and product development, new acquisitions, expanding into new markets, as well as absorbing the adverse impact of a weakening US dollar on overseas local currency expenses.

Total staff expense was $2.5 billion in 1985, up $437 million, or 21%, from 1984. The increase reflected the additional 10,300 people required to staff the expanding businesses, normal compensation increments, and higher benefits expenses.

Net premises and equipment expenses were $961 million for 1985, up $194 million, or 25%, from 1984. Acquisitions, business expansion, relocations, and write offs of outdated equipment were the primary contributors to this increase.

INCOME TAXES

Citicorp's effective tax rate was 41.8% in 1985 compared with 42.4% in 1984 and 46.5% in 1983. The lower rate in 1985 was due primarily to the reduction in New York State and City deferred taxes related to leveraged lease transactions.

GEOGRAPHIC DISTRIBUTION OF REVENUE, EARNINGS AND ASSETS

Citicorp attributes its net income to geographic regions based on the domicile of the customer. United States possessions are included in the respective geographic areas. In the accompanying table, the North American region includes the United States and Canada. In 1985, additional allocations were made so that items presented in the "Other Item" category in prior years have been redistributed to the geographic regions. The prior years' disclosures have been reclassified to conform with the current year's presentation. See page 65 for further discussion of the principal adjustments and allocations that are made to present results on a geographic basis.

Domestically, earnings were $463 million in 1985, an increase of $96 million over the prior year. This growth was paced by improved funds [illegible] revenues and by fees and commissions related to a variety of [illegible] activities in each of the core businesses. Within the domestic [illegible] business, interest based earnings increased significantly as a result of [illegible]sting loan portfolio—primarily mortgages and credit card [illegible]es—combined with wider net rate spreads. The growing credit [illegible]ness also accounted for sizable gains in card membership and merchant discount fees. Domestic revenue growth was further supported by improved fees in commissions from mergers and acquisitions, US corporate and trade related activities. Earnings from foreign exchange, sale of lease residuals also contributed to the increased profits in 1985.

However, partially offsetting the robust revenue performance were increases in the credit loss provision and operating expenses. Consumer loan losses rose due to the significant increase in the consumer loan portfolio coupled with a higher proportion of credit card receivables, which have a historically higher loss experience. The increase in the commercial loan losses was the result of continued weaknesses in certain industries, including shipping and energy. Improved service delivery, new product introduction, and aggressive market expansion led to higher operating expenses.

International net income of $535 million increased $12 million over last year. Higher cash payments received in some of the Latin American debt rescheduling countries contributed significantly to that region's $68 million increase in earnings. However, the improved performance in Latin America was partially offset by reduced earnings in the Asia/Pacific and Europe, Middle East and Africa regions. In Asia/Pacific, limited revenue growth, due to narrowing interest rate spreads, and increased write offs were responsible for the $39 million decline in earnings. The Europe, Middle East and Africa results reflect solid revenue growth outweighed by significantly higher loan losses and operating expenses. Total international foreign exchange and trading revenues increased from a year ago mainly due to strong gains in Europe and Asia. In addition, Latin America and Asia/Pacific benefited from the expanding international consumer business. For the year, operating expenses rose significantly from increased expenditures designed to improve base business performance and support expanding business initiatives, and as a result of the impact of a weakening US dollar on local currency expenses.

The accompanying chart provides a breakdown of Citicorp's earnings using the economic classifications designated by the Organization for Economic Cooperation and Development (OECD). While Citicorp businesses are diversified across a broad range of countries and economies, the OECD countries, at 65% in 1985, represent the largest source of earnings for Citicorp. The OECD countries' contribution to net income has grown steadily since 1983. Of these countries, primarily the industrialized nations of the world, the United States accounts for approximately 45% of total Citicorp earnings versus 39% last year. Within the Newly Industrialized Countries (NIC), which represent approximately 24% of corporate earnings, down slightly from last year, major contributors were Brazil, Argentina, and Mexico. The Less Developed Countries (LDC)/Other category was adversely affected by credit write offs.

NET INCOME

[illegible]	1985		1984		1983	
North America	$463	46%	$367	41%	$320	37%
Caribbean, Central and South America	245	25	177	20	234	28
Europe, Middle East and Africa	191	19	208	23	156	18
Asia/Pacific	99	10	138	16	150	17
TOTAL	$998	100%	$890	100%	$860	100%

NET INCOME OECD CLASSIFICATION

[illegible]	1985		1984		1983	
Total OECD*	$646	65%	$540	61%	$446	52%
Total NIC*	244	24	226	25	287	33
Total LDC/Other*	108	11	124	14	127	15
TOTAL	$998	100%	$890	100%	$860	100%

(*) See accompanying Geographic discussion

FINANCIAL REPORTING RESPONSIBILITY

The accompanying financial statements have been prepared by the management of Citicorp in conformity with generally accepted accounting principles appropriate in the circumstances. Where amounts must be based on estimates and judgments, they represent the best estimates and judgments of management. The financial information appearing throughout this annual report is consistent with that in the financial statements.

The financial control system of Citicorp is designed to provide reasonable assurance that the financial records are reliable for preparing financial statements and maintaining accountability for assets and that assets are safeguarded against loss from unauthorized use or disposition. The system in use at Citicorp provides such reasonable assurance, supported by the careful selection and training of staff, the establishment of organizational structures providing an appropriate and well defined division of responsibilities, and the communication of policies and standards of business conduct throughout the institution.

The accounting policies and system of internal accounting controls are under the general oversight of the Citicorp and Citibank Boards of Directors, acting through the Audit and Examining Committees described on page 83. These committees are composed solely of directors who are not officers or employees of Citicorp. The Chief Auditor of Citicorp, who reports directly to the Board of Directors, supervises an extensive program of audits and credit asset reviews worldwide, carried out by a staff of resident inspectors and reviewers and traveling teams. In addition, Peat, Marwick, Mitchell & Co., independent certified public accountants, is engaged to examine our financial statements.

Peat, Marwick, Mitchell & Co. obtains and maintains an understanding of our accounting and financial controls and conducts such tests and other auditing procedures as they consider necessary in the circumstances to express the opinions in their report that follows. Peat, Marwick, Mitchell & Co. has free access to the Audit and Examining Committees, with no members of management present, to discuss their examination and their findings as to the integrity of Citicorp's financial reporting and the adequacy of the system of internal accounting controls.

REPORT OF INDEPENDENT AUDITORS

PEAT MARWICK

Peat, Marwick, Mitchell & Co.
Certified Public Accountants

The Board of Directors and Stockholders of Citicorp:

We have examined the consolidated balance sheet of Citicorp and subsidiaries as of December 31, 1985 and 1984, the related consolidated statements of income, changes in stockholders' equity and changes in financial position for each of the years in the three year period ended December 31, 1985, and the consolidated balance sheet of Citibank, N.A. and subsidiaries as of December 31, 1985 and 1984. Our examinations were made in accordance with generally accepted auditing standards and, accordingly, included such tests of the accounting records and such other auditing procedures as we considered necessary in the circumstances.

In our opinion, the aforementioned consolidated financial statements present fairly the financial position of Citicorp and subsidiaries at December 31, 1985 and 1984, and the results of their operations and the changes in their financial position for each of the years in the three year period ended December 31, 1985, and the financial position of Citibank, N.A. and subsidiaries at December 31, 1985 and 1984, in conformity with generally accepted accounting principles applied on a consistent basis.

Peat, Marwick, Mitchell & Co.

Peat, Marwick, Mitchell & Co.

New York, New York
January 21, 1986

FINANCIAL STATEMENTS

CONSOLIDATED STATEMENT OF INCOME

CITICORP AND SUBSIDIARIES

IN MILLIONS OF DOLLARS EXCEPT PER SHARE AMOUNTS	1985	1984	1983
Interest Revenue			
Interest and Fees on Loans and Lease Financing	$15,528	$14,549	$12,376
Interest on Deposits with Banks	1,156	1,273	1,074
Interest on Federal Funds Sold and Securities Purchased Under Resale Agreements	1,087	936	757
Interest and Dividends on Investment Securities (Note 1)	643	655	531
Interest on Trading Account Assets	860	781	459
	$19,474	$18,194	$15,197
Interest Expense			
Interest on Deposits	$ 8,855	$ 8,631	$ 6,894
Interest on Other Borrowed Money (Note 6)	3,356	3,582	2,885
Interest on Long-Term Debt and Subordinated Capital Notes (Notes 7 and 8)	1,907	1,662	1,375
	$14,028	$13,875	$11,154
NET INTEREST REVENUE	$ 5,446	$ 4,319	$ 4,043
Provision for Possible Credit Losses (Note 4)	$ 1,243	$ 619	$ 520
NET INTEREST REVENUE AFTER PROVISION FOR POSSIBLE CREDIT LOSSES	$ 4,203	$ 3,700	$ 3,523
Fees, Commissions and Other Revenue			
Fees and Commissions	$ 2,123	$ 1,686	$ 1,288
Trading Account	210	143	82
Foreign Exchange	358	258	274
Investment Securities Transactions (Note 13)	59	16	11
Other Revenue	290	197	185
	$ 3,030	$ 2,300	$ 1,840
Other Operating Expense			
Salaries	$ 2,116	$ 1,749	$ 1,507
Staff Benefits (Note 12)	424	354	337
Total Staff Expense	$ 2,540	$ 2,103	$ 1,844
Net Premises Expense (Notes 5 and 17)	480	391	344
Equipment Expense (Notes 5 and 17)	441	376	331
Other Expense	2,016	1,586	1,238
	$ 5,517	$ 4,456	$ 3,757
Income Before Taxes	$ 1,716	$ 1,544	$ 1,606
Income Taxes (Note 13)	718	654	746
NET INCOME	$ 998	$ 890	$ 860
Earnings Per Share (Note 14)			
On Common and Common Equivalent Shares	$7.12	$6.45	$6.48
Assuming Full Dilution	$7.11	$6.36	$6.15

Accounting policies and explanatory notes on pages 53-68 form an integral part of the financial statements.

CONSOLIDATED BALANCE SHEET

CITICORP AND SUBSIDIARIES

In Millions of Dollars	DECEMBER 31 1985	DECEMBER 31 1984
Assets		
Cash and Due from Banks	$ 5,218	$ 3,528
Deposits at Interest with Banks	12,693	10,757
Investment Securities (Market value $9,892 in 1985 and $6,387 in 1984) (Note 1)	9,647	6,522
Trading Account Assets	6,403	5,145
Federal Funds Sold and Securities Purchased Under Resale Agreements	6,343	5,141
Loans and Lease Financing, Net (Notes 2, 3 and 4)		
Commercial (Net of unearned discount of $483 in 1985 and $410 in 1984)	$ 58,172	$ 58,799
Consumer (Net of unearned discount of $4,418 in 1985 and $4,524 in 1984)	55,518	42,661
Lease Financing	2,609	2,164
Loans and Lease Financing, Net of Unearned Discount	$116,499	$103,624
Allowance for Possible Credit Losses	(1,235)	(917)
Total Loans and Lease Financing, Net	$115,264	$102,707
Customers' Acceptance Liability	6,206	7,854
Premises and Equipment, Net (Note 5)	2,844	2,140
Interest and Fees Receivable	2,693	2,362
Other Assets	6,431	4,430
TOTAL	$173,597	$150,586
Liabilities		
Non Interest Bearing Deposits in Domestic Offices	$ 10,792	$ 8,111
Interest Bearing Deposits in Domestic Offices	30,344	34,535
Non Interest Bearing Deposits in Overseas Offices	3,424	2,807
Interest Bearing Deposits in Overseas Offices	51,399	44,896
Total Deposits	$104,959	$ 90,349
Purchased Funds and Other Borrowings (Note 6)	28,616	24,390
Acceptances Outstanding	6,598	7,970
Accrued Taxes and Other Expenses (Note 13)	3,581	3,028
Other Liabilities	5,023	3,741
Long Term Debt (Note 7)	16,316	12,993
Subordinated Capital Notes (Note 8)	1,699	1,649
Redeemable Preferred Stock (Note 9)	40	40
Stockholders' Equity		
Preferred Stock (Note 10)	$ 1,215	$ 640
Common Stock ($4.00 Par) (Note 11)	569	556
Issued Shares 142,265,429 in 1985 and 138,970,558 in 1984		
Surplus	1,056	958
Retained Earnings	5,300	4,637
Common Stock in Treasury at Cost	(375)	(365)
Shares 12,888,539 in 1985 and 12,702,161 in 1984		
Total Stockholders' Equity	$ 7,765	$ 6,426
TOTAL	$173,597	$150,586

Accounting policies and explanatory notes on pages 53-68 form an integral part of the financial statements

CONSOLIDATED STATEMENT OF CHANGES IN STOCKHOLDERS' EQUITY — CITICORP AND SUBSIDIARIES

In millions, for the years	1985	1984	1983
Preferred Stock (Note 10)			
Balance at Beginning of Year	$ 640	$ 540	$ —
Issuance of Stock	575	100	550
Purchase and Retirement of Stock	—	—	(10)
BALANCE AT END OF YEAR	**$1,215**	$ 640	$ 540
Common Stock (Note 11)			
Balance at Beginning of Year	$ 556	$ 549	$ 542
Shares 138,970,558 in 1985, 137,152,815 in 1984 and 135,525,454 in 1983			
Issuance of Stock under Savings Incentive, Stock Option and Stock Purchase Plans and Conversion of Convertible Notes (Notes 7 and 12)	13	7	7
Shares 3,294,871 in 1985, 1,917,743 in 1984 and 1,627,361 in 1983			
BALANCE AT END OF YEAR	$ 569	$ 556	$ 549
Shares 142,265,429 in 1985, 138,970,558 in 1984 and 137,152,815 in 1983			
Surplus			
Balance at Beginning of Year	$ 958	$ 911	$ 875
Preferred Stock Issuance Cost	(9)	(1)	(10)
Issuance of Stock under Savings Incentive, Stock Option, Stock Purchase and Executive Incentive Compensation Plans and Conversion of Convertible Notes (Notes 7 and 12)	107	48	
Gain on Purchase and Retirement of Preferred Stock	—	—	
BALANCE AT END OF YEAR	$1,056	$ 958	$ 911
Retained Earnings			
Balance at Beginning of Year	$4,637	$4,129	$3,579
Net Income	998	890	860
Cash Dividends Declared including preferred dividends of $59 in 1985, $56 in 1984 and $33 in 1983, and redeemable preferred dividends of $4 in 1985, 1984 and 1983)	(353)	(319)	(271)
Foreign Currency Translation (Accumulated amount of ($99) at December 31, 1985)	18	(63)	(39)
BALANCE AT END OF YEAR	$5,300	$4,637	$4,129
Common Stock in Treasury, at Cost			
Balance at Beginning of Year	$ (365)	$ (358)	$ (181)
Shares 12,702,161 in 1985, 12,577,465 in 1984 and 8,303,810 in 1983			
Treasury Stock Transactions, at Cost	(10)	(7)	(177)
Shares 186,378 in 1985, 124,696 in 1984 and 4,273,655 in 1983			
BALANCE AT END OF YEAR	$ (375)	$ (365)	$ (358)
Shares 12,888,539 in 1985, 12,702,161 in 1984 and 12,577,465 in 1983			
Total Stockholders' Equity			
Balance at Beginning of Year	$6,426	$5,771	$4,815
Changes during the Year Net	1,339	655	956
BALANCE AT END OF YEAR	$7,765	$6,426	$5,771

A reconciliation of retained earnings is shown on page 53. (It is an integral part of the financial statements.)

CONSOLIDATED STATEMENT OF CHANGES IN FINANCIAL POSITION

CITICORP AND SUBSIDIARIES

	1985	1984	1983
Funds Provided			
Net Income	$ 998	$ 890	$ 860
Increase in			
Deposits	14,610	10,555	3,256
Purchased Funds and Other Borrowings	2,226	2,091	—
Long Term Debt	3,323	812	1,655
Subordinated Capital Notes	250	1,649	—
Preferred Stock	575	100	540
Decrease in			
Cash and Due from Banks and Deposits at Interest with Banks	—	1,149	141
Other Net	548	—	—
TOTAL	$22,530	$17,246	$6,452
Funds Used			
Cash Dividends Declared	$ 353	$ 319	$ 271
Increase in			
Cash and Due from Banks and Deposits at Interest with Banks	3,625	—	—
Investment Securities and Trading Account Assets	4,388	2,043	1,261
Federal Funds Sold and Securities Purchased Under Resale Agreements	1,202	1,545	304
Loans and Lease Financing, Net	12,557	12,424	3,392
Premises and Equipment, Net	404	291	296
Decrease in			
Purchased Funds and Other Borrowings	—	—	558
Other Net	—	624	370
TOTAL	$22,530	$17,246	$6,452

CONSOLIDATED BALANCE SHEET

CITIBANK, N.A. AND SUBSIDIARIES

	DECEMBER 31 1985	DECEMBER 31 1984
Assets		
Cash and Due from Banks	$ 4,586	$ 3,138
Deposits at Interest with Banks	12,602	10,489
Investment Securities (Market value $8,596 in 1985 and $4,881 in 1984)	8,347	4,915
Trading Account Assets	2,725	2,028
Federal Funds Sold and Securities Purchased Under Resale Agreements	11,812	7,588
Loans and Lease Financing	$ 77,933	$ 71,568
Less: Allowance for Possible Credit Losses	(626)	(552)
Unearned Discount on Loans	(1,930)	(1,641)
Loans and Lease Financing, Net	$ 75,377	$ 69,375
Customers' Acceptance Liability	7,473	8,910
Premises and Equipment, Net	1,831	1,548
Interest and Fees Receivable	1,984	1,779
Other Assets	4,113	2,669
TOTAL	**$130,850**	**$112,439**
Liabilities		
Non Interest Bearing Deposits in Domestic Offices	$ 9,379	$ 7,521
Interest Bearing Deposits in Domestic Offices	27,280	22,652
Non Interest Bearing Deposits in Overseas Offices	3,512	2,7
Interest Bearing Deposits in Overseas Offices	51,039	44,7
Total Deposits	$ 91,810	$ 77,636
Purchased Funds and Other Borrowings	15,327	13,967
Acceptances Outstanding	7,671	8,991
Accrued Taxes and Other Expenses	2,606	1,869
Other Liabilities	3,506	1,827
Long Term Debt	2,091	1,831
Stockholder's Equity (Note 18)		
Capital Stock ($20.00 par)	$ 751	$ 751
Outstanding Shares: 37,534,553 in 1985 and 1984		
Surplus	1,493	1,078
Retained Earnings	4,793	4,489
Total Stockholder's Equity	$ 7,037	$ 6,318
TOTAL	**$130,850**	**$112,439**

STATEMENT OF ACCOUNTING POLICIES

BASIS OF PRESENTATION

The consolidated financial statements include the accounts of Citicorp, its wholly owned subsidiary Citibank, N.A., and their majority owned subsidiaries, after the elimination of all material intercompany transactions.

Affiliates which are 20% to 50% owned are carried under the equity method of accounting and the pro rata share of their income (loss) is included in other revenue. Income from investments in less than 20% owned companies is recognized when dividends are received.

Gains and losses on disposition of branches, subsidiaries, affiliates and other equity investments (including venture capital investments) and charges for management's estimate of permanent impairment in value are included in other revenue.

Foreign currency translation, which represents the effects of translating into US dollars, at current exchange rates, financial statements of overseas operations with a primary or functional currency other than the US dollar, is included in retained earnings in the accompanying consolidated balance sheet, along with related hedge and tax effects.

The effects of translating foreign currency financial statements of those overseas operations with the US dollar as the primary or functional currency, including those operating in a highly inflationary environment, are included in foreign exchange revenue, along with related hedge effects. Foreign exchange trading positions, including spot and forward contracts, are valued monthly at prevailing market rates, and the resulting gains and losses are included in foreign exchange revenue.

INVESTMENT SECURITIES AND TRADING ACCOUNT ACTIVITIES

Investment securities are carried at cost, adjusted for amortization of premiums to the earliest call date and accretion of discounts to maturity. Gains and losses on sales of investment securities are computed on a specific identified cost basis.

Trading account assets, consisting of securities and money market instruments, are presented net of obligations to deliver assets sold but not yet purchased, and are valued at market. Gains and losses, both realized and unrealized, are included in trading account revenue. Interest on trading account assets, net, is included in interest revenue.

Financial futures and forward contracts, interest rate swaps, and options are valued at market, with both realized and unrealized gains and losses included in trading account revenue, except for those specifically designated as hedges. Gains and losses related to financial futures and forward contracts, interest rate swaps, and options that are specifically designated as hedges are deferred and reflected as an adjustment to interest revenue or expense.

No transfers are made between investment securities and the trading account.

COMMERCIAL LOANS

Commercial loans are stated at their face amount, net of unearned discount.

When it is determined as a result of evaluation procedures that the payment of interest or principal on a commercial loan is doubtful of collection, the loan is placed on a cash (nonaccrual) basis. In any case where interest or principal is past due for 90 days or more, the loan is automatically placed on a cash basis irrespective of collateral or other favorable prospects. Any interest accrued on a loan placed on a cash basis is reversed and charged against current earnings. Interest on cash basis loans is thereafter included in earnings only to the extent actually received in cash.

CONSUMER LOANS

Consumer loans are stated at their face amount, net of unearned discount.

Consumer loans are written off upon reaching a predetermined number of days past due on a contractual basis. The number of days is set at an appropriate level by loan product and by country so as to result in the recognition of losses on a basis which makes the likelihood of subsequent recovery of those losses fall between 20% to 30%.

Interest on discount loans is accrued on a declining basis which results in an approximate level rate of return over the term of the loan. Interest accrued on nondiscount loans is based on the principal amount of loans outstanding.

LEASE FINANCING

Lease financing represents Citicorp's share of aggregate rentals on lease financing transactions and residual values net of related unearned income.

Lease financing transactions substantially represent direct financing leases and also include leveraged leases. Unearned income is amortized under a method which substantially results in an approximate level rate of return when related to the unrecovered lease investment.

Gains and losses from sales of residual values of leased equipment are included in other revenue.

ALLOWANCE FOR POSSIBLE CREDIT LOSSES

Additions to the allowance are made by means of the provision for possible credit losses charged to expense. Credit losses are deducted from the allowance, and subsequent recoveries are added. The level of net credit losses for the year is a significant factor in determining the appropriate level for the provision for possible credit losses. Based on management's judgment as to the appropriate level of the allowance for possible credit losses, the amount actually provided may be greater or less than the net credit losses for the year. The determination of the amount by which the provision should exceed or be less than net credit losses is based on management's current evaluation of the anticipated impact of domestic and international economic conditions, changes in the character and size of the portfolios, past and expected future loss experience, and other pertinent indicators. This evaluation includes an assessment of the ability of borrowers with foreign currency obligations to obtain the foreign exchange necessary for orderly debt servicing.

STAFF BENEFITS AND EARNINGS PER SHARE

Staff benefits expense includes prior and current service costs of retirement plans which are accrued on a current basis, contributions under the savings incentive plan, awards under the executive incentive plan, and costs of other staff benefits. No charges are reflected in earnings due to the granting or exercise of options under the stock option plans or the subscription for or purchase of stock under the stock purchase plans.

Common equivalent shares are included in the calculation of earnings per share representing shares issuable under the executive incentive compensation plan and the dilutive effect of rights and subscriptions to purchase shares under the stock option and stock purchase plans. Options and subscriptions may be for either market value or book value stock. Market value stock is Citicorp common stock that is not restricted by Citicorp as to resale but can be sold by the staff member in the market. Book value stock is Citicorp common stock that is issued at a price equal to book value per share and can be resold only to Citicorp at the per share book value at the time of sale but which has the same voting, dividend, and liquidation rights as market value stock. For outstanding options and subscriptions involving only market value shares, common equivalent shares are computed using the treasury stock method.

Under the stock option and stock purchase plans, options are also granted in tandem and subscription agreements are also entered into that give the staff member the alternative to purchase either market value or book value shares up to the end of the option or subscription period at exercise or purchase prices fixed at the date of grant or subscription.

If circumstances are such that purchase of market value shares clearly represents the economically preferable alternative to the staff member, the earnings per share calculation includes common equivalent shares representing the dilutive effect, computed by the treasury stock method, of the market value shares under option or subscription. If circumstances indicate that purchase of book value shares is the staff member's preferable alternative, the book value shares under option or subscription enter into the earnings per share calculation according to the two class method. This method recognizes the fact that there are effectively two classes of stock participating in earnings: one, outstanding shares of stock which share in all earnings; and another, book value shares under option or subscription which share only in undistributed earnings.

After issuance, book value shares are included in the weighted average number of shares of common stock outstanding used to calculate earnings per share.

Upon issuance of shares under the savings incentive, stock option, and stock purchase plans, proceeds received in excess of par value are credited to surplus. Upon issuance of treasury shares under the executive incentive compensation plan, the excess of the amount of the awards over the average cost of treasury shares is credited to surplus.

INCOME TAXES

Provision for deferred taxes is made for items of revenue and expense reported in the financial statements in different years than for tax purposes, including an appropriate provision for taxes on undistributed income of subsidiaries and affiliates.

Investment tax credits on leased equipment are recognized over a period of time related to the recovery of the lease investment which gives rise to such credits. Other investment tax credits are recognized in the year the asset is placed in service.

NOTES TO FINANCIAL STATEMENTS

1. INVESTMENT SECURITIES

	1985		1984	
	CARRYING VALUE	MARKET VALUE	[illegible]	[illegible]
US Treasury and Federal Agencies	$2,818	$2,919	$2,811	$2,701
State and Municipal	825	799	439	361
Other	6,004	6,174	3,272	3,225
TOTAL	$9,647	$9,892	$6,522	$6,337

Interest and Dividends on Investment Securities

	1985	1984	1983
US Treasury and Federal Agencies	$268	$290	$257
State and Municipal (Substantially all exempt from federal income tax)	34	31	36
Other	541	334	238
TOTAL	$843	$655	$531

2. COMMERCIAL LOANS

Commercial Loans Outstanding

	1985	1984
In Domestic Offices		
Commercial and Industrial[a]	$13,514	$16,028
Mortgage and Real Estate[a]	6,165	4,912
Loans to Financial Institutions[a]	1,353	1,003
	$21,032	$21,943
In Overseas Offices		
Commercial and Industrial[a]	$25,683	$25,235
Mortgage and Real Estate[a]	2,143	1,906
Loans to Financial Institutions	5,363	5,827
Governments and Official Institutions	4,434	4,298
	$37,623	$37,266
	$58,655	$59,209
Unearned Discount	(483)	(410)
COMMERCIAL LOANS, NET OF UNEARNED DISCOUNT	$58,172	$58,799

[illegible]

Citicorp's cash basis and renegotiated commercial loans amounted to $2,248 million, $2,418 million and $2,110 million at December 31, 1985, 1984 and 1983, respectively. Renegotiated loans are those commercial loans on which the rate of interest has been reduced as a result of the inability of the borrower to meet the original terms of the loan. Foregone revenue from cash basis and renegotiated commercial loans was as follows:

[illegible]	1985	1984	1983
Interest income that would have been accrued at original contractual rates[b]	$397	$466	$344
Amount recognized as interest income[b]	279	311	256
FOREGONE REVENUE	$118	$155	$ 88

[illegible]

3. CONSUMER LOANS

The consumer loan category represents loans managed by Citicorp's Individual Banking business. This is generally defined as including loans to individual consumers throughout the world to meet their borrowing requirements for housing, automobiles, and other personal and family purposes. The consumer category also includes indirect types of consumer finance such as dealer floor plan lending.

Consumer Loans Outstanding

In millions of dollars at year-end	1985	1984
In Domestic Offices		
Mortgage and real estate[1]	$21,719	$17,679
Installment, revolving credit and other consumer loans	27,490	21,913
	$49,209	$39,592
In Overseas Offices		
Mortgage and real estate[1]	$ 3,474	$ 2,654
Installment, revolving credit and other consumer loans	7,253	4,939
	$10,727	$ 7,593
	$59,936	$47,185
Unearned discount	(4,418)	(4,524)
CONSUMER LOANS, NET OF UNEARNED DISCOUNT	$55,518	$42,661

(1) Includes [illegible] secured primarily by real estate.

4. CHANGES IN THE ALLOWANCE FOR POSSIBLE CREDIT LOSSES

In millions of dollars	1985	1984	1983
Balance at Beginning of Year	$ 917	$771	$687
Deductions			
Commercial loan losses	$ 442	$277	$292
Commercial loan recoveries	(65)	(56)	(51)
Net commercial loan losses	$ 377	$221	$241
Consumer loan losses	$ 719	$386	$283
Consumer loan recoveries	(134)	(100)	(87)
Net consumer loan losses	$ 585	$286	$196
Additions			
Provision for possible credit losses	$1,243	$619	$520
Other (Principally from allowance balances of acquired companies and translation of overseas allowance balances)	37	34	1
BALANCE AT END OF YEAR	$1,235	$917	$771

5. PREMISES AND EQUIPMENT

Depreciation and amortization of premises and equipment was $349 million in 1985, $262 million in 1984, and $199 million in 1983. Generally, depreciation and amortization are computed on the straight line basis over the estimated useful life of the asset or the lease term.

6. PURCHASED FUNDS AND OTHER BORROWINGS

Purchased Funds and Other Borrowings, Original Maturities of Less Than One Year

(Dollars in Millions)	1985	1984	1983
Federal funds purchased and securities repurchase agreements (in domestic offices)[1]			
Amount outstanding at year end	$ 7,421	$ 9,597	$ 8,596
Average outstanding during the year	$10,064	$ 9,329	$ 8,379
Maximum outstanding at any month end	$10,769	$10,520	$10,096
Commercial paper[2]			
Amount outstanding at year end	$ 7,172	$ 4,976	$ 4,087
Average outstanding during the year	$ 4,977	$ 4,970	$ 3,766
Maximum outstanding at any month end	$ 7,172	$ 6,883	$ 4,578
Other funds borrowed[3]			
Amount outstanding at year end	$12,023	$ 9,817	$ 9,616
Average outstanding during the year	$10,405	$ 9,497	$ 8,498
Maximum outstanding at any month end	$ 023	$ 9,998	$10,139

(1) Weighted average interest rate was 8.42% during 1985, 11.42% during 1984 and 9.46% during 1983; 8.43% at year end 1985.

(2) Weighted average interest rate was 8.34% during 1985, 11.14% during 1984 and 9.14% during 1983; 8.29% at year end 1985, 9.63% at year end 1984 and 9.87% at year end 1983.

(3) Weighted average interest rate was 9.55% during 1985.

7. LONG-TERM DEBT

Long-Term Debt, Original Maturities of One Year or More[a]

	[illegible] Interest Rate Obligations	[illegible] Floating Interest Rate Obligations	1985 TOTAL	1984 TOTAL
Parent Company				
Due within 1 year	$ 1,513	$1,519	$ 3,032	$ 859
Due 1-2 years	25	167	417	2,813
Due 2-3 years	863	568	1,431	572
Due 3-4 years	1,042	284	1,326	336
Due 4-5 years	967	48	1,015	1,113
Due 5-10 years	1,430	446	1,876	1,041
Due 10-15 years	486	182	668	459
Due 15 years and over	584	939	1,523	674
	$ 7,135	$4,153	$11,288	$ 7,867
Subsidiaries				
Due within 1 year	$ 883	$ 446	$ 1,329	$ 854
Due 1-2 years	490	95	585	1,125
Due 2-3 years	606	66	672	599
Due 3-4 years	171	227	398	410
Due 4-5 years	347	78	425	373
Due 5-10 years	400	703	1,103	1,107
Due 10-15 years	11	503	514	676
Due 15 years and over	–	2	2	–
	$ 2,908	$2,120	$ 5,028	$ 5,126
TOTAL	$10,043	$6,273	$16,316	$12,993

[a] Maturity classifications based upon contractual maturities. Certain debt is repayable at the option of the holder due to required mandatory sinking fund payments or due [illegible]

Fixed rate long term debt matures over the period to 2015. The interest rates on fixed rate debt issues ranged from 4.25% to 21.00% at December 31, 1985 and 4.25% to 19.9[illegible] at December 31, 1984. The weighted average interest rates were [illegible]% and 11.75% at December 31, 1985 and 1984, respectively.

Floating rate long term debt matures [illegible] the period to 2035. The interest rates are determined periodically by formulas based on certain money market rates or, in certain instances, by minimum interest rates as specified in the agreements governing the respective issues. The interest rates on floating rate debt issues ranged from 6.10% to 18.50% at December 31, 1985 and 6.60% to 19.80% at December 31, 1984. The weighted average interest rates were 9.99% [illegible]% at December 31, 1985 and 1984, respectively.

At December 31, 1985 and 1984, $739 million and $816 million, respectively, of subsidiary long term debt was not guaranteed by Citicorp. The weighted average interest rates on such long-term debt were 12.43% and 13.14% at December 31, 1985 and 1984, respectively. Substantially all long term debt issued by subsidiaries not guaranteed by Citicorp is secured by the assets of the subsidiary.

At December 31, 1985 and 1984, outstanding 5¼% convertible subordinated notes due in 20[illegible] were $9 million and $12 million, respectively. During 1985 noteholders converted $3 million of convertible notes into 69,527 shares of common stock (none in 1984). During 1984, $337 million was retired pursuant to an offer to repurchase these notes, the gain on which was not material. The notes are convertible at the option of the holder into Citicorp common stock at a conversion price of $41 per share, subject to adjustment in certain events.

Certain of the agreements under which long term debt obligations were issued prohibit Citicorp, under certain conditions, from paying dividends in shares of Citibank capital stock and from creating encumbrances on such shares.

The prior year's disclosure of convertible notes and long-term debt has been reclassified to conform with the current financial statement presentation.

8. SUBORDINATED CAPITAL NOTES

IN MILLIONS OF DOLLARS AT YEAR-END	1985	1984
Floating rate subordinated capital notes due 1996	$1,050	$1,300
12½% subordinated capital notes due 1996	349	349
Floating rate subordinated capital notes due 1997	500	–
	$1,899	$1,649

Subordinated capital notes are unsecured subordinated obligations of Citicorp subsidiaries and are unconditionally guaranteed on a subordinated basis by Citicorp. The interest rates on the floating rate note issues are determined periodically by formulas based on certain money market rates, or in certain instances, by minimum interest rates as specified in the agreements governing the respective issues. During 1985, $250 million of floating rate subordinated capital notes due 1996 were repurchased, the gain on which was not material, and an additional $500 million of floating rate subordinated capital notes due 1997 were issued. The interest rates on floating rate note issues ranged from 7.938% to 8.520% at December 31, 1985 and 8.375% to 10.375% at December 31, 1984. The weighted average interest rates were 8.208% at December 31, 1985 and 9.322% at December 31, 1984.

At maturity, the notes will be exchanged for a security of Citicorp that qualifies as primary capital then having a value equal to the principal amount of the notes, or under certain circumstances redeemed, in whole or in part, for cash. At the option of the issuer, the exchange may be for common stock, nonredeemable preferred stock or other marketable permanent primary capital securities of Citicorp. Alternatively, the issuer will undertake to sell capital securities on behalf of the holders who elect to receive cash for capital securities upon an exchange of the notes in an amount sufficient to pay the principal of such notes. Because the type of securities to be issued at maturity will be at the option of the Citicorp subsidiary that issued the notes and because the amount of securities to be issued will depend on their future market values, the amount and type of securities to be issued at maturity of the notes cannot be determined. As a result, some dilution of earnings per share may occur.

The agreements under which the notes are issued prohibit Citicorp, under certain conditions, from paying dividends in shares of Citibank capital stock.

9. REDEEMABLE PREFERRED STOCK

At December 31, 1985 and 1984, 400,000 shares of non-voting redeemable preferred stock were issued and outstanding, subject to redemption at a price of $100 per share through a mandatory sinking fund. In 1990, $1 million must be retired with the remaining balance of $39 million being retired in years 1991 to 2013. Dividends, which are cumulative, are payable semiannually. Beginning in 1985 the dividend rate is determined every three years until 2009 by a formula based on certain money market rates. Prior to November 1985 dividends were paid at a fixed annual rate. Dividends amounted to $10.91 per share in 1985 and $11.00 per share in 1984 and 1983. Citicorp may be required to repurchase the preferred stock at $100 per share if loans are not extended to the preferred stockholder under certain circumstances.

10. PREFERRED STOCK

IN MILLIONS OF DOLLARS AT YEAR END	1985	1984
Adjustable Rate Preferred Stock, Second Series, 3,900,000 shares	$ 390	$390
Adjustable Rate Preferred Stock, Third Series, 1,500,000 shares	150	150
Price Adjusted Rate Preferred Stock, Fourth Series, 1,000,000 shares	100	100
Money Market Cumulative Preferred Stock, Series 5A through 5G, 1,150 shares	575	–
	$1,215	$640

Dividends on the Second, Third, and Fourth Series of preferred stock are cumulative and payable quarterly at rates determined quarterly by formulas based on interest rates of certain U.S. Treasury obligations. Dividends on the Second and Third Series of preferred stock are subject to certain minimum and maximum rates as specified in the agreements governing the respective instruments. The weighted average dividend rates on the Second, Third, and Fourth Series were 7.125%, 8.750%, and 7.718%, respectively, for 1985.

Dividends on Money Market Cumulative Preferred Stock, Series 5A through 5G, are cumulative. Rates are determined every 49 days by auction unless Citicorp fails to pay any dividend or redeem any shares for which it has given notice of redemption, in which case the dividend rate will be set at 150% of London Interbank Offered Rate (LIBOR). The maximum dividend rate in any auction is 110% of the 60-day "AA" Composite Commercial Paper Rate. During 1985, the weighted average dividend rates on Money Market Cumulative Preferred Stock Series 5A, 5B, 5C, 5D, 5E, 5F and 5G, which were issued at various dates during the year, were 5.434%, 5.424%, 5.669%, 5.683%, 5.750%, 6.125%, and 6.125%, respectively.

Citicorp may, at its option, redeem the Second Series on or after February 28, 1988 at $103 per share through February 28, 1993 and at $100 per share thereafter; may, at its option, redeem the Third Series on or after September 1, 1988 at $103 per share until August 31, 1989 and at amounts declining thereafter to $100 per share beginning September 1, 1992; and may, at its option, redeem the Fourth Series on or after February 15, 1986 at $100 per share.

Citicorp may, at its option, redeem the Money Market Cumulative Preferred Stock at $515,000 per share, plus accrued dividends, if redeemed within one year after the issuance date and at amounts declining to $500,000 per share if redeemed four or more years after the issuance date. These shares are also redeemable at the option of Citicorp, in whole but not in part, at $500,000 per share, plus accrued dividends, in the event that the dividend rate should equal or exceed the 60-day "AA" Composite Commercial Paper Rate.

All series rank prior to Common Stock as to dividends and liquidation and do not have general voting rights.

Authorized preferred stock (issuable as either redeemable or nonredeemable) was 20 million shares at December 31, 1985 and 1984. At December 31, 1985 and 1984, 6,401,150 shares and 6,400,000 shares, respectively, of nonredeemable preferred stock were issued and outstanding and 400,000 shares of redeemable preferred stock were issued and outstanding.

11. COMMON STOCK

At December 31, 1985 and 1984, authorized common stock was 325 million shares. The outstanding shares at December 31, 1985 and 1984 include 3.0 million and 2.2 million book value shares, respectively, issued in connection with certain staff benefit plans. Under the terms of the plans the payment for book value shares sold back to Citicorp can be settled in cash or in market value shares at the option of Citicorp.

At December 31, 1985, shares were reserved for issuance as follows: on conversion of convertible notes, 0.2 million shares; under the savings incentive plan, 12.4 million book value shares; under the 1973 stock option plan, a maximum of 3.7 million shares if issued at market value and a maximum of 5.9 million shares if issued at book value; under the 1983 stock option plan, under which options may be granted in tandem, a maximum of 9.7 million shares if issued at market value and a maximum of 14.7 million shares if issued at book value; under the stock purchase plan, 5.2 million shares; and under the executive incentive compensation plan, 1.1 million shares.

12. STAFF BENEFITS

Retirement Plans. There are a number of pension plans covering substantially all staff members. The cost of the principal plan amounted to $8 million in 1985, $8 million in 1984, and $44 million in 1983. In 1984, revisions of certain actuarial assumptions were made to more closely reflect recent experience and future expectations. If the previous set of assumptions, principally a lower assumed rate of return and a lower assumed annual rate of salary increase, were used, pension expense for 1984 would have been approximately $38 million greater ($21 million after taxes) than reported. The costs of all benefits under the plan are accrued and funded on a current basis. The actuarial cost method used for pension cost determination is the Frozen Initial Liability Method.

A comparison of the actuarial value of accumulated plan benefits and plan net assets for the principal benefit plan as of the most recent actuarial valuation date is presented below.

IN MILLIONS OF DOLLARS	JANUARY 1, 1985	1984
Retirement benefits earned by employees		
Vested	$378	$336
Non-vested	52	46
	$430	$382
Plan Net Assets Available for Benefits, at market	$932	$891

Retirement benefits earned by employees represent the present value of accumulated benefits earned based upon years of service. The present value of accumulated benefits earned was determined using a rate of return of 9.5% for active plan members and 12.0% for pensioners and former employees with deferred vested benefits.

Savings Incentive Plan. Under the Savings Incentive Plan, eligible staff members receive awards equal to 3% of their covered salary. Staff members have the option of receiving their award in cash or deferring some or all of it in various investment funds. Citicorp

grants an additional award equal to the amount deferred by the employee. Several investment options are available including Citicorp market value shares, which the fund acquires in the open market, and book value shares issued by Citicorp. The expense associated with the plan amounted to $48 million in 1985, $44 million in 1984, and $36 million in 1983.

Stock Option Plans. During 1983, the shareholders of Citicorp approved a new stock option plan, which became effective March 31, 1983. No further options may be granted pursuant to previous stock option plans. Options previously granted under a stock option plan that became effective April 2, 1973 and was extended and amended effective April 1, 1977 do not fully expire until 1992. Under both the 1983 plan and 1973 plan, as extended and amended, options have been granted to key staff members for terms up to 10 years to purchase common stock at not less than the fair market value of the shares at the date of grant. In addition, the 1983 plan and 1973 plan, as extended and amended, provide for the granting in tandem of options to purchase market value shares of common stock at not less than the market value at the date of grant or a proportionate number of book value shares of common stock at not less than the book value per share at the date of grant. Such a proportionate number of book value shares is determined based on the ratio of market value to book value per share at the date of grant. Under the 1983 plan and 1973 plan, 50% of the options granted are exercisable beginning on the first anniversary and 50% beginning on the second anniversary of the date of grant.

In the captions "shares under option" and "options granted" in the accompanying table, options granted in tandem are included on the basis that represents the economically preferable alternative to the staff member.

At December 31, 1985, options to purchase 5,019,180 shares were exercisable. At that date, 4,654,337 shares, were available to grant options to purchase market value shares and 4,573,801 shares (a proportionate number based on the price ratio of book value shares to market value shares) were available to grant options to purchase book value shares. Additional shares may become available for options to purchase market value shares under the plan to the extent presently outstanding options under the 1983 plan terminate or expire unexercised. As the number of market value shares available for options so increases, or if the price ratio of market value shares to book value shares increases, the number of book value shares available for options will increase proportionately, subject to a maximum of 15 million shares.

CHANGES IN OPTIONS AND SHARES UNDER OPTIONS

	NUMBER OF SHARES	OPTION PRICE PER SHARE
Shares under option at		
December 31, 1985	7,819,399	$18 to $50
December 31, 1984	7,453,492	$18 to $42
Options granted		
1985	2,020,961	$41 to $50
1984	1,879,495	$31 to $39
1983	1,635,364	$36 to $39
Options exercised		
1985	1,517,798	$18 to $44
1984	526,824	$20 to $42
1983	827,318	$18 to $42

Stock Purchase Plan. The plan permits all eligible staff members (two years employment with Citicorp or its subsidiaries) to purchase shares within a specified period not to exceed 24 months under agreements entered into with all such staff members from time to time at the fair market value or book value per share at the dates of the agreements.

Agreements aggregating $77 million were entered into on June 30, 1984. Outstanding subscriptions, which aggregated $36 million at December 31, 1985, may be used for the purchase of market value shares at $30.758 per share, book value shares at $43.788 per share or a combination of both. 1,006,109 market value shares and 899 book value shares were purchased in 1985, and 193,372 market value shares and 526 book value shares were purchased in 1984 under the terms of the June 30, 1984 agreements. These agreements expire on March 31, 1986.

Under agreements entered into on June 30, 1982 for the purchase of market value shares at $25.125 per share and book value shares at $35.637 per share, 785,583 market value and 50,364 book value shares were purchased in 1984, 474,637 market value and 306 book value shares were purchased in 1983, and 289,043 market value and 461 book value shares were purchased in 1982. These agreements expired on March 31, 1984.

Executive Incentive Compensation Plan. Under the Executive Incentive Compensation Plan, awards are made to key staff members, payable at the election of the participants, in cash, or in market value or book value shares of Citicorp common stock, in three installments or on a deferred basis.

The aggregate amount of the awards was approximately $14 million in 1985, $11 million in 1984, and $17 million in 1983.

13. INCOME TAXES

IN MILLIONS OF DOLLARS, FOR THE YEAR	1985	1984	1983
Domestic			
Current			
Federal*	$ 30	$ 28	$ 20
State and local	52	35	27
	$ 82	$ 63	$ 47
Deferred			
Federal	$ 56	$ 45	$ 80
State and local	(19)	6	7
	$ 37	$ 51	$ 87
Total domestic	$119	$114	$134
Foreign (substantially current)	599	540	612
TOTAL PROVISION	$718	$654	$746

Within the total provision, the tax effect of investment securities transactions amounted to a provision of $23 million in 1985 and $7 million in 1984 and $6 million in 1983.

Although not affecting the total provision, current income tax payments may differ from the amounts shown as current as a result of the final determination as to the timing of certain deductions and credits and will differ because of the availability of investment tax credits.

As a U.S. corporation, all of Citicorp's foreign pre-tax earnings are subject to domestic taxation currently if earned by a foreign branch, or when earnings are effectively repatriated if earned by a foreign subsidiary or affiliate. For 1985, foreign pre-tax earnings represented 67% of consolidated pre-tax income (approximately 70% in 1984 and 73% in 1983). In addition, certain of Citicorp's domestic income is subject to foreign income tax where the payor of such income is domiciled overseas.

Deferred taxes result from timing differences in the recognition of revenue and expense for tax and financial accounting purposes.

COMPONENTS OF DEFERRED TAXES

IN MILLIONS OF DOLLARS, FOR THE YEAR	1985	1984	1983
Lease financing transactions	$ 59	$ 86	$ (4)
Credit loss deduction	(62)	(9)	(27)
Interest income	(25)	(6)	(1)
Domestic taxes on overseas income:			
Foreign tax credits	—	—	34
Other	46	(67)	(43)
Investment tax credits	—	—	63
Other	19	47	65
TOTAL	$ 37	$ 51	$ 87

ANALYSIS OF EFFECTIVE RATE

FOR THE YEAR	1985	1984	1983
U.S. federal income tax rate	46.0%	46.0%	46.0%
Changes from statutory rate resulting from:			
Tax-exempt interest income	(4.7%)	(5.2%)	(2.6%)
Income subject to tax at capital gains rates	(.4%)	(.6%)	(.9%)
State and local income taxes, net of U.S. federal income tax benefit	1.0%	1.5%	1.1%
Taxes on income of overseas subsidiaries	(.4%)	.8%	1.8%
Income from 20%- to 50%-owned affiliates included on an after-tax basis	(1.2%)	(1.6%)	(1.7%)
Translation adjustment on foreign branch taxes	.3%	(.4%)	3.8%
Other	1.2%	1.9%	(1.0%)
TOTAL*	41.8%	42.4%	46.5%

*U.S. Federal income taxes in these analyses do not include amounts which, in the opinion of management, represent a de facto additional Federal tax burden that is paid currently. Banks effectively incur this tax in the form of earnings remitted to the U.S. Treasury by the Federal Reserve, representing the Fed's investment earnings on the non-interest bearing reserves that banks are required to maintain with Federal Reserve Banks. For Citicorp, it is estimated that this de facto additional tax approximated $68 million, $59 million and $66 million for the years 1985, 1984 and 1983, respectively, based on average reserve deposits of $823 million, $738 million and $866 million in 1985, 1984 and 1983, respectively. The total effective tax rate for such years, adjusted for these amounts and including an equivalent adjustment to increase income before income tax, would be 44.1%, 44.5% and 48.6%, respectively. The de facto additional tax is calculated based on Citicorp's bank subsidiaries' average reserve deposits as a percentage of average total Federal Reserve assets, applied to the earnings remitted to the U.S. Treasury by the Federal Reserve. While no single method can precisely quantify this additional Federal tax burden, Citicorp believes the foregoing method is an appropriate estimate of such tax burden.

Not included above is the effect of investments in tax-exempt state and municipal securities, assets which yield lower rates of interest than would be the case if the income was taxable.

14. EARNINGS PER SHARE

The accompanying table shows the calculation of earnings per share on common and common equivalent shares for net income after deduction of dividends on redeemable preferred stock and preferred stock. Shares issuable under stock option grants and stock purchase plan subscriptions which give staff members the alternative to purchase either market value or book value shares are either included as common equivalent shares or enter into the earnings per share calculation according to the two-class method based upon the economically preferable alternative to staff members, as further described in the Statement of Accounting Policies.

Calculation of Earnings Per Share

IN MILLIONS EXCEPT PER SHARE AMOUNTS	1985	1984	1983
Net Income Available for Common Stockholders			
a. Distributed portion (dividends)	$290	$259	$234
b. Undistributed portion	645	571	589
TOTAL	$935	$830	$823
Shares			
Weighted average common shares outstanding—Market value	125.4	123.4	123.1
Weighted average common shares outstanding—Book value	2.5	2.0	1.7
Common stock equivalents[1]	1.8	1.1	1.2
c. Shares applicable to distributed portion	129.7	126.5	126.0
Book value shares issuable under stock option and stock purchase plans	2.6	3.2	1.5
d. Shares applicable to undistributed portion	132.3	129.7	127.5
Earnings Per Share			
a+c Distributed portion	$2.24	$2.05	$1.86
b+d Undistributed portion	4.88	4.40	4.62
TOTAL	$7.12	$6.45	$6.48

(1) Common stock equivalents represent shares issuable under the executive incentive compensation plan and the dilutive effect of market value shares issuable under stock option and stock purchase plans computed using the treasury stock method

The fully diluted calculation assumes conversion of all outstanding convertible notes and the maximum dilutive effect of common stock equivalents. The number of shares issuable on conversion of the notes (0.2 million in 1985, 2.4 million in 1984, and 8.5 million in 1983) and the additional common stock equivalents (0.1 million in 1985 and 0.2 million in 1984) are added to the number of shares included in the calculation (resulting in a total of 132.6 million shares in 1985, 132.3 million shares in 1984, and 136.0 million shares in 1983), and the related after-tax interest expense ($0.3 million in 1985, $3.7 million in 1984, and $10.8 million in 1983) is eliminated.

15. GEOGRAPHIC DISTRIBUTION OF REVENUE, EARNINGS AND ASSETS

Citicorp attributes total revenue, income before taxes, net income and average total assets to operations based on the domicile of the customer. U.S. possessions are included in their respective geographic areas.

Because of the integration of global activities, it is not practicable to make a precise separation, and various assumptions must be made in arriving at allocations and adjustments to be used in presenting this data.

The principal allocations and adjustments are: (1) charges for all funds employed that are not generated locally are calculated on the amount and nature of the assets and based on a marginal cost of funds concept; Citicorp stockholders' equity is treated as generated and earned based on each area's percentage of total assets; (2) allocation of expenses incurred by one area on behalf of another, including administrative costs, based on methods intended to reflect services provided; (3) allocation of tax expenses; (4) allocation of the difference between actual net credit losses and the provision for possible credit losses; and (5) allocation of corporate staff costs (other than those charged to the core businesses) and other corporate items including certain start-up activities. The prior years' disclosures have been reclassified to conform with the current year's presentation.

The Securities and Exchange Commission requires that an allowance for loan losses applicable to loans related to foreign activities be disclosed in a note to the financial statements. Citicorp makes no such allocation, and no portion of the allowance for possible credit losses is restricted to any individual loans or groups of loans. For the purpose of meeting the requirement under generally accepted accounting principles to calculate earnings and assets attributable to foreign operations, $486 million at December 31, 1985, $350 million at December 31, 1984 and $301 million at December 31, 1983 of the allowance is allocated to foreign operations. In the judgment of management, such allocation is not meaningful, since the entire amount of the allowance is available to absorb losses with respect to both domestic and foreign loans.

Geographic Distribution of Revenue, Earnings and Assets

IN MILLIONS OF DOLLARS	TOTAL REVENUE[1]			INCOME BEFORE TAXES			NET INCOME			AVERAGE TOTAL ASSETS		
	1985	1984	1983	1985	1984	1983	1985	1984	1983	1985	1984	1983
North America[2][4]	$4,938	$3,653	$2,980	$ 762[4]	$ 590[4]	$ 571[4]	$463	$367	$320	$ 85,653	$ 70,407	$ 55,668
Caribbean, Central and South America[3]	1,183	919	1,014	403	277	452	245	177	234	19,094	18,785	18,734
Europe, Middle East and Africa	1,567	1,330	1,176	364	391	284	191	208	156	33,899	31,197	30,819
Asia/Pacific	788	717	713	187	286	299	99	138	150	21,859	22,242	22,702
TOTAL	$8,476	$6,619	$5,883	$1,716	$1,544	$1,606	$998	$890	$860	$160,505	$142,631	$127,923

(1) Includes Net Interest Revenue and Fees, Commissions and Other Revenue.
(2) Includes amounts attributed to United States operations (in 1985, 1984 and 1983, respectively as follows: total revenue, $4,843 million, $3,556 million and $2,904 million; income before taxes, $728 million, $547 million and $540 million; net income, $453 million, $343 million and $305 million; and average total assets, $82,246 million, $67,534 million and $52,966 million.
(3) Includes amounts attributed to Brazil operations (in 1985, 1984 and 1983, respectively as follows: total revenue, $375 million, $370 million and $401 million; income before taxes, $102 million, $241 million and $281 million; net income, $170 million, $140 million and $141 million; and average total assets denominated in cruzeiros and other currencies, $6,375 million, $6,271 million and $6,109 million.
(4) In North America, income before taxes includes approximately $112 million in 1985, $76 million in 1984 and $69 million in 1983 of tax-exempt income, reducing the federal income tax provision attributed to the United States.

16. NON-FUNDS RELATED FINANCIAL PRODUCTS

Citicorp offers various financial products to its customers to meet their needs for liquidity, credit enhancement, foreign exchange, and interest rate protection. Many of these products were developed in response to the growing sophistication of the financial markets and customers' needs for flexible ways to manage funding costs and foreign exchange exposure. In addition, the offering of these products may serve to reduce rather than increase Citicorp's own exposure to movements in interest and foreign exchange rates.

All products offered by Citicorp are subject to its normal stringent credit standards, financial controls, and risk limiting and monitoring procedures. Many of these products do not entail present or future funded asset or liability positions but are instead in the nature of commitments, guarantees, or executory contracts.

Following are discussions of certain significant products with indications of gross volumes.

Loan Commitments. At December 31, 1985, Citicorp and its subsidiaries had outstanding unused commitments of $34.4 billion to make or purchase loans, to purchase third party receivables, to provide note issuance facilities or revolving underwriting facilities, or to extend credit in the form of lease financing. Substantially all of these commitments are contingent upon customers' maintaining specific credit standards. In addition, Citicorp and its subsidiaries are obligated under various recourse provisions related to sales of loans or sales of participations in pools of loans. At December 31, 1985, the maximum obligation under all recourse provisions was $1.7 billion, of which approximately 81% relates to sales of residential mortgages. Estimated losses pursuant to these obligations are not expected to be material.

Standby Letters of Credit. Standby letters of credit are used in various transactions to enhance the credit standing of Citibank customers. Standby letters of credit are irrevocable assurances that Citibank will make payment in the event that a Citibank customer cannot perform its obligations to third parties.

Citibank issues standby letters of credit on behalf of its customers for four primary purposes: to ensure contract performance and irrevocably assure payment by the customer under supply service, and maintenance contracts or construction projects; to provide a payment mechanism for a customer's third party obligations or act as a substitute for an escrow account; to assure payment by a foreign reinsurer to a domestic insurer; and to assure payment of specified financial obligations of a customer. Fees are recognized ratably over the term of the standby letter of credit. Losses have not been material.

At December 31, 1985, $22.4 billion of standby letters of credit were outstanding, including $6.5 billion supported by marketable collateral or participated to other financial institutions. Approximately 13% of total outstanding standby letters of credit were issued to support reinsurance transactions, and 40% were issued to assure payment of customers' specified financial obligations. The remainder ensure contract performance or provide a payment mechanism.

Municipal Bond Insurance. AMBAC Indemnity Corporation, a majority owned subsidiary of Citibank, provides default insurance on bonds issued by U.S. municipalities. Under municipal bond insurance policies, if a bond issuer defaults on an insured issue, the insurer promises to pay the principal and interest in accordance with the original payment schedule. Acceleration of payment under the insurance policy by the insured is not permitted.

AMBAC's insurance underwriting procedures include a rigorous credit review along with an ongoing risk monitoring process. AMBAC limits its exposure to losses by underwriting only investment grade municipal bonds, by diversifying its risk geographically, by type of bond and by single issue limitations, and by obtaining reinsurance. Premiums are recognized over the term of the insurance policy. Reserves for losses are provided for when default by the bond issuer is reasonably anticipated; such losses have not been material. At December 31, 1985, the principal amount of municipal bond insurance in force retained by AMBAC was $29.1 billion. The municipal bonds insured have a weighted average life of 17.7 years.

Interest Rate and Foreign Exchange Products. Citicorp offers interest rate and foreign exchange futures, forwards, options and swaps which enable customers to transfer, modify or reduce their interest rate and foreign exchange risks. Futures and forward contracts are commitments to buy or sell at a future date a financial instrument or currency at a contracted price and may be settled in cash or through delivery. Swap contracts are commitments to settle in cash at a future date or dates based on differentials between specified financial indices as applied to a notional principal amount. Option contracts give the buyer for a fee the right but not the obligation to buy or sell within a limited time a financial instrument or currency at a contracted price and may also settle in cash based on differentials between specified indices.

In most cases, Citicorp manages the exposures related to these products as part of its overall interest rate and foreign exchange trading activities, which include both funded asset and liability positions and non funded positions. For example, Citicorp may hold a security in its trading portfolio and at the same time have futures contracts to sell that security. The losses on one position may substantially offset gains on the other position. These products are also utilized by Citicorp to reduce exposures outside the trading portfolios, as hedges of interest rate gaps and foreign exchange positions.

The market and credit risks inherent in traditional banking services are also present in these specialized financial products, as are the various operating risks that exist in all financial activities. Notional principal amounts are often used to express the volume of these transactions, but do not represent the much smaller amounts potentially subject to risk.

Market risk is the exposure created by fluctuations in interest and foreign exchange rates, and is a function of the type of product, the volume of the transaction, the tenor and terms of the agreement, and the volatility of the underlying interest rate or exchange rate. Market risk is affected by the mix of the aggregate portfolio and the extent to which positions have offsetting exposures. The market risk of an interest rate swap, for example, will be reduced by the presence of securities, financial futures, or other interest rate swap positions with offsetting exposures. Citicorp manages its trading activities in these specialized financial products on a market value basis which recognizes in earnings the gains or losses resulting from changes in market

est or exchange rates. Trading limits and monitoring procedures are used to control the overall exposure to market risk.

Credit risk is the exposure to loss in the event of non-performance by the other party to a transaction, and is a function of the ability of the counterparty to honor its obligations to Citicorp. For these specialized financial products the amounts due from or due to the counterparty will change as a result of movements in market rates, and the amount subject to credit risk is limited to this fluctuating amount. Citicorp controls credit risk through credit approvals, limits and monitoring procedures, and the recognition in earnings of unrealized gains on these transactions is dependent on management's assessment as to collectibility.

Citicorp has significant presence in the markets for these interest rate and foreign exchange products. At December 31, 1985, the notional principal amount of Citicorp's outstanding interest rate swaps was $36.4 billion; commitments to purchase and sell money market instruments or securities and commitments to settle against financial indices under interest rate futures, forward and option contracts were $38.3 billion; commitments to purchase and sell currencies under foreign currency spot, forward and option transactions were $167.5 billion. These amounts are gross volume indicators only and do not reflect the extent to which positions may offset one another. As discussed above, the amounts potentially subject to market and credit risk are substantially smaller than the gross volumes indicated here.

17. COMMITMENTS AND CONTINGENT LIABILITIES

Citicorp and its subsidiaries are obligated under a number of noncancelable leases for premises and equipment, most of which have renewal or purchase options. Minimum rental commitments on noncancelable leases, net of sublease income, are $186 million in 6, $181 million in 1987, $149 million in 1988, $133 million in 1989, million in 1990, and $460 million thereafter, totalling $1,224 million. ntal expense was $256 million in 1985 net of $55 million sublease rental income, $209 million in 1984 net of $53 million sublease rental income, and $194 million in 1983 net of $49 million sublease rental income.

At December 31, 1985, certain investment securities, trading account assets, and other assets with a carrying value of $13,347 million were pledged as collateral for borrowings, to secure public and trust deposits and for other purposes.

Various legal proceedings are pending against Citicorp and its subsidiaries. Management of Citicorp considers that the aggregate liability, if any, resulting from these proceedings will not be material.

18. STOCKHOLDER'S EQUITY OF CITIBANK, N.A.

Authorized capital stock of Citibank was 40 million shares at December 31, 1985, 1984 and 1983.

Changes in Stockholder's Equity

MILLIONS OF DOLLARS	1985	1984	1983
Balance at Beginning of Year	$6,318	$5,924	$5,485
Additions			
Net income	$ 807	$ 777	$ 753
Contribution from Parent Company	405	—	—
Other additions, net	10	—	7
	$1,222	$ 777	$ 763
Deductions			
Dividends declared	$ 360	$ 292	$ 272
Foreign currency translation	29	42	30
Write-off of intangibles associated with acquisition of subsidiaries and affiliates	114	30	22
Other deductions, net	—	19	—
	$ 503	$ 383	$ 324
BALANCE AT END OF YEAR	$7,037	$6,318	$5,924

Citibank charges retained earnings with the amount of goodwill associated with investments by Citibank in overseas subsidiaries and affiliates to the extent required to carry the investments at a value not in excess of underlying book value. In accordance with generally accepted accounting principles, such charges are not reflected in the Citicorp financial statements, and the related amounts, net of amortization, aggregating $256 million, $109 million, and $101 million at December 31, 1985, 1984, and 1983, respectively, are included in other assets in the Citicorp consolidated balance sheet. Citicorp's equity investment in Citibank amounted to $7,293 million, $6,427 million, and $6,025 million at December 31, 1985, 1984 and 1983, respectively.

19. CITICORP (Parent Company Only) Condensed Balance Sheet

IN MILLIONS OF DOLLARS	DECEMBER 31 1985	DECEMBER 31 1984
Assets		
Deposits with Subsidiary Banks, principally interest bearing	$ 4,073	$ 4,318
Investment Securities at Cost (Market value $111 in 1985 and $259 in 1984)	117	280
Investments in and Advances to Subsidiaries Other Than Banks	17,599	13,665
Investments in and Advances to Citibank, N.A. and Other Subsidiary Banks	10,851	7,746
Other Assets	253	217
TOTAL	$32,893	$26,226
Liabilities and Stockholders' Equity		
Purchased Funds and Other Borrowings	$11,463	$ 9,064
Advances from Subsidiaries	998	1,494
Other Liabilities	1,339	1,335
Long-Term Debt and Redeemable Preferred Stock (Notes 7 and 9)	11,328	7,907
Stockholders' Equity	7,765	6,426
TOTAL	$32,893	$26,226

Condensed Statement of Income

IN MILLIONS OF DOLLARS	1985	1984	1983
Revenue			
Dividends from Subsidiary Banks	$ 360	$ 292	$ 272
Interest from Subsidiaries	1,295	1,421	1,094
Other (principally interest on investment securities)	34	46	58
	$1,689	$1,759	$1,424
Expense			
Interest on Other Borrowed Money	$ 857	$ 907	$ 682
Interest and Fees Paid to Subsidiaries	167	316	358
Interest on Long-Term Debt	1,005	802	583
Other Expense	11	9	7
	$2,040	$2,034	$1,630
Loss before Taxes and Equity in Undistributed Net Income of Subsidiaries	$ (351)	$ (275)	$ (206)
Income Tax Benefit—Current	367	261	202
Equity in Undistributed Net Income of Subsidiaries	982	904	864
NET INCOME	$ 998	$ 890	$ 860

Condensed Statement of Changes in Financial Position

IN MILLIONS OF DOLLARS	1985	1984	1983
Funds Provided			
Net Income	$ 998	$ 890	$ 860
Deduct Equity in Undistributed Net Income of Subsidiaries	982	904	864
Funds Derived from Operations	$ 16	$ (14)	$ (4)
Increase in			
Purchased Funds and Other Borrowings	2,399	1,028	655
Long-Term Debt and Redeemable Preferred Stock	3,421	1,087	2,814
Preferred Stock	575	100	540
Decrease in			
Deposits with Subsidiary Banks	245	1,203	—
Investment Securities	163	—	99
Investments in and Advances to Subsidiaries	—	—	191
Other, Net	87	308	—
TOTAL	$6,906	$3,712	$4,295
Funds Used			
Cash Dividends Declared	$ 353	$ 319	$ 271
Increase in			
Deposits with Subsidiary Banks	—	—	3,834
Investment Securities	—	48	—
Investments in and Advances to Subsidiaries	6,057	2,288	—
Decrease in			
Advances from Subsidiaries	496	1,057	140
Other, Net	—	—	50
TOTAL	$6,906	$3,712	$4,295

Various legal restrictions limit the extent to which certain subsidiaries of Citicorp can supply funds to Citicorp or its other subsidiaries and affiliates. In addition, the approval of the Comptroller of the Currency is required if total dividends declared by a national bank in any calendar year exceed the bank's net profits (as defined) for that year combined with its retained net profits for the preceding two calendar years. Under the formula as it applies to Citicorp's national bank subsidiaries (which at December 31, 1985 had combined net assets of approximately $8.6 billion), Citicorp can receive dividends from such bank subsidiaries in 1986 without approval of the Comptroller of the Currency of approximately $1.4 billion, plus an additional amount equal to their net profits for 1986 up to the date of any such dividend declaration.

INFLATION ADJUSTED DATA SUPPLEMENT

The accompanying data have been prepared according to guidelines issued by the Financial Accounting Standards Board to illustrate certain aspects of how inflation affects Citicorp. The data are intended to supplement, but not replace, the basic historical financial statements. The audited financial statements and other traditional financial data included in this report continue to represent Citicorp's actual operating results. The inflation adjusted data reflect the effects of general inflation using the historical cost/constant dollar method, with the U.S. Consumer Price Index for All Urban Consumers being used to show data in average 1985 dollars. Current cost information, which shows the effect of changing prices of specific goods and services used by a company, has not been presented since such information does not differ significantly from the constant dollar data.

The assets and liabilities of a financial institution are primarily monetary in nature. As such, they represent obligations to pay or receive fixed and determinable amounts of money which are not affected by future changes in prices. During periods of inflation, monetary assets lose value in terms of purchasing power, while monetary liabilities have corresponding purchasing power gains. The assets of a financial institution also include items such as trading account assets and premises and equipment that are considered nonmonetary and, therefore, do not give rise to purchasing power losses in the inflation-adjusted data.

1985 Constant Dollar Data

IN MILLIONS OF DOLLARS	
Net income, as reported in the consolidated statement of income	$998
Adjustment to restate depreciation for the effects of general inflation[1]	(13)
NET INCOME, ADJUSTED FOR GENERAL INFLATION	$985
Purchasing power gain on net monetary liabilities in 1985[2]	$ 54

Financial Data Restated for the Effects of General Inflation

IN MILLIONS EXCEPT PER SHARE DATA. RESTATED AMOUNTS ARE IN AVERAGE 1985 DOLLARS	1985	1984	1983	1982	1981
Total Revenue					
As reported	$8,476	$6,619	$5,883	$5,121	$4,053
Restated	8,476	6,855	6,352	5,707	4,794
Net Income					
As reported	$ 998	$ 690	$ 860	$ 723	$ 531
Restated	985	814	843	730	550
Net Assets at Year-End					
As reported	$7,765	$6,426	$5,771	$4,815	$4,281
Restated	8,670	7,500	6,998	6,400	5,879
Purchasing Power Gain on Net Monetary Liabilities[2]	$ 54	$ 37	$ 18	$ 44	$ —
Per Share					
Net Income[3]					
As reported	$ 7.12	$ 6.45	$ 6.18	$ 5.60	$ 4.20
Restated	7.01	5.85	6.32	5.65	4.37
Cash Dividends Declared					
As reported	$ 2.26	$ 2.06	$ 1.88	$ 1.72	$ 1.56
Restated	2.26	2.13	2.03	1.92	1.85
Market Price at Year-End					
As reported	$49.38	$38.75	$37.12	$32.50	$25.25
Restated	48.54	39.57	39.42	35.81	28.90
Average Consumer Price Index (1967=100)	322.2	311.1	298.4	289.1	272.4

(1) Adjustments reflecting the effects of general inflation do not assume any income tax benefit or cost
(2) Premises and equipment and net trading account assets, among other items, are treated as nonmonetary items
(3) On common and common equivalent shares.

FINANCIAL STATISTICS

QUARTERLY FINANCIAL INFORMATION

CITICORP AND SUBSIDIARIES

IN MILLIONS OF DOLLARS EXCEPT PER SHARE AMOUNTS	1985 4th	1985 3rd	1985 2nd	1985 1st	1984 4th	1984 3rd	1984 2nd	1984 1st
Net Interest Revenue	$1,533	$1,368	$1,311	$1,234	$1,203	$1,065	$1,063	$ 988
Fees, Commissions and Other Revenue	844	751	740	695	694	555	525	526
TOTAL REVENUE	$2,377	$2,119	$2,051	$1,929	$1,897	$1,620	$1,588	$1,514
Provision for Possible Credit Losses	$ 394	$ 346	$ 280	$ 223	$ 253	$ 146	$ 139	$ 81
Operating Expense	1,609	1,407	1,310	1,191	1,224	1,137	1,091	1,004
TOTAL EXPENSE	$2,003	$1,753	$1,590	$1,414	$1,477	$1,283	$1,230	$1,085
Income Before Taxes	$ 374	$ 366	$ 461	$ 515	$ 420	$ 337	$ 358	$ 429
Income Taxes	131	139	210	238	159	137	152	206
NET INCOME	$ 243	$ 227	$ 251	$ 277	$ 261	$ 200	$ 206	$ 223
Per Share								
Net Income[1]								
On Common and Common Equivalent Shares	$1.69	$1.60	$1.81	$2.02	$1.90	$1.42	$1.49	$1.64
Assuming Full Dilution	$1.68	$1.60	$1.81	$2.02	$1.90	$1.42	$1.48	$1.56
TOTAL ASSETS	$173,597	$169,082	$159,580	$154,603	$150,586	$144,731	$143,509	$141,841
Cash Dividends Declared								
Redeemable Preferred and Preferred Stock	$19	$16	$14	$14	$15	$17	$15	$13
Common Stock	$73	$73	$72	$72	$65	$65	$65	$64
Common Stock, Per Share	$.565	$.565	$.565	$.565	$.515	$.515	$.515	$.515
Common Stock Price Range								
High	50⅜	51¾	50	47⅛	40½	39	34⅛	39⅛
Low	40½	40	42¼	36⅞	33¼	27½	27⅜	33⅛
Close	49⅜	40½	49⅜	43¼	38¾	36¼	30⅛	34

(1) On Net Income available for Common Stockholders after deducting Total Preferred Dividends.

RATIOS

	1985	1984	1983
Return on Average Total Assets[1]	.62%	.62%	.67%
Return on Common Stockholders' Equity[2]	15.1%	15.0%	16.5%
Return on Total Stockholders' Equity[3]	14.1%	14.4%	16.0%
Average Common Stockholders' Equity as a Percentage of Average Total Assets	3.9%	3.9%	3.9%
Average Total Stockholders' Equity as a Percentage of Average Total Assets	4.4%	4.3%	4.2%
Dividends Per Common Share as a Percentage of Net Income Per Common Share	31.7%	31.9%	29.0%

(1) Net Income as a percentage of Average Total Assets
(2) Net Income less Total Preferred Stock Dividends as a percentage of Average Common Stockholders' Equity
(3) Net Income less Redeemable Preferred Stock Dividends as a percentage of Average Total Stockholders' Equity

1985 FORM 10-K CROSS-REFERENCE INDEX

Securities and Exchange Commission
Washington, D.C. 20549

Annual Report Pursuant to Section 13 or 15(d)
of The Securities Exchange Act of 1934
For the fiscal year ended December 31, 1985
Commission File Number 1-5738

CITICORP

Incorporated in the State of Delaware
IRS Employer Identification Number 13-2614988
Address: 399 Park Avenue, New York, NY 10043
Telephone: (212) 559-1000

SECURITIES REGISTERED PURSUANT TO SECTION 12(b) OF THE ACT:

A list of Citicorp securities registered pursuant to Section 12(b) of the Securities Exchange Act of 1934 is available from the Office of the Secretary, 399 Park Avenue, New York, NY 10043.

As of December 31, 1985, Citicorp had 129,376,890 shares of Common Stock outstanding.

Citicorp (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.

The aggregate market value of Citicorp common stock held by non-affiliates on January 31, 1986 was approximately $6.5 billion.

This Annual Report and Form 10-K incorporates into a single document the requirements of the accounting profession and the Securities and Exchange Commission, including a comprehensive explanation of 1985 results.

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*Citicorp's 1986 Proxy Statement is incorporated herein by reference

Certain statistical data required by the Securities and Exchange Commission are included on pages 20 to 23, pages 31 to 32, pages 33 to 34, page 70, and pages 72 to 76.

FINANCIAL DATA SUPPLEMENT

AVERAGE BALANCES AND INTEREST RATES

CITICORP AND SUBSIDIARIES

TAXABLE EQUIVALENT BASIS[1]

IN MILLIONS OF DOLLARS	1985 AVERAGE VOLUME	1985 INTEREST	1985 % AVERAGE RATE	1984 AVERAGE VOLUME	1984 INTEREST	1984 % AVERAGE RATE	1983 AVERAGE VOLUME	1983 INTEREST	1983 % AVERAGE RATE
INTEREST REVENUE									
Loans and Lease Financing (Net of Unearned Discount)[2]									
Commercial Loans									
In Domestic Offices									
Commercial and Industrial	$ 13,212	$ 1,822	13.79	$ 14,082	$ 2,069	14.69	$ 16,285	$ 1,960	12.04
Mortgage and Real Estate	5,200	581	11.18	4,331	509	11.75	3,421	372	10.86
Loans to Financial Institutions	604	84	13.91	1,189	128	10.77	2,198	234	10.63
In Overseas Offices	38,967	5,738	14.73	39,425	6,101	15.68	38,677	5,703	14.75
Total Commercial Loans	$ 58,083	$ 8,225	14.16	$ 58,027	$ 8,807	15.18	$ 60,581	$ 8,269	13.65
Consumer Loans									
In Domestic Offices	$ 40,566	$ 5,735	14.14	$ 30,671	$ 4,431	14.45	$ 19,610	$ 2,847	14.51
In Overseas Offices	7,171	1,186	16.54	6,084	1,013	16.65	5,307	948	17.86
Total Consumer Loans	$ 47,737	$ 6,921	14.50	$ 36,755	$ 5,444	14.81	$ 24,923	$ 3,795	15.19
Total Loans	$103,820	$15,156	14.32	$ 94,782	$14,251	15.04	$ 85,504	$12,064	14.10
Lease Financing	2,424	463	19.10	1,900	392	20.63	1,774	362	20.39
Total Loans and Lease Financing	$106,244	$15,619	14.43	$ 96,682	$14,643	15.15	$ 87,278	$12,426	14.23
Funds Sold and Resale Agreements (Principally in domestic offices)	$ 6,835	$ 1,087	15.90	$ 4,908	$ 936	19.07	$ 4,297	$ 757	17.62
Investment Securities									
In Domestic Offices									
U.S. Treasury and Federal Agencies	$ 2,505	$ 268	10.70	$ 2,745	$ 304	11.07	$ 2,187	$ 245	11.18
State and Municipal	395	48	12.15	419	52	12.41	454	59	13.00
Other	788	105	13.32	704	71	10.09	382	26	6.76
In Overseas Offices (Principally local government issues)	3,448	486	13.52	2,313	279	12.06	1,924	232	12.06
Total	$ 7,136	$ 907	12.43	$ 6,181	$ 706	11.42	$ 4,947	$ 562	11.35
Trading Account Assets									
U.S. Treasury and Federal Agencies	$ 817	$ 98	12.00	$ 1,075	$ 134	12.47	$ 749	$ 78	10.43
State and Municipal	864	71	8.22	396	53	13.38	218	26	11.99
Other (Principally in overseas offices)	4,888	709	14.50	3,248	611	18.81	2,228	366	16.43
Total	$ 6,569	$ 878	13.37	$ 4,719	$ 798	16.91	$ 3,195	$ 470	14.72
Interest-Bearing Deposits (Principally in overseas offices)	$ 11,811	$ 1,156	9.79	$ 11,577	$ 1,273	11.00	$ 10,702	$ 1,074	10.04
Total Interest Earning Assets	$140,595	$19,827	13.96	$124,067	$18,356	14.80	$110,419	$15,279	13.84
Non Interest Earning Assets	19,910			18,564			17,504		
TOTAL ASSETS	$160,505			$142,631			$127,923		
INTEREST EXPENSE									
Deposits									
In Domestic Offices									
Savings Deposits[3]	$ 14,295	$ 968	6.77	$ 11,629	$ 894	7.69	$ 6,252	$ 479	7.66
Negotiable Certificates of Deposit	2,314	241	10.41	1,573	151	9.60	3,525	326	9.26
Other Time Deposits	19,553	1,895	9.69	16,162	1,918	11.87	9,608	1,008	10.27
Total Domestic Interest Bearing Deposits	$ 36,162	$ 3,104	8.58	$ 29,364	$ 2,963	10.09	$ 19,585	$ 1,813	9.26
In Overseas Offices	50,228	5,761	11.45	46,786	5,668	12.11	47,735	5,081	10.65
Total	$ 86,490	$ 8,865	10.25	$ 76,150	$ 8,631	11.33	$ 67,320	$ 6,894	10.24
Funds Borrowed									
In Domestic Offices									
Purchased Funds and Other Borrowings									
Federal Funds Purchased and Securities Sold Under Agreements to Repurchase	$ 10,064	$ 835	8.30	$ 9,329	$ 972	10.42	$ 8,379	$ 809	9.66
Commercial Paper	4,877	415	8.34	4,970	525	10.56	3,766	344	9.14
Other Purchased Funds	6,396	597	9.33	5,648	568	10.06	4,951	483	9.75
Long Term Debt and Subordinated Capital Notes	12,032	1,335	11.10	9,063	1,034	11.41	6,488	690	10.64
Total in Domestic Offices	$ 33,469	$ 3,202	9.57	$ 29,008	$ 3,099	10.68	$ 23,584	$ 2,326	9.86
In Overseas Offices	7,915	1,961	24.78	8,098	2,145	26.49	7,976	1,934	24.24
Total	$ 41,384	$ 5,163	12.48	$ 37,106	$ 5,244	14.13	$ 31,560	$ 4,260	13.50
Total Interest Bearing Liabilities	$127,874	$14,028	10.97	$113,256	$13,875	12.25	$ 98,880	$11,154	11.28
Demand Deposits in Domestic Offices	7,258			6,021			6,867		
Other Non Interest Bearing Liabilities	18,349			17,195			16,824		
Total Stockholders' Equity	7,024			6,159			5,352		
TOTAL LIABILITIES AND STOCKHOLDERS' EQUITY	$160,505			$142,631			$127,923		
NET INTEREST REVENUE AS A PERCENTAGE OF AVERAGE INTEREST-EARNING ASSETS									
In Domestic Offices	$ 72,965	$ 3,267	4.48	$ 60,936	$ 2,312	3.79	$ 48,356	$ 2,089	4.32
In Overseas Offices	67,630	2,332	3.45	63,131	2,169	3.44	62,061	2,036	3.28
TOTAL	$140,595	$ 5,599	3.96	$124,067	$ 4,481	3.61	$110,419	$ 4,125	3.74

(1) The taxable equivalent adjustment is based on the marginal tax rate of 46%.
(2) Loans and lease financing balances include cash basis loans and leases.
(3) Savings Deposits consist of Insured Money Market Rate accounts, NOW accounts and other Savings Deposits.

ANALYSIS OF CHANGES IN NET INTEREST REVENUE

TAXABLE EQUIVALENT BASIS

IN MILLIONS OF DOLLARS	1985 vs. 1984 INCREASE (DECREASE) DUE TO CHANGE IN AVERAGE VOLUME	AVERAGE RATE	NET CHANGE*	1984 vs. 1983 INCREASE (DECREASE) DUE TO CHANGE IN AVERAGE VOLUME	AVERAGE RATE	NET CHANGE*
Loans—Commercial						
In Domestic Offices	$ (66)	$ (143)	$ (209)	$ (201)	$ 341	$ 140
In Overseas Offices	88	(451)	(363)	(37)	435	398
Total	$ 22	$ (594)	$ (572)	$ (238)	$ 776	$ 538
Loans—Consumer						
In Domestic Offices	$1,397	$ (93)	$1,304	$1,596	$ (12)	$1,584
In Overseas Offices	179	(6)	173	125	(50)	75
Total	$1,576	$ (99)	$1,477	$1,721	$ (62)	$1,659
Lease Financing						
In Domestic Offices	$ 51	$ 2	$ 53	$ 17	$ 7	$ 24
In Overseas Offices	30	(12)	18	(3)	9	6
Total	$ 81	$ (10)	$ 71	$ 14	$ 16	$ 30
Total Loans and Lease Financing	$1,679	$ (703)	$ 976	$1,497	$ 730	$2,227
Funds Sold & Resale Agreements (Principally in domestic offices)	$ 261	$ (110)	$ 151	$ 114	$ 65	$ 179
Investment Securities						
In Domestic Offices	$ (22)	$ 16	$ (6)	$ 93	$ 4	$ 97
In Overseas Offices	150	37	187	47	—	47
Total	$ 128	$ 53	$ 181	$ 140	$ 4	$ 144
Trading Account Assets						
In Domestic Offices	$ 83	$ (36)	$ 47	$ 112	$ 23	$ 135
In Overseas Offices	82	(49)	33	117	76	193
Total	$ 165	$ (85)	$ 80	$ 229	$ 99	$ 328
Interest-Bearing Deposits (Principally in overseas offices)	$ 26	$ (143)	$ (117)	$ 92	$ 107	$ 199
TOTAL INTEREST REVENUE	$2,259	$ (988)	$1,271	$2,072	$1,005	$3,077
Deposits						
In Domestic Offices	$ 397	$ (256)	$ 141	$ 975	$ 175	$1,150
In Overseas Offices	342	(249)	93	(99)	686	587
Total	$ 739	$ (505)	$ 234	$ 876	$ 861	$1,737
Funds Borrowed						
In Domestic Offices	$ 321	$ (218)	$ 103	$ 568	$ 205	$ 773
In Overseas Offices	(47)	(137)	(184)	30	181	211
Total	$ 274	$ (355)	$ (81)	$ 598	$ 386	$ 984
TOTAL INTEREST EXPENSE	$1,013	$ (860)	$ 153	$1,474	$1,247	$2,721
NET INTEREST REVENUE	$1,246	$ (128)	$1,118	$ 598	$ (242)	$ 356

(1) Rate/Volume variance is allocated based on the percentage relationship of changes in volume and changes in rate to the total "Net Change"

INVESTMENT SECURITIES
CARRYING VALUE AND YIELD**
BY MATURITY DATE AS OF DECEMBER 31, 1985

IN MILLIONS OF DOLLARS	US TREASURY AND FEDERAL AGENCIES AMOUNT	US TREASURY AND FEDERAL AGENCIES YIELD	STATE AND MUNICIPAL AMOUNT	STATE AND MUNICIPAL YIELD	OTHER (PRINCIPALLY IN OVERSEAS OFFICES) AMOUNT	OTHER (PRINCIPALLY IN OVERSEAS OFFICES) YIELD
Due Within 1 Year	$ 597	10.32%	$171	5.37%	$1,733	*
After 1 but Within 5 Years	594	9.65%	60	4.32%	2,517	*
After 5 but Within 10 Years	443	9.17%	236	6.96%	1,281	*
After 10 Years	1,184	10.16%	358	5.98%	473	*
TOTAL	$2,818	9.90%	$825	6.19%	$6,004	*
Carrying Value and Yield** As of December 31, 1984	$2,811	10.60%	$439	6.68%	$3,272	*
Carrying Value and Yield** As of December 31, 1983	$2,823	10.69%	$477	6.67%	$2,534	*

*Yield information not readily available
**Computed by dividing annual interest (net of amortization of premium or accretion of discount) by the carrying value of the respective investment securities at December 31, 1985, 1984 and 1983.

LOANS AND LEASE FINANCING OUTSTANDING

IN MILLIONS OF DOLLARS AT YEAR END	1985	1984	1983	1982	1981
Commercial Loans					
In Domestic Offices					
Commercial and Industrial[1]	$ 13,514	$ 16,028	$14,910	$17,817	$16,104
Mortgage and Real Estate[2]	6,165	4,912	3,975	2,915	2,635
Loans to Financial Institutions[3]	1,353	1,003	2,341	2,623	1,287
	$ 21,032	$ 21,943	$21,226	$23,355	$20,026
In Overseas Offices					
Commercial and Industrial[1]	$ 25,683	$ 25,235	$27,592	$29,590	$29,4
Mortgage and Real Estate[2]	2,143	1,906	1,822	2,745	2,65
Loans to Financial Institutions	5,363	5,827	5,914	4,151	3,403
Governments and Official Institutions	4,434	4,298	4,074	3,140	3,635
	$ 37,623	$ 37,266	$39,402	$39,626	$39,159
	$ 58,655	$ 59,209	$60,628	$62,981	$59,185
Unearned Discount	(483)	(410)	(386)	(463)	(423)
Commercial Loans, Net of Unearned Discount	$ 58,172	$ 58,799	$60,242	$62,518	$58,762
Consumer Loans					
In Domestic Offices					
Mortgage and Real Estate[2]	$ 21,719	$ 17,679	$10,751	$ 9,261	$ 5,925
Installment, Revolving Credit and Other	27,490	21,913	15,418	11,213	9,556
	$ 49,209	$ 39,592	$26,169	$20,474	$15,481
In Overseas Offices	10,727	7,593	6,856	6,824	6,806
	$ 59,936	$ 47,185	$33,025	$27,298	$22,287
Unearned Discount	(4,418)	(4,524)	(4,030)	(4,093)	(3,759)
Consumer Loans, Net of Unearned Discount	$ 55,518	$ 42,661	$28,995	$23,205	$18,528
Lease Financing					
Lease Financing, Net of Unearned Income	$ 2,809	$ 2,164	$ 1,817	$ 1,855	$ 1,891
Allowance for Possible Credit Losses	$ (1,235)	$ (917)	$ (771)	$ (687)	$ (581)
TOTAL LOANS AND LEASE FINANCING, NET	$115,264	$102,707	$90,283	$86,891	$78,600

(1) Includes loans not otherwise separately categorized
(2) Includes only loans secured primarily by real estate
(3) Includes loans to governments and official institutions of $434 million in 1985, $273 million in 1984, $475 million in 1983, $243 million in 1982, and $10 million in 1981

DETAIL OF CREDIT LOSS EXPERIENCE

IN MILLIONS OF DOLLARS	1985	1984	1983	1982	1981
ALLOWANCE FOR POSSIBLE CREDIT LOSSES AT BEGINNING OF YEAR	**$ 917**	$771	$687	$581	$513
Deductions					
Gross Loan Losses					
Commercial Loans					
Mortgage and Real Estate:					
In Domestic Offices	**$ 2**	$ 5	$ 3	$ 4	$ 6
In Overseas Offices	**15**	3	11	8	4
Governments and Official Institutions	**44**	40	47	11	—
Loans to Financial Institutions:					
In Domestic Offices	**—**	—	—	—	3
In Overseas Offices	**19**	9	23	—	—
Commercial and Industrial:					
In Domestic Offices	**84**	83	81	91	46
In Overseas Offices	**278**	137	127	131	68
Consumer Loans[1]					
In Domestic Offices	**642**	320	210	197	207
In Overseas Offices	**77**	66	73	69	63
	$1,161	$663	$575	$511	$397
Loan Recoveries					
Commercial Loans					
Mortgage and Real Estate:					
In Domestic Offices	**$ 2**	$ 6	$ 10	$ 11	$ 12
In Overseas Offices	**1**	4	1	1	12
Governments and Official Institutions	**8**	—	—	—	—
Loans to Financial Institutions:					
In Domestic Offices	**—**	—	8	9	8
In Overseas Offices	**—**	—	—	—	—
Commercial and Industrial:					
In Domestic Offices	**25**	25	11	3	16
In Overseas Offices	**29**	21	21	29	19
Consumer Loans[1]					
In Domestic Offices	**111**	81	67	62	57
In Overseas Offices	**23**	19	20	20	17
	$ 199	$156	$138	$135	$141
Net Loan Losses					
In Domestic Offices	**$ 590**	$296	$198	$207	$169
In Overseas Offices	**372**	211	239	169	87
	$ 962	$507	$437	$376	$256
Additions					
Provision for Possible Credit Losses	**$1,243**	$619	$520	$473	$305
Other (Principally from allowance balances of acquired companies and translation of overseas allowance balances)	**37**	34	1	9	19
	$1,280	$653	$521	$482	$324
ALLOWANCE FOR POSSIBLE CREDIT LOSSES AT END OF YEAR	**$1,235**	$917	$771	$687	$581
Excess of Provision over Net Loan Losses	**$ 281**	$112	$ 83	$ 97	$ 49
Cumulative Excess of Provision over Net Loan Losses (since 1980)	**$ 622**	$341	$229	$146	$ 49
Cumulative Increase in Allowance (since 1980)	**$ 722**	$404	$258	$174	$ 68

(1) Consumer loan losses primarily relate to installment and revolving credit loans

LOAN MATURITIES AND SENSITIVITY TO CHANGES IN INTEREST RATES

THE MATURITIES OF THE GROSS COMMERCIAL LOAN PORTFOLIO AS OF DECEMBER 31, 1985

IN MILLIONS OF DOLLARS	DUE WITHIN 1 YEAR	OVER 1 BUT WITHIN 5 YEARS	OVER 5 YEARS	TOTAL
In Domestic Offices				
Commercial and Industrial Loans	$ 8,106	$ 3,124	$2,284	**$13,514**
Mortgage and Real Estate	3,833	1,525	807	**6,165**
All Other Loans	817	300	236	**1,353**
In Overseas Offices	21,367	10,856	5,400	**37,623**
TOTAL	$34,123	$15,805	$8,727	**$58,655**

The following table represents the sensitivity of the above loans due after one year to changes in interest rates:

Loans at Predetermined Interest Rates	$ 5,473	$3,397
Loans at Floating or Adjustable Interest Rates	10,332	5,330
TOTAL	$15,805	$8,727

TIME DEPOSITS IN DOMESTIC OFFICES

($100,000 OR MORE)
IN MILLIONS OF DOLLARS AT YEAR END

	CERTIFICATES OF DEPOSIT	OTHER TIME DEPOSITS
Under 3 months	$3,134	$2,504
3 to 6 months	968	747
6 to 12 months	638	614
Over 12 months	942	2,162

AVERAGE DEPOSIT LIABILITIES IN OVERSEAS OFFICES

IN MILLIONS OF DOLLARS	1985 AVERAGE BALANCE	1985 % AVERAGE INTEREST RATE	1984 AVERAGE BALANCE	1984 % AVERAGE INTEREST RATE	1983 AVERAGE BALANCE	1983 % AVERAGE INTEREST RATE
Banks[1]	**$17,501**	**11.37**	$17,816	11.27	$19,352	10.38
Other demand deposits	**6,470**	**4.20**	4,782	5.51	6,667	4.25
Other time and savings deposits[1]	**28,958**	**12.04**	26,467	12.83	24,008	11.62
TOTAL	**$52,929**	**10.86**	$49,065	11.55	$50,027	10.16

(1) Primarily consists of time certificates of deposit and other time deposits in denominations of $100,000 or more

PROPERTIES

The principal offices of Citicorp and Citibank, N.A. ("Citibank") are located at 399 Park Avenue, New York, New York, a 39-story building owned by Citibank. Citibank also owns Citicorp Center, a 59-story building located at 153 East 53rd Street across from 399 Park Avenue. Approximately 67% of the Citicorp Center and 399 Park Avenue complex is occupied by Citicorp. In addition, Citibank also owns other properties in New York, including 111 Wall Street which is totally occupied by Citicorp and its affiliates and 55 Wall Street, a nine-story building of which 34% is so occupied. Citicorp also has major corporate real estate holdings in Los Angeles and San Francisco.

Internationally, Citicorp also owns major corporate premises in various cities throughout the world including Paris, London, Dusseldorf, Brussels, Buenos Aires, Rio de Janeiro, Sao Paulo, Mexico City, San Juan, Caracas, Hong Kong, Manila and Tokyo. In all, some 36% of Citicorp owned corporate real estate is located outside the United States. Of the approximately 2,200 offices and other facilities of Citicorp located throughout the world, approximately 445 are owned and the balance are leased.

CONSENT OF INDEPENDENT AUDITORS

PEAT MARWICK

Peat, Marwick, Mitchell & Co.
Certified Public Accountants

...rd of Directors

We consent to incorporation by reference of our report dated January 21, 1986, relating to the consolidated balance sheet of Citicorp and subsidiaries as of December 31, 1985 and 1984 and the related consolidated statements of income, changes in stockholders' equity and changes in financial position for each of the years in the three-year period ended December 31, 1985 and the consolidated balance sheet of Citibank, N.A. and subsidiaries as of December 31, 1985 and 1984, which report appears on page 47 of the 1985 Citicorp Annual Report and Form 10-K, in the following Registration Statements: of Citicorp, Nos. 2-47647, 2-47648, 2-58678, 2-58679, 2-77058, and 2-82298 on Form S-8 and Nos. 2-95728, 2-96725, 2-97198, 33-2978, 33-784, and 33-3114 on Form S-3; and of Citibank, N.A. No. 2-60415, 2-98882, 33-780, 33-3142, and 33-3161 on Form S-11.

Peat, Marwick, Mitchell & Co.

New York, New York
February 28, 1986

Peat, Marwick, Mitchell & Co.

EXHIBITS, FINANCIAL STATEMENT SCHEDULES, AND REPORTS ON FORM 8-K

Financial Statements Filed:
Citicorp and Subsidiaries:
Consolidated Statement of Income
Consolidated Balance Sheet
Consolidated Statement of Changes in Stockholders' Equity
Consolidated Statement of Changes in Financial Position

Citicorp filed no Form 8-K Current Report for any month in the year ended December 31, 1985.

Citicorp's significant subsidiaries (as defined) and their place of incorporation or organization include:

Citibank, N.A.	United States
Citicorp Banking Corporation	Delaware
Citicorp Holdings, Inc.	Delaware

Other subsidiaries of Citicorp and their place of incorporation or organization include:

Citibank (New York State), N.A.	United States
Citicorp Trust, N.A. (California)	United States
Citicorp Trust, N.A. (Florida)	United States
Citicorp International Group, Inc.	Delaware
Citicorp Securities Markets, Inc.	Delaware
Citilease, Inc.	Delaware
Citicorp Retail Services, Inc.	Delaware

Citicorp's Articles of Incorporation and By-laws, Instruments Defining the Rights of Securities Holders, including Indentures and constituent instruments relating to various executive and staff benefit plans, have been previously filed with the Commission as Exhibits to various Citicorp registration statements.

Stockholders may obtain copies of such documents by writing Citicorp, Office of the Secretary, 399 Park Avenue, New York, New York 10043.

SIGNATURES

Pursuant to the requirements of Section 13 or 15(d) of the Securities Exchange Act of 1934, the registrant has duly caused this report to be signed on its behalf by the undersigned, thereunto duly authorized.

CITICORP
(Registrant)

Paul Kotterjahn
Senior Vice President—Secretary

February 28, 1986

Pursuant to the requirements of the Securities Exchange Act of 1934, this report has been signed on February 28, 1986 by the following persons in the capacities indicated.

Donald S. Howard
Executive Vice President
(Principal Financial Officer)

Thomas E. Jones
Senior Vice President and Chief Accounting Officer
(Principal Accounting Officer)

John S. Reed (Citicorp's Principal Executive Officer) and the Directors of Citicorp (listed below) executed a power of attorney appointing Paul Kotterjahn their attorney-in-fact, empowering him to sign this report on their behalf.

Hans H. Angermueller
Richard S. Braddock
Colby H. Chandler
Paul J. Collins
James H. Evans
James D. Farley
Lawrence E. Fouraker
Arthur Furer
Clifton C. Garvin, Jr.
Harry J. Gray
John W. Hanley
John P. Harbin
H.J. Haynes
Amory Houghton, Jr.
Juanita Kreps
C. Peter McColough
Roger Milliken
Charles M. Pigott
Donald V. Seibert
Mario Henrique Simonsen
Lawrence M. Small
Darwin E. Smith
Thomas C. Theobald
Franklin A. Thomas

CITICORP AND CITIBANK SENIOR MANAGEMENT

HANS H. ANGERMUELLER,
61, vice chairman of Citicorp and Citibank, is policymaking officer for Citicorp's and Citibank's legal, regulatory and external affairs. In 1985, Mr. Angermueller was chairman of the Corporation's Country Risk Review Committee. He joined Citibank in 1973 as senior vice president and general counsel.

ROBERT D. BAILEY,
46, group executive of Citicorp and Citibank, assumed responsibility in 1985 for the Asia/Pacific Group in the Institutional Bank. His previous assignments include service in Citibank's branches in Venezuela, senior officer in charge of operations in Mexico, and senior officer for Italy. In 1975 he was named Area Corporate Officer in charge of activities in the United Kingdom, the Republic of Ireland and Scandinavia. In 1980 he was named Country Head for Brazil. He joined Citibank in 1963.

RICHARD S. BRADDOCK,
44, sector executive of Citicorp and Citibank, heads the Individual Bank. He joined Citibank in 1973 and became a senior vice president and director of marketing for the New York branch system in 1975. He served as division head of Citibank's European consumer operations and returned to the U.S. in 1979 to direct the Card Products Division. In 1982 he assumed responsibility for the Consumer Banking, Travel and Entertainment Group, and in 1984 was named head of domestic businesses for the Individual Bank. He assumed his current responsibilities in September 1985.

MICHAEL A. CALLEN,
45, group executive of Citicorp and Citibank, assumed responsibility in 1985 for the North American Finance Group and is responsible for the development and management of financial services to commercial, industrial and service businesses in the United States and Canada. His previous assignments include various posts in Southeast Asia, the Middle East, and Saudi Arabia, and as chief executive officer for Citibank's affiliate, the Saudi American Bank in Riyadh. He has also had responsibility for treasury funding, foreign exchange activities, and the investment portfolio in the U.S. He joined Citibank in 1965.

PEI-YUAN CHIA,
47, group executive of Citicorp and Citibank, assumed responsibility in 1985 for the U.S. Card Products Group of the Individual Bank. He joined Citibank in 1971 and was responsible for marketing and the ATM program in the New York branch system. He was Managing Director of Famibank, Belgium, and returned to the U.S. in 1980 to direct the Carte Blanche/Diners Club business. He was promoted to Senior Vice President in 1981. He assumed responsibility for the Development Division of the Individual Bank in 1982, and for the Citicorp Savings Division late in 1984.

GEORGE J. CLARK,
61, executive vice president of Citibank, assists in representing Citicorp internationally, and manages the country-risk exposure lending limits. Before this assignment, he was division head for the Western Caribbean, South America, Canada, the Middle East, Asia and Africa in the International Banking Group. He joined Citibank in 1964.

PAUL J. COLLINS,
49, senior corporate officer of Citicorp and Citibank, is responsible for North America. He is also the chief planning officer for Citicorp and Citibank. Previously, he was chief investment officer, head of Corporate Planning, supervised the Corporation's accounting and control functions, head of the Financial Markets Group and most recently was head of the Investment Bank. He joined Citibank in 1961.

JAMES D. FARLEY,
59, vice chairman of Citicorp and Citibank, is responsible for international debt restructurings and special worldwide customer relations. He is also chairman of the Corporation's internal Personnel Planning Committee. Previously he headed the Institutional Bank's operations in the Caribbean, Central and South American Group. He joined Citibank in 1950 and rose through a series of positions, including service in Argentina and Canada and as head of the consumer banking operation in New York and the Merchant Banking Group.

PAMELA P. FLAHERTY,
41, became the Citicorp and Citibank's Senior Personnel Officer in 1985 when she assumed the position of Senior Human Resources Officer. She joined Citibank in 1968 in the International Banking Group and served as head of financial control and planning for that Group, and was involved in developing support systems for consumer finance in the U.S. and abroad. Prior to her current assignment she held key managerial positions in Citibank's branch system becoming business manager for half of the 280 branches in the nine-county metropolitan New York area. Most recently she was director of marketing and development for Citibank's Northeast Division retail banking activities.

DAVID E. GIBSON,
45, group executive of Citicorp and Citibank, assumed responsibility in 1985 for the Private Banking Group in the Individual Bank. He has broad experience in corporate banking in New York, Japan and Brazil. He also served as country head for the World Corporation Group in Brazil, and chief of staff for the Caribbean, Central and South American Banking Group. In 1981 he was appointed division head of the Australasia and Southeast Asia Division of the Institutional Bank based in Singapore. He joined Citibank in 1969.

PAUL F. GLASER,
59, is chairman of the Corporate Technology Committee. He is responsible for establishing technology policy and standards, for introducing new technology and for evaluating the quality and direction of systems efforts. Until 1985 he was also chairman of Transaction Technology Inc. responsible for the design, development and operation of advanced electronic systems and networks for delivering financial services to Citibank and Citicorp customers. He joined Citibank in 1973.

LAWRENCE R. GLENN,
47, chairman credit policy committee, is the chief lending officer of both Citicorp and Citibank. He is responsible for establishing credit rules and policies and providing general supervision of the soundness of the loan portfolio. He joined the Credit Policy Committee in 1981 and assumed his present responsibilities in June 1982. Previous assignments include division head in charge of the Real Estate Industries of the North American Banking Group and senior officer in the field for countries in the Northern Caribbean Region. He joined Citibank in 1963.

GUENTHER E. GREINER,
46, group executive of Citicorp and Citibank, assumed responsibility in 1985 for the Institutional Bank's Europe/Middle East/Africa Group. He previously served as head of Corporate Banking in Frankfurt, and in 1978 as general manager in Stuttgart. From 1974 until 1978 he served as group head for corporate business in Germany. In 1979 he was appointed area corporate officer for Germany, Austria and Eastern Europe and in 1982 became a senior vice president. His most recent assignment was as eastern division head of the North American Banking Group of the Institutional Bank. He joined Citibank in 1965.

GEORGE E. HAGERMAN, JR.,
52, group executive of Citicorp and Citibank, heads the Financial Institutions Group, which maintains the bank's operational and marketing relationships with domestic and international correspondent banks and other financial institutions. He joined Citibank's overseas division in 1957 where he was assigned to key management positions in Venezuela, Argentina and Brazil. He has served as division head for Central and South America and the Caribbean. He assumed his present responsibilities in January 1980.

WILLIAM J. HERON, JR.,
44, group executive of Citicorp and Citibank, heads the U.S. Consumer Banking Group of the Individual Bank. He joined Citibank in 1969 as a member of Citicorp's strategic planning and development unit. He was responsible for the acquisition, development and repositioning of Citicorp's subsidiary, Citicorp Person-to-Person. Since 1976, Mr. Heron has held various positions in the Card Products Division and the New York Banking Division. In 1982 he was appointed division executive for New York consumer banking business, which in 1984 also included Upstate New York, New Jersey and Connecticut. He assumed his present responsibilities in 1985.

EDWIN P. HOFFMAN,
43, group executive of Citicorp and Citibank, directs the Institutional Bank's Caribbean, Central and South America Group. His previous assignments included senior management positions in Colombia, the Middle East and North Africa and supervision of the Western Hemisphere Group of the Individual Bank overseeing Citicorp's domestic consumer subsidiaries, its Savings and Loan Associations, the upstate New York branches and Latin America. He joined Citibank in 1969.

DONALD S. HOWARD,
57, executive vice president, is the Chief Financial Officer of Citicorp and Citibank, responsible for worldwide liquidity, capital structure planning, the development of Citicorp's long range funding plan and management of all interme diate and long term debt issues. He joined Citibank in 1957.

ANTHONY C. HOWKINS,
61, is group executive of Citicorp and Citibank, Investment Bank. His assignments in the Investment Bank have included responsibilities for activities in Europe, the Middle East, Africa, Asia and Australia. He was most recently in charge of Investment Bank activities in Latin America and International Private Banking. He joined Citibank in 1951 and has served as head of the Investment Management Group, senior vice president in the World Corporation Group and senior corporate officer in Bra/

RICHARD L. HUBER,
49, group executive of Citicorp and Citibank, is responsible for U.S. Equity Finance, the Latin American Investment Bank and Global Insurance. He joined Citibank in 1973 and in 1977 became area corporate officer for Japan and Guam. He was appointed senior vice president in 1978. In 1980 he was named head of the Institutional Bank's North East Asia division, and most recently was in charge of the Asia Pacific Banking Group of the Institutional Bank. He assumed his current responsibilities in September 1985.

DANIEL T. JACOBSEN,
53, chief auditor of Citicorp and Citibank, is responsible for worldwide Citicorp/Citibank audits and loan reviews. He has held international posts in Mexico, Canada, Japan, Hong Kong, and most recently the Philippines, where he was country senior officer from 1975 to 1980. He joined Citibank in 1959. As chief auditor he reports directly to the Board of Directors.

THOMAS E. JONES,
47, senior vice president-chief accounting officer, is the financial controller for Citicorp and Citibank. Since joining Citibank in 1980, he has been responsible for the Corporation's accounting, MIS, operational planning and tax functions. In 1985 he served as chairman of the Acquisition and Divestiture Committee.

MARK F. KESSENICH,
47, group executive of Citicorp and Citibank, is responsible for the Investment Bank in North America. Previously he served as a trader and as manager of Citibank's Municipal Bond Dealer Department. His most recent assignment was senior vice president/division head of the Money Market Division. Mr. Kessenich joined Citibank in 1964.

PAUL KOLTERJAHN,
61, was appointed senior vice president-secretary of Citicorp and Citibank in 1983. He is responsible for the Corporate Secretary's Office including Directors' activities, stockholder relations, exchange listings, proxy and annual meeting matters, head office contributions, public issues and corporate security. Previously he was responsible for Administration and Credit Management for the Metropolitan New York branch system. He joined Citibank in 1949.

RICHARD J. LEHMANN,
41, senior corporate officer of Citicorp and Citibank, is responsible for Europe and the Middle East. His previous assignments included posts in Europe for the International Bank. In 1977 he was appointed president and chief executive officer of Citicorp's Nationwide Financial Services Corp., which became the backbone of the Person-to-Person network. Most recently Mr. Lehmann was U.S. division executive for the Western Hemisphere Consumer Group in charge of domestic consumer banking outside the New York City area. He joined Citibank in 1969.

[illegible] E. LONG,
[illegible]tive vice president, of [illegible]and Citibank, supervises Legal and External Affairs, which includes the Office of the General Counsel, the Corporate Secretary's Office, Government Relations, Public Affairs and Advertising, and administers the Audit Division. Previously, he had responsibility for consumer financial services overseas and the operating activities of the Personal Banking Group. He took on his current assignment in August 1982. Mr. Long joined Citibank in 1972.

ANTHONY G. MANTZAVINOS,
57, group executive of Citicorp and Citibank, assumed responsibility in 1985 for the Institutional Bank's World Corporation Group serving major corporate multinational clients around the world, and shipping accounts. His previous assignments included responsibility for the Asia/Australia/Middle East Africa banking group and the Financial Institutions division, as well as senior officer in Spain, Portugal, Cyprus, Greece and Canada. His most recent assignment was head of the Institutional Bank in Europe/Middle East-Africa banking group. He joined Citibank in 1964.

VICTOR MENEZES,
36, senior corporate officer of Citicorp and Citibank assumed responsibility for Latin America/Africa in 1985. His previous assignments include posts in India and New York. In 1978 he was appointed senior officer for India. His most recent assignment, in 1983, was country corporate officer for Hong Kong and China. He joined Citibank in 1972.

GLEN R. MORENO,
42, group executive of Citicorp and Citibank, is responsible for the Investment Bank for Europe, the Middle East and Africa. Prior to this appointment, he was officer in charge in Germany, headed the South Asia/Australia division of the Institutional Bank and most recently served as senior corporate officer for Europe, the Middle East and North Africa. He joined Citibank in 1969.

JOHN S. REED,
47, chairman and chief executive officer of Citicorp and Citibank is top policy making officer of Citicorp and Citibank. He joined Citibank in 1965 and has held various positions in the overseas division, operating group, consumer services group, and until September 1985 was responsible for the Individual Bank.

WILLIAM R. RHODES,
51, is chairman, restructuring committee of Citicorp and Citibank. The committee is responsible for establishing and implementing Citicorp's sovereign debt restructuring policies. Previously, he was senior corporate officer responsible for the Caribbean, Central and South America and Sub Sahara Africa. He has held several positions in the Latin American and Caribbean area. Mr. Rhodes joined Citibank in 1957.

IRA S. RIMERMAN,
47, group executive of Citicorp and Citibank, assumed responsibility in 1985 for the Individual Bank's Consumer Services Group, International. Previously, he had been chief financial officer of a Citicorp subsidiary, head of Citibank's Urban Affairs Department's Economic Development Center, and in 1976 was assigned responsibility for Citibank's consumer business in Hong Kong. In 1981 he was selected to head Citibank's Visa and MasterCard business. This included our operations in South Dakota, Nevada and Maryland. Subsequently, the Citibank Financial Account, Choice card and private label businesses were added to his area of responsibility. Mr. Rimerman joined Citibank in 1971.

PETER H. SCHUPING,
45, group executive of Citicorp and Citibank directs the Investment Bank in Asia-Pacific. He has had responsibility for lending activities of Citibank's wholly-owned subsidiaries in Canada, was senior officer for Spain, Portugal and Andorra, and most recently, was division head for the Institutional Bank Argentina, Bolivia, Chile, Paraguay, Peru and Uruguay. Mr. Schuping joined Citibank in 1963.

LAWRENCE M. SMALL,
44, sector executive of Citicorp and Citibank, is in charge of the Institutional Bank. He joined Citibank in 1964 and has previously worked in Chile, managed a number of operating departments and the upstate New York banking subsidiaries. He also served as Citicorp/Citibank Senior Personnel Officer. His most recent assignment was responsibility for the Institutional Bank's North American Banking Group. He assumed his current responsibilities in September 1985.

THOMAS C. THEOBALD,
48, vice chairman/sector executive of Citicorp and Citibank, has responsibility for Citicorp's Investment Bank. Mr. Theobald is also chairman of the Corporation's Finance Committee. Previously, he was in charge of the International Banking Group, the World Corporation Group, the Investment Management Group, a consumer finance affiliate in Australia and the Institutional Bank. He joined Citibank in 1960.

DAVID S. VAN PELT,
44, senior corporate officer of Citicorp and Citibank, is responsible for the Asia/Pacific region. Previously he held posts in various units of the Commercial Banking Group in New York and was division head for the World Corporation Group. His most recent assignment was division head for the Institutional Bank in Northern Europe. Mr. Van Pelt joined Citibank in 1967.

CITICORP AND CITIBANK DIRECTORS

The Boards of Directors of Citicorp and Citibank meet on the third Tuesday of every month to administer the affairs of the organizations. Certain specific operations and areas of the corporation and the bank are regularly monitored by the directors' committees, whose activities are described on the following page.

' Director of Citicorp
△ Director of Citibank

HANS H. ANGERMUELLER ' △
Vice Chairman
Citicorp and Citibank, N.A.

RICHARD S. BRADDOCK ' △
Sector Executive
Citicorp and Citibank, N.A.

COLBY H. CHANDLER ' △
Chairman and
Chief Executive Officer
Eastman Kodak Company

PAUL J. COLLINS ' △
Senior Corporate Officer
Citicorp and Citibank, N.A.

JAMES H. EVANS ' △
Former Chairman
Union Pacific Corporation

JAMES D. FARLEY ' △
Vice Chairman
Citicorp and Citibank, N.A.

DR. LAWRENCE E. FOURAKER ' △
Professor Emeritus,
Graduate School of
Business Administration
Harvard University

DR. ARTHUR FURER '
Chairman
Bank Leu AG.

CLIFTON C. GARVIN, JR. ' △
Chairman of the Board and
Chief Executive Officer
Exxon Corporation

HARRY J. GRAY ' △
Chairman
United Technologies
Corporation

JOHN W. HANLEY ' △
Director and Former
Chairman of the Board
Monsanto Company

JOHN P. HARBIN ' △
Former Director and
Chairman of the Board and
Chief Executive Officer
Halliburton Company

H.J. HAYNES ' △
Senior Counselor
Bechtel Group, Inc.

AMORY HOUGHTON, JR. ' △
Chairman of the
Executive Committee
Corning Glass Works

DR. JUANITA M. KREPS '
Former United States
Secretary of Commerce

C. PETER McCOLOUGH ' △
Chairman of the
Executive Committee
Xerox Corporation

ROGER MILLIKEN ' △
Chairman of the Board
and Chief Executive Officer
Milliken & Company

CHARLES M. PIGOTT ' △
President
PACCAR Inc

JOHN S. REED ' △
Chairman
Citicorp and Citibank, N.A.

DONALD V. SEIBERT ' △
Director and Former Chairman
of the Board
J.C. Penney Company, Inc.

DR. MARIO HENRIQUE SIMONSEN '
Vice Chairman
Brazilian Institute of Economics
The Getulio Vargas Foundation

LAWRENCE M. SMALL ' △
Sector Executive
Citicorp and Citibank, N.A.

DARWIN E. SMITH ' △
Chairman of the Board and
Chief Executive Officer
Kimberly-Clark Corporation

THOMAS C. THEOBALD ' △
Vice Chairman/
Sector Executive
Citicorp and Citibank, N.A.

FRANKLIN A. THOMAS ' △
President
The Ford Foundation

CITICORP SENIOR MANAGEMENT

Hans H. Angermueller
Robert D. Bailey
Richard S. Braddock
Michael A. Callen
Pei Yuan Chia
Paul J. Collins
James D. Farley
Pamela P. Flaherty
David E. Gibson
Lawrence R. Glenn
Guenther E. Greiner
George E. Hagerman, Jr.
William J. Heron, Jr.
Edwin P. Hoffman
Donald S. Howard
Anthony C. Howkins
Richard L. Huber
Daniel T. Jacobsen
Thomas E. Jones
Mark F. Kessenich
Paul Koltenahn
Richard J. Lehmann
Charles E. Long
Anthony G. Mantzavinos
Victor Menezes
Glen R. Moreno
Patrick J. Mulhern
John S. Reed
William R. Rhodes
Ira S. Rimerman
Peter H. Schuring
Lawrence M. Small
Thomas C. Theobald
David S. Van Pelt

BOARDS OF DIRECTORS' COMMITTEES

Audit Committee: supervises independent audits of Citicorp and oversees the establishment of appropriate accounting policies for Citicorp and Citibank.

Members: Darwin E. Smith, Chairman; Colby H. Chandler, Dr. Lawrence E. Fouraker, John W. Hanley, John P. Harbin, C. Peter McColough, Charles M. Pigott and Dr. Mario H. Simonsen.

The Audit Committee, whose members are all independent outside directors, all but one of whom serve jointly on the Examining Committee of Citibank, meets at least four times each year with the corporation's public accountants, its chief accounting officer and the chief auditor.

One of its principal functions is to review the audit plans and scope of examination of both the independent auditors and the corporation's internal audit division. In addition, it is the responsibility of this committee to recommend to the Board the annual appointment of the outside auditors. The Board accepted the recommendation that Peat, Marwick, Mitchell & Co. be retained for 1986 and this proposal will be presented to the stockholders for approval at the annual meeting.

During joint meetings with the Examining Committee, the findings of internal and external auditors and external regulatory agencies are reviewed and responses to their findings are monitored to insure appropriate follow-up measures are taken. These are reviewed with and without the presence of management, and in separate meetings with Peat, Marwick, Mitchell & Co., with no members of management present. The results of these examinations, along with our own findings, are reported regularly to the full Board.

It is also the function of this committee to oversee the accounting policies used in preparing the financial statements of Citicorp and Citibank.

Darwin E. Smith

DARWIN E. SMITH
Chairman

Committee on Directors: recommends qualified candidates for membership on the Boards of Directors of Citicorp and Citibank.

Members: Citicorp: John S. Reed, Chairman; Clifton C. Garvin, Jr., John P. Harbin, Dr. Juanita M. Kreps, Roger Milliken and Darwin E. Smith. Citibank, N.A.: John S. Reed, Chairman; Clifton C. Garvin, Jr., John P. Harbin, Roger Milliken and Darwin E. Smith.

The Committee on Directors actively solicits recommendations for prospective directors from their current members and stockholders and, consistent with the needs of the corporation and representation of the various services and customers, recommends the approval of a candidate. The nominees are then presented to the full board, which proposes the slate of directors to be submitted to the stockholders at the annual meeting. In addition, the committee is charged with keeping current and recommending changes in directors' compensation.

John S. Reed

JOHN S. REED
Chairman

Examining Committee: conducts a continuous examination into the affairs of Citibank.

Members: Darwin E. Smith, Chairman; Colby H. Chandler, Dr. Lawrence E. Fouraker, John W. Hanley, John P. Harbin, C. Peter McColough and Charles M. Pigott.

The Examining Committee, whose members are all independent outside directors, conducts a continuous examination into the affairs of Citibank and together with the Audit Committee, reports its findings to the Board. The Committee meets jointly with the Audit Committee, the chief accounting officer, the chief auditor and the corporation's public accountants.

The Examining Committee closely monitors examinations by the bank's principal regulator, the Comptroller of the Currency, as well as internal and external auditors, and follows up to insure appropriate action is taken by management in response.

Darwin E. Smith

DARWIN E. SMITH
Chairman

Executive Committee: provides backup for the Boards of Directors of Citicorp and Citibank.

Members: Citicorp: James H. Evans, Clifton C. Garvin, Jr., Harry J. Gray, Dr. Juanita M. Kreps, Donald V. Seibert and Franklin A. Thomas. Citibank, N.A.: James H. Evans, Clifton C. Garvin, Jr., Harry J. Gray, C. Peter McColough, Donald V. Seibert and Franklin A. Thomas. Ex Officio Members Both Committees: John S. Reed, Hans H. Angermueller, James D. Farley and Thomas C. Theobald.

This committee acts on behalf of the Boards of Directors should an urgent matter arise that requires a decision before the Board is next scheduled to meet. The Executive Committee has nearly all the powers of the Boards of Directors, except for certain powers expressly reserved to the Board of Directors.

John S. Reed

JOHN S. REED
Chairman

Fiduciary Review Committee: oversees the administration of the fiduciary powers of Citicorp.

Members: Donald V. Seibert, Chairman; Dr. Arthur Furer, Harry J. Gray, John P. Harbin, Amory Houghton, Jr., Roger Milliken and Franklin A. Thomas.

The Fiduciary Review Committee, which meets four times a year, monitors fiduciary activities conducted through subsidiaries and affiliates around the world. These activities include the management and administration of trust and agency accounts such as pension trusts and other employer-sponsored benefit plans, personal trusts, estates, investment advisory accounts and corporate trusteeships. The committee also reviews policies and controls in such areas of fiduciary responsibility as investment standards and conflicts of interest. The Committee was established by the Board of Citicorp in May 1985 to reflect the increased fiduciary activities conducted in vehicles other than Citibank and replaced a similar committee of the Board of Citibank.

Donald V. Seibert

DONALD V. SEIBERT
Chairman

Personnel Committee: oversees employee policies and programs of Citicorp and Citibank.

Members: Clifton C. Garvin, Jr., Chairman; Harry J. Gray, H.J. Haynes, Donald V. Seibert, and Franklin A. Thomas.

The Personnel Committee reviews and approves compensation policy and other personnel-related programs to maintain an environment at Citicorp/Citibank that attracts and retains people of high capability, commitment and integrity. In addition, the committee oversees management development programs, succession planning, and employee benefit programs.

Clifton C. Garvin, Jr.

CLIFTON C. GARVIN, JR.
Chairman

Public Issues Committee: reviews Citicorp's policies and performance on matters of public concern.

Members: Franklin A. Thomas, Chairman; Hans H. Angermueller, James H. Evans, Dr. Arthur Furer, John W. Hanley and Dr. Juanita M. Kreps.

The Public Issues Committee's mission is to assure that the public interest is maintained in the performance of our business roles and in achieving a more competitive business environment.

F. A. Thomas

FRANKLIN A. THOMAS
Chairman

STOCKHOLDER INFORMATION

NOTICE OF THE ANNUAL MEETING

The annual meeting of stockholders will be held on Tuesday, April 15, 1986, at 11 a.m., in the auditorium of Citicorp Headquarters at 399 Park Avenue, New York, NY.

A formal notice of this meeting, together with a proxy and proxy statement, has been included with this annual report. Stockholders are urged to sign and return their proxies promptly, to assure that the stock of the corporation will be represented as fully as possible at the meeting.

Citicorp has approximately 51,000 common stockholders of record. About 83% of the Citicorp shares entitled to vote were voted in person or by proxy at the last annual stockholders' meeting on April 16, 1985. Additionally, there are 233 Equity Holders of 5¼% Convertible Subordinated Notes Due 2000.

Additional copies of this annual report are available. Write to Citicorp, Public Affairs Department, 399 Park Avenue, 18th Floor, New York, NY 10043.

Copies of the written transcript and tape recording of the proceedings at Citicorp stockholder meetings are available to Citicorp stockholders at cost from the Office of the Secretary, 399 Park Avenue, New York, NY 10043.

Other reports available from the Public Affairs Department include: *Evolving Concepts of Bank Capital Management* and *Corporate Giving*, which describes Citibank/Citicorp contributions to community, cultural, education, health, and urban revitalization organizations throughout the country.

Supplemental financial data are published quarterly and are available from Citicorp Investor Relations Department, 399 Park Avenue, New York, NY 10043.

TRANSFER AGENT

Citibank, N.A., Corporate Trust Services, Box 4855, New York, NY 10043

CO-TRANSFER AGENTS

The First National Bank of Chicago, Corporate Trust Department, One First National Plaza, Chicago, IL 60670

First Interstate Bank of California, 707 Wilshire Boulevard, Los Angeles, CA 90017

REGISTRAR

United States Trust Company of New York, 45 Wall Street, New York, NY 10005

CO-REGISTRARS

The First National Bank of Chicago, Corporate Trust Department, One First National Plaza, Chicago, IL 60670

First Interstate Bank of California, 707 Wilshire Boulevard, Los Angeles, CA 90017

JAPANESE SHAREHOLDER SERVICE ORGANIZATION AND PAYING BANK

The Yasuda Trust and Banking Company, Limited, Stock Transfer Department, Yasuda Seimei Daini Building, 10-1, Nishi Shinjuku 1-chome, Shinjuku-ku, Tokyo, Japan

CITICORP STOCK LISTED

New York Stock Exchange
Midwest Stock Exchange
Pacific Stock Exchange
London Stock Exchange
Amsterdam Stock Exchange
Tokyo Stock Exchange
Zurich Stock Exchange
Geneva Stock Exchange
Basel Stock Exchange

Citicorp/Citibank
399 Park Avenue
New York, NY 10043
212/559-1000

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SERVICE EXCELLENCE AWARD

Citicorp

teamwork rests on the collective achievements of many individuals. But within a crowded field of exceptional performers, there are individuals whose work shines. The Service Excellence Award goes to those who embody the Citicorp standard of customer service. These people were among 1583 so recognized in 1985.

COSTAS VIOTIS
UNITED STATES

REBECCA YEE
HONG KONG

DAVID MARSHALL
UNITED KINGDOM

MARYANN McCLAIN
UNITED STATES

HUSSEIN HAMDAN
LEBANON

MARIA TERESA LLANOS
CHILE

JOHN LAW
TAIWAN

KEREM CARDENES
DOMINICAN REPUBLIC

GALAL MAHMOUD SALIH
SUDAN

CITICORP

SECURITIES AND EXCHANGE COMMISSION

WASHINGTON, D.C. 20549

FORM 10-Q

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

For Quarter Ended March 31, 1986 Commission file number 1-5738

CITICORP
(Exact name of registrant as specified in its charter)

Delaware	13-2614988
(State or other jurisdiction of incorporation or organization)	(I.R.S. Employer Identification No.)
399 Park Avenue, New York, New York (Address of principal executive offices)	10043 (Zip Code)

Registrant's telephone number, including area code (212) 559-1000

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 X No ____

Citicorp Common Stock..... ($4.00 Par)	131,547,334 (Shares Outstanding on March 31, 1986)

FORM 10-Q CROSS-REFERENCE INDEX

This document serves both as an analytical review for analysts, stockholders and other interested persons and as the quarterly report filed on Form 10-Q with the Securities and Exchange Commission.

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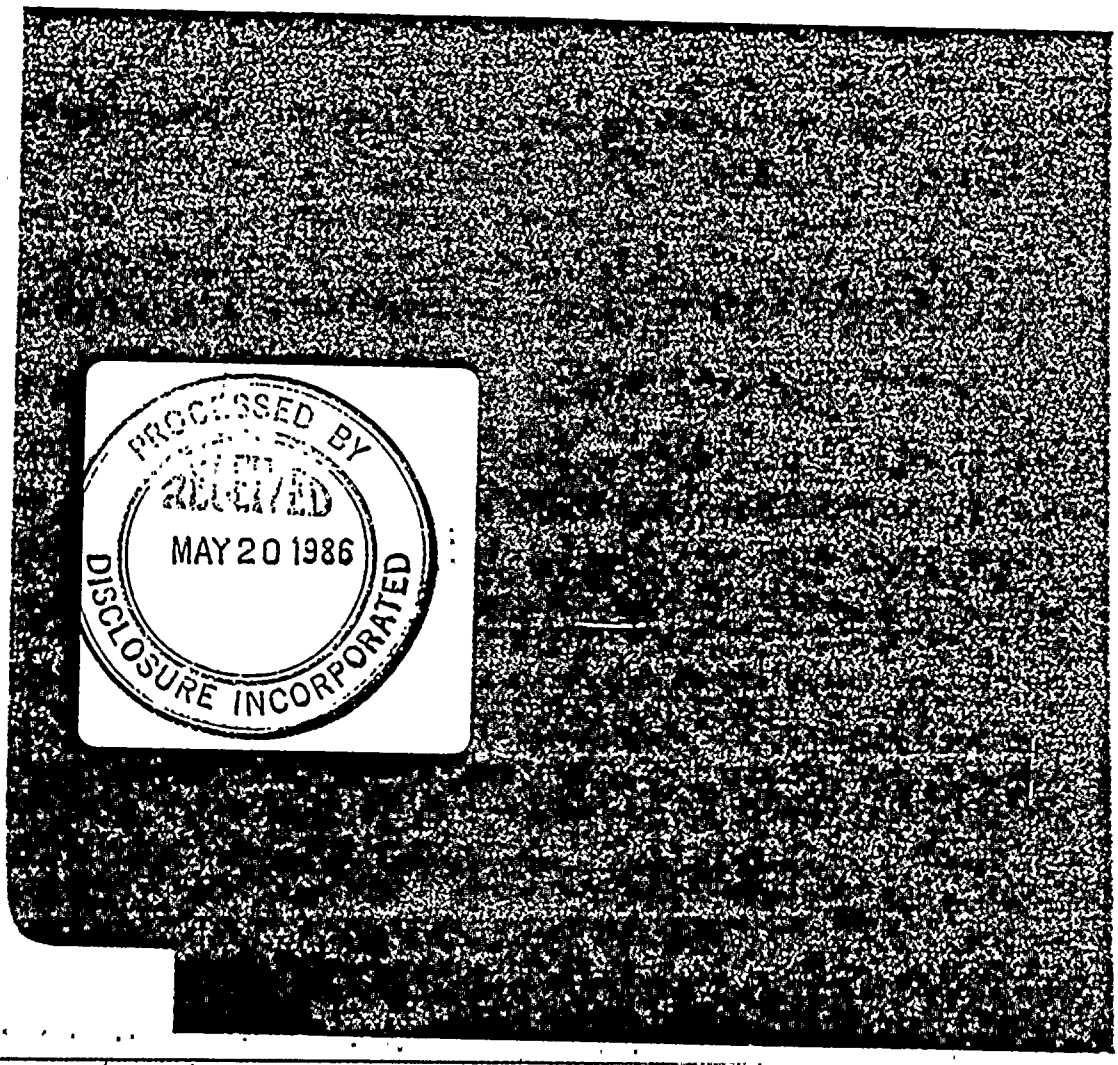
In the opinion of the management of Citicorp, all adjustments necessary for a fair presentation of the results of operations for the three months ended March 31, 1986 and 1985 have been included.

C375725 36P. 117693
3/31/86

CITICORP

Financial Review and Form 10Q

First Quarter 1986



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FINANCIAL HIGHLIGHTS - SELECTED INCOME STATEMENT ITEMS — CITICORP and Subsidiaries

(In Millions Except Per Share Amounts)	First Quarter 1986	1985	Change	%
NET INCOME PER SHARE *				
On Common & Common Equivalent Shares	$ 1.87	$ 2.02	$ (.15)	(7)
Assuming Full Dilution	$ 1.87	$ 2.02	$ (.15)	(7)
Common Dividends Declared Per Share	$ .615	$ .565	$ .05	9
Common Stockholders' Equity Per Share	$51.78	$47.16	$ 4.62	10
Net Interest Revenue	$1,431	$1,234	$ 197	16
Total Fees, Commissions and Other Revenue	959	695	264	38
Total Revenue	2,390	1,929	461	24
Provision for Possible Credit Losses	429	223	206	92
Operating Expense	1,499	1,191	308	26
Net Income	270	277	(7)	(3)
SECTOR EARNINGS				
Earnings of the Three Core Businesses (not including items retained at the corporate level)	$ 379	$ 340	$ 39	11
RETURN ON ASSETS AND EQUITY**				
Return on Total Assets (1)	.61%	.74%	(.13)%	-
Return on Common Stockholders' Equity (2)	15.2%	18.0%	(2.8)%	-
Return on Total Stockholders' Equity (3)	13.8%	17.0%	(3.2)%	-

* On net income available for common stockholders after deducting preferred stock dividends of $20 million and million in the first quarter of 1986 and 1985, respectively.

**Based on annualized results.

(1) Net income as a percentage of average total assets.
(2) Net income less total preferred stock dividends as a percentage of average common stockholders' equity.
(3) Net income less redeemable preferred stock dividends as a percentage of average total stockholders' equity.

FINANCIAL HIGHLIGHTS - SELECTED BALANCE SHEET ITEMS

(In Millions)	March 31 1986	1985	Change	%
Loans and Lease Financing, Net				
Commercial	$ 58,503	$ 57,624	$ 879	2
Consumer	57,243	44,634	12,609	28
Lease Financing	2,865	2,257	608	27
Loans and Lease Financing, Net of Unearned Discount	$118,611	$104,515	$ 14,096	13
Allowance for Possible Credit Losses	(1,366)	(957)	409	43
Total Loans and Lease Financing, Net	$117,245	$103,558	$ 13,687	13
Total Assets	181,896	154,603	27,293	18
Total Stockholders' Equity	8,026	6,655	1,371	21
Total Capital (4)	17,688	12,487	5,201	42
Primary Capital (5)	11,370	9,197	2,173	24

(4) Total Capital includes Primary Capital, Redeemable Preferred Stock, and gross Qualifying Debt restated in compliance with new regulatory requirements.

(5) Primary Capital, as defined by the Federal Reserve, includes Total Stockholders' Equity, Qualifying Subordinated Capital Notes, the Allowance for Possible Credit Losses and minority interest in consolidated subsidiaries.

FINANCIAL SUMMARY

Citicorp's first-quarter 1986 fully diluted earnings per share of $1.87, declined 7% from th[illegible].02 reported for the same period last year. First-quarter net income of $270 mi[illegible] was 3% below the $277 million reported a year ago.

Total sector earnings of $379 million were up $39 million, or 11% versus 1985. Individual Banking earned $97 million for the quarter, up $27 million over the same period in 1985. Institutional Relationships reported income of $205 million during the period, a decline of $25 million from the prior year. Investment Banking earned $147 million in the quarter, exceeding 1985's first quarter by $47 million.

Citicorp continued to strengthen its total capital base with increases in common equity, issuances of qualifying debt, as well as additions to the loan and lease loss allowance. Total capital at the end of the quarter was $17.7 billion or 9.65% of total assets, up from $15.9 billion, or 9.12% of total assets at year-end 1985 and up from $12.5 billion, or 8.03% of total assets as of March 31, 1985.

The Corporation's loan and lease loss allowance continued to be built during the period, with a pretax charge of $126 million to earnings, up $87 million from last year. At March 31, 1986, the allowance totaled $1,366 million, up $409 million from March 31, 1985 and $131 million over year-end 1985. Of the total, $286 million has been allocated to the Individual Bank, representing .50% of the consumer loan portfolio. The Institutional Bank has been allocated $351 million of the allowance or .60% of commercial loans. The remaining $729 million was reported at the corporate level. The total represents 1.15% of period-end loans and leases.

First-quarter revenue of $2,390 million was up 24%, or $461 million, over last year. Hi[illegible] revenues from asset-related credit products, driven by higher volumes, in addition to [illegible]reased fees and other revenues, propelled first-quarter revenue growth. Operating expenses were down 7% compared to the fourth quarter 1985, but increased 26% over last year's first quarter. Operating expenses rose over last year due to the base expense increases required to support expanding businesses, additional investments in new business initiatives, service improvement and market development. The loan loss provision for the first quarter was at a higher level than a year ago, primarily due to higher consumer write-offs reflecting greater volumes (particularly in credit cards) and the build-up of the credit loss allowance mentioned earlier.

First-quarter return on common stockholders' equity was 15.2% compared to 18.0% in the first quarter of 1985 and 15.1% for the full year. Return on assets of .61% represented a decrease from 1985's first quarter return of .74% and .62% for the full year.

SECTOR EARNINGS AND CORPORATE ITEMS

Citicorp reports the three core business sectors of Individual Banking, Institutional Relationships and Investment Banking. Details of earnings by sector have been disclosed since 1983 in order to present a better understanding of Citicorp's core businesses. Consistent with this objective, our presentation of sector results now reflects three changes which were made beginning with the 1985 Annual Report and are described below. In addition, this quarter's reporting contains certain refinements to the definition of Institutional Relationships.

The first change reflects the reorganization that was made in late 1985, in which the treasury function was transferred from the Institutional Bank to the Investment Bank and the International Private Banking activities were moved from the Investment Bank to the In[illegible]ual Bank.

The second change that has been made is to the allocation of the total credit loss allowance to reflect management's philosophy of how its businesses should be charged with the credit losses which may be expected over a protracted period of time. Citi[redacted] now charges its sectors with a credit loss provision that maintains an allowance at [redacted]vel that provides a measurement of costs against revenue generation consistent with the manner in which Citicorp manages its businesses and makes incremental business decisions. In any time period, the total allowance required to present the total loan portfolio in accordance with generally accepted accounting principles may be more than that allocated to the businesses. The additional amount along with its related provision is recorded at the corporate level. Refer to page 3 for a discussion of Citicorp's allowance for possible credit losses at March 31, 1986.

The third change concerns certain tax expenses, which had previously been held at the corporate level. The allocation of these taxes to the businesses more appropriately reflects sector performance and is necessitated by the increasing impact of these taxes on the Corporation.

As a result of the above changes, the amounts held at the corporate level will contain: the credit loss provision that represents the build-up of the credit allowance beyond that charged to the businesses; unallocated corporate staff costs; and other corporate items including certain start-up activities. The sectors are not charged for these items which reflect corporate level decisions and which, if allocated, would detract from an understanding of how the core businesses are performing.

The following table summarizes net income by product contribution. A discussion of sector results by customer relationship follows.

(In Millions)	First Quarter 1986	1985	Change	[redacted]
Net Income				
Individual Bank Products*	$ 97	$ 70	$ 27	39
Institutional Bank Products delivered to Institutional Relationships*	135	170	(35)	(21)
Investment Bank Products delivered to Institutional Relationships	70	60	10	17
Other Investment Bank Products	77	40	37	93
Sector Earnings	$ 379	$ 340	$ 39	11
Corporate Items (after-tax):				
Credit Loss Provision	(58)	(13)	(45)	-
Other Corporate Items	(51)	(50)	(1)	(2)
Total Corporate Items	$(109)	$ (63)	$ (46)	(73)
Total Citicorp	$ 270	$ 277	$ (7)	(3)

* If the corporate allowance for possible credit losses was allocated to reflect core business results in conformity with generally accepted accounting principles, Individual Banking and Institutional Banking products would reflect incremental provisions of $36 million and $83 million for the first quarter of 1986 and $20 million and $7 million for the first quarter of 1985, respectively, bringing the ratio of allowance to loans for these businesses respectively to .90% and 1.44% for 1986 and .78% and 1.05% for 1985.

INDIVIDUAL BANKING - FINANCIAL PERFORMANCE AND DISCUSSION

Citicorp's Individual Banking activities provide a complete range of financial services to consumers in the United States and, through its Private Banking and International Groups, to consumers around the world. These activities include transactional services, savings products, loans, insurance -- particularly life, accident and health, where permissible -- and investment services, specifically, discount brokerage and tax-exempt money market funds.

(In Millions of Dollars)	First Quarter 1986	1985	Change	%
Total Revenue	$1,288	$922	$366	40
Provision for Possible Credit Losses	227	115	112	97
Operating Expenses	881	680	201	30
Net Income	97	70	27	39
Average Assets ($ Billions)	66	50	16	32
Return on Assets (%)	.60	.57	.03	-
Return on Equity (%)	14.9	14.2	.7	-

The Individual Bank continued its substantial growth in revenue and overall profitability with revenue momentum continuing to be provided by the New York branch system, domestic card products, worldwide Private Banking, and the International Group. Total revenues advanced 40% to $1,288 million, benefiting from growth in customer assets and the favorable rate environment, as well as from Individual Banking's continuing program of selling mortgage pass-throughs and mortgage-backed securities. The ability to originate, package and sell mortgage-backed securities is a key component of the Individual Bank's strategic goal of becoming the preeminent domestic mortgage bank.

Revenue and asset growth momentum was also sustained during the period by the domestic card businesses, with outstanding cards exceeding 17.5 million. Earnings of the Private Banking group were well diversified geographically; approximately one half of which were attributed to domestic operations. During the first quarter, efforts continued to incorporate the 1985 acquisitions in Italy, Belgium and Chile into the International Group's global distribution network. Additionally, the first quarter saw the acquisition of an insurance brokerage in the United Kingdom.

The substantial loan growth over the last year was accompanied by an increase in net credit write-offs. First quarter write-offs of $221 million were up $116 million over the corresponding period last year. While much of this increase is attributable to increased volumes, the continuing shift in the portfolio toward a higher proportion of credit card receivables was also a factor. Card products, which are the fastest growing segment of the business, have an historically higher credit loss experience, particularly during the early years of a credit card portfolio. The higher write-offs were reflected in the comparative first quarter ratios of net loan losses to average loans: 1.59% versus .99% in the previous year.

Consistent with the change in the way the Corporation reports sector results, Individual Bank earnings were charged an amount to build the total allowance for possible credit losses equal to .50% of consumer loan growth from quarter-to-quarter. This charge in the first quarter of 1986 was $6 million, down $4 million from the same period last year, with the allowance allocated to the sector amounting to $286 million as of March 31, 1986 compared to $223 million at March 31, 1985.

During the first quarter, operating expenses were 2% lower than the final quarter of 1985 a 30% higher than last year's first quarter. The variance to last year's fourth quarter w largely due to lower promotional expenditures, while the increase over 1985's first quarter w attributable to the higher infrastructure expenses required to support greater vo[illegible]s, a additional investments in new business initiatives, including aquisitions.

The major Individual Banking businesses - Bankcards, the New York branch system, Private Banki worldwide and the International Group - substantially exceeded corporate return targets, b returns from other developing areas reduced overall key performance indicators.

Detail of Consumer Credit Losses (primarily installment and revolving credit loans)

(In Millions)	1st Qtr 1986	4th Qtr 1985	3rd Qtr 1985	2nd Qtr 1985	1 Q 19
Gross Loan Losses					
In Domestic Offices	$238	$210	$170	$147	$1
In Overseas Offices	26	25	21	15	
	$264	$235	$191	$162	$1
Loan Recoveries					
In Domestic Offices	$ 35	$ 33	$ 30	$ 27	$
In Overseas Offices	8	8	5	5	
	$ 43	$ 41	$ 35	$ 32	$
Net Loan Losses					
In Domestic Offices	$203	$177	$140	$120	$
In Overseas Offices	18	17	16	10	
	$221	$194	$156	$[illegible]	$1
Net Loan Losses as a Percentage of Average Consumer Loans	1.59%	1.45%	1.26%	1.15%	.9

A strict contractual write-off policy dictates that consumer loans will be written off after predetermined number of days. Those loans not yet written off and with principal or intere payment delinquencies of 90 days or more comprised 1.86% of the total March 31, 1986 consum loan portfolio, compared with the March 31, 1985 ratio of 1.59%. The policy for suspendi accruals of interest on consumer loans varies based on the terms, security and ri characteristics of each product, and in consideration of write-off criteria in place. Consum loans for which accruals of interest had been suspended were $635 million at March 31, 198 Consumer loans with delinquencies of 90 days or more for which interest continued to be accru were $485 million at March 31, 1986.

INSTITUTIONAL RELATIONSHIPS - FINANCIAL PERFORMANCE AND DISCUSSION

Institutional Relationships' results include earnings from the delivery of Institutional Banking and Investment Banking products to corporations, governments and financial institutions worldwide. Refer to page 8 for an analysis of earnings by product.

(In Millions of Dollars)	First Quarter 1986	1985	Change	%
Total Revenue	$872	$845	$ 27	3
Provision for Possible Credit Losses	83	81	2	2
Operating Expenses	415	366	49	13
Net Income	205	230	(25)	(11)
Average Assets ($ Billions)	77	73	4	5
Return on Assets (%)	1.08	1.27	(.19)	-
Return on Equity (%)	26.9	31.8	(4.9)	-

Revenues from Institutional Relationships were diversified over a broad range of products. The 3% increase in total revenue over the first quarter of last year reflected improvements in fees, commissions and other revenues. Asset-related credit revenue was unchanged from quarter to quarter, while foreign exchange was lower. Write-offs were flat with the first quarter of 1985. Operating expenses were up $49 million, or 13%, over 1985's first quarter. This increase over the first quarter included costs associated with improved service delivery and product development.

Key performance indicators continued to surpass corporate hurdles with a 26.9% return on equity and a 1.08% return on assets. Average assets at $77 billion grew by 5% over the same period last year.

Geographically, Institutional Relationships' earnings in the first quarter were diversified with approximately half attributed to North American operations.

Earnings that result from the delivery of Institutional Banking products to the institutional customer base were $135 million for the first quarter of 1986, $35 million lower than for the same period in 1985.

Institutional Banking Products (In Millions of Dollars)	First Quarter 1986	1985	Change	%
Total Revenue	$681	$688	$ (7)	(1)
Operating Expenses	356	315	41	13
Net Income	135	170	(35)	(21)

Total revenue was down $7 million, or 1%, from the first quarter of last year. The improvement in fees, commissions and other revenues from Institutional Banking products was not sufficient to offset lower foreign exchange, last year's sale of aircraft lease residuals and other assets, as well as the beneficial effect of a contract settlement in 1985. Asset-related credit revenue remained flat to last year. Operating expenses of $356 million were up 13% over the first quarter of 1985. Average assets at $75 billion grew by 6% over the same period last year.

Net commercial loan write-offs were $82 million, compared to $79 million in the first quarter of 1985, reflecting continuing weaknesses in certain industries. Citicorp continued to maintain a conservative posture in the recognition of both public and private-sector write-offs. Consistent with the change in the way the Corporation reports sector results, Institutional Relationships' credit loss provision was increased $1 million in order to maintain its allowance for possible credit losses at .60% of commercial loans. The comparable increase in the first quarter of 1985 was $2 million.

Cash basis loans totaled $2,196 million at quarter end, down $29 million from 1985's first quarter and a decrease of $52 million from year end. The ratio of cash basis loans to total loans decreased from 2.2% a year ago and from 2.0% at the end of the fourth quarter to the current level of 1.9%.

Earnings that result from the delivery of Investment Banking products to the institutional customer base were $70 million for the first quarter of 1986, $10 million higher than for the same period of 1985.

Investment Banking Products (In Millions of Dollars)	First Quarter 1986	1985	Change	%
Total Revenue	$191	$157	$ 34	22
Operating Expenses	59	51	8	16
Net Income	70	60	10	17

Total revenue in the first quarter was $191 million, 22% higher than the first quarter of last year, reflecting improved fees, commissions and other revenues from Investment Banking products. Asset-related credit revenue remained flat to last year. Operating expenses at $59 million were up 16% over the first quarter of 1985. These results are also included in the discussion of Investment Banking on page 15.

Products Delivered to Institutional Relationships

The table below shows net income by product for the first quarter of 1986. Detailed descriptions of these products are presented in Citicorp's 1985 Annual Report.

(In Millions of Dollars)	First Qtr. 1986
Core Lending	$ 60
Debt Products/Money Market Services	37
Foreign Exchange Services	15
Specialized Finance	28
Liquidity Insurance, Financial Guarantees & Asset Intermediation	28
Advisory, Trade, Transaction Processing & Other	37
Total Institutional Relationships	$205

il of Commercial Loan Losses

Millions)	1st Qtr 1986	4th Qtr 1985	3rd Qtr 1985	2nd Qtr 1985	1st Qtr 1985
s Loan Losses					
Domestic Offices	$ 15	$ 30	$ 21	$ 13	$ 22
Overseas Offices	83	138	79	74	65
	$ 98	$168	$100	$ 87	$ 87
Recoveries					
Domestic Offices	$ 7	$ 13	$ 2	$ 7	$ 5
Overseas Offices	9	13	15	7	3
	$ 16	$ 26	$ 17	$ 14	$ 8
Loan Losses					
Domestic Offices	$ 8	$ 17	$ 19	$ 6	$ 17
Overseas Offices	74	125	64	67	62
	$ 82	$142	$ 83	$ 73	$ 79
Loan Losses as a Percentage of erage Commercial Loans	.57%	.96%	.56%	.51%	.55%

BAS ND RENEGOTIATED COMMERCIAL LOANS

basis (nonaccrual) loans are those on which, as a result of doubt as to collection, income ecognized only to the extent cash is received. Renegotiated loans are those on which the of interest has been reduced as a result of the borrower's inability to meet the original s.

corp follows strict cash basis practices whereby loans are classified as cash basis whenever reach 90 days past due status, irrespective of collateral or any other favorable prospects. e Citicorp's policy allows for exceptions in unusual circumstances, any such exceptions have insignificant in amount.

basis and renegotiated commercial loans at March 31, 1986 were $2,196 million, down $29 ion from a year ago. Of the $2,196 million, approximately 30% was to borrowers in countries Central and South America, primarily in Argentina, Venezuela, Brazil and Mexico. The /Pacific region accounted for 27% of cash basis loans mainly in the Philippines.

Cash basis lease financings were $30 million at March 31, 1986 and $70 million at March 3 1985.

The classification of loans as cash basis and renegotiated is a specialized diagn[redacted] to used by financial institutions. Citicorp's experience, as well as the experience o[redacted]ther generally has shown that a substantial percentage of cash basis and renegotiated loans a ultimately collected.

Real estate acquired in settlement of loans, included in other assets in the financi statements, totaled $242 million at March 31, 1986, down $10 million from a year ago and do $8 million from December 31, 1985. Domestic real estate, which represented $187 million the total real estate at March 31, 1986, accounted for substantially all of the decrease total real estate acquired since March 31, 1985.

	March 31, 1986						
(In Millions)	Cash Basis	Renego-tiated	Total	Dec. 31 1985	Sept. 30 1985	June 30 1985	Mar. 3 1985
Cash Basis and Renegotiated Loans:							
In Domestic Offices							
Real Estate Loans.....	$ 89	$ 10	$ 99	$ 101	$ 95	$ 113	$ 192
Other Commercial Loans.....	348	7	355	392	549	501	332
In Overseas Offices.....	1,715	27	1,742	1,755	1,840	1,762	1,701
Total Cash Basis and Renegotiated Loans.....	$2,152	$ 44	$2,196	$2,248	$2,484	$2,376	$2,225
Cash Basis and Renegotiated Loans as a % of Commercial Loans....			3.8%	3.9%	4.1%	4.1%	[redacted].9%
Cash Basis and Renegotiated Loans as a % of Total Loans.....			1.9%	2.0%	2.2%	2.3%	2.2%

INTERNATIONAL FINANCING ACTIVITIES

International financing activities are discussed in Citicorp's Annual Report and Form 10-K for the year ended December 31, 1985. The following is a summary of developments in certain countries concerning efforts toward the resolution of payment problems experienced by [redacted] countries. While no absolute assurance can be given, Citicorp management bel[redacted] that these developments will not ultimately have a material adverse effect on Citicorp's financial condition.

MEXICO

The government of Mexico and the participating international banks have signed agreements to implement the previously reported restructuring of medium-term maturities. Through these agreements, which affect $48.7 billion of Mexican public-sector debt, certain amounts that would have matured through 1990 have been rescheduled through 1998. The last of these agreements became effective during the first quarter of 1986.

Citicorp's share of the restructuring, which is described in detail in the 1985 Annual Report and Form 10-K, is approximately $1.4 billion. In addition, the 13-member Bank Advisory Group, of which Citibank, N.A. is a member, has endorsed a Mexican request that maturities aggregating $950 million, due in the fourth quarter of 1985 under a previous financing, be extended until the third and fourth quarters of 1986.

Mexico is reassessing its 1986 financial plan in the context of the recent oil price decline. Mexico has indicated that its discussions with the IMF and World Bank continue in order to obtain the support of these institutions for its 1986 program.

During the three months ended March 31, 1986, no additional cross-border advances were made to Mexican public-sector borrowers, and approximately $3 million of principal was repaid. Interest on Mexican public-sector outstandings included in income for the quarter amounted to $42 million, and such interest received in cash amounted to $40 million.

BRA[redacted]

Discussions with Brazilian officials to reschedule and extend 1985 and 1986 maturities of public and private-sector debt, including maintenance of trade and interbank facilities, have concluded. An agreement has been reached with the Brazil Advisory Committee on a proposal which has been sent to the international banking community for approval. The agreement affects principal of approximately $6.1 billion of 1985 maturities and $9.6 billion of 1986 maturities. Under the agreement the debt that fell due in 1985 will be rescheduled through 1993, with principal payments beginning in 1991. The 1986 maturities will be rolled forward on a demand basis with the Brazilian Central Bank. The debt will have interest rate margins of 1 1/8% over Libor or over an adjusted certificate of deposit (or comparably priced domestic) rate, compared to the previous spreads of 2% over Libor or 1 3/4% over prime. Citicorp's share of the restructuring includes $109 million of debt previously priced over prime and $959 million of debt which utilized Libor as its reference rate. Also, interbank and trade lines of approximately $16 billion (Citicorp's share is $661 million) will be maintained for another year as part of the proposed agreement. Pending the effectiveness of the proposed agreement, provision has been made on an interim basis to extend or roll forward 1985 and 1986 maturities through August 15, 1986.

During the three months ended March 31, 1986, cross-border outstandings in Brazil were affected by additions of approximately $89 million and reductions of approximately $28 million, primarily due to principal payments. Approximately $144 million of gross interest revenue was earned on cross-border and foreign currency outstandings, and approximately $155 million was collected in cash.

ARGENTINA

Based on IMF support for Argentina's new economic program, the participating international banks have executed agreements with Argentina providing for a new $3.7 billion, 10-year term credit, with principal payments beginning after three years, and a new $500 million, four-year trade credit and deposit facility. Banks have also agreed to commit for one year to a trade credit maintenance facility and a money market facility. In addition, substantial progress has been made in the execution and implementation of agreements for refinancing $9.9 billion of public-sector maturities and $3.5 billion of private-sector debt. The public-sector refinancing covers maturities from 1982 to 1985 and provides for tenors of up to 12 years. The private-sector refinancing covers 1984 and 1985 maturities plus certain 1982 and 1983 maturities not previously covered and provides for tenors of 10 years.

The agreements are described in detail in the 1985 Annual Report and Form 10-K. Citicorp is participating in the new lending in an amount approximating $226 million, and its share of the public and private-sector refinancing amounts to $387 million. Citicorp's commitments under the trade credit maintenance facility and money market facility are $95 million and $156 million, respectively.

A drawdown under the IMF standby originally scheduled for January, 1986 was made on March 14, 1986 after completion of discussions and the reaching of an agreement between the IMF and Argentina with respect to Argentine compliance with certain IMF performance criteria. Because of this delay, the IMF standby was reduced by the amount of one drawdown.

After considering a request from the government of Argentina, the Bank Advisory Committee agreed in January to roll over public and private-sector principal maturities falling due during the period January 1, 1986 through April 30, 1986 for 90 and 180-day periods, respectively.

In April 1986, representatives of the government of Argentina met with the Bank Advisory Committee to discuss a 1986-87 refinancing program. In the course of these discussions, the commercial banks agreed to roll over principal maturities during the period May 1, 1986 through September 30, 1986 for an additional 180-day period.

During the three months ended March 31, 1986, Citicorp's cross-border advances to Argentina were increased by additions of $64 million. Approximately, $108 million of principal was repaid. Interest on cross-border outstandings included in income was approximately $38 million, and approximately $30 million was received in cash. Of the cash received, approximately $6 million represented interest on cash basis loans for years prior to 1986.

VENEZUELA

Agreements were signed by Venezuela and the participating international banks in February, 1986, encompassing the restructuring of $21.2 billion of Venezuelan public-sector debt. The restructuring covers principal payments maturing through 1988 and provides for the rescheduling of these maturities over 12 years with quarterly payments commencing in 1988 and ending in 1997. A $750 million principal payment is to be made upon the effectiveness of the rescheduling. A program for making foreign exchange available at preferential rates for private-sector debtors is in the process of implementation.

Citicorp's share of the public-sector restructuring, which is described in detail in the 1985 Annual Report and Form 10-K is $709 million.

During the three months ended March 31, 1986, no cross-border advances to Venezuelan public-sector borrowers were made, and no principal was repaid. Interest on Venezuelan public-sector outstandings included in income for the quarter amounted to $18 million and $12 million of interest on such outstandings was received in cash.

PHILIPPINES

In the Philippines, Citibank and other banks have signed an agreement that provides for a new $925 million, 9-year term loan and have committed to maintain approximately $2.9 billion of short-term trade credit facilities through 1986. In addition, the Philippine government and the 12-member Bank Advisory Committee for the Philippines have agreed in principle to reschedule approximately $5.8 billion of existing bank debt, and the IMF has agr[illegible]to provide a standby credit. The availability of funds under the standby credit is su[illegible] to compliance with IMF targets and conditionalities.

Citicorp's share of the new term loan is approximately $126 million, and its commitment under the trade credit facilities is approximately $751 million. The rescheduling of existing bank debt will involve approximately $371 million of Citicorp's Philippine outstandings.

CROSS-BORDER AND FOREIGN CURRENCY OUTSTANDINGS (1)
Adjusted for Net Local Currency Outstandings, External Guarantees and Collateral

(In Billions)	Total Adjusted Outstandings (2) Mar. 31, 1986	Dec. 31, 1985
Countries With Outstandings Exceeding 3/4% of Total Assets		
Japan	5.2	5.8
Brazil	4.7	4.7
United Kingdom	3.9	3.6
Mexico	2.8	2.8
Federal Republic of Germany	2.7	2.4
Canada	2.5	2.8
Philippines	1.8	1.8
[illegible]alia	1.6	1.8
[illegible]e	1.6	1.5
Argentina (3)	1.3	1.4
Korea (3)	1.3	1.4

(1) Outstandings are presented on a regulatory reporting basis, and include all loans, deposits at interest with banks, acceptances, other interest-bearing investments and other monetary assets.

(2) Legally binding cross-border and foreign currency commitments, including irrevocable letters of credit and commitments to extend credit, after adjustment to assign externally guaranteed commitments to the country of the guarantor, amounted to $.7 billion in Australia , $.8 billion in Canada, $.5 billion in the Federal Republic of Germany, $1.4 billion in France, $.6 billion in Japan, $.5 billion in Korea, and $1.9 billion in the United Kingdom at March 31, 1986. Commitments were not material in relation to adjusted outstandings in any other country in the table.

(3) Less than 3/4% of total assets at March 31, 1986.

Included in overseas cash basis loans are a number of loans in countries which ar currently in the process of refinancing their external debt or which have completed suc refinancings. In view of investor interest in this aspect of Citicorp's activities, th table below provides additional details of cross-border and foreign currency outstanding and also local and foreign currency cash basis loans in the affected countries; t[redacted]hir column of the table shows the impact on Citicorp's earnings (after-tax), th three-month period ending March 31, 1986 spread among various countries. The amount include interest reversed when loans are placed on a cash basis status, plus the cost o funding the cash basis loans, reduced by interest received in cash and included in income.

DETAILS OF REFINANCING COUNTRIES
At March 31, 1986

	Adjusted Total Cross-Border And Foreign Currency Outstandings (3) (In Billions)	Cash Basis Loans (1) (In Millions)	Estimated Impact Of Cash Basis Loans on Y-T-D Earnings (In Millions)
Argentina	$ 1.3	$ 87	$ 1.0
Brazil	4.7	111	3.7
Chile	0.6	15	(0.1)
Dominican Republic	0.1	8	0.2
Ecuador	0.4	8	0.2
Jamaica	0.1	-	-
Mexico	2.8	54	(0.2)
Morocco	0.1	-	
Nigeria	0.1	2	[redacted]
Panama	0.3	3	
Peru	0.1	38	(0.5)
Philippines	1.8	163	1.3
Poland	0.1	105	0.8
South Africa	0.7	6	-
Uruguay	0.3	3	-
Venezuela	1.3	275	(1.3)
Yugoslavia	0.2	-	-
All Other (2)	0.2	108	(0.2)
TOTAL	$15.2	$986	$ 4.9

(1) Includes both local and foreign currency loans.
(2) 14 countries under $50 million of Cross-Border and Foreign Currency Outstandings: Bolivia, Costa Rica, Honduras, Ivory Coast, Liberia, Malagasy, Malawi, Mozambique, Nicaragua, Senegal, Sudan, Togo, Zaire, Zambia.
(3) Legally binding cross-border and foreign currency commitments, including irrevocable letters of credit and commitments to extend credit, after adjustment to assign externally guaranteed commitments to the country of the guarantor, amounted to $.1 in South Africa at March 31, 1986. Commitments were not material in relation to adjusted outstandings in any other refinancing country.

INVESTMENT BANKING - FINANCIAL PERFORMANCE AND DISCUSSION

Citicorp's Investment Banking business includes global investment and merchant banking, funding, foreign exchange services, venture capital investment, securities brokerage, insurance, and financial advisory services provided to both Institutional and Investment Banking clients.

(In Millions of Dollars)	First Quarter 1986	1985	Change	%
Total Revenue	$ 465	$ 340	$ 125	37
Operating Expenses	226	167	59	35
Net Income	147	100	47	47
Average Assets ($ Billions)	37	30	7	23
Return on Assets (%)	1.59	1.35	.24	-
Return on Equity (%)	39.6	33.7	5.9	-

Investment Banking achieved substantial growth during first quarter of 1986 with revenues rising 37% and net income up 47% over first quarter of 1985.

The trend of falling interest rates worldwide and a weakening dollar continued during the period. Against this background, strong securities trading results were posted on the international side particularly in Europe and Asia, and global foreign exchange earnings for the quarter rose 28%.

Equity products showed major increases through significant venture capital gains. Fee and commission income for the quarter was up 45% over the prior year with increases coming from public finance, loan syndication, financial advisory, investor services and investment management activities.

Operating expenses rose 35% over first quarter of last year. Over one third of this increase related to newly acquired businesses, primarily AMBAC, a municipal bond insurance and financial guarantee company acquired in mid-1985. The remaining two thirds reflected continued business and technological development investments.

The Investment Bank's global distribution network expanded during the quarter as new activities started up in several locations in Europe, Asia and in global insurance. In addition, strategic steps were taken to benefit from opportunities arising out of the liberalization of banking rules in key countries.

Investment Banking's returns on assets and equity for the quarter improved to 1.59% and 39.6%, respectively, and continued to exceed corporate targets.

Investment Bank Products

The table below summarizes Investment Banking earnings by type of product. It includes the products delivered to the Institutional customer base as well as other Investment Banking products. Detailed descriptions of these products are presented in Citicorp's 1985 Annual Report.

(In Millions of Dollars)	First Qtr. 1986
Debt Products/Money Market Services	$ 52
Equity Products	34
Foreign Exchange Services	54
Advisory Products	5
Other	2
Total Investment Banking	$147

OTHER ITEMS

(In Millions of Dollars)	First Quarter 1986	1985	Change	
Total Revenue	$ (44)	$ (21)	$ (23)	-
Operating Expenses	36	29	7	24
Provision for Possible Credit Losses	119	27	92	-
Net Income	(109)	(63)	(46)	(73)

The components of the Corporation's activities that are not identified with the three core businesses are presented in aggregate within this category. The items primarily include (i) the credit loss provision that represents the build-up of the credit loss allowance beyond that charged to the businesses; (ii) unallocated corporate staff costs; and (iii) other corporate items including start-up activities.

The $46 million decrease in net income was primarily attributable to the $92 million increase in the provision for possible credit losses which was recorded at the corporate level. The corporate portion of the total allowance at March 31, 1986 was $729 million as compared with $388 million at March 31, 1985. Refer to pages 5 and 8 for a discussion of the provision charged to Individual Banking and Institutional Relationships.

STATEMENT OF INCOME ANALYSIS (See page 23)

NET INTEREST REVENUE (Taxable Equivalent Basis)

Net interest revenue for the first quarter of 1986 was $1,496 million, up $221 million or 17% from the same period last year. This strong performance was fueled primarily by a $2 billion, or 17%, rise in average interest-earning assets accompanied by a slight increase in the net rate spread (3.90% vs. 3.88%). The volume increase resulted mainly from substantial growth in the consumer loan portfolio, particularly domestic card products and shelter finance.

First-quarter net interest revenue decreased $61 million, or 4%, compared to the fourth quarter of 1985 as the net rate spread dropped 22 basis points quarter-to-quarter (3.90% vs. 4.12%). However, the $5.9 billion increase in average interest-earning assets largely offset the impact of the decline in the net rate spread.

CREDIT LOSS EXPENSE AND ALLOWANCE

Citicorp has continued to maintain a conservative posture in recognizing loan losses in current earnings. In the first quarter of 1986, the total credit loss provision was $429 million and included $303 million of net loan and lease losses, while adding $126 million to the allowance. In the first quarter of 1985, Citicorp reported a total credit loss provision of $223 million, made up of $184 million in net losses and $39 million in addition to the allowance. The fourth quarter of 1985 recorded a credit loss provision of $394 million consisting of $336 million in net losses and $58 million in addition to the allowance.

The Corporation's loan and lease loss allowance totaled $1,366 million, up $409 million from March 31, 1985 and $131 million over year-end 1985. The allowance represented 1.15% of the total period-end loans and leases, an increase of 9 basis points over year-end 1985 and 23 basis points above the prior year's first quarter.

For the first three months of 1986, net commercial loan losses totaled $82 million, up $3 million over the first quarter of 1985 reflecting continuing weaknesses in certain industries; however, current quarter losses were $60 million below last year's fourth quarter. First quarter recoveries of $16 million improved $8 million over the corresponding period last year and were derived primarily from commercial and industrial loans.

Net consumer loan losses for the first quarter of 1986 amounted to $221 million, an increase of $116 million over 1985's first quarter and $27 million higher than the fourth quarter of last year. The higher write-offs were primarily produced by the growth in asset volumes and the continuing shift in the loan portfolio toward a greater proportion of credit card receivables. Refer to the Individual Bank's financial discussion for further details. The higher write-offs were reflected in the comparative ratios of net loan losses to average loans: 1.59% versus .99% in the previous year.

FEE AND COMMISSION REVENUE

Total fee and commission revenue in the first quarter rose $197 million, or 43%, to $659 million from the $462 million level a year ago. The Individual Bank accounted for approximately half of the increase as growth in the credit card portfolios continued, resulting in increased membership, merchant discount and interchange fees. Fee and commission revenue from Institutional Bank products rose 21% versus the first quarter last year, primarily in financial guarantees and trade-related service fees. The Investment Bank recorded a 45% increase in fee and commission revenue over the comparable period a year ago, diversified over various business activities, which include corporate and public finance fees and financial advisory services fees.

Compared with the fourth quarter of 1985, total fees and commissions increased $31 million, or 5%, benefiting from increased credit card volumes. . . .

TRADING ACCOUNT

Securities trading revenue was $35 million for the first quarter of 1986, up $4 millio from the comparable period last year and down $6 million, or 15%, from the previou quarter's results. The first quarter-to-first quarter improvement was prima[illegible]y th result of good trading performances recorded in European and Asian trading cen[illegible]whic more than offset declines in domestic securities trading. The fourth quarter-to-firs quarter decrease reflects the impact of interest rate fluctuations on the domesti government security and municipal bond activities.

FOREIGN EXCHANGE

First-quarter foreign exchange revenue of $99 million increased $7 million, or 8%, ove the first quarter of last year and $29 million, or 41%, compared to the fourth quarter o 1985. The increases were driven primarily by higher foreign exchange revenue fro overseas locations, particularly when compared to the fourth quarter of 1985. Revenue attributable to New York operations were approximately flat compared to the first an fourth quarters of 1985. Foreign exchange revenue generated through customer commercia transactions and trading continued to be diversified across many trading centers.

Accumulated foreign currency translation, which represents the after-tax effect o translating certain foreign currency statements into U.S. dollars, is included in retaine earnings in the consolidated balance sheet and amounted to a gain of $22 million in th first quarter of 1986 compared with a $3 million loss in the first quarter of 1985 and $4 million gain in the fourth quarter.

INVESTMENT SECURITIES TRANSACTIONS

Gains from investment securities transactions were $29 million for the first three month of 1986 compared with $6 million in the same period last year and $24 million in th fourth quarter of 1985. Bolstered by the impact of current economic conditions - fallin interest rates worldwide and a weakening dollar - 1986's first quarter gains [illegible]ease both domestically and internationally versus the same period a year ago. Compar[illegible]o th fourth quarter of 1985, profits from investment securities transactions grew in the U.S. but declined overseas.

OTHER REVENUE

(In Millions)	First Qtr 1986	Incr./(Decr.) vs. Fourth Qtr 1985	Incr./(Decr.) vs. First Qtr 1985
Affiliate Earnings	$ 19	$14	$ (2)
Net Gains on Sale/ Disposition of Assets	108	43	98
Gains on Sale of Residual Value of Leased Equipment	8	1	(24)
Other Items	2	(2)	(39)
Total	$137	$56	$ 33

First quarter 1986 other revenue of $137 million advanced $33 million, or 32%, over the same period a year ago. The first quarter-to-first quarter growth was driven by a $98 million rise in gains on the sale/disposition of assets, with profits from the sales of mortgage pass-throughs and mortgage-backed securities, and from the sales of venture capital investments contributing equally to the increase. However, the strong performance in asset sales during the first quarter of 1986 was partially offset by profits from the sale of aircraft and railcar lease residuals and amounts received in a contract settlement during the first quarter of 1985.

Compared to the fourth quarter of 1985, other revenue increased $56 million primarily due to gains from the sales of mortgage pass-throughs and mortgage-backed securities and venture capital investments.

TOTAL OTHER OPERATING EXPENSE

For the first quarter of 1986, other operating expenses rose $308 million, or 26%, over the comparable period a year ago. The increased expense base was largely the result of increased product volumes, business and technology development and other programs. See separate sector financial performance and discussions.

Compared with the fourth quarter of 1985, total other operating expense declined by $110 million, or 9%.

INCOME TAXES

Applicable income taxes for the first quarter of 1986 were $192 million, down $46 million, or 19%, from last year's first quarter and $61 million, or 47%, higher than 1985's fourth quarter.

The decrease in the effective tax rate compared with the first quarter of last year - from 46% to 42% - reflects a higher level of tax exempt income in 1986 and the capital gains tax rate applied to the first quarter 1986 venture capital gains. The increase in the Corporation's tax rate relative to last year's fourth quarter - from 35% to 42% - was largely a result of the impact of tax credits in the earlier period.

GEOGRAPHIC DISTRIBUTION OF NET INCOME

Based on internal allocations and adjustments, earnings are categorized between domesti and overseas as follows:

(In Millions)	Domestic		Overseas		Tota
1986					
First Quarter.....	$115	43%	$155	57%	$ 270
1985					
Fourth Quarter.....	$154	63%	$ 89	37%	243
Third Quarter.....	87	38%	140	62%	227
Second Quarter.....	115	46%	136	54%	251
First Quarter.....	97	35%	180	65%	277
Full Year.....	$453	45%	$545	55%	$998

Because of the integration of global activities, it is not practical to make a precise separation, and various assumptions must be made in arriving at allocations and adjustments to be used in presenting this data.

The principal allocations and adjustments are: (1) charges for all funds employed that are not generated locally are calculated on the amount and nature of the assets and based on a marginal cost of funds concept, Citicorp stockholders' equity is treated as generated and earned based on each area's percentage of total assets; (2) allocation of expenses incurred by one area on behalf of another, including administrative costs, is based on methods intended to reflect services provided; (3) allocation of tax expens (4) allocation of the difference between actual net credit losses and the provi for possible credit losses; and (5) allocation of corporate staff costs (other than those charged to the core businesses) and other corporate items including certain start-up activities. The prior year's disclosures have been reclassified to conform with the current year's presentation.

In the first quarter of 1986, Citicorp's domestic consumer and corporate businesses continued to build revenue momentum, with increases in asset-related credit revenues, fees and commissions and other revenue over the year earlier period. Consumer asset volumes - particularly in shelter finance and domestic card products - continued to grow resulting in higher asset-related credit revenues and fees and commissions. Additionally, the increase was bolstered by gains on sales of mortgage pass-throughs and mortgage-backed securities and gains from sales of venture capital investments. Domestic trading account profits were lower than in last year's first quarter. Higher domestic consumer credit write-offs and the increased addition to the credit loss allowance raised the provision for credit losses domestically. Higher operating expenses reflected continued business development, expansion and improvements to product delivery.

Versus the fourth quarter of 1985, domestic earnings decreased with the comparison particularly affected by the weaker trading performance and increased consumer credit losses.

Overseas earnings in the first quarter declined compared with the same period a year ago. Stronger fees and commissions, securities trading and asset-related credit revenues were partially offset by declines in other revenue, primarily the result of last year's contract settlement. Additionally, higher commercial write-offs in certain geo phic regions and higher operating expenses of several newly acquired businesses impa the comparison.

First quarter overseas earnings increased significantly over fourth quarter results reflecting higher trading profits, foreign exchange, fees and commissions, and other revenues partially offset by lower asset-related credit results. The improvement was also affected by lower commercial write-offs and lower operating expense levels.

NET INTEREST REVENUE STATISTICS*

	Domestic	Overseas	Total
NET INTEREST REVENUE (Taxable Equivalent Basis) (In Millions)			
1986			
First Quarter	$ 917	$ 579	$1,496
1985			
Fourth Quarter	$ 903	$ 654	$1,557
Third Quarter	848	567	1,415
Second Quarter	776	576	1,352
First Quarter	740	535	1,275
Full Year	$3,267	$2,332	$5,599
AVERAGE EARNING ASSETS (In Billions)			
1986			
First Quarter	$ 81.3	$ 74.3	$155.6
1985			
Fourth Quarter	$ 77.1	$ 72.7	$149.8
Third Quarter	73.1	69.1	142.2
Second Quarter	71.6	65.5	137.1
First Quarter	70.1	63.2	133.3
Full Year	73.0	67.6	140.6
NET RATE SPREAD (Taxable Equivalent Basis) (Percent)			
1986			
First Quarter	4.57	3.16	3.90
1985			
Fourth Quarter	4.65	3.57	4.12
Third Quarter	4.60	3.26	3.95
Second Quarter	4.35	3.52	3.96
First Quarter	4.28	3.43	3.88
Full Year	4.48	3.45	3.98

* Prior year's amounts have been restated to conform with the current year's presentation.

LIQUIDITY AND CAPITAL FUNDS ANALYSIS

Citicorp's total capital (as defined by regulators) increased by $1,740 million during the quarter and totaled $17,688 million or 9.65% of total assets on March 31, 1986, up $5,201 million or 42% from a year earlier. The increase in first quarter total capital resulted primarily from strong internal equity generation, additions to the allowance for possible credit losses, the issuance of $250 million of Fixed Rate Subordinated Capital Notes due in 1998, and other qualifying term debt. Primary capital (as defined by regulators) was $11,370 million or 6.20% of total assets on March 31, 1986. This represents an increase of $2,173 million, or 24%, over the same date last year and a $478 million, or 4%, increase over year-end 1985. The increase in primary capital over the prior year-end reflects internal equity generation of $261 million, and additions to the allowance for possible credit losses of $131 million. Citicorp continues to have the largest total capital of any private financial institution in the world.

In the first quarter, Citicorp was an active borrower in the term debt market thereby enhancing liquidity. Fixed rate debt of $912 million was issued in the U.S. with maturities from two to thirty years, $650 million of which qualifies for inclusion in total capital. Fixed rate debt of $352 million was issued in the Euromarket with maturities from three to twelve years, $202 million of which qualifies for inclusion in total capital. Citicorp also issued, domestically and overseas, $783 million of floating rate debt with one to twelve year final maturities, $500 million of which qualifies for inclusion in total capital.

At March 31, 1986 Citicorp's total assets were $181.9 billion, up $27.3 billion, or 18%, from the comparable period last year. Consumer loans increased $12.6 billion or 28% from the first quarter of 1985, largely through higher credit card receivables and significant growth in mortgages.

The Corporation's $27.3 billion asset growth in the twelve months since March 31, 1985 has been largely funded by increases in interest-bearing deposits (including significant increases in consumer deposits), the components of total capital, and issuance of other term debt.

Ratios

Percent	1st Qtr 1986	4th Qtr 1985	3rd Qtr 1985	2nd Qtr 1985	1st Qtr 1985
Total Capital (1) as a Percentage of Total Assets (2).....	9.65	9.12	8.37	8.20	8.03
Primary Capital (1) as a Percentage of Total Assets (2).....	6.20	6.23	6.05	6.06	5.91
Common Stockholders' Equity Generation Rate (3).....	10.32	9.32	8.65	10.78	13.08
Dividend Payout Ratio.....	32.1	32.4	34.49	30.45	27.35

(1) See page 2 for definitions.
(2) Total assets, prior to deducting the allowance for possible credit losses, in compliance with regulatory requirements.
(3) Net income available for common stockholders less common stockholders' dividend as a percentage of average common stockholders' equity.

CONSOLIDATED STATEMENT OF INCOME - QUARTERLY — CITICORP and Subsidiaries

(In Millions Except Per Share Amounts)	1986 First	1985 Fourth	1985 Third	1985 Second	1985 First
INTEREST REVENUE					
Interest and Fees on Loans and Lease Financing	$4,038	$3,997	$3,870	$3,895	$3,76
Interest on Deposits with Banks	285	279	289	296	29
Interest on Federal Funds Sold and Securities Purchased Under Resale Agreements	318	322	266	239	26
Interest and Dividends on Investment Securities					
U.S. Treasury and Federal Agencies	61	63	63	68	7
State and Municipal	15	10	8	8	
Other (Principally in overseas offices)	175	162	138	126	11
Interest on Trading Account Assets	218	237	195	217	21
Total Interest Revenue	$5,110	$5,070	$4,829	$4,849	$4,72
INTEREST EXPENSE					
Interest on Deposits	$2,262	$2,170	$2,206	$2,271	$2,21
Interest on Other Borrowed Money	892	882	800	836	83
Interest on Long-Term Debt and Subordinated Capital Notes	525	485	455	431	43
Total Interest Expense	$3,679	$3,537	$3,461	$3,538	$3,49
NET INTEREST REVENUE	$1,431	$1,533	$1,368	$1,311	$1,23
LOAN LOSS EXPENSE					
Provision for Possible Credit Losses	$ 429	$ 394	$ 346	$ 280	$ 22
NET INTEREST REVENUE AFTER PROVISION FOR POSSIBLE CREDIT LOSSES	$1,002	$1,139	$1,022	$1,031	$1,01
FEES, COMMISSIONS AND OTHER REVENUE					
Fees and Commissions	$ 659	$ 628	$ 512	$ 521	$ 46
Trading Account	35	41	58	80	3
Foreign Exchange	99	70	118	78	9
Investment Securities Transactions	29	24	25	4	
Other Revenue	137	81	38	57	10
Total Fees, Commissions and Other Revenue	$ 959	$ 844	$ 751	$ 740	$ 69
OTHER OPERATING EXPENSE					
Salaries	$ 600	$ 591	$ 546	$ 509	$ 47
Staff Benefits	117	116	107	102	9
Total Staff Expense	$ 717	$ 707	$ 653	$ 611	$ 56
Net Premises Expense	133	142	118	115	10
Equipment Expense	135	144	122	114	10
Other Expense	514	616	514	470	41
Total Other Operating Expense	$1,499	$1,609	$1,407	$1,310	$1,19
Income Before Taxes	$ 462	$ 374	$ 366	$ 461	$ 51
Income Taxes	192	131	139	210	23
NET INCOME	$ 270	$ 243	$ 227	$ 251	$ 27
NET INCOME PER SHARE*					
On Common and Common Equivalent Shares	$ 1.87	$ 1.69	$ 1.60	$ 1.81	$ 2.0
Assuming Full Dilution	$ 1.87	$ 1.68	$ 1.60	$ 1.81	$ 2.0

* On net income available for common stockholders after deducting preferred stock dividends of $20 million in the first quarter of 1986, $19 million in the fourth quarter of 1985, $16 million in the third quarter of 1985, $14 million in the second quarter of 1985, and $14 million in the first quarter of 1985.

CONSOLIDATED BALANCE SHEET — CITICORP and Subsi

(In Millions)	1986 Mar. 31	1985 Dec. 31	1985 Sept. 30	1985 June 30	Mar
ASSETS					
Cash and Due from Banks	$ 6,978	$ 5,218	$ 4,888	$ 4,277	$ 4
Deposits at Interest with Banks	12,643	12,693	12,118	12,463	11
Investment Securities					
U.S. Treasury and Federal Agencies	2,446	2,818	2,514	2,576	2
State and Municipal	720	825	485	441	
Other (Principally in overseas offices)	6,373	6,004	5,027	3,791	3
Trading Account Assets	9,622	6,408	6,198	5,216	5
Federal Funds Sold and Securities Purchased Under Resale Agreements	5,780	6,343	6,495	6,419	6
Loans and Lease Financing, Net					
Commercial	$ 58,503	$ 58,172	$ 60,665	$ 58,124	$ 57
Consumer	57,243	55,518	51,644	47,129	44
Lease Financing	2,865	2,809	2,641	2,407	2
Loans and Lease Financing, Net of Unearned Discount	118,611	116,499	114,950	107,660	104
Allowance for Possible Credit Losses	(1,366)	(1,235)	(1,146)	(1,034)	
Total Loans and Lease Financing, Net	$117,245	$115,264	$113,804	$106,626	$103
Customers' Acceptance Liability	5,958	6,396	7,332	7,943	8
Premises and Equipment, Net	2,650	2,544	2,452	2,280	2
Interest and Fees Receivable	2,629	2,653	2,492	2,384	2
Other Assets	8,852	6,431	5,257	5,164	4
TOTAL	$181,896	$173,597	$169,062	$159,	$154
LIABILITIES					
Non-Interest-Bearing Deposits in Domestic Offices	$ 10,216	$ 10,792	$ 9,842	$ 8,549	$ 7
Interest-Bearing Deposits in Domestic Offices	39,771	39,344	36,905	36,820	35
Non-Interest-Bearing Deposits in Overseas Offices	3,322	3,424	3,517	2,942	2
Interest-Bearing Deposits in Overseas Offices	57,479	51,399	52,686	48,771	48
Total Deposits	$110,788	$104,959	$102,950	$ 97,082	$ 94
Purchased Funds and Other Borrowings	26,779	26,616	25,086	23,810	23
Acceptances Outstanding	6,093	6,598	7,495	8,052	8
Accrued Taxes and Other Expenses	3,722	3,581	3,593	3,402	2
Other Liabilities	6,657	5,823	5,716	4,817	4
Long-Term Debt	17,644	16,316	14,925	13,695	12
Subordinated Capital Notes	2,147	1,899	1,899	1,649	1
Redeemable Preferred Stock	40	40	40	40	
STOCKHOLDERS' EQUITY					
Preferred Stock (Without Par Value)	$ 1,215	$ 1,215	$ 990	$ 840	$
Common Stock ($4.00 par) Issued Shares: 144,403,544; 142,265,429; 141,466,614; 140,919,455; and 140,221,356, respectively	577	569	566	564	
Surplus	1,120	1,056	1,030	1,014	
Retained Earnings	5,492	5,300	5,145	4,986	4
Common Stock in Treasury, at Cost Shares: 12,856,210; 12,888,539; 12,830,383; 12,792,471; and 12,688,493, respectively	(378)	(375)	(373)	(371)	
Total Stockholders' Equity	$ 8,026	$ 7,765	$ 7,358	$ 7,033	$ 6
TOTAL	$181,896	$173,597	$169,062	$159,580	$154

ONSOLIDATED STATEMENT OF CHANGES IN STOCKHOLDERS' EQUITY – QUARTERLY — CITICORP and Subsidiaries

(In Millions)	1986 First	1985 Fourth	1985 Third	1985 Second	1985 First
REFERRED STOCK					
alance at Beginning of Period	$1,215	$ 990	$ 840	$ 640	$ 640
Shares: 6,401,150; 6,400,700; 6,400,400 and 6,400,000, respectively					
Issuance of Stock	–	225	150	200	–
Shares: 450, 300 and 400, respectively					
alance at End of Period	$1,215	$1,215	$ 990	$ 840	$ 640
Shares: 6,401,150; 6,400,700; 6,400,400 and 6,400,000, respectively					
OMMON STOCK					
alance at Beginning of Period	$ 569	$ 566	$ 564	$ 560	$ 556
Shares: 142,265,429; 141,466,614; 140,919,455; 140,221,356; and 138,970,558, respectively					
Issuance of Stock under Savings Incentive, Stock Option, Stock Purchase Plans and Conversion of Convertible Notes	8	3	2	4	4
Shares: 2,138,115; 798,815; 547,159; 698,099; and 1,250,798, respectively					
lanc End of Period	$ 577	$ 569	$ 566	$ 564	$ 560
s: 144,403,544; 142,265,429; 141,466,614; ,919,455; and 140,221,356, respectively					
RPLUS					
lance at Beginning of Period	$1,056	$1,030	$1,014	$ 996	$ 958
Preferred Stock Issuance Cost	–	(3)	(3)	(3)	–
Issuance of Stock under Savings Incentive, Stock Option, Stock Purchase and Executive Incentive Compensation Plans and Conversion of Convertible Notes	64	29	19	21	38
lance at End of Period	$1,120	$1,056	$1,030	$1,014	$ 996
TAINED EARNINGS					
lance at Beginning of Period	$5,300	$5,145	$4,986	$4,825	$4,637
Net Income	270	243	227	251	277
Cash Dividends Declared					
Common	(80)	(73)	(73)	(72)	(72)
Preferred	(20)	(19)	(16)	(14)	(14)
Foreign Currency Translation	22	4	21	(4)	(3)
lance at End of Period	$5,492	$5,300	$5,145	$4,986	$4,825
MMON STOCK IN TREASURY, AT COST					
lance at Beginning of Period	$ (375)	$ (373)	$ (371)	$ (366)	$ (365)
hares: 12,888,539; 12,830,383; 12,792,471; 12,688,493; and 12,702,161, respectively					
Other Treasury Stock Transactions, at Cost	(3)	(2)	(2)	(5)	(1)
Shares: (32,329); 58,156; 37,912; 103,978; and (13,668), respectively					
lance at End of Period	$ (378)	$ (375)	$ (373)	$ (371)	$ (366)
hares: 12,856,210; 12,888,539; 12,830,383; 12,792,471; and 12,688,493, respectively					
TAL STOCKHOLDERS' EQUITY					
lance Beginning of Period	$7,765	$7,358	$7,033	$6,655	$6,426
s during Period, Net	261	407	325	378	229
lance End of Period	$8,026	$7,765	$7,358	$7,033	$6,655

CONSOLIDATED STATEMENT OF CHANGES IN FINANCIAL POSITION	CITICORP and Subsidiari	
	Three [redacted]s En	
(In Millions)	1986	19
FUNDS PROVIDED		
Net Income	$ 270	$ 2
Increase in		
Deposits	5,829	3,6
Purchased Funds and Other Borrowings	163	
Long-Term Debt	1,328	
Subordinated Capital Notes	248	
Decrease in		
Federal Funds Sold and Securities Purchased Under Resale Agreements	563	
Other, Net	-	9
TOTAL	$ 8,401	$ 4,9
FUNDS USED		
Cash Dividends Declared	$ 100	$
Increase in		
Cash and Due From Banks and Deposits at Interest with Banks	1,710	1,6
Investment Securities and Trading Account Assets	3,106	2
Federal Funds Sold and Securities Purchased Under Resale Agreements	-	1,0
Loans and Lease Financing, Net	1,981	8
Premises and Equipment, Net	106	
Decrease in		
Purchased Funds and Other Borrowings	-	8
Long-Term Debt	-	
Other, Net	1,398	
TOTAL	$ 8,401	[redacted]4,9

CALCULATION OF NET INCOME PER SHARE On Common and Common Equivalent Shares (1)		
	Three Months End March 31	
(In Millions Except Per Share Amounts)	1986	198
Net Income Available for Common Stockholders		
a. Distributed portion (dividends)	$ 80	$ 7
b. Undistributed portion	170	19
TOTAL	$ 250	$ 26
Shares		
Weighted average common shares outstanding - Market value	127.0	124.
Weighted average common shares outstanding - Book value	3.0	2.
Common stock equivalents (2)	2.1	1.
c. Shares applicable to distributed portion	132.1	128.
Book value shares issuable under stock option and stock purchase plans	2.3	2.
d. Shares applicable to undistributed portion	134.4	130.
Net Income Per Common and Common Equivalent Share		
a÷c Distributed portion	$ .61	$ .5
b÷d Undistributed portion	1.26	1.4
TOTAL	$ 1.87	$ 2.0

(1) The fully diluted calculation assumes conversion of all outstanding convertible notes and the maxi dilutive effect of common stock equivalents. The number of shares issuable on conversion of the no and the additional common stock equivalents (0.7 million in 1986 and 0.1 million in 1985) [redacted]dded the number of shares included in the calculation (resulting in a total of 135.1 million sh[redacted]in 1 and 131.0 million shares in 1985), and the related after-tax interest expense ($0.1 million [redacted] 1986 $0.1 million in 1985) is eliminated.

(2) Common stock equivalents represent shares issuable under the executive incentive compensation plan the dilutive effect of market value shares issuable under stock option and stock purchase plans compu using the treasury stock method.

NSOLIDATED BALANCE SHEET — CITIBANK, N.A. and Subsidiaries

n Millions)	1986 Mar. 31	1985 Dec. 31	1985 Sept. 30	1985 June 30	1985 Mar. 31
SETS					
sh and Due from Banks	$ 6,288	$ 4,586	$ 4,389	$ 3,729	$ 4,199
posits at Interest with Banks	13,180	12,602	12,674	12,761	12,012
vestment Securities					
U.S. Treasury and Federal Agencies	1,755	2,097	1,517	1,675	1,780
State and Municipal	697	801	462	417	419
Other (Principally in overseas offices)	5,770	5,449	4,483	3,045	2,874
ading Account Assets	5,083	2,725	3,178	2,701	2,126
deral Funds Sold and Securities Purchased Under esale Agreements	8,976	11,812	10,104	9,074	8,459
ans and Lease Financing	$ 80,583	$ 77,933	$ 77,911	$ 73,058	$ 71,385
ess: Allowance for Loan and Lease Financing Losses	(700)	(626)	(626)	(576)	(543)
Unearned Discount on Loans	(2,047)	(1,930)	(1,824)	(1,621)	(1,596)
Total Loans and Lease Financing, Net	$ 77,836	$ 75,377	$ 75,461	$ 70,861	$ 69,246
stomers' Acceptance Liability	7,287	7,473	8,117	8,352	8,739
emises and Equipment, Net	1,903	1,831	1,767	1,648	1,601
terest and Fees Receivable	1,955	1,984	1,859	1,808	1,849
her As	5,799	4,113	3,052	3,269	2,268
TAL	$136,529	$130,850	$127,063	$119,340	$115,572
ABILITIES					
n-Interest-Bearing Deposits in Domestic Offices	$ 8,890	$ 9,379	$ 8,915	$ 7,526	$ 6,282
terest-Bearing Deposits in Domestic Offices	27,341	27,280	24,652	24,309	23,631
n-Interest-Bearing Deposits in Overseas Offices	3,184	3,512	3,774	2,876	2,788
terest-Bearing Deposits in Overseas Offices	56,800	51,639	51,507	48,841	48,867
Total Deposits	$ 96,215	$ 91,810	$ 88,848	$ 83,552	$ 81,568
rchased Funds and Other Borrowings	16,145	15,327	14,922	13,714	12,696
ceptances Outstanding	7,417	7,671	8,269	8,454	8,862
crued Taxes and Other Expenses	2,689	2,608	2,416	2,311	1,839
her Liabilities	3,906	3,506	3,278	3,054	2,627
ng-Term Debt	2,915	2,891	2,593	1,600	1,500
OCKHOLDER'S EQUITY					
pital Stock ($20.00 par)	$ 751	$ 751	$ 751	$ 751	$ 751
tstanding Shares: 37,534,553 in each period					
rplus	1,501	1,493	1,091	1,085	1,083
tained Earnings	4,990	4,793	4,895	4,819	4,646
Total Stockholder's Equity	$ 7,242	$ 7,037	$ 6,737	$ 6,655	$ 6,480
TAL	$136,529	$130,850	$127,063	$119,340	$115,572

AVERAGE BALANCES AND INTEREST RATES
(Taxable Equivalent Basis) (1)

(In Millions)	First Quarter 1986 Average Volume	Interest	% Average Rate	Fourth Quarter 1985 Average Volume	Interest	% Average Rate
INTEREST REVENUE						
Loans and Lease Financing (Net of Unearned Discount) (2)						
Commercial Loans						
In Domestic Offices						
Commercial and Industrial	$ 12,930	$ 443	13.89	$ 12,768	$ 425	13.21
Mortgage and Real Estate	6,256	165	10.70	5,872	156	10.54
Loans to Financial Institutions	455	16	14.26	559	20	14.19
In Overseas Offices	38,842	1,381	14.42	39,666	1,414	14.14
Total Commercial Loans	$ 58,483	$2,005	13.90	$ 58,865	$2,015	13.58
Consumer Loans						
In Domestic Offices	$ 46,385	$1,592	13.92	$ 44,236	$1,505	13.50
In Overseas Offices	9,858	358	14.73	8,812	353	15.89
Total Consumer Loans	$ 56,243	$1,950	14.06	$ 53,048	$1,858	13.90
Total Loans	$114,726	$3,955	13.98	$111,913	$3,873	13.73
Lease Financing	2,782	118	17.20	2,746	126	18.20
Total Loans and Lease Financing	$117,508	$4,073	14.06	$114,659	$3,999	13.84
Funds Sold and Resale Agreements	$ 8,361	$ 318	15.42	$ 7,542	$ 322	16.94
Investment Securities						
In Domestic Offices						
U.S. Treasury and Federal Agencies	$ 2,546	$ 64	10.19	$ 2,574	$ 65	10.02
State and Municipal	432	10	9.39	440	12	10.82
Other	1,330	31	9.45	726	31	16.94
In Overseas Offices (Principally local government issues)	5,491	161	11.89	4,485	137	12.12
Total	$ 9,799	$ 266	11.01	$ 8,225	$ 245	11.82
Trading Account Assets						
U.S. Treasury and Federal Agencies	$ (56)	$ 1	(7.24)	$ 433	$ 10	9.16
State and Municipal	1,197	39	13.21	1,093	25	9.07
Other (Principally in overseas offices)	6,228	193	12.57	5,360	214	15.84
Total	$ 7,369	$ 233	12.82	$ 6,886	$ 249	14.35
Interest-Bearing Deposits (Principally in overseas offices)	$ 12,591	$ 285	9.18	$ 12,463	$ 279	8.9[illegible]
Total Interest-Earning Assets	$155,628	$5,175	13.49	$149,775	$5,094	13[illegible]
Non-Interest-Earning Assets	22,938			21,467		
TOTAL ASSETS	$178,566			$171,242		
INTEREST EXPENSE						
Deposits						
In Domestic Offices						
Savings Deposits (3)	$ 15,636	$ 247	6.41	$ 15,239	$ 251	6.53
Negotiable Certificates of Deposit	2,138	52	9.86	2,131	54	10.05
Other Time Deposits (3)	21,783	488	9.09	20,419	415	8.06
Total Domestic Interest-Bearing Deposits	$ 39,557	$ 787	8.07	$ 37,789	$ 720	7.56
In Overseas Offices	56,131	1,475	10.66	54,957	1,450	10.47
Total	$ 95,688	$2,262	9.59	$ 92,746	$2,170	9.28
Funds Borrowed						
In Domestic Offices						
Purchased Funds and Other Borrowings						
Federal Funds Purchased and Securities Sold Under Agreements To Repurchase	$ 10,283	$ 206	8.12	$ 9,869	$ 210	8.44
Commercial Paper	5,169	101	7.92	5,677	114	7.97
Other Purchased Funds	6,973	162	9.42	6,387	148	9.19
Long-Term Debt, Convertible Notes and Subordinated Capital Notes	15,111	385	10.33	13,597	356	10.39
Total in Domestic Offices	$ 37,536	$ 854	9.23	$ 35,530	$ 828	9.25
In Overseas Offices	9,628	563	23.71	8,630	539	24.78
Total	$ 47,164	$1,417	12.18	$ 44,160	$1,367	12.28
Total Interest-Bearing Liabilities	$142,852	$3,679	10.44	$136,906	$3,537	10.25
Demand Deposits in Domestic Offices	8,666			8,224		
Other Non-Interest-Bearing Liabilities	19,144			18,591		
Total Stockholders' Equity	7,904			7,521		
TOTAL LIABILITIES AND STOCKHOLDERS' EQUITY	$178,566			$171,242		
NET INTEREST REVENUE AS A PERCENTAGE OF AVERAGE INTEREST-EARNING ASSETS		$1,496	3.90		$1,557	4[illegible]

(1) The Taxable Equivalent Adjustment is based on the marginal tax rate of 46% for each quarter.

(2) Loans and lease financing balances include cash basis loans and leases.

(3) Savings Deposits consist of Insured Money Market Rate acounts, NOW accounts and other Savings Deposits.

Third Quarter 1985			Second Quarter 1985			First Quarter 1985		
Average Volume	Interest	Average Rate	Average Volume	Interest	Average Rate	Average Volume	Interest	Average Rate
$ 12,869	$ 412	12.70	$ 13,506	$ 478	14.20	$ 13,705	$ 507	15.00
5,436	147	10.73	5,148	161	12.54	4,744	127	10.86
565	17	11.94	623	16	10.30	669	16	9.70
39,594	1,400	14.03	38,179	1,475	15.50	38,430	1,449	15.29
$ 58,464	$1,976	13.41	$ 57,456	$2,130	14.87	$ 57,548	$2,099	14.79
$ 41,595	$1,490	14.21	$ 39,371	$1,409	14.35	$ 37,060	$1,331	14.57
7,419	314	16.79	6,431	269	16.78	6,022	250	16.84
$ 49,014	$1,804	14.60	$ 45,802	$1,678	14.69	$ 43,082	$1,581	14.90
$107,478	$3,780	13.95	$103,258	$3,808	14.79	$100,630	$3,680	14.83
2,537	117	18.30	2,289	110	19.28	2,123	110	21.01
$110,015	$3,897	14.05	$105,547	$3,918	14.89	$102,753	$3,790	14.96
$ 6,917	$ 266	15.26	$ 6,465	$ 239	14.83	$ 6,415	$ 260	16.44
$ 2,347	$ 66	11.16	$ 2,595	$ 64	9.89	$ 2,506	$ 73	11.81
345	11	12.65	389	12	12.37	406	13	12.99
751	26	13.74	860	27	12.59	815	21	10.45
3,641	118	12.86	3,032	109	14.42	2,634	102	15.70
$ 7,084	$ 221	12.38	$ 6,876	$ 212	12.37	$ 6,361	$ 209	13.33
$ 390	$ 15	15.26	$ 599	21	14.06	$ 1,846	$ 52	11.42
1,075	23	8.49	802	22	11.00	487	16	13.32
4,735	165	13.83	4,948	182	14.75	4,508	148	13.31
$ 6,200	$ 203	12.99	$ 6,349	$ 225	14.21	$ 6,841	$ 216	12.81
$ 11,980	$ 289	9.57	$ 11,862	$ 296	10.01	$ 10,940	$ 292	10.82
$142,196	$4,876	13.60	$137,099	$4,890	14.31	$133,310	$4,767	14.50
19,790			19,168			19,214		
$161,986			$156,267			$152,524		
$ 14,503	$ 240	6.57	$ 14,012	$ 243	6.96	$ 13,426	$ 234	7.07
2,263	59	10.34	2,577	72	11.21	2,286	56	9.93
18,471	473	10.16	19,820	481	9.73	19,501	526	10.94
$ 35,237	$ 772	8.69	$ 36,409	$ 796	8.77	$ 35,213	$ 816	9.40
51,489	1,434	11.05	48,488	1,475	12.20	46,376	1,402	12.26
$ 86,726	$2,206	10.09	$ 84,897	$2,271	10.73	$ 81,589	$2,218	11.03
$ 10,549	$ 224	8.42	$ 10,366	$ 209	8.09	$ 9,474	$ 212	9.08
4,250	85	7.93	4,789	102	8.54	5,190	114	8.91
6,401	124	7.69	6,208	182	11.76	6,588	143	8.80
12,400	337	10.78	11,325	321	11.37	10,805	321	12.05
$ 33,600	$ 770	9.09	$ 32,688	$ 814	9.99	$ 32,057	$ 790	9.99
7,934	485	24.25	7,763	453	23.41	7,334	484	26.76
$ 41,534	$1,255	11.99	$ 40,451	$1,267	12.56	$ 39,391	$1,274	13.12
$128,260	$3,461	10.71	$125,348	$3,538	11.32	$120,980	$3,492	11.71
7,436			7,452			5,921		
19,091			16,658			19,056		
7,199			6,809			6,567		
$161,986			$156,267			$152,524		
	$1,415	3.95		$1,352	3.96		$1,275	3.88

CITICORP FINANCIAL STATISTICS

NET INCOME

Year	Quarter	Net Income (in millions)	Net Income Per Share: On Common and Common Equivalent Shares	Net Income Per Share: Assuming Full Dilution
1986	First	$270	$1.87	$1.87
1985	Fourth	$243	$1.69	$1.68
	Third	227	1.60	1.60
	Second	251	1.81	1.81
	First	277	2.02	2.02

COMMON DIVIDENDS

Year	Quarter	Date Declared	Record Date	Date Paid	Dividends Declared (in millions)	Dividends Declared Per Share	Annual Dividend Rate
1986	First	3-18-86	3-28-86	5-1-86	$80	$.615	$2.46
1985	Fourth	12-17-85	12-30-85	2-3-86	$73	$.565	$2.26
	Third	9-17-85	9-27-85	11-1-85	73	.565	2.26
	Second	6-18-85	6-28-85	8-1-85	72	.565	2.26
	First	3-19-85	3-29-85	5-1-85	72	.565	2.26

STOCKHOLDERS' EQUITY AND SELECTED RETURNS

Year	Quarter	Common Stockholders' Equity Per Share	Primary Capital (1) (in millions)	Total Capital (1) (in millions)	Common Shares Outstanding (in thousands)	Return on Total Assets (2)	Return on Common Stock-holders' Equity (2)	Retu On Tot Stockh Equi
1986	First	$51.78	$11,370	$17,688	131,547	.61%	15.2%	13
1985	Fourth	$50.63	$10,892	$15,948	129,377	.56%	13.8%	12
	Third	49.50	10,290	14,243	128,636	.56	13.2	12
	Second	48.34	9,733	13,165	128,127	.65	15.5	14
	First	47.16	9,197	12,487	127,533	.74	18.0	17

LOANS AND LEASE FINANCING OUTSTANDING

(In Millions)	1986 March 31	1985 Dec. 31	1985 Sept. 30	1985 June 30	1985 March 31
Commercial Loans	$ 58,992	$ 58,655	$ 61,110	$ 58,577	$ 58,075
Unearned Discount	(489)	(483)	(445)	(453)	(451)
Commercial Loans, Net of Unearned Discount	$ 58,503	$ 58,172	$ 60,665	$ 58,124	$ 57,624
Consumer Loans	$ 61,648	$ 59,936	$ 56,093	$ 51,488	$ 49,072
Unearned Discount	(4,405)	(4,418)	(4,449)	(4,359)	(4,438)
Consumer Loans, Net of Unearned Discount	$ 57,243	$ 55,518	$ 51,644	$ 47,129	$ 44,634
Lease Financing, Net of Unearned Income	$ 2,865	$ 2,809	$ 2,641	$ 2,407	$ 2,257
Allowance for Possible Credit Losses	$ (1,366)	$ (1,235)	$ (1,146)	$ (1,034)	$ (957)
Total Loans and Lease Financing, Net	$117,245	$115,264	$113,804	$106,626	$103,558

(1) See Page 2 for definitions.
(2) Based on annualized quarterly results.

IL OF CREDIT LOSS EXPERIENCE

(In Millions Of Dollars)	1st Qtr 1986	4th Qtr 1985	3rd Qtr 1985	2nd Qtr 1985	1st Qtr 1985
ALLOWANCE FOR POSSIBLE CREDIT LOSSES AT BEGINNING OF PERIOD	$1,235	$1,146	$1,034	$ 957	$ 917
Deductions					
Gross Loan Losses					
Commercial Loans					
In Domestic Offices	$ 15	$ 30	$ 21	$ 13	$ 22
In Overseas Offices	83	138	79	74	65
Consumer Loans					
In Domestic Offices	238	210	170	147	115
In Overseas Offices	26	25	21	15	16
	$ 362	$ 403	$ 291	$ 249	$ 218
Loan Recoveries					
Commercial Loans					
In Domestic Offices	$ 7	$ 13	$ 2	$ 7	$ 5
In Overseas Offices	9	13	15	7	3
Consumer Loans					
In Domestic Offices	35	33	30	27	21
In Overseas Offices	8	8	5	5	5
	$ 59	$ 67	$ 52	$ 46	$ 34
Net Loan Losses					
In Domestic Offices	$ 211	$ 194	$ 159	$ 126	$ 111
In Overseas Offices	92	142	80	77	73
	$ 303	$ 336	$ 239	$ 203	$ 184
Additions					
Provision for Possible Credit Losses	$ 429	$ 394	$ 346	$ 280	$ 223
Other (Principally from allowance balances of acquired companies and translation of overseas allowance balances)	5	31	5	-	1
	$ 434	$ 425	$ 351	$ 280	$ 224
ALLOWANCE FOR POSSIBLE CREDIT LOSSES AT END OF PERIOD	$1,366	$1,235	$1,146	$1,034	$ 957
Excess of Provision over Net Loan Losses	$ 126	$ 58	$ 107	$ 77	$ 39
Allowance for Credit Losses as a Percentage of Period-End Loans and Leases	1.15%	1.06%	1.00%	.96%	.92%

INVESTMENT SECURITIES

(In Millions)	1986 Mar. 31	1985 Dec. 31	Sept. 30	June 30	Mar.
Carrying Value					
U.S. Treasury and Federal Agencies	$2,446	$2,818	$2,514	$2,576	$2,8
State and Municipal	720	825	485	441	4
Other (Principally in overseas offices)	6,373	6,004	5,027	3,791	3,6
	$9,539	$9,647	$8,026	$6,808	$6,9
Market Value					
U.S. Treasury and Federal Agencies	$2,628	$2,919	$2,516	$2,598	$2,7
State and Municipal	731	799	445	400	3
Other (Principally in overseas offices)	6,593	6,174	5,246	3,935	3,7
	$9,952	$9,892	$8,207	$6,933	$6,8

INVESTMENT SECURITIES
Maturity Distributions at March 31, 1986

Carrying Value	Due Within 1 Year	Due 1-5 Years	Due 5-10 Years	Due Over 10 Years	Tot
U.S. Treasury and Federal Agencies	$ 236	$ 528	$ 503	$1,179	$2,4
State and Municipal	12	48	228	432	7
Other (Principally in overseas offices)	1,499	2,923	1,229	722	6,3
Total	$1,747	$3,499	$1,960	$2,333	$9,5

LONG-TERM DEBT
(With final original maturities of more than one year) (1)
Maturity Distributions at March 31, 1986

(In Millions)	
Parent Company	
Due Within 1 Year	$ 2,527
Due 1-2 Years	389
Due 2-3 Years	2,253
Due 3-4 Years	856
Due 4-5 Years	1,474
Due 5-10 Years	2,155
Due 10-15 Years	1,251
Due 15 Years and Over	1,725
	$12,630
Subsidiaries	
Due Within 1 Year	$ 1,418
Due 1-2 Years	564
Due 2-3 Years	691
Due 3-4 Years	332
Due 4-5 Years	425
Due 5-10 Years	1,063
Due 10-15 Years	520
Due 15 Years and Over	1
	$ 5,014
TOTAL	$17,644

(1) Maturity distribution is based upon contractual maturities or earlier dates at which debt is repayable at the option of the holder or due to required mandatory sinking fund payments or due to call notices issued.

Item 6 - Exhibits and Reports on Form 8-K.

(b) Reports on Form 8-K.

Citicorp filed no Form 8-K Current Report for any month in the quarter ended March 31, 1986.

SIGNATURES

Pursuant to the requirements of the Securities Exchange Act of 1934, the registrant has duly caused this report to be signed on its behalf by the undersigned thereunto duly authorized.

CITICORP
Registrant

By: _____
Thomas E. Jones
Senior Vice President
Chief Accounting Officer

By: _____
Christopher C. York
Assistant Secretary

Date: May 15, 1986

E60 2500

SECURITIES AND EXCHANGE COMMISSION

WASHINGTON, D.C. 20549

FORM 10-K

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

For the fiscal year ended September 30, 1985

47751

Commission file number 1-278

EMERSON ELECTRIC CO.

(Exact name of registrant as specified in its charter)

DEC 12 1985

Missouri	43-0259330
(State or other jurisdiction of Incorporation or organization)	(I.R.S. Employer Identification No.)
8000 W. Florissant Ave., St. Louis, Missouri	63136
(Address of principal executive offices)	(Zip Code)

Registrant's telephone number, including area code: (314) 553-2000

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Securities registered pursuant to Section 12(b) of the Act:

Title of each class	Name of each exchange on which registered
Common Stock of $1.00 par value per share	New York Stock Exchange Midwest Stock Exchange
Skil Corporation 5% Convertible Subordinated Debentures due 1992	New York Stock Exchange

Securities registered pursuant to Section 12(g) of the Act:

None

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, and (2) has been subject to such filing requirements for the past 90 days. Yes ✓ No ____

Aggregate market value of the voting stock held by nonaffiliates of the registrant as of close of business on October 31, 1985: $5,033 million.

Common stock outstanding at October 31, 1985 — 73,866,811 shares

Documents Incorporated by Reference

1. Portions of Emerson Electric Co. Annual Report for 1985. (Parts I and II of Form 10-K).
2. Portions of Emerson Electric Co. Notice of Annual Meeting of the Stockholders and Proxy Statement to be filed within 120 days of the close of the fiscal year. (Part III of Form 10-K).

PART I

Item 1. Business

Emerson was incorporated in Missouri in 1890. Originally engaged in the manufacture and sale of electric motors and fans prior to World War II and aircraft armament items during the war, Emerson's product lines were subsequently expanded through internal growth and acquisition. Emerson is now engaged principally in the design, manufacture and sale of a broad range of electrical-electronic products and systems.

The products manufactured by Emerson may be classified into three industry segments: commercial and industrial components and systems, consumer products, and government and defense systems. Net sales, earnings before income taxes and total assets attributable to each industry segment for the three years ended September 30, 1985 are set forth in Note 11 of Notes to Consolidated Financial Statements on page 49 of the Emerson Electric Co. 1985 Annual Report to Stockholders (the "1985 Annual Report"), which note is hereby incorporated by reference.

COMMERCIAL AND INDUSTRIAL COMPONENTS AND SYSTEMS

Beginning with a selected line of electric motors for industrial and heavy commercial applications, Emerson's products for industrial automation include certain kinds of integral horsepower motors, gear drives, pump motors and electronic variable speed drives. Emerson also produces electronic uninterruptible power supplies, power conditioning and distribution equipment, and modular power systems used in communications and information processing applications.

Emerson manufactures and sells components for the transmission and regulation of mechanical power, such as certain kinds of chain, sprockets, gears, bearings, couplings and speed reducers, and a line of cam-operated index drives, programmable motion controllers and automation accessories. These products are used primarily in industrial and commercial markets requiring the transmission of mechanical motion or drive systems of various types.

Products used in process industries include various types of meters and instrumentation for measurement and control of fluid flow such as rotameters, positive displacement meters, magnetic flow meters, turbine meters, direct mass flow meters and laboratory instruments. Other products are meters and control systems for use in irrigation, sewage and water management; bulk liquid and solids storage controls and indicators; solid state telemetering equipment and various types of pressure and vacuum relief valves. In addition, Emerson manufactures and sells temperature sensors, pressure sensors and transmitters used to measure and/or control temperature, pressure, air speed, altitude and rate and amount of flow, as well as process gas chromatographs and infrared, oxygen and trace moisture analyzers.

Other products for process industry application include a line of plastic-lined plug and butterfly-type valves and related actuators and controllers. Emerson also manufactures electric circulation heaters, fluid heat transfer systems, component heating elements and electronic measurement and data acquisition equipment for use in industrial processing.

Emerson also manufactures a line of multi-purpose pressure and solenoid valves, pressure, vacuum and temperature switches, automatic transfer switches, remote control switches, and electric power control systems. These products are widely used in the automation of equipment and industrial processes and for the control of emergency electric power.

Emerson manufactures and sells potentiometers, trimming potentiometers, resistor networks, thermistors, varistors, digital multimeters and power supplies used in electronic instruments, in computer peripherals and systems, communications systems and specialized industrial processes.

Emerson also produces a variety of industrial and commercial ultrasonic products for applications such as cleaning, sealing, welding, flaw detection and semiconductor wafer processing.

Emerson manufactures and sells a variety of components and systems for service equipment and comfort control applications, including certain sizes of hermetic motors and terminals for hermetically sealed compressors in freezers, air conditioners and coolers; fractional and sub-fractional horsepower motors for selected appliance, office equipment, ventilating equipment, pump, heater and other motor-driven machine applications. Automatic temperature controls and thermo-protective devices are manufactured for gas and electric heating systems, refrigeration and air conditioning equipment and various large and small appliances. Emerson also manufactures and sells a variety of electric heating elements and electrostatic air cleaners.

Emerson manufactures a broad line of components, tools and equipment used in the electrical distribution and telecommunications markets, including utility construction and line maintenance tools, pole line hardware and electrical distribution system components.

Current and noncurrent carrying electrical distribution devices such as panelboards, receptacles, fittings and cable handling reels are manufactured by Emerson for use in hazardous and nonhazardous environments.

Emerson manufactures vibratory separating equipment, oil field equipment, and metal finishing equipment primarily used in the oil well drilling, chemical and petro-chemical, food processing, pulp and paper, ceramic and metal-working markets.

Commercial and industrial components and systems are sold primarily to original equipment manufacturers and to a lesser extent to distributors and users.

CONSUMER PRODUCTS

Selected lighting fixtures are manufactured and sold for use in commercial, institutional and industrial buildings. These lighting fixtures include fluorescent, incandescent and high intensity discharge light sources.

Emerson manufactures and sells a line of electrical products primarily for the residential markets, including console humidifiers, door chimes, intercom systems, electric waste disposers, hot water dispensers, electric comfort heating systems, ventilating equipment and exhaust fans.

Emerson is a producer of selected professional and hardware tools and service equipment. These products include certain kinds of wrenches, thread cutters, pipe cutters, reamers, vises, pipe and bolt threading machines and sewer and drain cleaning equipment. The principal markets for these professional tools and service equipment include plumbing, heating and air conditioning contractors, construction and maintenance companies, petroleum and gas producers, refiners and processors and farm and home consumers.

Emerson is also a producer of selected portable electric tools. These products include circular saws, drills, grinders, hammer drills, reciprocating saws, sanders and accessories. The principal markets include construction, manufacturing, maintenance, tradesmen and home owners.

Emerson also produces a variety of gas cutting and welding equipment, a specialized line of light-duty industrial bench power tools, hobbyists' tools, power chain saws, monofilament line lawn trimmers, and ladders and scaffolding and related accessories. Also produced by Emerson for marketing by a major retailer are shop vacuum cleaners, a line of bench power tools for home workshop use and a line of hand tools including adjustable wrenches, screwdrivers, pliers and chisels.

Consumer products are sold principally to distributors and, to a lesser extent, to retailers.

GOVERNMENT AND DEFENSE SYSTEMS

Emerson is engaged in the research, development, support, manufacture and sale of government and defense systems, principally for the United States Government under contracts with the Air Force, Army, Navy, National Aeronautics and Space Administration and United States Postal Service. Sales of defense systems are also made to international customers. Products include radar systems; electronic warfare systems; telemetry tracking systems; missile launching systems; power conversion equipment; communications systems; simulator systems for training; satellite communications systems; airborne, ground and surface armament systems; guidance and control systems; automatic test equipment; special tactical vehicles; anechoic chambers; microwave systems; radar antennas; and material and mail processing and handling systems.

The major portion of Emerson's contracts with the United States Government are firm fixed price, some of which contain price redetermination provisions. Most of the contracts are subject to cancellation at any time for the convenience of the Government.

PRODUCTION

Emerson utilizes various production operations and methods. The principal production operations are metal stamping, forming, casting, machining, welding, heat treating, painting, mechanical assembly and electrical and electronic assembly. In addition, Emerson also uses specialized production operations, including automatic and semi-automatic testing, automated material handling and storage, ferrous and nonferrous machining and special furnaces for heat treating and foundry applications. Management believes the machinery and equipment used in the above processes are of modern design and well maintained.

RAW MATERIALS AND ENERGY

Emerson's major requirements for basic raw materials include steel, copper, cast iron, aluminum and brass and, to a lesser extent, plastics and other petroleum-based chemicals. Emerson has multiple sources of supply for each of its material requirements. The raw materials and various purchased components required for its products have generally been available in sufficient quantities.

Emerson uses various forms of energy, principally natural gas and electricity, obtained from public utilities. A majority of the plants have the capability of being converted to use alternative higher-cost sources of energy.

PATENTS, TRADEMARKS, LICENSES AND FRANCHISES

The Company has a number of patents, trademarks, licenses and franchises, none of which is considered material to any segment of its consolidated operations.

BACKLOG

The estimated consolidated backlog of the Company was $1,392 million and $1,381 million at September 30, 1985 and 1984, respectively. Of the September 30, 1985 amount, $255 million is expected to extend beyond one year.

COMPETITION

All categories of Emerson's business are highly competitive and the methods of competition vary across all industry segments served by Emerson. Although no one company competes directly with Emerson in all of its product lines, there are a number of companies which compete in one or more of Emerson's product lines. Some of these companies have substantially greater sales and assets than Emerson. In addition, Emerson experiences competition from many smaller companies, particularly in products sold to the construction and contracting industry.

RESEARCH AND DEVELOPMENT

Costs associated with Company-sponsored research, new product development and product improvement were $140.0 million in 1985, $120.3 million in 1984 and $96.8 million in 1983.

ENVIRONMENT

Compliance with laws regulating the discharge of materials into the environment or otherwise relating to the protection of the environment has not had a material effect upon Emerson's capital expenditures, earnings or competitive position. It is not anticipated that Emerson will have material capital expenditures for environmental control facilities during the next fiscal year.

EMPLOYEES

Emerson and its subsidiaries had an average of approximately 61,900 employees during 1985.

UNITED STATES AND FOREIGN OPERATIONS

International sales were $985 million in 1985, $883 million in 1984 and $865 million in 1983, including exports of $287 million, $344 million and $401 million in 1985, 1984 and 1983, respectively. Although there are additional risks attendant to foreign operations, such as nationalization of facilities, currency fluctuations and restrictions on the movement of funds, Emerson's financial position has not been materially affected thereby to date. See Notes 9 and 11 of Notes to Consolidated Financial Statements on pages 48 and 49 of the 1985 Annual Report for further information with respect to foreign operations. These notes are hereby incorporated by reference.

Item 2. Properties

At September 30, 1985, Emerson had 178 manufacturing locations worldwide, with 57 located in 12 foreign countries. The Company occupied a total of 30.2 million square feet, with the majority, approximately 24.7 million square feet, devoted to manufacturing, assembly and storage. This space is occupied by industry segments as follows: 65 per cent commercial and industrial, 26 per cent consumer and 9 per cent government and defense. Of the 30.2 million square feet occupied, 21.3 million square feet are owned or occupied under capital lease obligations, and 8.9 million square feet are occupied under operating leases. The Company considers its facilities suitable and adequate for the purposes for which they are used.

Item 3. Legal Proceedings

Emerson is a party to a number of pending legal proceedings, several of which claim substantial amounts of damages. However, these legal proceedings are not expected to have a material effect on the Company's business or financial position.

As reported on the Company's Form 10-Q for the quarter ended March 31, 1985, A. B. Chance Co., a subsidiary of the Company, is a third party defendant in United States of America v. Conservation Chemical Co., et al. v. Aeroquip Corporation, et al., filed in the United States District Court for the Western District of Missouri. The third party complaint filed June 19, 1984 alleges that A. B. Chance Co. and approximately 150 other third party defendants are jointly and severally liable for the costs of remedying the conditions existing at the Conservation Chemical Co. waste disposal site in Kansas City, Missouri, including the payment of all cleanup costs, response costs, expenses, damages and costs of suit related thereto. The Company has reached a tentative settlement of substantially all of its potential liability in such proceeding in the amount of $121,000. Management believes this matter will not result in a liability that would materially affect the Company's financial position.

Item 4. Submission of Matters to a Vote of Security Holders

There were no matters submitted to a vote of security holders during the quarter ended September 30, 1985.

Executive Officers of the Registrant

The following sets forth certain information as of October 1, 1985 with respect to Emerson's executive officers. These officers have been elected to terms which will expire February 4, 1986:

Name	Position	Age	First Served as Officer In
C. F. Knight*	Chairman of the Board and Chief Executive Officer	49	1972
W. A. Rutledge*	Vice Chairman and Director	61	1974
E. L. Keyes, Jr.*	President and Director	56	1973
J. J. Adorjan	Executive Vice President	46	1975
J. F. Hardymon	Executive Vice President	50	1979
R. W. Staley	Executive Vice President	50	1975
A. E. Suter	Executive Vice President	50	1979
J. K. Ver Hagen	Executive Vice President	47	1977
W. C. Bousquette	Senior Vice President and Chief Financial Officer	48	1984
C. A. Dill	Senior Vice President	45	1973
C. Hansen	Senior Vice President - Secretary and General Counsel	59	1979
J. C. Wilson	Vice President of Finance, Controller and Chief Accounting Officer	60	1963

*Also Chairman or member of certain committees of the Board of Directors.

There are no family relationships between any of the executive officers and directors.

Each of the above has served as an officer or in a supervisory capacity with Emerson for the last five years, except W. C. Bousquette. Mr. Bousquette was elected an officer of the Company effective March 1984, prior to which he was Vice President, Corporate Finance - Controls for Rockwell International Corporation. Prior to joining Rockwell International in 1981, he was with Ford Motor Company in various control and financial positions, most recently as Assistant Corporate Controller.

PART II

Item 5. Market for the Registrant's Common Equity and Related Stockholder Matters

The information regarding the market for the Company's common stock, quarterly market price ranges and dividend payments on page 52 of the 1985 Annual Report and the information under "Approximate number of stockholders at year end" under the column headed 1985 on page 34 of the 1985 Annual Report are hereby incorporated by reference.

Item 6. Selected Financial Data

Information under "As Restated for Poolings of Interests" for years 1981 through 1985 for net sales, net earnings, earnings per common share, cash dividends per common share, long-term debt and total assets on pages 34 and 35 of the 1985 Annual Report is hereby incorporated by reference.

Item 7. Management's Discussion and Analysis of Financial Condition and Results of Operations

Information appearing under "Financial Review" on pages 36 through 38 and under "The Effects of Inflation on Reported Results" on pages 52 and 53 of the 1985 Annual Report is hereby incorporated by reference.

Item 8. Financial Statements and Supplementary Data

The consolidated financial statements of the Company and its subsidiaries on pages 39 through 50, the report thereon of Peat, Marwick, Mitchell & Co. appearing on page 51 and the supplementary financial information on pages 52 and 53 of the 1985 Annual Report are hereby incorporated by reference.

Item 9. Disagreements on Accounting and Financial Disclosure

None.

PART III

Item 10. Directors and Executive Officers of the Registrant

Information regarding directors appearing under "Nominees for Election as Directors" in the Emerson Electric Co. Notice of Annual Meeting of the Stockholders and Proxy Statement for the February 1986 annual stockholders' meeting (the "1986 Proxy Statement") is hereby incorporated by reference. Information regarding executive officers is set forth in Part I of this report.

Item 11. Executive Compensation

Information appearing under "Board of Directors and Committees", "Executive Compensation", "Life Insurance Program", "Performance Shares Bonus Plans", "Employee Benefit Plans", "Retirement Plans", "Employee Stock Options" and "Proposal to Approve the 1986 Stock Option Plan" in the 1986 Proxy Statement is hereby incorporated by reference.

Item 12. Security Ownership of Certain Beneficial Owners and Management

The information regarding benaficial ownership of shares by directors and officers of the Company appearing under "Nominees for Election as Directors" in the 1986 Proxy Statement is hereby incorporated by reference.

Item 13. Certain Relationships and Related Transactions

Information appearing under "Certain Business Relationships" in the 1986 Proxy Statement is hereby incorporated by reference.

PART IV

Item 14. Exhibits, Financial Statement Schedules and Reports on Form 8-K

A) Documents filed as a part of this report:

1. The consolidated financial statements of the Company and its subsidiaries on pages 39 through 50 and the report thereon of Peat, Marwick, Mitchell & Co. appearing on page 51 of the 1985 Annual Report.

2. Financial Statement Schedules
   V - Property, Plant and Equipment
   VI - Accumulated Depreciation of Property, Plant and Equipment

   All others are omitted because they are not required, not applicable or the information is given in the financial statements or notes thereto.

3. Exhibits (Listed by numbers corresponding to the Exhibit Table of Item 601 in Regulation S-K).

3(a)	Restated Articles of Incorporation of Emerson Electric Co. and amendment thereto, incorporated by reference to Emerson Electric Co. 1984 Form 10-K, Exhibit 3(a).
3(b)	By-laws of Emerson Electric Co., incorporated by reference to Emerson Electric Co. Form 10-Q for the quarter ended June 30, 1985, Exhibit 1.
4	No long-term debt instruments are filed since the total amount of securities authorized under any such instrument does not exceed 10 per cent of the total assets of Emerson Electric Co. and its subsidiaries on a consolidated basis. Emerson Electric Co. agrees to furnish a copy of such instruments to the Securities and Exchange Commission upon request.
10(a)	1981 Performance Shares Bonus Plan, incorporated by reference to Emerson Electric Co. 1981 Proxy Statement dated January 2, 1981 (Appendix I).
10(b)	1985 Performance Shares Bonus Plan, incorporated by reference to Emerson Electric Co. 1985 Proxy Statement dated December 20, 1984 (Appendix I).
10(c)	1971 Non-qualified Stock Option Plan, as amended, incorporated by reference to Emerson Electric Co. 1981 Form 10-K, Exhibit 10(d).
10(d)	1974 Non-qualified Stock Option Plan, as amended, a copy of which is filed herewith.
10(e)	1982 Incentive Stock Option Plan, incorporated by reference to Emerson Electric Co. 1981 Form 10-K, Exhibit 10(f).
10(f)	Employment Agreement made as of October 1, 1975, by and between C. F. Knight and Emerson Electric Co., incorporated by reference to Emerson Electric Co. 1981 Form 10-K, Exhibit 10(g).
13	Annual Report to Stockholders for the year ended September 30, 1985. Except for the portions incorporated by reference as indicated in this Form 10-K, the 1985 Annual Report to Stockholders is furnished for the information of the Securities and Exchange Commission and is not to be deemed "filed" as part of this Form 10-K.
22	Subsidiaries of Emerson Electric Co.
24	Accountants' Consent
25	Power of Attorney

B) No reports on Form 8-K were filed during the quarter ended September 30, 1985.

SIGNATURES

Pursuant to the requirements of Section 13 or 15(d) of the Securities Exchange Act of 1934, the registrant has duly caused this report to be signed on its behalf by the undersigned, thereunto duly authorized.

EMERSON ELECTRIC CO.

By J. C. Wilson
J. C. Wilson
Vice President of Finance, Controller and Chief Accounting Officer

Date: December 6, 1985

Pursuant to the requirements of the Securities Exchange Act of 1934, this report has been signed below on December 6, 1985, by the following persons on behalf of the registrant and in the capacities indicated.

Signature	Title
* C. F. Knight	Chairman of the Board, Chief Executive Officer and Director
* W. C. Bousquette	Senior Vice President and Chief Financial Officer
J. C. Wilson	Vice President of Finance, Controller and Chief Accounting Officer
* G. K. Beare	Director
* L. L. Browning, Jr.	Director
* A. A. Busch III	Director
* L. J. Conti	Director
* J. A. Frates	Director
* J. J. Kerley	Director
* E. L. Keyes, Jr.	Director
* G. A. Lodge	Director
* V. R. Loucks, Jr.	Director

* _____ Director
W. R. Persons

* _____ Director
R. D. Potts

* _____ Director
W. A. Rutledge

* _____ Director
B. A. Schriever

* _____ Director
W. H. Van Cleve

* _____ Director
E. F. Williams, Jr.

* By J. C. Wilson
J. C. Wilson
Attorney-in-fact

ACCOUNTANTS' REPORT

The Board of Directors and Stockholders
Emerson Electric Co.:

Under date of November 4, 1985, we reported on the consolidated balance sheets of Emerson Electric Co. and subsidiaries as of September 30, 1985 and 1984 and the related consolidated statements of earnings, stockholders' equity, and changes in financial position for each of the years in the three-year period ended September 30, 1985, as contained in the 1985 Annual Report to Stockholders. These financial statements and our report thereon are incorporated by reference in this Annual Report on Form 10-K for the year 1985. In connection with our examinations of the aforementioned consolidated financial statements, we also examined the related financial statement schedules listed under Item 14 of this Annual Report on Form 10-K.

In our opinion, such financial statement schedules, when considered in relation to the basic consolidated financial statements taken as a whole, present fairly in all material respects the information set forth therein.

Peat, Marwick, Mitchell & Co.

PEAT, MARWICK, MITCHELL & CO.

St. Louis, Missouri
November 4, 1985

EMERSON ELECTRIC CO. AND SUBSIDIARIES

SCHEDUL

Property, Plant and Equipment
Years Ended September 30, 1985, 1984 and 1983

	Millions of Dollars					
	Balance at Beginning of Period	Additions at Cost	Retirements and Sales	Other Additions	Translation Adjustments	Balan at Cl of Per
Year Ended September 30, 1985						
Land and land improvements	$ 45.0	5.2	1.2	.9	.1	5(
Buildings	341.6	44.5	2.2	1.6	2.5	38(
Machinery and equipment	955.9	148.6	49.0	.8	4.5	1,06(
Construction in progress	67.3	8.3	1.5	-	.3	7(
	$1,409.8	206.6	53.9	3.3	7.4	1,57
Year Ended September 30, 1984						
Land and land improvements	$ 42.1	1.3	2.5	4.5	(.4)	4
Buildings	327.4	11.1	11.8	19.0	(4.1)	34
Machinery and equipment	830.6	137.1	51.2	46.0	(6.6)	95
Construction in progress	51.5	21.3	7.1	1.9	(.3)	6
	$1,251.6	170.8	72.6	71.4	(11.4)	1,40
Year Ended September 30, 1983						
Land and land improvements	$ 38.1	1.9	1.5	3.9	(.3)	4
Buildings	297.8	21.8	4.6	14.9	(2.5)	32
Machinery and equipment	738.0	106.8	39.1	28.7	(3.8)	83
Construction in progress	49.9	.8	.2	1.1	(.1)	5
	$1,123.8	131.3	45.4	48.6	(6.7)	1,25

Note: Other additions represent acquired companies and adjustment to conform fiscal year of pooled company.

EMERSON ELECTRIC CO. AND SUBSIDIARIES

SCHEDUL

Accumulated Depreciation of
Property, Plant and Equipment
Years Ended September 30, 1985, 1984 and 1983

	Millions of Dollars					
	Balance at Beginning of Period	Additions Charged to Operations	Retirements and Sales	Other Additions	Translation Adjustments	Bala at C of Pe
Year Ended September 30, 1985						
Land improvements	$ 5.5	.8	.3	-	-	6
Buildings	119.4	14.9	1.0	-	.8	134
Machinery and equipment	507.4	120.3	40.6	-	2.4	589
	$632.3	136.0	41.9	-	3.2	729
Year Ended September 30, 1984						
Land improvements	$ 5.0	.8	.3	-	-	
Buildings	113.5	13.2	6.2	(.1)	(1.0)	119
Machinery and equipment	449.0	106.0	44.2	.2	(3.6)	507
	$567.5	120.0	50.7	.1	(4.6)	637
Year Ended September 30, 1983						
Land improvements	$ 4.6	.7	.3	-	-	
Buildings	101.6	15.4	2.7	-	(.8)	113
Machinery and equipment	399.9	86.6	35.5	-	(2.0)	449
	$506.1	102.7	38.5	-	(2.8)	567

Note: Other additions represent adjustment to conform fiscal year of pooled company.

EXHIBITS

TO THE EMERSON ELECTRIC CO.

SECURITIES AND EXCHANGE COMMISSION

FORM 10-K

FOR THE FISCAL YEAR ENDED

SEPTEMBER 30, 1985

INDEX TO EXHIBITS

Exhibits are listed by numbers corresponding to the Exhibit Table of Item 601 in Regulation S-K.

Exhibit No.	Exhibit	Page No.
10(d)	1974 Non-qualified Stock Option Plan, as amended	19
13	Annual Report to Stockholders for the year ended September 30, 1985	24
22	Subsidiaries of Emerson Electric Co.	84
24	Accountants' Consent	89
25	Power of Attorney	90

See Item 14(A)(3) for a list of exhibits incorporated by reference.

EXHIBIT 10(d)

EMERSON ELECTRIC CO.

1974 NON-QUALIFIED STOCK OPTION PLAN

(As Amended Effective February 5, 1980)

1. Purpose of the Plan.

The 1974 Non-Qualified Stock Option Plan (the "Plan") of Emerson Electric Co. (the "Company") is intended as an incentive to, and to encourage ownership of the Company's stock by, certain key executive employees of the Company and its subsidiaries.

2. Stock Subject to the Plan.

400,000 shares of the authorized but unissued Common Stock, of the par value of $1.00 per share, of the Company have been allocated to the Plan and will be reserved for issue upon the exercise of options granted under the Plan. The Company may, in its discretion, use shares held in the Treasury in lieu of authorized but unissued shares. If any such option shall expire or terminate for any reason without having been exercised in full, the unpurchased shares subject thereto shall again be available for the purposes of the Plan.

3. Administration.

The Plan shall be administered by the Committee referred to in Paragraph 4 (hereinafter called the "Committee"). Subject to the express provisions of the Plan, the Committee shall have plenary authority, in its discretion, to determine the individuals to whom, and the time or times at which, options shall be granted and the number of shares to be subject to each option. In making such determinations the Committee may take into account the nature of the services rendered by the respective individuals, their present and potential contributions to the Company's success and such other factors as the Committee, in its discretion, shall deem relevant. Subject to the express provisions of the Plan, the Committee shall also have plenary authority to interpret the Plan, to prescribe, amend and rescind rules and regulations relating to it, to determine the terms and provisions of the respective stock option agreements (which need not be identical) and to make all other determinations necessary or advisable for the administration of the Plan. The Committee's determinations on the matters referred to in this Paragraph 3 shall be conclusive.

4. The Committee.

The Committee shall consist of three or more members of the Board of Directors of the Company who are not eligible to receive options under the Plan. The Committee shall be appointed by the Board of Directors, which may from time to time appoint members of the Committee in

substitution for members previously appointed and may fill vacancies, however caused, in the Committee. The Committee may select one of its members as its Chairman, and shall hold its meetings at such times and places as it may determine. A majority of its members shall constitute a quorum. All determinations of the Committee shall be made by a majority of its members. Any decision or determination reduced to writing and signed by a majority of the members shall be fully as effective as if it had been made by a majority vote at a meeting duly called and held. The Committee may appoint a secretary, shall keep minutes of its meetings and shall make such rules and regulations for the conduct of its business as it shall deem advisable.

5. Eligibility.

Options may be granted only to key executive employees of the Company or its subsidiaries. The term "key executive employees" is not limited to, but includes, officers, whether or not they are directors, but does not include directors who are not also executive employees of the Company, or a subsidiary thereof. The term "subsidiary" shall have the meaning ascribed to it in Section 425 of the Internal Revenue Code.

6. Option Prices.

The purchase price of the Common Stock under each option shall be determined by the Committee, but shall not be less than 85% of the fair market value of the stock at the time of the granting of the option, as determined by the Committee. Such fair market value shall generally be considered to be the mean between the high and low prices of the Company's Common Stock as traded on the New York Stock Exchange on the day the option is granted; provided, however, that the Committee may adopt any other criterion for the determination of the fair market value of the Company's Common Stock on the day any option is granted. The purchase price is to be paid in full in cash upon the exercise of the option; *provided, however, that in lieu of cash an optionee may, with the approval of the Committee, exercise his option by tendering to the Company shares of the Common Stock of the Company, owned by him and with the certificates therefor registered in his name, having a fair market value equal to the cash exercise price applicable to his option, with the fair market value of such stock to be determined in such appropriate manner as may be provided for by the Committee or as may be required in order to comply with or to conform to the requirements of, any applicable or relevant laws or regulations.* The proceeds of sale of stock subject to option are to be added to the general funds of the Company and used for its corporate purposes as the Board of Directors shall determine.

7. Exercise of Options.

The term of each option shall be not more than ten (10) years from the date of granting thereof. Within such limit options will be exercisable at such time or times, and subject to such restrictions and conditions, as the Committee shall, in each instance, approve, which need not be uniform for all

optionees. The holder of an option shall have none of the rights of a stockholder with respect to the shares subject to option until such shares shall be issued to him upon the exercise of his option.

8. Non-Transferability of Options.

No option granted under the Plan shall be transferable otherwise than by will or the laws of descent and distribution and an option may be exercised, during the lifetime of the holder thereof, only by him.

9. Agreement to Serve.

Each individual receiving an option shall agree that he will remain in the service of the Company or a subsidiary of the Company for a period of at least two (2) years from the date of the granting of the option, at the pleasure of the Board of Directors of the Company and at such compensation as such Board of Directors or any Committee thereof shall reasonably determine from time to time.

10. Investment Purpose.

Each option under the Plan shall be granted only on the condition that all purchases of stock thereunder shall be for investment purposes, and not with a view to resale or distribution, except that the Committee may make such provision in options granted under this Plan as it deems necessary or advisable for the release of such condition upon the registration with the Securities and Exchange Commission of stock subject to the option, or upon the happening of any other contingency warranting the release of such condition.

11. Adjustments Upon Changes in Capitalization.

Notwithstanding any other provisions of the Plan, the option agreements may contain such provisions as the Committee shall determine to be appropriate for the adjustment of the number and class of shares subject to each outstanding option and the option prices in the event of changes in the outstanding Common Stock of the Company by reason of stock dividends, recapitalization, mergers, consolidations, splitups, combinations or exchanges of shares and the like, and, in the event of any such change in the outstanding Common Stock of the Company, the aggregate number and class of shares available under the Plan and the maximum number of shares as to which options may be granted to any individual shall be appropriately adjusted by the Committee, whose determination shall be conclusive.

12. Amendment and Termination.

The Board of Directors of the Company may at any time terminate the Plan, or make such modifications of the Plan as it shall deem advisable, provided, however, that the Board of Directors

may not, without further approval by the holders of Common Stock of the Company, increase the maximum numbers of shares as to which options may be granted under the Plan (except under the anti-dilution provisions hereof), or change the class of employees to whom options may be granted, or change the manner of determining the minimum option prices or withdraw the authority to administer the Plan from a committee consisting of directors of the Company not eligible to receive options granted under the Plan. No termination or amendment of the Plan may, without the consent of the employee to whom any option shall theretofore have been granted, adversely affect the rights of such employee under such option.

13. Effectiveness of the Plan.

The Plan shall become effective only if it shall be approved by the stockholders of the Company, on or before February 28, 1975 at a regular meeting of the stockholders or at a special meeting duly called and held for such purpose.

14. Time of Granting of Options.

An option grant under the Plan shall be deemed to be made on the date on which the Committee, by formal action of its members, duly recorded in the records thereof, makes an award of an option to an eligible employee of the Company or its subsidiaries; provided, however, that such option is evidenced by a written option agreement duly executed on behalf of the Company and on behalf of the optionee within 21 days of the date of the Committee action.

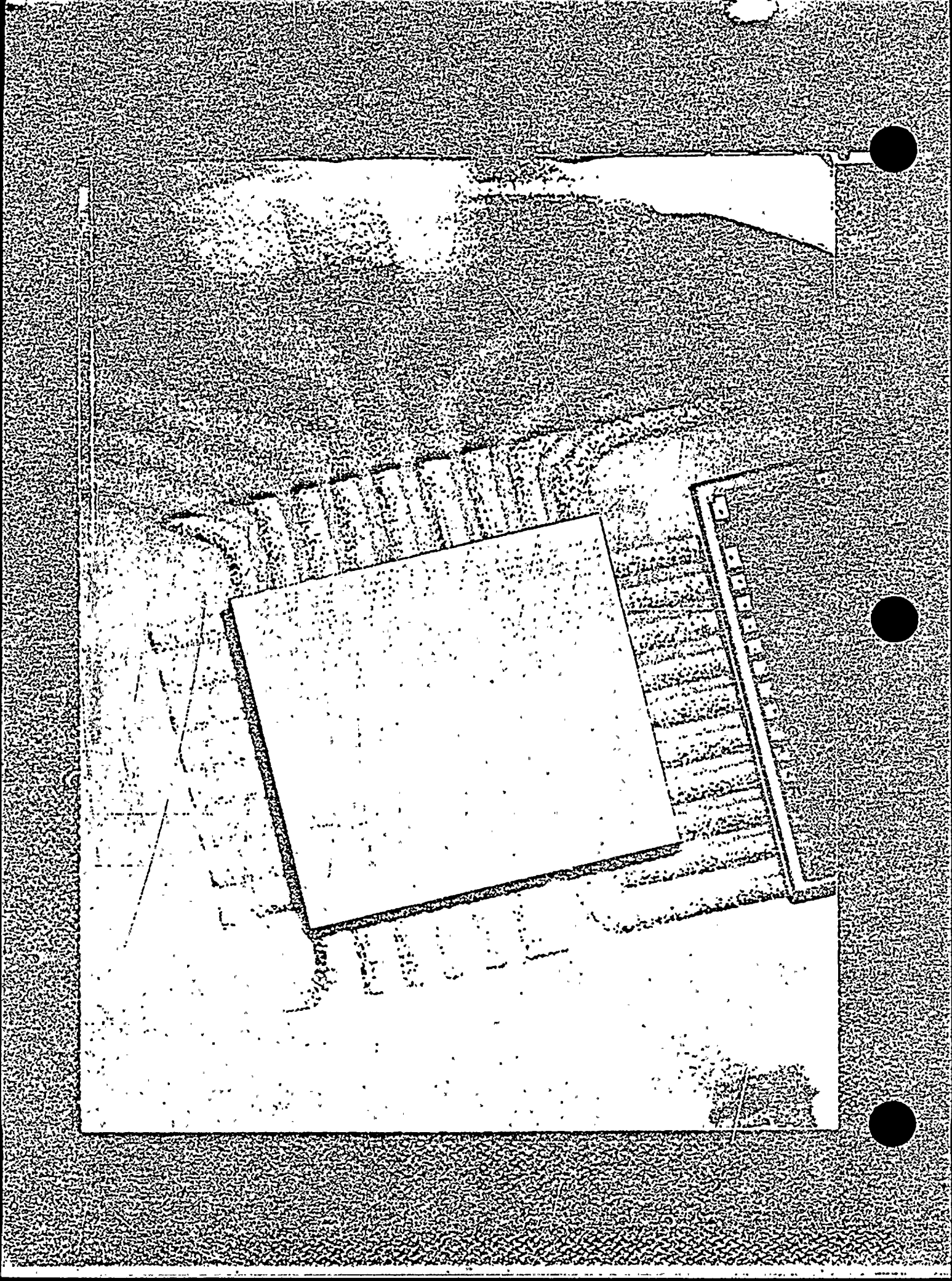
15. Alternative Stock Appreciation Rights.

(a) Grant. At the time of grant of an option, or at any time thereafter, the Committee, in its discretion, may grant to the grantee or holder of an unexercised option under the Plan an Alternative Stock Appreciation Right ("SAR") for all or any part of the number of shares covered by his unexercised option. Any subsequent exercise of an option by the holder thereof who also holds an alternative SAR shall reduce his alternative SAR by the same number of shares as to which his option is exercised. Any exercise of his alternative SAR shall reduce his option by the same number of shares as to which his SAR is exercised. An alternative SAR granted to an option holder may provide that such SAR, if exercised, must be exercised within the time period specified therein and such time period specified may be less than the time period during which the corresponding option may be exercised. The failure of the holder of the alternative SAR to exercise such SAR within the time period specified shall not reduce his option rights. If an alternative SAR is granted for a number of shares less than the total number of shares covered by the corresponding option the Committee may later grant to the option holder an additional alternative SAR covering additional shares, provided, however, that the aggregate amount of all alternative SARs held by any option holder shall at no time exceed the total number of shares covered by his unexercised options.

(b) Exercise. The holder of any option which by its terms is exercisable who also holds an alternative SAR may, in lieu of exercising his option, elect to exercise his alternative SAR; subject, however, to the limitations on time of exercise hereinafter set forth. Such SAR shall be exercised by the delivery to the Company of a written notice which shall state that the optionee elects to exercise his SAR as to the number of shares specified in the notice and which shall further state what portion, if any, of the SAR exercise amount (hereinafter defined) the holder thereof requests be paid to him in cash and what portion, if any, he requests be paid to him in Common Stock of the Company. The Committee promptly shall cause to be paid to such holder the SAR exercise amount either in cash, in Common Stock of the Company, or any combination of cash and stock as it may determine. Such determination may be either in accordance with the request made by the holder of the SAR or otherwise, in the discretion of the Committee. The SAR exercise amount is the excess of the fair market value of one share of the Company's Common Stock on the date of exercise over the per share option price for the option in respect of which the alternative SAR was granted multiplied by the number of shares as to which the SAR is exercised. For the purposes hereof fair market value of one share of the Company's Common Stock on the date of exercise shall be the mean between the high and low prices of the Company's Common Stock on the New York Stock Exchange—Composite Tape on such date.

(c) Limitation on Date of Exercise. No exercise of any SAR as hereinabove provided for shall be made prior to the expiration of six months after the date the SAR is granted and thereafter shall not be made except during the third business day through the twelfth business day following the release for publication of the Company's regular quarterly or annual summary statements of sales and earnings.

(d) Other Provisions of Plan Applicable. All provisions of this Plan applicable to options granted hereunder shall apply with equal effect to alternative SARs. Not in limitation of the prior sentence it is expressly provided that no SAR shall be transferable otherwise than by will or the laws of descent and distribution and an SAR may be exercised, during the lifetime of the holder thereof, only by such holder.



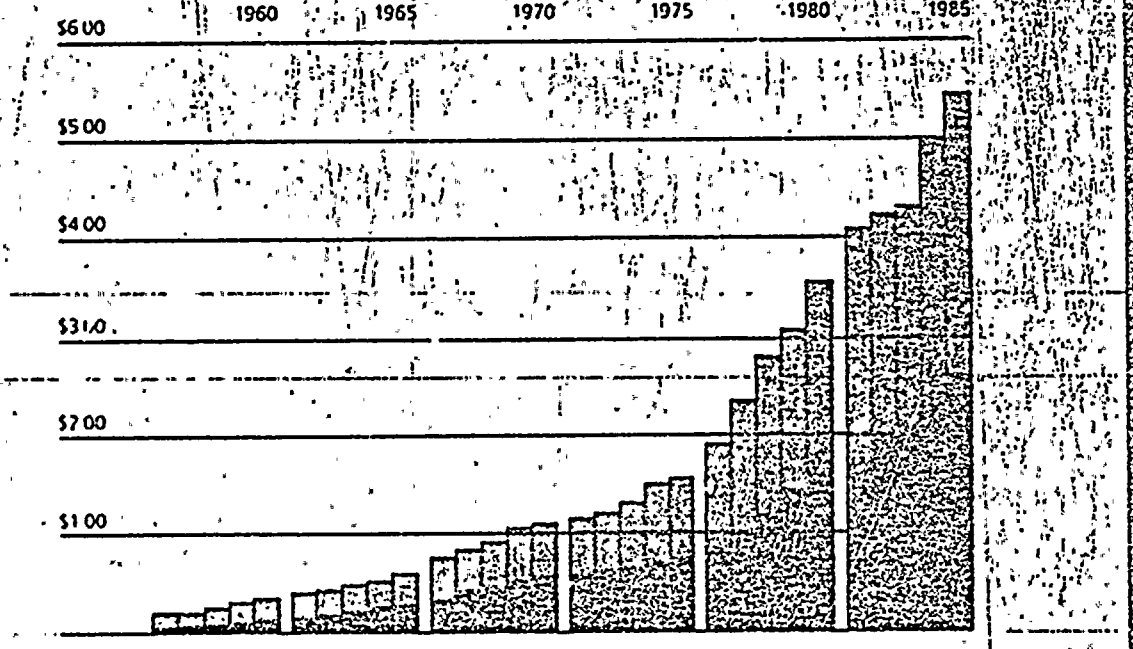
FINANCIAL HIGHLIGHTS

Years Ended September 30 Dollars in Millions Except Per Share Amounts	1985	1984	Per Cent Increase
Net sales	$4,649.2	4,355.1	6.8%
Net earnings	$ 401.1	369.0	8.7%
Per cent of net sales	8.6%	8.5%	
Earnings per common share	$ 5.43	5.00	8.6%
Dividends per common share	$ 2.60	2.30	13.0%
Return on average stockholders' equity	19.0%	19.2%	
Total assets	$3,256.8	3,133.4	3.9%
Capital expenditures	$ 206.6	170.8	21.0%
Stockholders' equity	$2,222.2	2,004.4	10.9%
Total debt/total capital	10.9%	14.4%	

Earnings & Dividends Per Common Share 1956-1985

Twenty-Eight Consecutive Years of Increased Earnings Per Share

Twenty-Nine Consecutive Years of Increased Dividends Per Share



Fiscal 1985 represented Emerson Electric's 28th consecutive year of increased net earnings and earnings per share. Net earnings in 1985 were $401 million, an increase of 8.7 per cent from the previous year. Earnings per share increased 8.6 per cent to $5.43, and net sales reached a record of more than $4.6 billion, a gain of 6.8 per cent.

Emerson's balanced diversification and continuing shift toward higher growth industrial electronic products and components for factory automation and process control helped the Company outperform a sluggish economy. These products now constitute approximately 36 per cent of total sales. Emerson's international business also contributed significantly in 1985 with record sales of $985 million, an 11.6 per cent increase. Foreign subsidiary sales and profits showed strong improvement, but export sales declined as a result of the continued strength of the dollar and prior year completion of foreign government and defense contracts. Government and defense sales and orders remained strong with the backlog reaching a record $735 million at year end.

New product sales continued to gain momentum in 1985, increasing by more than 19 per cent from last year. Sales of new products reached $625 million, or a record 13.4 per cent of total sales. Emerson's new product performance is the result of the continuing commitment to engineering and technology development throughout the Company. Research and development expenditures reached 3.0 per cent of sales for the first time, representing a record investment of $140 million. In addition, the Company formed a $15 million research and development partnership to develop special purpose electronic variable speed controls for motors used in appliances and heating, ventilating and air conditioning systems.

Profitability continued at high levels with return on average stockholders' equity at 19.0 per cent and return on average total operating capital at 17.4 per cent. Cost reductions totaling $222 million exceeded the 1985 target of $212 million and contributed to Emerson's improved operating profit margin. The Company continued to support its best cost producer strategy with record capital expenditures totaling $207 million, an increase of 21.0 per cent over 1984.

During 1985, Emerson continued to diversify and expand its technology base in components for factory automation and process control markets through the acquisition of Automatic Switch Company and Kiowa Corporation. Automatic Switch is a leader in the design and manufacture of industrial solenoid valves and products for the control of fluids and the flow of electric power. Kiowa manufactures electronic motion control pro[illegible].

The fiscal 1985 dividend of $2.60 per share represented the 29th consecutive year of increased dividend payout. Emerson's Directors have voted to increase the quarterly dividend by 6.2 per cent, to an annualized rate of $2.76, effective with the December payment. The Company's financial position at the close of 1985 was the strongest in its recent history. Emerson is strategically positioned to fund future growth with total debt only 10.9 per cent of total capital.

In June, August A. Busch III, Chairman and President of Anheuser-Busch Companies, Inc., was elected to the Board of Directors. Also during the year, the Company realigned the responsibilities of the Office of the Chief Executive. Executive vice presidents James F. Hardymon and Albert E. Suter assumed responsibility for Emerson's operating divisions. Robert W. Staley, also an executive vice president, assumed responsibility for the Company's administrative and financial functions. Laurance L. Browning, [illegible]ired from active management effective October 1, 1985, and James J. Kerley will retire from acti[illegible]agement effective January 1, 1986. We are pleased that both will remain as Directors of the Company.

We anticipate that we will continue to operate in an uncertain and difficult economic environment during the first half of fiscal 1986. Our organization is geared to respond to this challenge as we have in the past during times of recession and special challenge.

This year's Annual Report features the companies that make up Emerson with emphasis on their product/market leadership through continued commitment to technology driven products and the best cost producer strategy.

We appreciate the continuing support of Emerson's Directors, and we express our thanks to our valued customers, our skilled and dedicated employees who develop, produce and market our products around the globe and our 30,200 stockholders.

On behalf of the Office of the Chief Executive,

Charles F. Knight

Charles F. Knight
Chairman of the Board
& Chief Executive Officer

November 5, 1985

E L Keyes, Jr. J K Vivian Hagen C A Dill R W Staley W C Bousquette

J J Adorjan A E Suter J F Hardyman W A Rutledge

C F Knight

Emerson has established a consistent record of above-average earnings growth combined with high levels of profitability and return on equity. This performance record is a direct result of an effective management process and well established long-term objectives and strategies that drive the Company. A review of Emerson's performance over the past ten years illustrates the basic elements of the Company's strategy.

EMERSON'S PERFORMANCE
(Dollars in millions except per share amounts)

	1975	1985	Ten-Year Growth Rate
Net sales	$1,535.1	4,649.2	11.7%
Net earnings	$ 114.5	401.1	13.4%
Per cent of net sales	7.5%	8.6%	
Earnings per common share	$ 1.58	5.43	13.1%
Dividends per common share	$ .7375	2.60	13.4%
Stockholders' equity	$ 723.8	2,222.2	11.9%
Return on average stockholders' equity	16.7%	19.0%	
Return on average total operating capital	14.9%	17.4%	
Per cent total debt to total capital	16.1%	10.9%	

- ***Achieved consistent, above-average sales and earnings growth in a volatile economic environment.***

During the past ten years, Emerson continued its record of above-average sales and earnings growth. Emerson's sales grew at 11.7 per cent for the ten years compared to all manufacturers at 8.1 per cent. Earnings for the ten-year period grew at an annualized rate of 13.4 per cent while those of all manufacturers increased 7.0 per cent.

This performance compares favorably with the growth in the economy during the past ten years, despite the fact that the last six years, 1980 through 1985, have been a period of unusual economic challenge. From 1980 through 1985, all manufacturers' earnings were down in four of the six years. The major reasons were:

- Two economic recessions;
- A strong US dollar and weak foreign economies which reduced exports and increased foreign competition in domestic markets;
- Disinflation, combined with low levels of capacity utilization, continued inventory reductions and increased foreign competition which created a difficult price environment; and
- High real interest rates which helped drive down inventories and dampen the fixed investment sector of the economy.

Emerson's performance in the years of recession and special challenge during this period are summarized in the following table.

RESULTS IN PERIODS OF RECESSION AND SPECIAL CHALLENGE

	1958 vs. 1957	1961 vs. 1960	1967 vs. 1966	1970 vs. 1969	1975 vs. 1974	1980 vs. 1979	1982 vs. 1981	1983 vs. 1982	1985 vs. 1984
Sales									
Emerson(1)	+6.5%	+32.7%	+13.2%	+3.9%	−2.2%	+9.9%	−3.2%	−2.4%	+1.3%
All Mfgrs.(2)	−5.8%	+1.1%	+5.3%	+4.7%	+4.1%	+10.4%	−3.0%	−0.4%	+2.3%(3)
Earnings									
Emerson(1)	+0.8%	+15.3%	+13.3%	+9.7%	+0.8%	+13.1%	+5.5%	+1.9%	+6.4%
All Mfgrs.(2)	−28.8%	−12.9%	−4.9%	−10.0%	−17.3%	−4.3%	−22.9%	−6.1%	−12.1%(3)

(1) Excluding acquisitions for each two year period.
(2) Based on U.S. Commerce Department figures and years ending September 30.
(3) Projection by DRI Economics based on three quarters of actual data.

• ***Improved the profitability of the Company.***

Emerson's profitability improved significantly between 1975 and 1985. A management commitment to producing quality products at the best cost has been key to continuing to improve profit margins. Over the past ten years, Emerson's return on equity has averaged 19.6 per cent and has consistently outperformed the Standard & Poor's 400 Industrials return on equity, which has averaged 14.4 per cent. The Company's return on equity has increased from 16.7 per cent to 19.0 per cent despite a decrease in financial leverage.

PROFITABILITY

	1975	1976	1977	1978	1979	1980	1981	1982	1983	1984	1985
Net margin	7.5%	7.7%	8.0%	8.0%	7.8%	7.9%	8.2%	8.6%	8.8%	8.5%	8.6%
Return on average stockholders' equity	16.7%	17.8%	19.5%	20.5%	20.4%	20.4%	20.9%	19.6%	18.2%	19.2%	19.0%

The Company's increased return on equity has occurred during a time of significant decline in the inflation rate, as measured by the GNP deflator, thereby improving the real return on stockholders' equity. Emerson's real return on equity has more than doubled, from 6.8 per cent in 1975 to 15.4 per cent in 1985.

• ***Increased global commitment.***

Emerson's international sales have grown at an annualized rate of 12.9 per cent over the past ten years. Our served markets have become more global and consequently, in recent years we have moved away from the export-led strategy toward a global product/market strategy. In addition, we are committing the capital required to establish Emerson's operations to serve world markets at the lowest cost. One indicator of the impact of the global product strategy is 1985 foreign subsidiary sales which were up 29.5 per cent.

INTERNATIONAL SALES

(Dollars in millions)

	1975	1976	1977	1978	1979	1980	1981	1982	1983	1984	1985
International sales	$294	$359	$428	$520	$634	$829	$844	$853	$865	$883	$985

Recently, Emerson has made several strategic international investments. Two of these are in the Far East process control market with the acquisition of Ueshima and a 21 per cent interest in Oval Engineering. In October 1985, a third investment was made for 25 per cent of J.H. Fenner (Holdings) PLC in Great Britain. Fenner is one of the largest international power transmission companies and should provide an expanded worldwide power transmission base for Emerson.

• ***Built a major defense supplier.***

In 1975, Emerson's government and defense businesses had sales of $103 million and represented only 8 per cent of the Company's total sales. These defense related businesses have grown at a compound annual rate of 18.3 per cent for the last ten years to sales of $555 million, and now represent 12 per cent of Emerson's total sales.

GOVERNMENT AND DEFENSE SALES
(Dollars in millions and as originally reported)

	1975	1976	1977	1978	1979	1980	1981	1982	1983	1984	1985
Gov't. and Defense sales	$103	$125	$146	$176	$199	$239	$288	$368	$423	$481	$555

Emerson's government and defense businesses today are broadly diversified over a relatively large number of programs which have increased in technological complexity. The defense businesses finished 1985 with a record backlog of $735 million.

• *Continued a balanced diversification.*

Emerson operates in broadly diversified electrical product markets on a global basis. Through the years, we have constantly positioned the Company into higher growth niches of the marketplace and, at the same time, tried to balance the inherent volatility of those market segments through diversification. Emerson has continued to reposition itself through internal growth, acquisitions and divestitures. Appliance components, industrial motors and drives and electrical distribution products have declined as a percentage of total sales, while higher technology businesses such as measurement and control instrumentation, power conversion, electronic products, factory automation components and defense have increased substantially.

Growth of our existing businesses has historically accounted for the majority of our increases in sales and earnings. This emphasis on internal growth will continue to be the major component of our future growth. In addition, the Company has pursued a selective acquisition policy, which has also contributed to our sales and earnings growth. Acquisitions have been an effective means of entering attractive related market segments or for obtaining specific product, marketing or technical capabilities.

Less publicized, but important to the process of repositioning the Company, are divestitures of product lines which no longer meet Emerson's growth and return objectives. Over the last ten years, Emerson has made 29 product line divestitures with combined annual sales of $174 million in the year of divestiture.

A major shift in Emerson's product mix in the past ten years has been toward electronic products. Sales of electronic-based products exceeded $1.2 billion during 1985 and represented 25.9 per cent of Emerson's total sales. Electronic products, which grew at an annualized rate of 23.9 per cent from 1975 to 1985, have been a major contributor to Emerson's overall growth and to our new products program.

ELECTRONIC PRODUCT SALES
(Dollars in millions and as originally reported)

	1975	1976	1977	1978	1979	1980	1981	1982	1983	1984	1985
Electronic product sales	$141	$193	$257	$308	$390	$434	$490	$595	$655	$1,001	$1,205
Per cent of net sales	11.3%	12.8%	14.2%	14.1%	14.9%	14.2%	14.3%	17.0%	18.8%	24.0%	25.9%

In addition, the factory automation and process control markets are key sources of growth. At present, 22 Emerson companies provide component products for these rapidly growing markets. Sales in 1985 reached $1.7 billion, representing 35.7 per cent of total sales, and have grown at an annualized rate of 18.8 per cent over the last ten years. We expect industrial electronic products for factory automation and process control to continue to be major contributors to internal growth.

FACTORY AUTOMATION AND PROCESS CONTROL SALES
(Dollars in millions and as originally reported)

	1975	1976	1977	1978	1979	1980	1981	1982	1983	1984	1985
Sales	$298	$357	$385	$442	$568	$744	$853	$903	$852	$1,247	$1,661
Per cent of net sales	23.8%	23.7%	21.3%	20.3%	21.7%	24.3%	24.9%	25.8%	24.5%	29.8%	35.7%

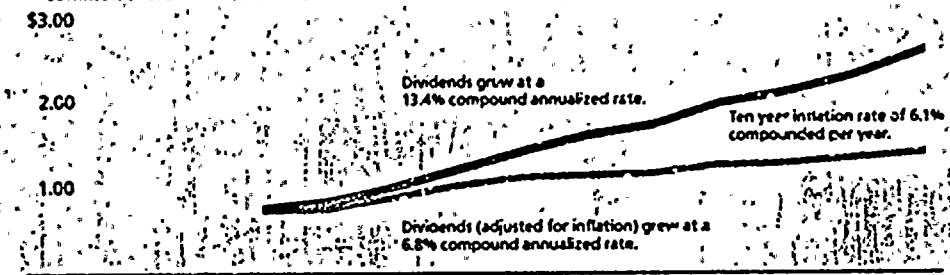
Emerson has continued to reposition the Company into even stronger market leadership positions. In 1975, 69 per cent of Emerson's sales were generated by products that held the number one or number two position in their markets. By 1985, 82 per cent were in the number one or two position, with 51 per cent holding the top spot. Contributing to this gain in market penetration is the trend toward source consolidation.

• *Financed above-average growth and maintained a AAA balance sheet.*

In the process of tripling sales and improving profitability over the decade, Emerson invested $2.5 billion in the Company, paid $1.2 billion in cash dividends and improved the balance sheet. Emerson's annual dividend per common share has increased for twenty-nine consecutive years. Over the past ten years, the Company's dividends have increased at an annualized rate of 13.4 per cent. Using fiscal 1975 as the base, this chart shows real dividend growth has averaged [illegible] per cent.

DIVIDENDS

	1975	1976	1977	1978	1979	1980	1981	1982	1983	1984	1985
Dividends per common share	$.7375	$.7875	$1.00	$1.20	$1.44	$1.60	$1.76	$2.00	$2.10	$2.30	$2.60



Capital expenditures represented more than 50 per cent of the $2.5 billion invested; a substantial portion was for cost reduction and productivity improvement programs.

CAPITAL EXPENDITURES AND COST REDUCTIONS
(Dollars in millions)

	1975	1976	1977	1978	1979	1980	1981	1982	1983	1984	1985
Capital expenditures	$55	$77	$79	$108	$128	$141	$147	$145	$151	$171	$207
Per cent of net sales	3.6%	4.3%	3.7%	4.3%	4.3%	4.2%	3.9%	4.0%	3.6%	3.9%	4.4%
Cost reductions	$54	$62	$66	$77	$90	$110	$135	$161	$176	$193	$222

Emerson is one of a select few industrial companies rated AAA by the major rating agencies. The Company views its strong financial position as a valuable resource in meeting competitive global challenges and in funding growth opportunities. The following chart details Emerson's financial position during the past ten years.

FINANCIAL POSITION

	1975	1976	1977	1978	1979	1980	1981	1982	1983	1984	1985
Current ratio	3.3:1	3.0:1	2.8:1	2.7:1	2.6:1	2.7:1	2.6:1	2.9:1	3.0:1	2.3:1	2.7:1
Interest coverage	18.0X	23.5X	24.3X	30.2X	17.2X	16.7X	20.1X	28.8X	35.3X	24.7X	19.9X
Long-term debt to long-term capital	12.7%	12.7%	10.2%	9.3%	14.0%	12.1%	10.1%	7.6%	7.4%	6.1%	4.9%
Total debt to total capital	16.1%	16.4%	14.2%	14.1%	18.5%	15.9%	13.3%	10.6%	9.3%	14.4%	10.9%

• *Maintained a sustained commitment to new products and technology.*

An integral part of maintaining Emerson's growth strategy is our emphasis and commitment to planning and development of new products and technology. Fiscal 1985 was the eleventh year of the formalized new products program. New product sales reached $625 million in 1985, or 13.4 per cent of the Company's total sales. Sales growth generated by this program has far exceeded our original plan, which projected new product sales to be 10 per cent of total sales in 1985. We expect this area to continue to be an important source of growth based on a record number of 575 active new product programs. Nearly 70 per cent of these new product programs are "world" products in support of Emerson's global commitment.

NEW PRODUCT SALES
(Dollars in millions)

	1975	1976	1977	1978	1979	1980	1981	1982	1983	1984	1985
New product sales	$16	$33	$62	$103	$160	$256	$312	$356	$402	$524	$625
Per cent of net sales	1.3%	2.2%	3.4%	4.7%	6.1%	8.3%	9.1%	10.2%	11.6%	12.5%	13.4%

Divisions undertake their own development work, aided by a Strategic Investment Program for projects beyond the normal scope of divisional resources. The Company has invested $21 million in three advanced development centers in areas of strategic importance since 1981, and more than $30 million in 31 venture capital investments focused on high technology interests. In 1985, Emerson formed its second research partnership to fund the further development of electronic variable speed controls for fractional motors used in appliances and in heating, ventilating and air conditioning systems. Including our first research partnership, Two Way Automatic Communication System (an electronic load management system), formed in 1984, the investment committed to these research partnerships exceeds $30 million.

RESEARCH AND DEVELOPMENT SPENDING
(Dollars in millions and as originally reported)

	1975	1976	1977	1978	1979	1980	1981	1982	1983	1984	1985
Expenses	$24	$30	$37	$45	$53	$68	$78	$90	$93	$116	$140
Per cent of net sales	1.92%	1.99%	2.05%	2.07%	2.03%	2.12%	2.27%	2.57%	2.68%	2.78%	3.01%

In support of our commitment to new product and technology programs, Emerson has increased its engineering and development expenditures every year since 1975. Total expenditures have grown substantially faster than sales, from $24 million or 1.92 per cent of sales in 1975, to $140 million or 3.01 per cent of sales in 1985. During the ten-year period, engineering and development expenses have increased at a compound average growth rate of 19.3 per cent. Even though Emerson has increased research and development expenditures as a per cent of sales, the Company has been able to improve profitability. As such, we have successfully invested for future growth of our businesses through new product development and technology innovations, without sacrificing performance.

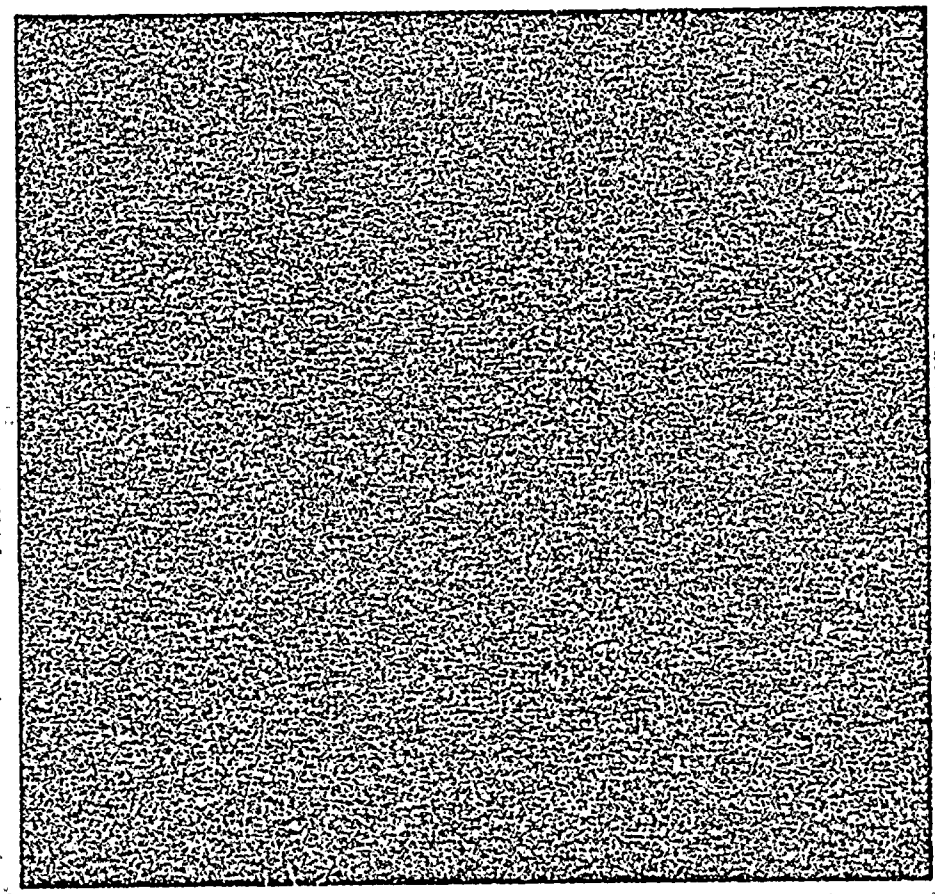
• *The challenge for the years ahead.*

The challenge in the next five years remains essentially unchanged -- to identify and successfully implement investment opportunities to

- ACHIEVE CONSISTENT ABOVE AVERAGE GROWTH RATES, AND
- MAINTAIN HIGH LEVELS OF PROFITABILITY AND RETURN ON EQUITY.

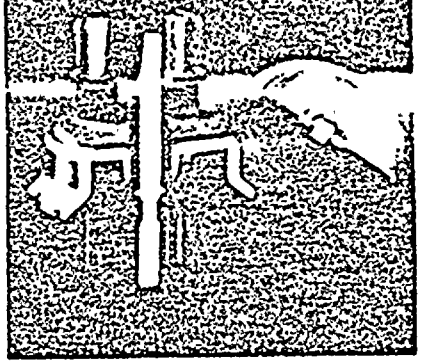
In the years ahead, Emerson plans to concentrate on the markets, products and technologies that we know best. The strategy of blending the Company's requirements for consistent performance with an aggressive resource commitment to evolving electronic and other technologies should lead to increased new product growth, major cost reductions and further market share gains.

This program to increase internal growth will be supplemented by continued growth in international and government and defense markets. In addition, we have in place a proven acquisition program to continue the process of repositioning Emerson's businesses into faster growing market niches, balancing market diversification and enhancing product/market positions. This growth strategy, combined with a commitment to be the world's best cost producer, should permit the Company to continue to improve profitability and maintain high levels of return on equity.



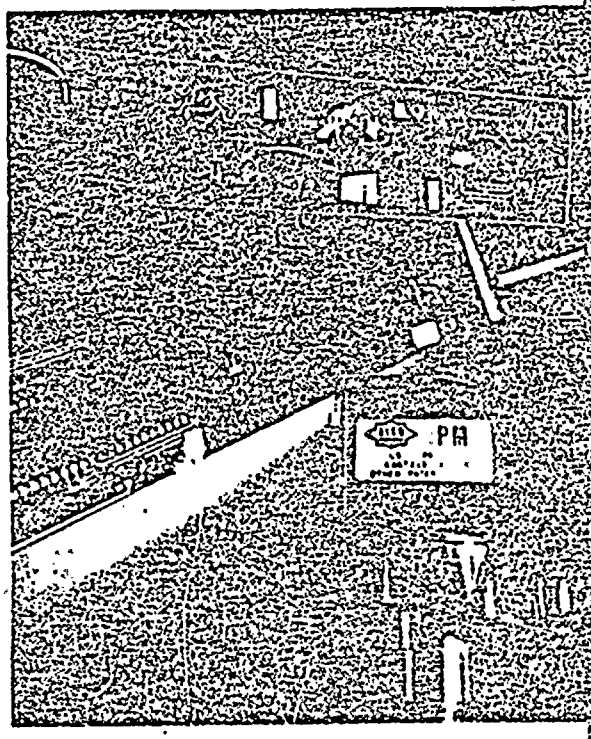
The next section highlights the individual companies that make up Emerson and the diversity of products they produce. The following pages bring to life each division's commitment to best cost products — products which enable the Company to achieve market leadership, continued growth and profitability year after year.

seven-day
programmable
control center
WHITE-RODGERS



▲ **FUSITE**

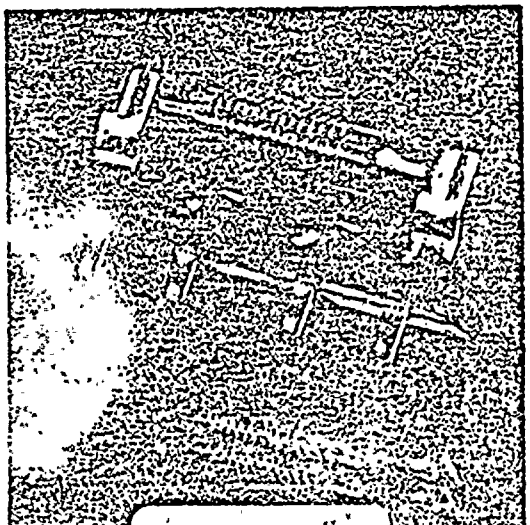
Fusite is a leading manufacturer of hermetic terminal assemblies for refrigeration, air conditioning compressors and battery seals. The terminal shown improves compressor safety through internal mechanical fusing, over pressure protection and improved electrical isolation. A lithium battery terminal seal, a new product shown at right, developed through our experience on materials and technology has also matured. Fusite is a major supplier of terminal seals.



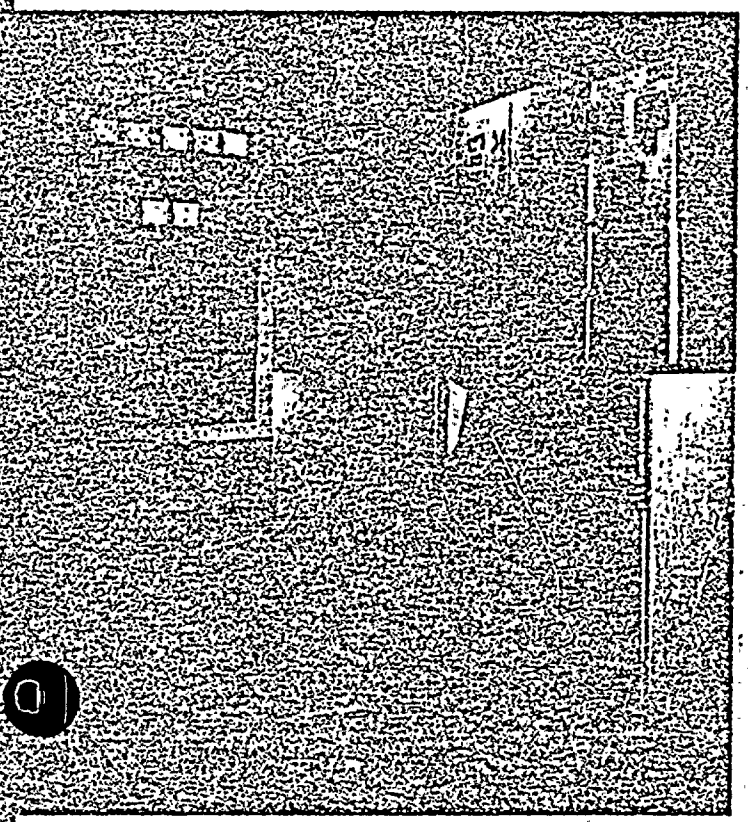
➤ **ALCO CONTROLS**

Alco Controls is a successful leader in the design and manufacture of electronic automatic and electronic temperature controls for motor vehicle, heavy refrigeration and appliance industries. The new microprocessor controlled [illegible] systems used in [illegible] a new [illegible] temperature sensor and [illegible] improving operating efficiency.

◀ **WHITE RODGERS**



◀ **THERM-O-DISC**



➤ **EMERSON MOTOR DIVISION**

A major producer of fractional horsepower motors, Emerson Motor Division has a major development program underway for low cost variable speed control. This technology will be applied to a wide range of appliances to provide greater operational features and significant energy savings. The continued development of this product is being funded through a Research and Development Limited Partnership.

▲ **EMERSON INDUSTRIAL CONTROLS**

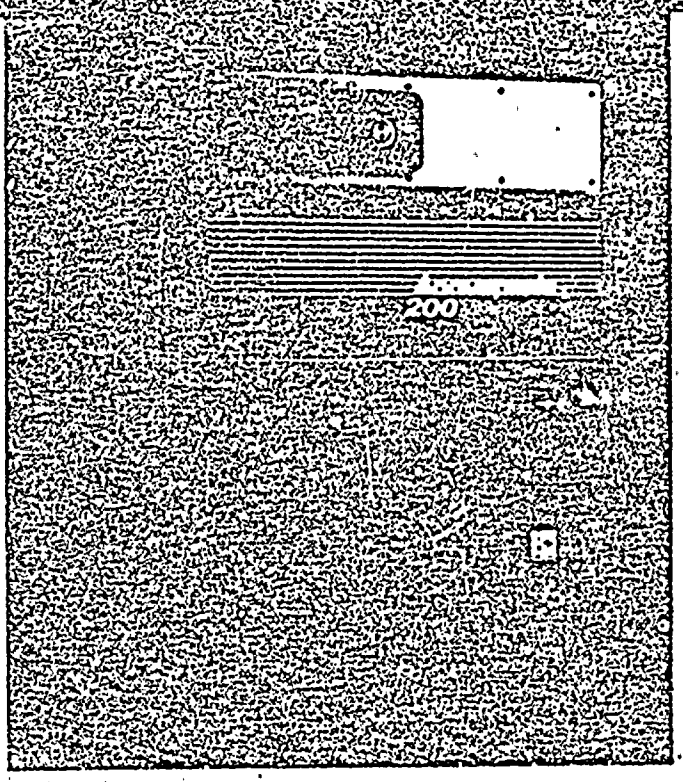
A leading worldwide manufacturer of Uninterruptible Power Systems (UPS) for computers of all sizes, Industrial Controls is also one of the largest manufacturers of industrial adjustable speed drives. Shown is a family of UPS products ranging from 5 KVA to 600 KVA.

➤ **COMPUTER POWER SYSTEMS**

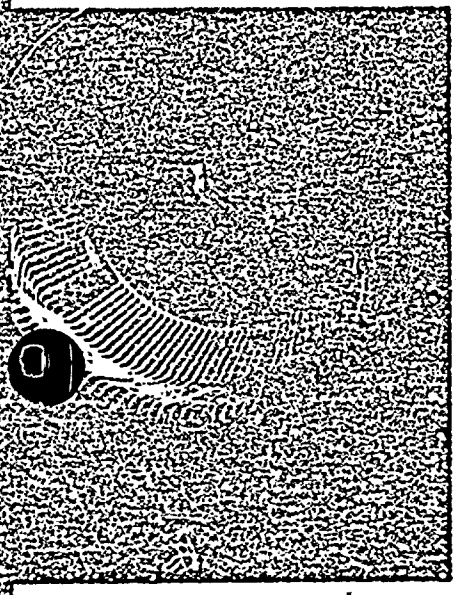
Computer Power Systems manufactures power distribution and regulation equipment for the computer industry. The CPS Series 1000 system is a microprocessor controlled pedestal device which not only provides clean regulated power to computers, but also monitors computer room air condition ing, fire and security

GAMARSON

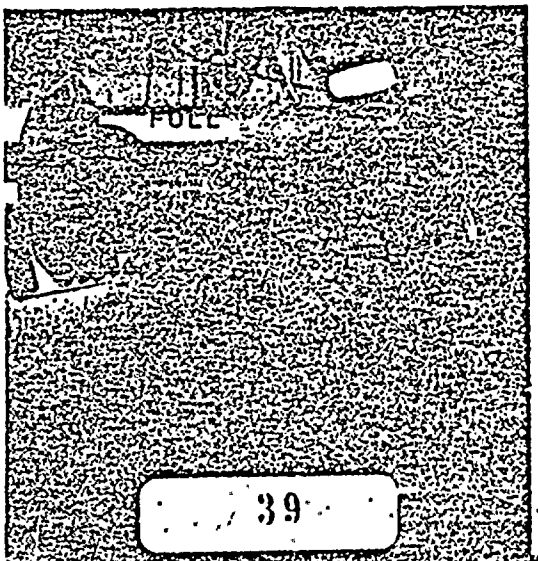
▼ **INDUSTRIAL SERVICE DIVISION**
Industrial Service provides complete repair and maintenance services for electric motors, electronic and mechanical drive equipment. State of the art repair facilities and processes such as vacuum pressure impregnation add years of life to equipment at a fraction of replacement cost. Pictured below is 950 horsepower A.C. motor being rebuilt.



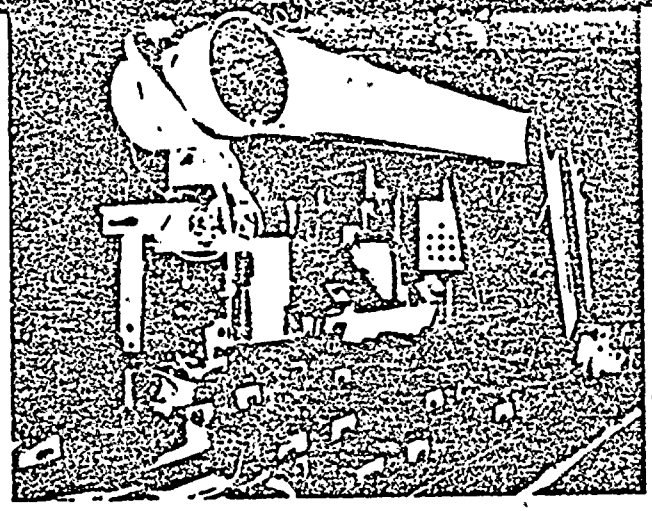
A U.S. ELECTRICAL MOTORS
U.S. Electrical Motors manufactures a wide variety of electric motors. Unimount motors, with their unique combination of electrical and mechanical features, have enabled U.S. Electrical Motors to improve its position in the integral horsepower motor market. High efficiency and low operating temperature make the Unimount the ideal motor for variable frequency drive applications.



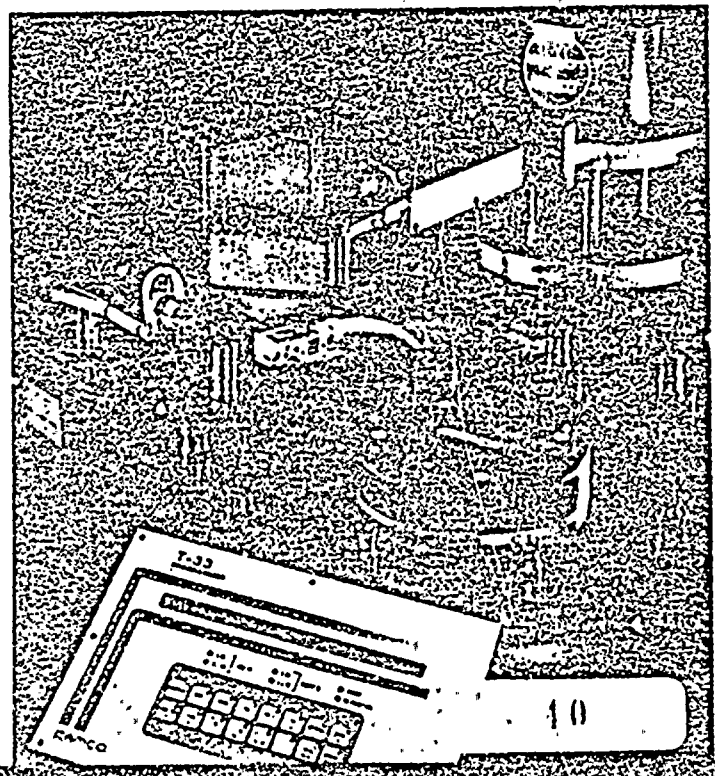
➤ **SWECO**
SWECO manufactures custom and stock separation equipment, vibratory screening, grinding and finishing equipment for industrial and service clients. The LM-3 Separator represents state of the art "fine wet classifying" and solids removal from steel mill operations.



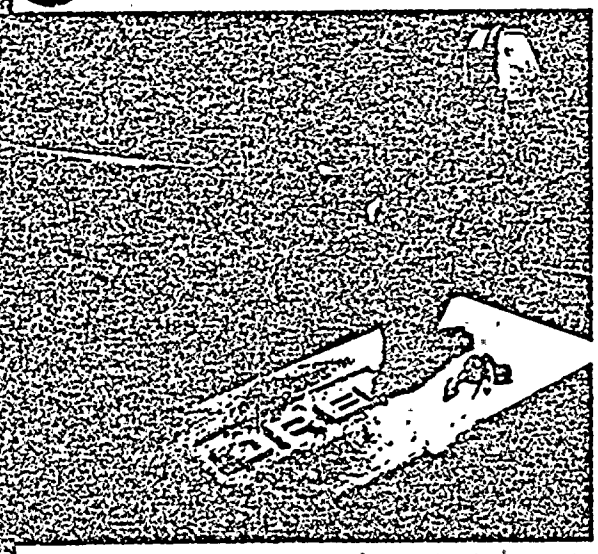
MORSE INDUSTRIAL



CAMCO

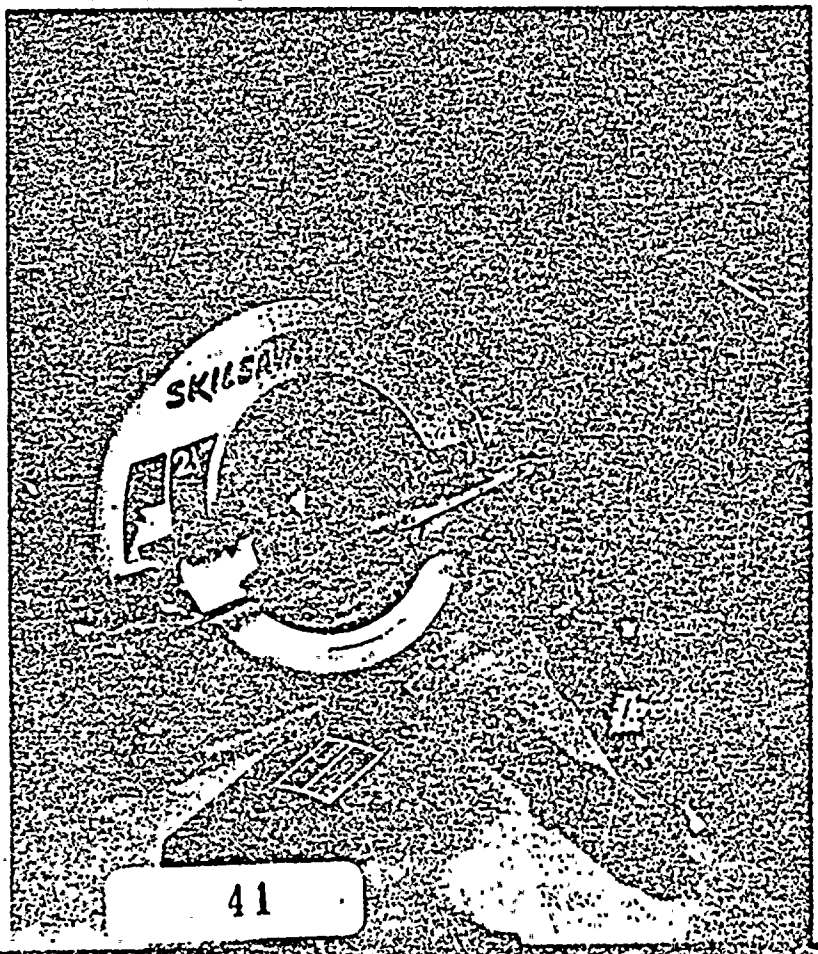


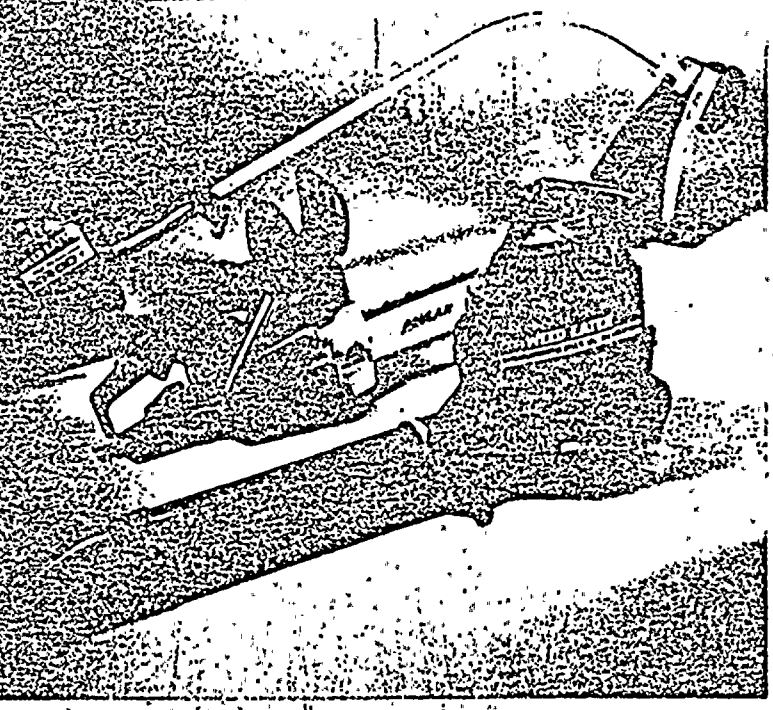
BROWNING DIVISION



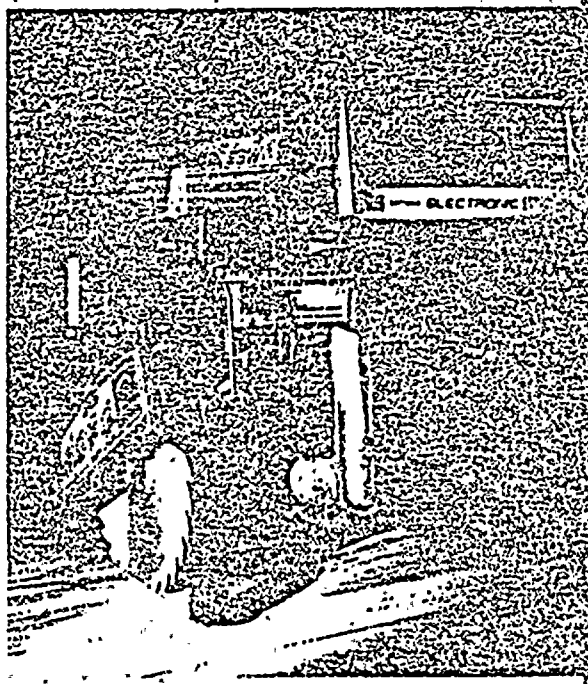
◀ **DREMEL**
Dremel manufactures a broad line of compact power bench tools and hand held rotary power tools for do it-yourself, hobbyist and craftsman markets. The Moto-Tool pictured in the foreground is the market leader in the hand held rotary tool category.

➤ **SKIL**
Innovation, quality and world-design are driving forces behind product development at Skil, a manufacturer of hand held power tools. The Skil Twist power cordless screwdriver, the Slugger hammer drill, Vari Orbit Scroller jig saw, Autotrak belt sander and consumer Circular Saw are new products being marketed successfully worldwide.



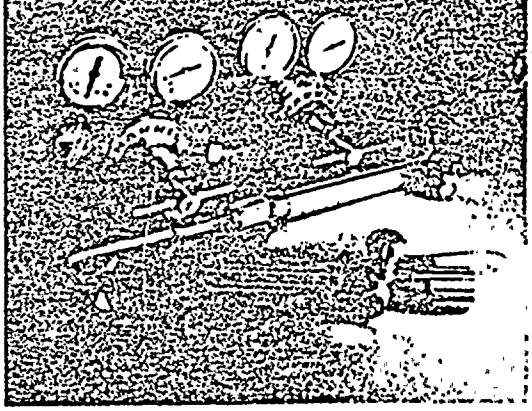


◀ BEAIRD-POULAN/ WEED EATER
Weed Eater Line Trimmer, Poulan Chain Saws and the new Weed Eater Hand Held Blower/Vac are examples of integrating high performance, state of the art two-cycle engines into lightweight, top quality products for consumer and professional markets.



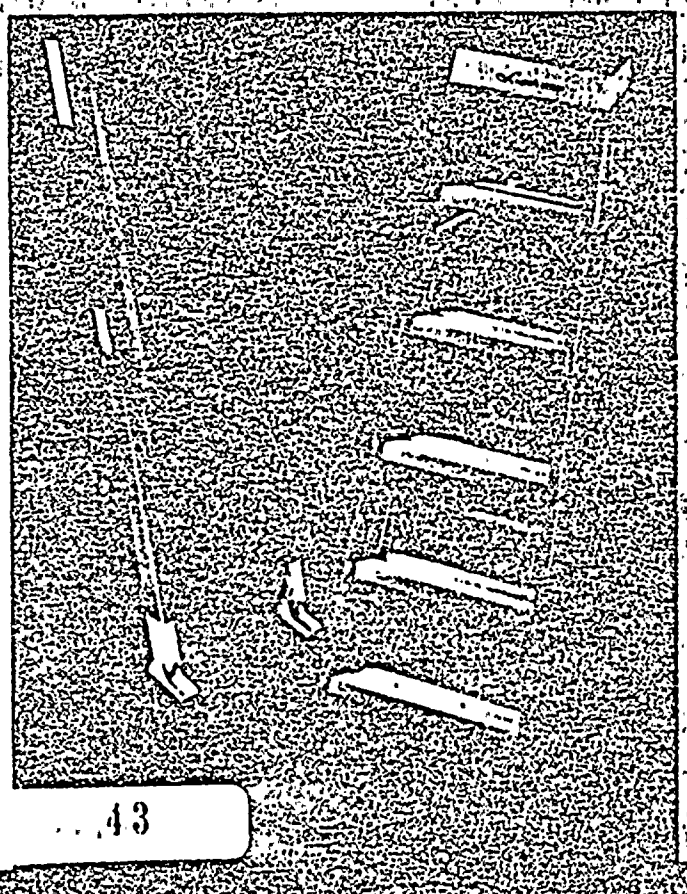
▶ SPECIAL PRODUCTS DIVISION
Special Products manufactures Craftsman stationary and bench top power tools, welders and welding vises for Sears, Roebuck and Company. The 10" Electronic Radial Arm Saw is the first digital read-out, automated consumer stationary power tool in mass distribution.

HARRIS CALORIFIC
Harris designs and manufactures gas welding and cutting apparatus for professional and industrial use. Products include torches, regulators and tips that are specifically designed for cutting, welding, brazing and heating. Harris equipment is in use worldwide, in both industrial automated and manual welding and cutting operations.



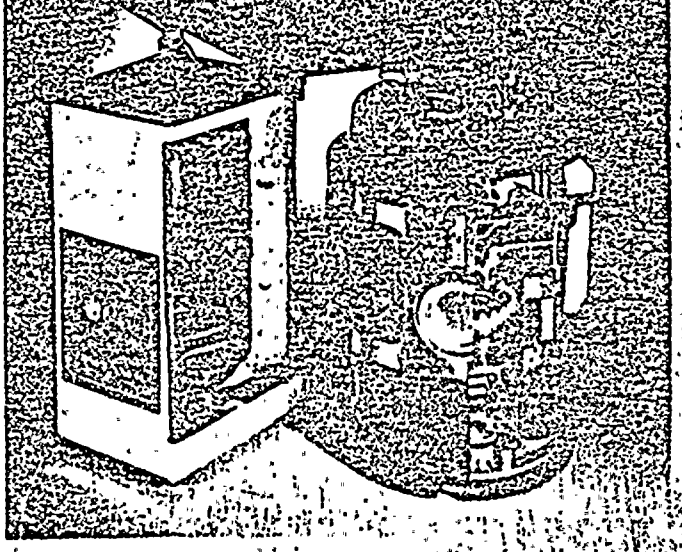
➤ RIDGE TOOL COMPANY
Ridge Tool manufactures professional hand and power tools for plumbing, industrial, electrical and commercial markets. The RIDGID 1224 is a world class machine, unmatched in quality, and designed to thread a full range of ⅛" to 4" diameter pipe or rod.

◀ WESTERN FORGE
Western Forge produces a wide range of private labeled hand tools for both professional and consumer markets. Pictured is a jaw being forge formed for Ridge Tool's 48" RIDGID Brand pipe wrench.

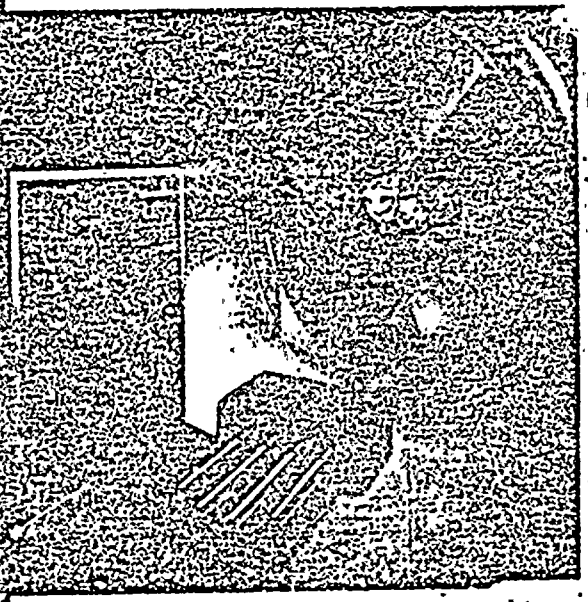


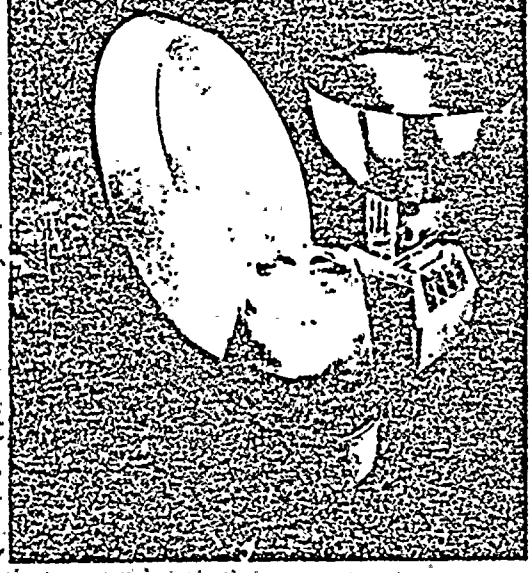
➤ LOUISVILLE LADDER
Louisville Ladder is the only company producing complete lines of fiberglass, aluminum, wood and steel ladders. Fiberglass is a ladder material Louisville Ladder pioneered. The extension ladder pictured is all non-conductive fiberglass with unique "D" shaped rungs. The fiberglass stepladder has a Louisville Ladder developed one-piece injection molded top that is non-conductive and extremely impact resistant.

➤ IN-SINK-ERATOR
In-Sink-Erator is the largest manufacturer of residential and commercial food waste disposers and hot water dispensers in the world. Pictured are cutaways of the In-Sink-Erator Classic model garbage disposer and Steaming Hot hot water dispenser, which provides 190° water at the turn of the tap.

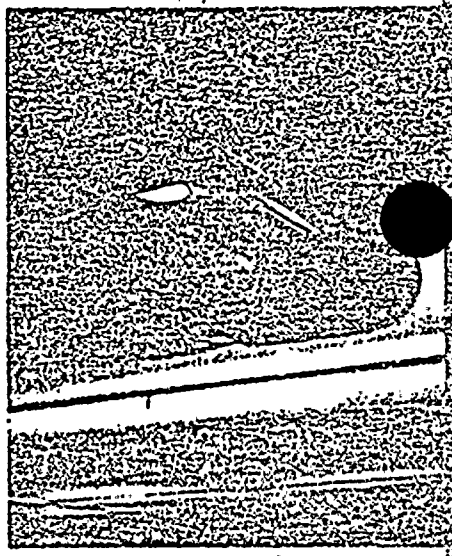


◀ BUILDER PRODUCTS DIVISION
Builder products produces a wide range of plumbing, [illegible] and [illegible] products for the [illegible] industry. Pictured are [illegible] components of the complete [illegible] system.

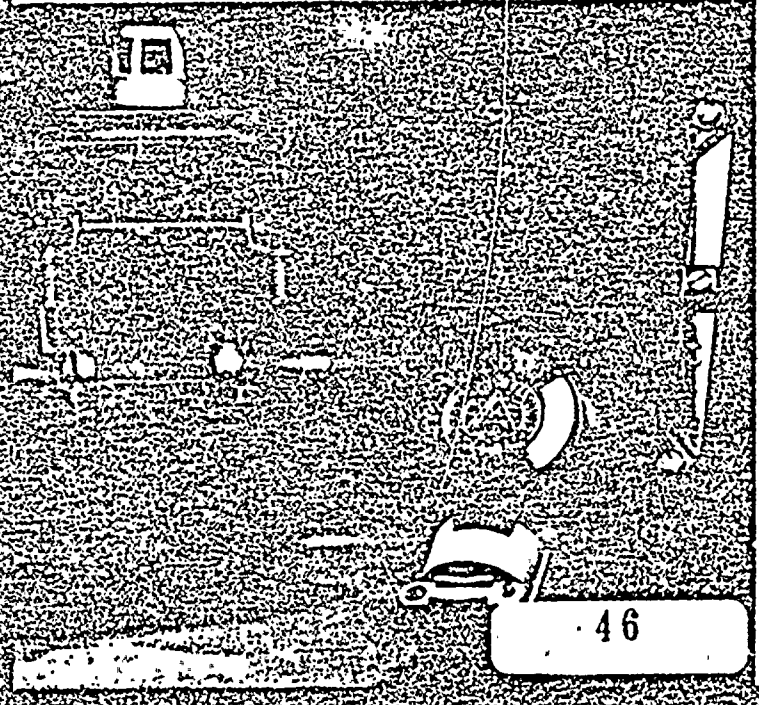




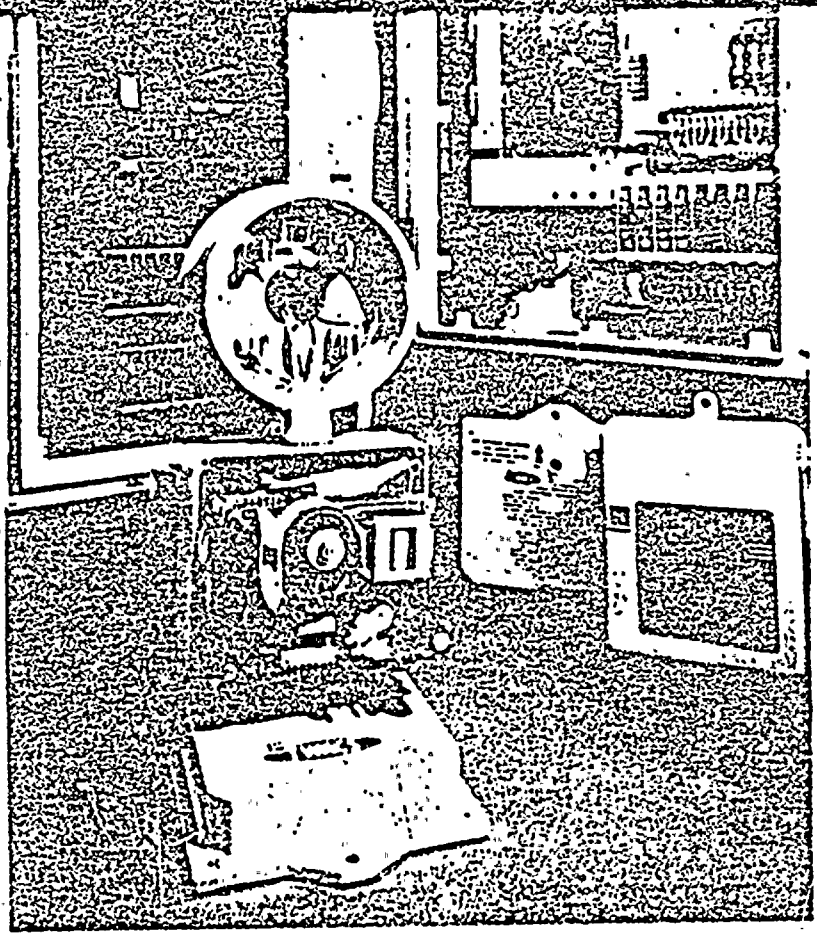
◀ **DAY-BRITE LIGHTING**
Day-Brite Lighting is an industry leader in the manufacture and sale of premium quality commercial and industrial lighting fixtures. Day-Brite's commitment to new product development features several HID (High Intensity Discharge) industrial products, the first in a complete line of indoor and outdoor lighting products that will expand Emerson's lighting package to one of the broadest in the industry.



▶ **mcPhilben/OMEGA LIGHTING**
A manufacturer of lighting fixtures and modular systems for upscale contemporary retail and commercial environments. mcPhilben/Omega systems permit lighting to fit display requirements and interior architecture, while conserving energy.



◀ **APPLETON ELECTRIC COMPANY**
Appleton manufactures more than 15,000 electrical products for both hazardous and non-hazardous environments. Patented new product innovations include the Intraground corrosion-resistant, imbedded metal grounding enclosure, the first UL listed non-metallic enclosure for use in hazardous environments. At right is the SR Switched Receptacle, a new concept in plug-receptacle design with virtually effortless insertion and withdrawal, an important consideration for plugs with up to 100 ampere capacities.

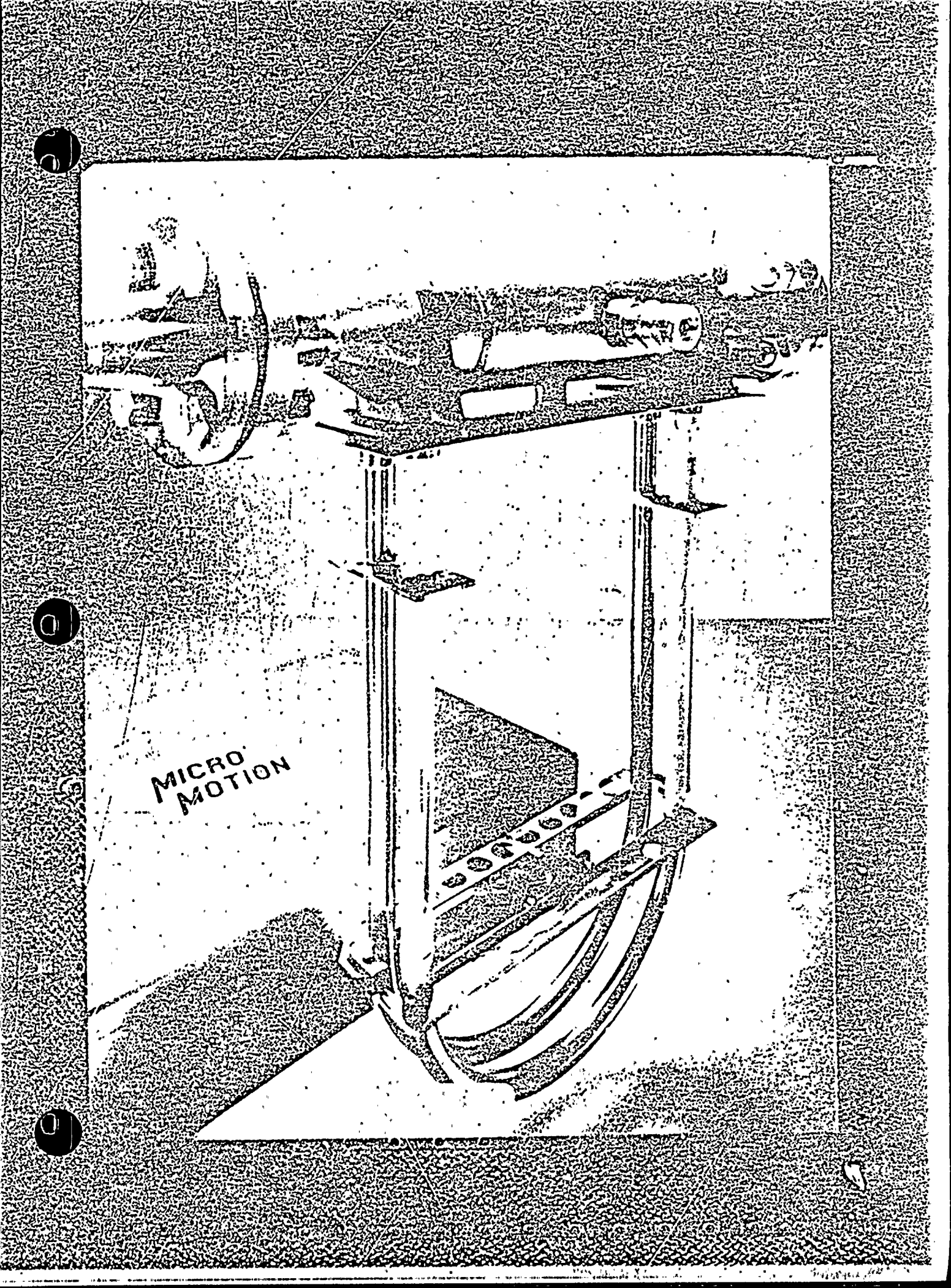


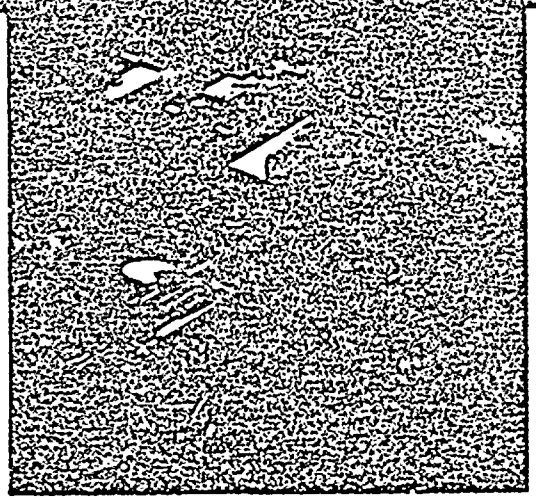
◀ CHANCE LOAD MANAGEMENT SYSTEMS

▶ ROSEMOUNT

▶ A B CHANCE

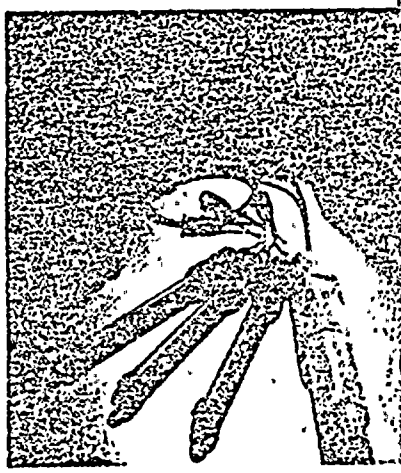
268


MICRO
MOTION

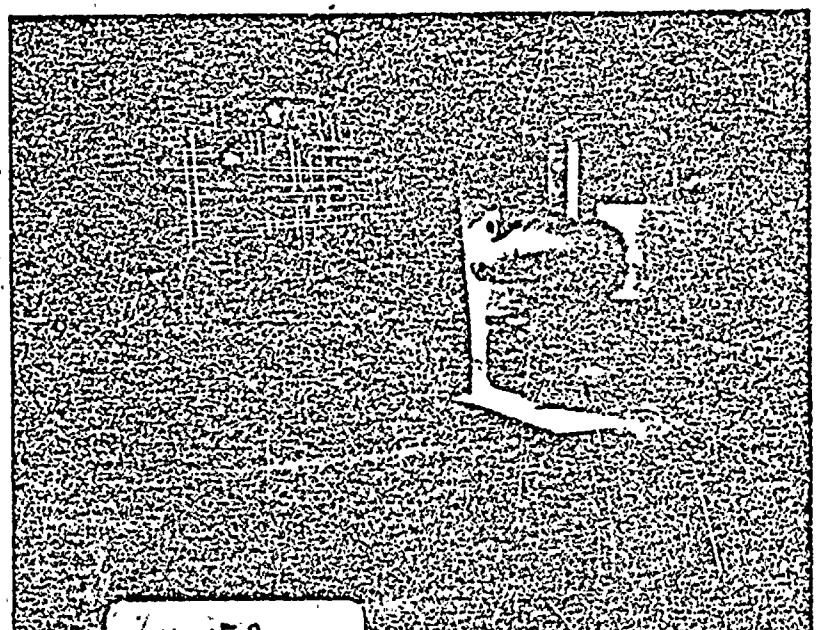


◀ **XOMOX**
Xomox manufactures special and flow control products for the chemical, petrochemical and process industries. The Tufline Automated Valve package consists of a fully lined valve, Matryx actuator and a Tufswitch magnetic limit switch for precise operation in the harshest environments. The Tufline Bellows Seal Valve provides total protection against external leakage.

◀ **MICRO MOTION**
Direct mass flow measurement for fluids was developed by Micro Motion in the mid-1970's. The measurement of mass flow is a function of the degree of deflection of the vibrating tubes on the D Model meter shown in the photograph. Without moving parts, this meter is uniquely capable of handling almost any fluid.

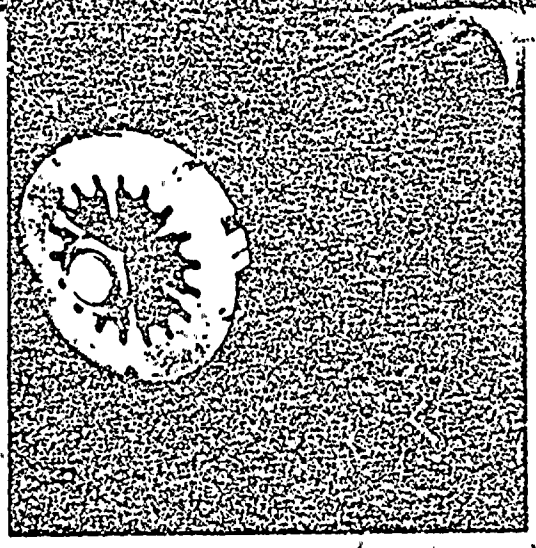


▶ **UNILOC**
The innovative leader in liquid analytical sensors and instrumentation, Uniloc is at the forefront of technology in pH, conductivity, dissolved oxygen and residual chlorine measurement and control. The Model 5100 Carbon Monoxide microprocessor control monitor is at the leading edge of process gas analysis technology.

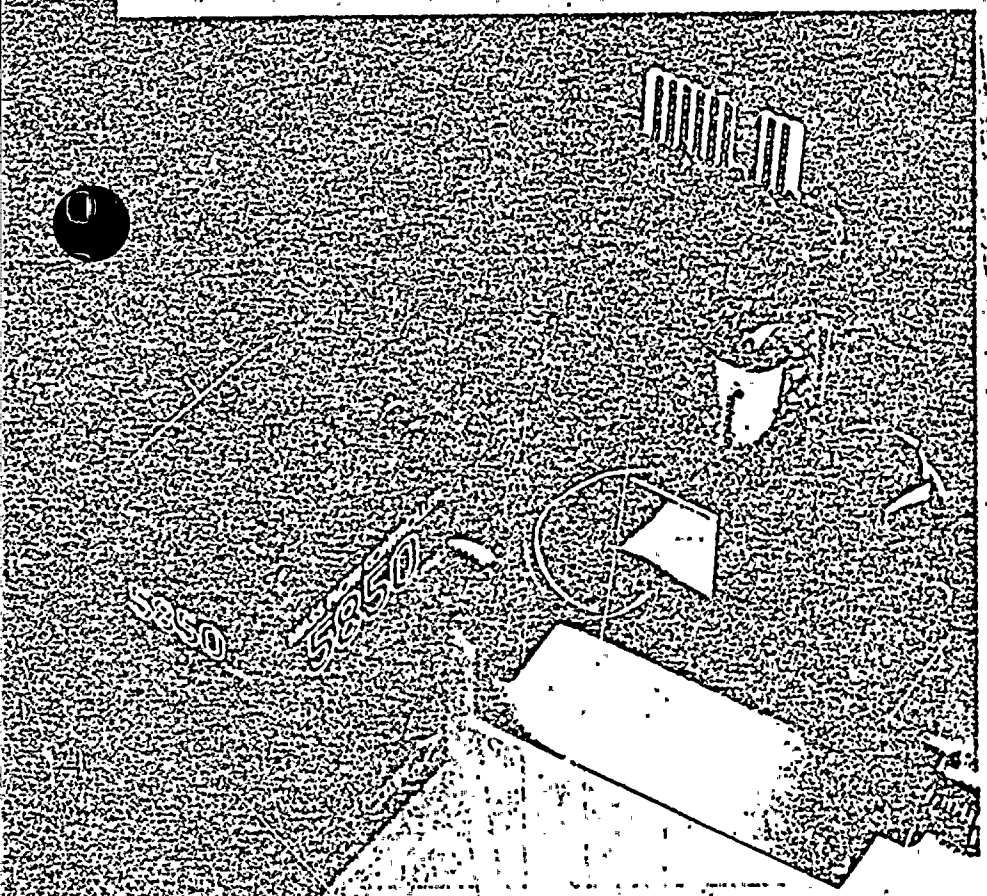


▶ **VAREC**
Varec is the recognized name in tank liquid level measurement in the petroleum and chemical industries. The System VI Computerized Monitoring and Liquid Storage Facility Control Center, plus the revolutionary Level/Mass Multi-Parameter Hydrostatic Tank Gauge represent breakthrough technology in level gauging and liquid inventory management.

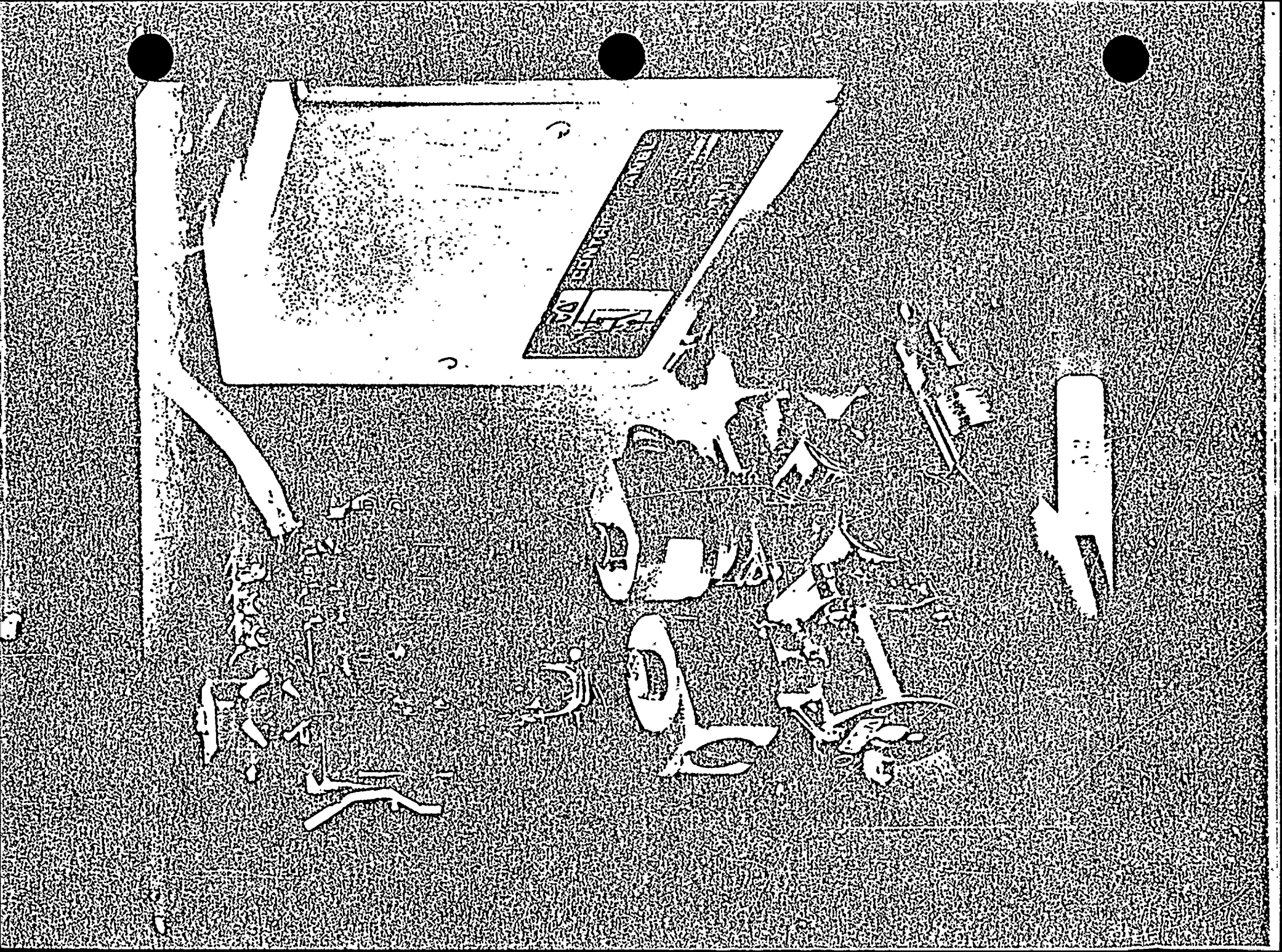
➤ VACCO INDUSTRIES
Vacco is an international multi-product engineering and manufacturing company. Its proprietary precision etched metal disc components are assembled as high pressure filters and valves for use in energy, aerospace, defense, electronics and waste management applications.



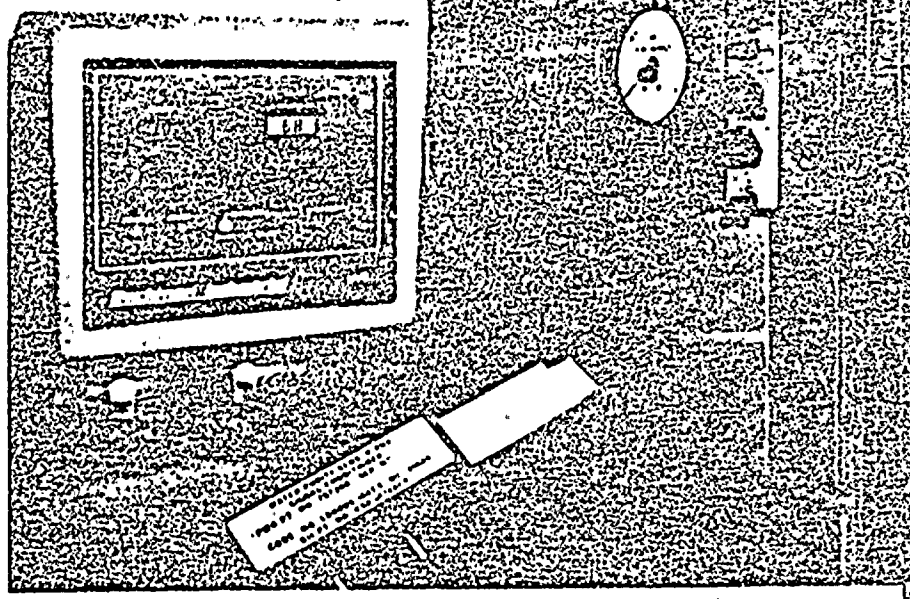
◀ BROOKS INSTRUMENT
Worldwide, Brooks manufactures the most technologically diverse line of flow measurement and control instrumentation. These products are applied to a broad range of industries to meter fluids from extremely low gas flows to crude oil. Shown is the Brooks Mass Flow Controller which precisely measures and controls low flow rates of gas in a wide range of process control applications.



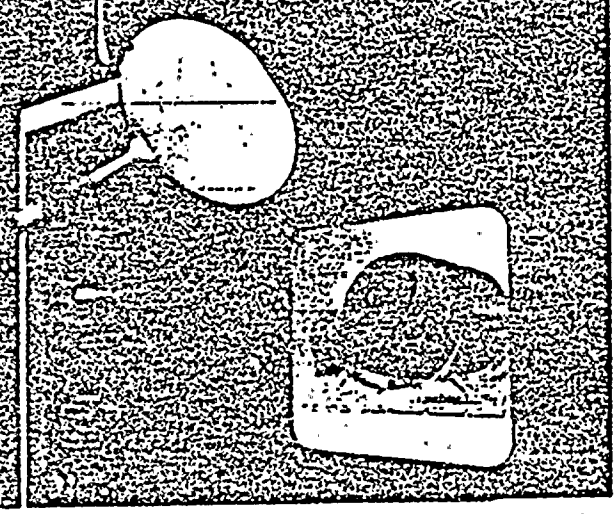
➤ AUTOMATIC SWITCH COMPANY
Automatic Switch (ASCO) is the world's leading manufacturer of both solenoid valves and automatic transfer switches. Solenoid valves for gas and fluid control, shown in the foreground, are used in factory automation applications to automate equipment and process control. The automatic transfer switch, shown with its control unit is used to operate an on-site engine generator set for standby or emergency power.



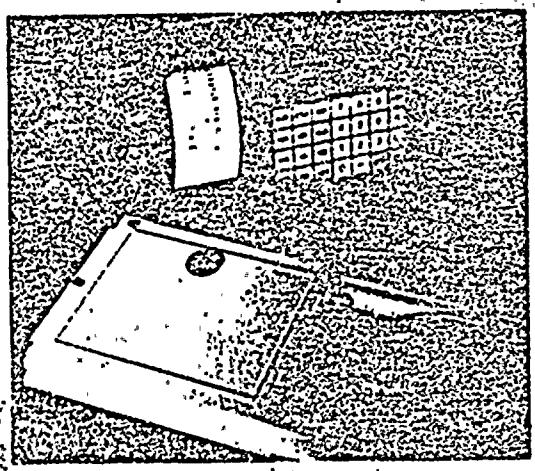
► BECKMAN INDUSTRIAL (PROCESS DIVISION)



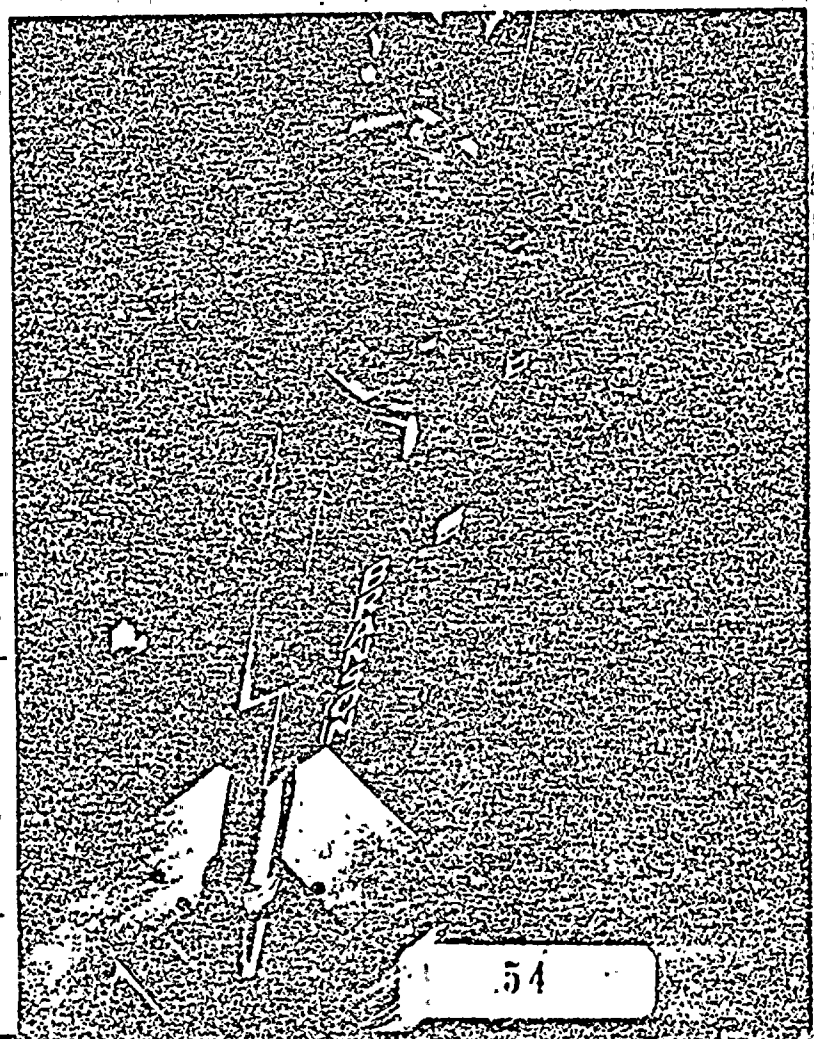
◄ BRANSON INTERNATIONAL PLASMA



▶ DORIC SCIENTIFIC
Doric produces digital instrumentation for use in measuring and monitoring temperatures and other physical parameters. The Digitrend 245 Datalogger uses a microprocessor to convert analog temperature, pressure and level signals into digital information for display and recording. The unique Front End Module (FEM) enables signals to be captured up to a mile away, and because of the Digitrend's design, data can be scanned and logged from up to 200 remote measurement points.



◀ BRANSON SONIC POWER
The leading worldwide manufacturer of ultrasonic and vibration welding equipment, Branson Sonic Power products are designed for manual, semi-automatic and totally automated production systems, ranging from bench setups, as pictured, to computer integrated manufacturing lines. The markets served by ultrasonic and vibration welding equipment are industries utilizing thermo-plastic materials such as automotive, appliance, medical, packaging, textiles and toys.



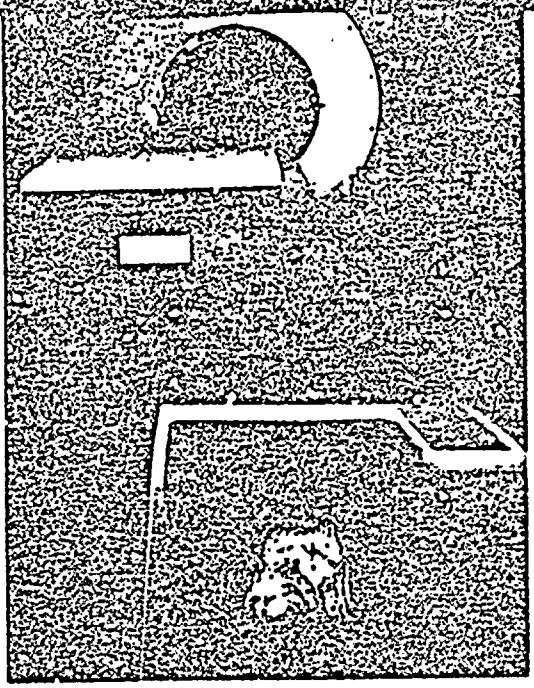
Krautkramer Branson

◀ **KRAUTKRAMER BRANSON**

[illegible]

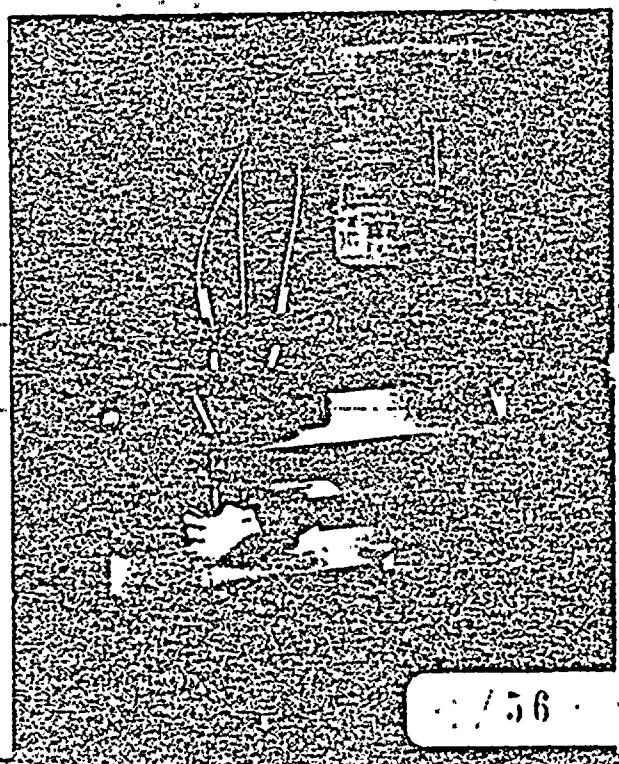
▼ **BECKMAN INDUSTRIAL (TECHNOLOGIES)**

A micro-hybrid assembly used as a Linear Variable Differential Transformer (LVDT) for industrial and military applications is shown during fabrication using an automatic wire bonder that connects wire from integrated circuit pads to a metal electronic assembly. The circuit is typical of the over 2000 different types of custom circuits designed and manufactured by Beckman Industrial



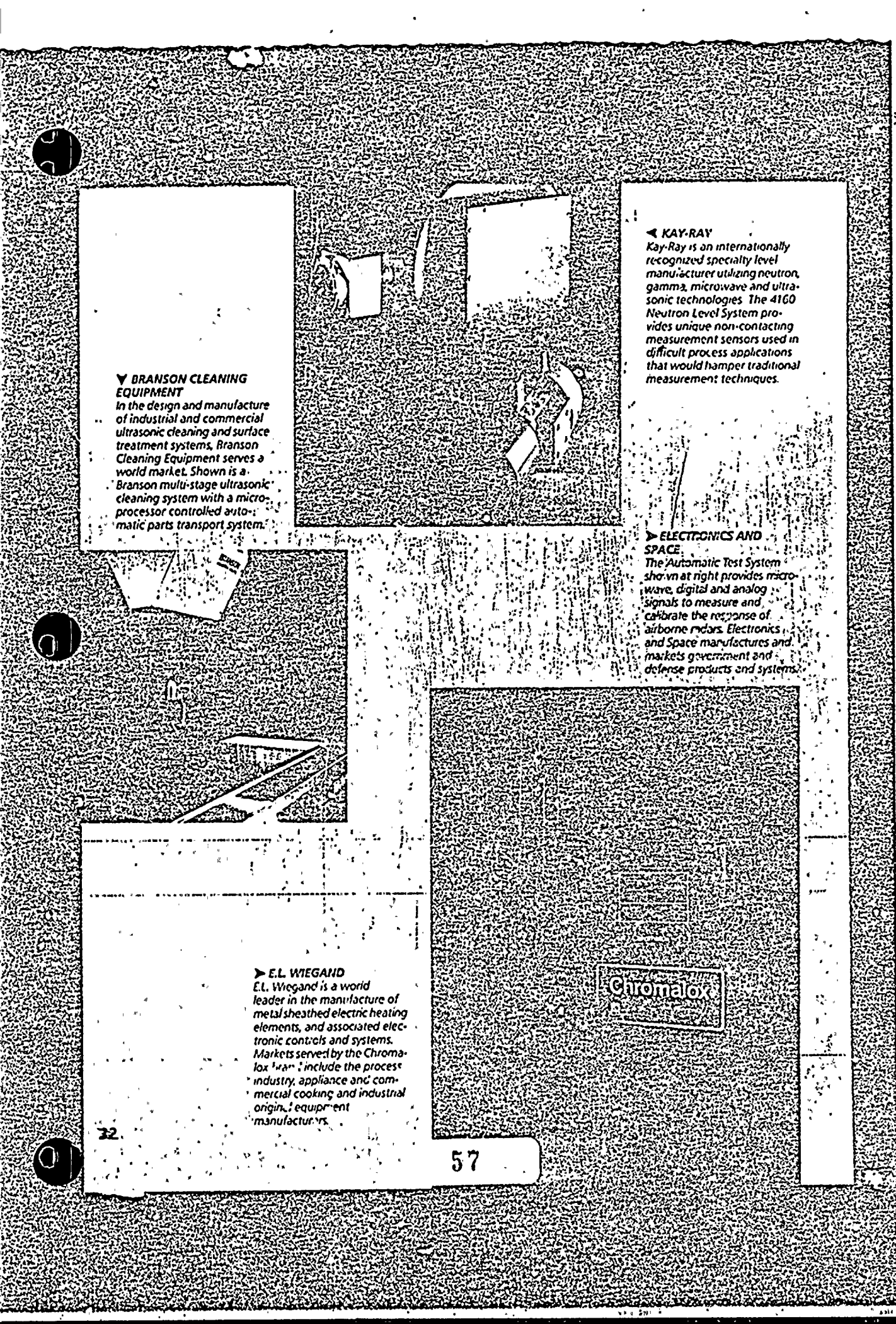
◀ **ELECTRONIC NAVIGATION INDUSTRIES**

[illegible]



▲ **ACDC ELECTRONICS**

[illegible]



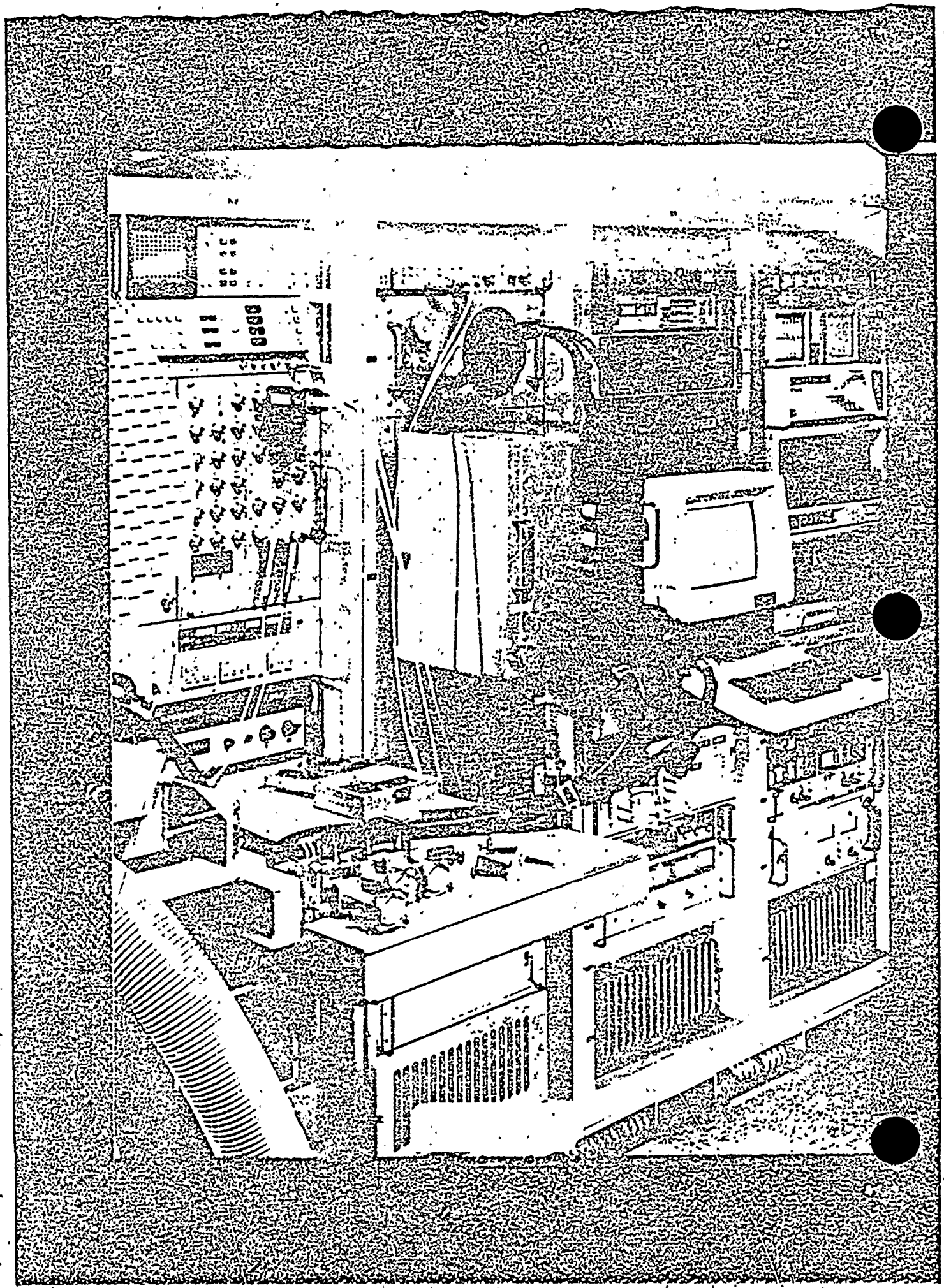
▼ **BRANSON CLEANING EQUIPMENT**
In the design and manufacture of industrial and commercial ultrasonic cleaning and surface treatment systems, Branson Cleaning Equipment serves a world market. Shown is a Branson multi-stage ultrasonic cleaning system with a microprocessor controlled automatic parts transport system.

◀ **KAY-RAY**
Kay-Ray is an internationally recognized specialty level manufacturer utilizing neutron, gamma, microwave and ultrasonic technologies. The 4160 Neutron Level System provides unique non-contacting measurement sensors used in difficult process applications that would hamper traditional measurement techniques.

➤ **ELECTRONICS AND SPACE**
The Automatic Test System shown at right provides microwave, digital and analog signals to measure and calibrate the response of airborne radars. Electronics and Space manufactures and markets government and defense products and systems.

➤ **E.L. WIEGAND**
E.L. Wiegand is a world leader in the manufacture of metal sheathed electric heating elements, and associated electronic controls and systems. Markets served by the Chromalox team include the process industry, appliance and commercial cooking and industrial original equipment manufacturers.

Chromalox



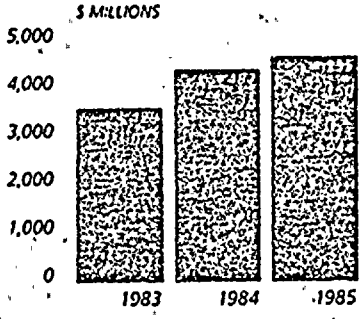
EMERSON ELECTRIC CO. AND SUBSIDIARIES
Dollars in Millions Except Per Share Amounts

Years ended September 30		1985	1984
As Restated for Poolings of Interests			
Summary of Operations	Net sales	$4,649.2	4,355.1
	Gross profit	$1,677.3	1,545.7
	Interest expense	$ 36.8	27.7
	Earnings before income taxes	$ 694.1	656.1
	Income taxes	$ 293.0	287.1
	Net earnings	$ 401.1	369.0
	Per cent of net sales	8.6%	8.5%
	Return on average stockholders' equity	19.0%	19.2%
	Return on average total operating capital	17.4%	18.2%
Per Share of Common Stock	Earnings	$ 5.43	5.00
	Cash dividends	$ 2.60	2.30
	Book value	$ 30.08	27.13
Year-End Financial Position	Working capital	$1,307.6	1,145.6
	Current ratio	2.7 to 1	2.3 to 1
	Property, plant and equipment, net	$ 843.6	777.5
	Total assets	$3,256.8	3,133.4
	Long-term debt	$ 114.6	130.5
	Stockholders' equity	$2,222.2	2,004.4
	Per cent total debt to total capital	10.9%	14.4%
Other Data	Capital expenditures	$ 206.6	170.8
	Depreciation	$ 136.0	120.0
	Taxes of all kinds, including income taxes	$ 432.9	419.1
	Salaries and wages	$1,244.7	1,160.7
	Average number of employees	61,900	60,400
	Approximate number of stockholders at year end	30,200	30,800
	Average number of common shares used in computing earnings per share (in thousands)	73,913	73,853
As Originally Reported in the Company's Annual Reports			
	Net sales	$4,649.2	4,178.8
	Earnings before income taxes	$ 694.1	617.9
	Net earnings	$ 401.1	349.2
	Per cent of net sales	8.6%	8.4%
	Earnings per common share	$ 5.43	5.10
	Working capital	$1,307.6	1,036.5
	Long-term debt	$ 114.6	130.5
	Stockholders' equity	$2,222.2	1,869.2

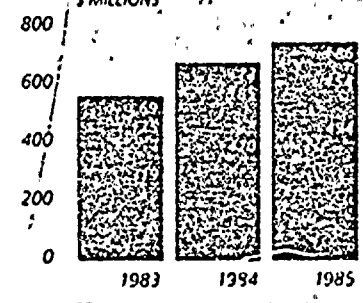
1983	1982	1981	1980	1979	1978	1977	1976
3,635.9	3,660 1	3,739.5	3,337 8	2,957 0	2,521.3	2,123.2	1,773.7
1,282.1	1,309 6	1,304 2	1,141.7	1,015.1	865.1	731.7	602.3
16.6	20.4	29.1	30.5	26.3	13 0	13 8	11.6
568.7	566.1	555.3	478 8	426.7	379.7	321.9	260.7
249.1	249 8	249.1	214 8	195.9	178.1	152 9	124.1
319 6	316.3	306.2	264.0	230.8	201.6	169 0	136.6
8.8%	8.6%	8.2%	7.9%	7.8%	8 0%	8.0%	7.7%
18.2%	19.6%	20.9%	20.4%	20 4%	20.5%	19.5%	17.6%
17.6%	18.1%	18.9%	17.7%	17.9%	18 8%	18.2%	16.3%
4.32	4.28	4.13	3.58	3.15	2.78	2.33	1.88
2.10	2.00	1.76	1.60	1.44	1.20	1.00	.7875
24.79	22.73	21.08	18.71	16.56	14.45	12.71	11.26
1,246.4	1,129 4	1,082.4	961.1	858.2	701.7	626 3	576.1
3 0 to 1	2.8 to 1	2.6 to 1	2.7 to 1	2 6 to 1	2.7 to 1	2.8 to 1	3.0 to 1
684.1	617.7	600.1	539.7	487 0	402.2	350 0	321.1
2,660.9	2,457.1	2,421.2	2,125 8	1,950.5	1,557.6	1,369 1	1,219.8
146.1	138.6	174.4	130.3	198 4	107.0	104.9	118.4
1,830.7	1,680.0	1,557 3	1,376 8	1,217.1	1,046 3	919 4	814.3
9.3%	10.6%	13.3%	15.9%	18.5%	14.1%	14.2%	16.4%
131.3	144.7	146.6	140.8	128.5	108 0	79 0	76.9
102.7	100.1	94.1	83.2	71.4	60.3	51.5	45.4
360.7	354.4	349.4	303.9	270 1	240 6	205.5	169.1
939.4	926 7	967.8	874 4	775 4	660.7	572.6	486.0
52,500	55,100	60,300	58,900	57,200	54,300	50,500	46,000
31,800	31,500	31,500	30,400	30,200	28,200	27,300	27,400
73,895	73,947	74,072	73,759	73,174	72,609	72,536	72,482
3,475.7	3,502.3	3,429.3	3,066 8	2,614.1	2,177.5	1,809.2	1,505.0
537.6	534 8	491 4	429 6	371 0	321 6	270.1	222.6
302.9	300 1	273 3	237.7	201.0	169.7	142.1	116 8
8.7%	8 6%	8 0%	7.8%	7.7%	7.8%	7 9%	7.8%
4 42	4 37	4 26	3.72	3.37	2.93	2 47	2.05
1,091.6	1,015.8	935 3	849.7	725.7	576.7	523 0	487.2
146.1	138 6	164 2	179 6	180.5	82.1	89.6	104 5
1,701.7	1,558.7	1,386 4	1,229 8	1,045.0	880 0	774.2	688.7

60

SALES
$ MILLIONS



EARNINGS BEFORE INCOME TAXES
$ MILLIONS



RESULTS OF OPERATIONS

Net Sales

Sales for 1985 were a record $4 6 billion, up 6 8 per cent from the 1984 sales of $4.4 billion. Acquisitions made in 1984 and new products contributed to this sales growth. The major 1985 acquisition (Automatic Switch Company) has been accounted for as a pooling of interests.

Commercial and Industrial sales increased 9.1 per cent in 1985 Government and Defense sales were up 14 0 per cent, and the year-end backlog for this segment reached a record $735 million. Sales for the Consumer Products segment were down 1.7 per cent, reflecting the adverse impact of the economy.

In 1984, sales of $4 4 billion were up 19 8 per cent from 1983, reflecting market growth, new products and the acquisition of new businesses. Commercial and Industrial sales were up 26.4 per cent, Government and Defense 13.5 per cent and Consumer Products 9.1 per cent.

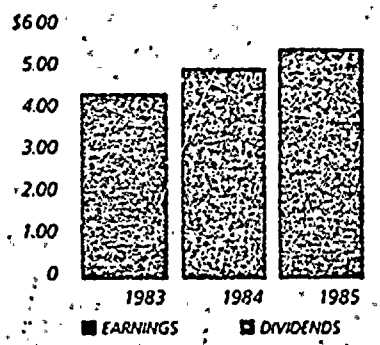
Earnings Before Income Taxes

Earnings before income taxes were $694 million in 1985, up 5 8 per cent from the $656 million in 1984. This gain resulted from improved segment margins as well as acquisitions made in 1984. Strong earnings growth in 1985 was achieved in the Commercial and Industrial segment with earnings up 17 6 per cent Government and Defense earnings increased 19 4 per cent. Earnings of the Consumer Products segment declined 16 8 per cent, reflecting difficult market conditions. Fiscal 1985 earnings before income taxes for the business segments totaled $734 million, up 8 4 per cent This profit gain outpaced the sales increase of 6 8 per cent, reflecting the continued success of the Company's cost reduction and productivity improvement programs

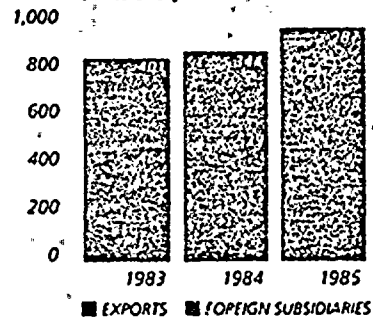
In 1984, the Company's earnings before income taxes increased 15 4 per cent over 1983, with gains of 31 7 per cent for the Commercial and Industrial segment, 5 7 per cent for the Consumer Products segment and 4 3 per cent for Government and Defense. In 1984 and 1983, the program of plant closings and consolidations resulted in expenses of $12 million and $14 million, respectively Segment financial data are summarized on page 49

In 1985, interest expense was $37 million, up from $28 million in 1984 and $17 million in 1983 The increase reflected the impact of higher debt incurred to finance the 1984 acquisitions Corporate items in 1983 primarily reflected gains on the sales of investments

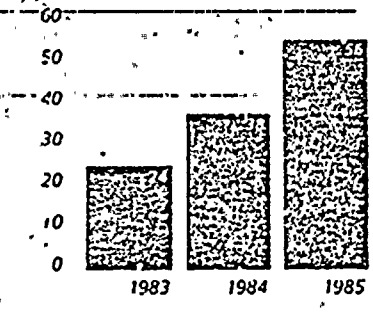
EARNINGS AND DIVIDENDS PER SHARE



INTERNATIONAL SALES $ MILLIONS



NET EARNINGS OF FOREIGN SUBSIDIARIES $ MILLIONS



Net Earnings

Fiscal 1985 marked the 28th consecutive year of increased earnings. Net earnings of $401 million were up 8.7 per cent over the 1984 net earnings of $369 million. In 1984, net earnings were up 15.5 per cent from 1983.

Earnings per common share were $5.43 in 1985, up 8.6 per cent from 1984. In 1984, earnings of $5.00 per common share were up 15.7 per cent over 1983.

Dividends

Fiscal 1985 was the 29th consecutive year of increased dividends. The dividend per share of $2.60 was up 13.0 per cent from $2.30 in 1984.

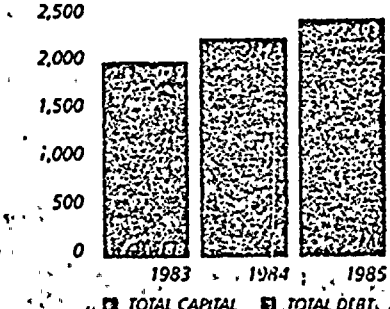
On November 5, 1985, the Board of Directors approved an increase in the quarterly dividend to $0.69 per share. This dividend will be paid on December 10, 1985 to stockholders of record as of November 22, 1985.

International Operations

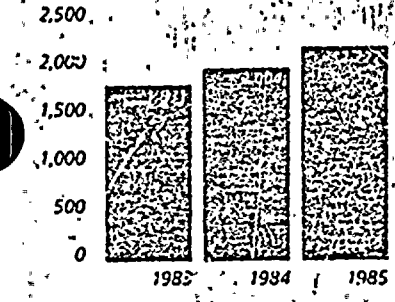
The strong performance of the Company's international operations represented a major factor in its 1985 sales and earnings growth. International sales, including exports, were $985 million for 1985, up 11.6 per cent from the $883 million in 1984. This gain was achieved despite the adverse impact of the strong dollar on U.S. exports and foreign subsidiaries' sales. Sales by the Company's foreign subsidiaries were $698 million for 1985, up 29.5 per cent over the $539 million for 1984. Export sales were $287 million in 1985 compared with $344 million in 1984, reflecting both the impact of the strong dollar and Company programs to supply international markets from non-U.S. production. Acquisitions made in 1984 contributed to both foreign subsidiary and export sales and earnings. In 1984, international sales, including exports, increased 2.1 per cent from 1983.

Net earnings of foreign subsidiaries were $56 million in 1985, up 47.4 per cent from the $38 million in 1984. This increase followed a year of strong growth in 1984 when earnings were up 58.3 per cent from the $24 million in 1983. These gains resulted from both higher sales and improved operating margins, as well as the acquisitions made in 1984. International financial data are summarized on page 49.

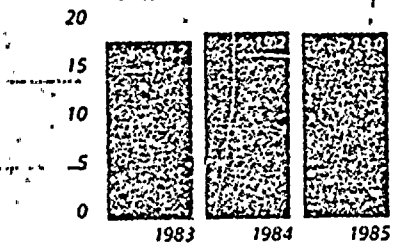
TOTAL DEBT AND TOTAL CAPITAL
$ MILLIONS



STOCKHOLDERS' EQUITY
$ MILLIONS



RETURN ON EQUITY
PER CENT



FINANCIAL POSITION

Emerson has maintained its strong financial position as evidenced by the continuation of its AAA credit rating from the major rating agencies. Ample resources remain available to meet operating requirements, fund capital spending programs and provide for the continuation of the dividend payout ratio.

Capital Structure and Liquidity

The continuation of a sound capital structure is a key factor in the Company's plan for growth. Total debt as a per cent of total capital (total debt plus stockholders' equity) was 10.9 per cent at year-end 1985, down from 14.4 per cent for 1984. The slight increase from the 9.3 per cent level of 1983 reflects the impact of cash acquisitions made in 1984. Long-term debt as a per cent of long-term capital (long-term debt plus stockholders' equity) was 4.9 per cent in 1985, down from 6.1 per cent in 1984 and 7.4 per cent in 1983.

The Company's current ratio was a strong 2.7 to 1 at year-end 1985 compared with 2.3 to 1 for 1984 and 3.0 to 1 for 1983. The decline from 1983 was primarily the result of acquisitions made in 1984.

The Company has in place a $300 million revolving line of credit and foreign bank credit facilities of $155 million to insure availability of funds.

Capital Expenditures

Capital expenditures were $207 million in 1985 compared with $171 million in 1984 and $131 million in 1983. Emphasis has been placed on new products, cost reduction projects and programs designed to increase productivity by incorporating advanced processes and technology into existing facilities.

Stockholders' Equity

Total stockholders' equity continued its steady growth reaching $2.2 billion ($30.08 per share) at year-end 1985. Stockholders' equity increased 10.9 per cent during 1985 and 9.5 per cent during 1984.

Return on Equity

During 1985, Emerson's return on average stockholders' equity continued at a high level. For 1985, the return was 19.0 per cent compared with 19.2 per cent in 1984 and 18.2 per cent in 1983.

Impact of Inflation

Estimates, using the experimental techniques sanctioned by the Financial Accounting Standards Board, have been developed to adjust Emerson's financial results for effects of changing prices in 1985. This information is shown in "Supplementary Financial Information--The Effects of Inflation on Reported Results" on pages 52 and 53.

CONSOLIDATED STATEMENT OF EARNINGS

EMERSON ELECTRIC CO. AND SUBSIDIARIES
Years ended September 30

	Millions of Dollars Except Per Share Amounts		
	1985	1984	1983
Net sales	$4,649.2	4,355.1	3,635.9
Costs and expenses:			
Cost of sales	2,971.3	2,809.4	2,353.8
Selling, general and administrative expenses	937.8	862.7	720.9
Interest expense	36.8	27.7	16.6
Other (income) deductions, net	8.6	(8)	(24.1)
Total costs and expenses	3,955.1	3,699.0	3,067.2
Earnings before income taxes	694.1	656.1	568.7
Income taxes	293.0	287.1	249.1
Net earnings	$ 401.1	369.0	319.6
Earnings per common share	$ 5.43	5.00	4.32

See accompanying notes to consolidated financial statements

EMERSON ELECTRIC CO. AND SUBSIDIARIES
September 30

ASSETS

	Millions of Dollars	
	1985	1984
Current assets		
Cash	$ 9.1	18.6
Short-term investments, at cost which approximates market	79.4	133.3
Receivables, less allowances of $13.7 million in 1985 and $12.4 million in 1984	723.2	693.1
Costs and estimated earnings on long-term contracts, less progress billings of $123.6 million in 1985 and $75.2 million in 1984	30.8	10.4
Inventories:		
Finished products	410.6	388.9
Raw materials and work in process	745.1	733.0
Total inventories	1,155.7	1,121.9
Other current assets	87.2	70.6
Total current assets	2,085.4	2,047.9
Property, plant and equipment		
Land	50.0	45.0
Buildings	388.0	341.6
Machinery and equipment	1,060.8	955.9
Construction in progress	74.4	67.3
	1,573.2	1,409.8
Less accumulated depreciation	729.6	632.3
Net property, plant and equipment	843.6	777.5
Other assets		
Excess of cost over net assets of purchased businesses	156.8	154.4
Other	171.0	153.6
Total other assets	327.8	308.0
	$3,256.8	3,133.4

See accompanying notes to consolidated financial statements

LIABILITIES AND STOCKHOLDERS' EQUITY

	Millions of Dollars	
	1985	1984
Current liabilities		
Short-term borrowings and current maturities of long-term debt	$ 156.0	107.6
Accounts payable	229.7	253.6
Advance payments on long-term contracts, less costs incurred of $16.1 million in 1985 and $32.3 million in 1984	48.6	66.1
Accrued expenses	301.2	292.4
Income taxes	42.3	82.6
Total current liabilities	771.8	902.3
Other liabilities	142.2	96.2
Long-term debt, less current maturities	114.6	130.5
Stockholders' equity		
Preferred stock of $2.50 par value per share. Authorized 3,400,000 shares, issued—none	—	—
Common stock of $1 par value per share. Authorized 150,000,000 shares; issued 74,483,359 shares in 1985 and 74,416,719 shares in 1984	74.5	74.4
Additional paid-in capital	100.4	100.5
Retained earnings	2,154.3	1,942.4
Cumulative translation adjustments	(73.0)	(84.8)
	2,256.2	2,032.5
Less cost of common stock in treasury: 599,533 shares in 1985 and 528,167 shares in 1984	34.0	28.1
Total stockholders' equity	2,222.2	2,004.4
	$3,256.8	3,133.4

CONSOLIDATED STATEMENTS OF STOCKHOLDERS' EQUITY

EMERSON ELECTRIC CO. AND SUBSIDIARIES
Years ended September 30

	Millions of Dollars		
	1985	1984	1983
Common stock			
Beginning balance—As restated	$ 74.4	74.2	74.2
Stock plans	—	.1	—
Conversion of debentures	—	.1	—
Common stock issued in connection with business combination	.1	—	—
Ending balance	74.5	74.4	74.2
Additional paid-in capital			
Beginning balance—As restated	100.5	94.2	92.0
Stock plans	(.3)	2.6	.5
Conversion of debentures	.2	3.7	.7
Ending balance	100.4	100.5	94.2
Retained earnings			
Beginning balance—As restated	1,942.4	1,742.7	1,574.7
Net earnings	401.1	369.0	319.6
Cash dividends:			
Common stock (per share: 1985, $2.60; 1984, $2.30; 1983, $2.10)	(185.3)	(157.6)	(144.0)
By pooled company prior to combination	(4.6)	(8.2)	(7.6)
Business combination	.7	—	—
Adjustment to conform fiscal year of pooled company	—	(3.3)	—
Ending balance	2,154.3	1,942.4	1,742.7
Cumulative translation adjustments			
Beginning balance—As restated	(84.8)	(61.9)	(49.6)
Translation adjustments	11.8	(23.4)	(12.3)
Adjustment to conform fiscal year of pooled company	—	.5	—
Ending balance	(73.0)	(84.8)	(61.9)
Treasury stock			
Beginning balance	(28.1)	(18.5)	(11.3)
Stock plans	4.2	4.1	1.7
Other treasury stock transactions	(10.1)	(13.7)	(8.9)
Ending balance	(34.0)	(28.1)	(18.5)
Total stockholders' equity	$2,222.2	2,004.4	1,830.7

See accompanying notes to consolidated financial statements.

EMERSON ELECTRIC CO. AND SUBSIDIARIES
Years ended September 30

	Millions of Dollars		
	1985	1984	1983
Funds provided (used)			
Operations			
Net earnings	$ 401.1	369.0	319.6
Depreciation and amortization	148.0	126.5	106.7
Changes in working capital (see table below)	(164.1)	(103.3)	34.3
Other	7.4	19.0	16.1
Total from operations	392.4	411.2	476.7
Dividends paid	(189.9)	(165.8)	(151.6)
Investments			
Capital expenditures	(206.6)	(170.8)	(131.3)
Realization of benefits from tax leases including amounts repayable in future years	19.7	21.9	20.4
Purchase of businesses, excluding cash and short-term investments acquired:			
Net working capital	(3.1)	(113.4)	(39.6)
Property, plant and equipment	(3.3)	(71.3)	(48.6)
Other assets	1.7	(205.2)	(8.3)
Long-term debt and other liabilities	.4	18.3	12.0
Total investments	(191.2)	(520.5)	(195.4)
Financing			
Short-term borrowings and current maturities of long-term debt, net	(52.5)	148.2	(18.6)
Proceeds from long-term debt	.6	9.1	9.2
Reduction of long-term debt	(17.6)	(31.0)	(13.4)
Common stock transactions	(5.2)	(3.1)	(5.0)
Total financing	(74.7)	123.2	(27.8)
Increase (decrease) in cash and short-term investments	$ (63.4)	(151.9)	101.9
Funds provided by (used for) changes in working capital			
Receivables and costs and estimated earnings on long-term contracts	$ (47.5)	(50.3)	(10.7)
Inventories	(31.3)	(66.3)	23.1
Accounts payable and advance payments on long-term contracts	(42.2)	8.1	14.8
Effect of foreign currency translation on working capital	5.8	(17.5)	(8.8)
Other	(48.9)	22.7	15.9
	$(164.1)	(103.3)	34.3

See accompanying notes to consolidated financial statements

EMERSON ELECTRIC CO AND SUBSIDIARIES

(1) SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES

Principles of Consolidation
The consolidated financial statements include the accounts of the Company and its majority owned subsidiaries except for a wholly owned finance subsidiary accounted for by the equity method All significant intercompany transactions, profits and balances are eliminated in consolidation Common stock investments of 20 to 50 per cent are accounted for by the equity method. Investments of less than 20 per cent are carried at cost.

Inventories
Inventories are stated at the lower of cost or market. The majority of inventory values are based upon standard costs which approximate average costs, while the remainder are principally valued on a first-in, first-out basis. Standard costs are revised at the beginning of the fiscal year and variances incurred during the year are allocated between inventories and cost of sales.

Property, Plant and Equipment
The Company records investments in land, buildings and machinery and equipment at cost. Improvements are capitalized, while repair and maintenance costs are charged to expense as incurred. When assets are retired or disposed of, the related cost and accumulated depreciation are removed from the accounts; gains or losses are included in operating results.

Depreciation is computed principally using accelerated methods over estimated service lives. Service lives for principal assets are 30 to 40 years for buildings and 8 to 12 years for machinery and equipment.

Excess of Cost Over Net Assets of Purchased Businesses
Assets and liabilities related to business combinations accounted for as purchase transactions are recorded at their respective fair values. Excess of cost over net assets of purchased businesses is amortized in equal installments over the periods estimated to be benefited, the most extended period being 40 years.

Start-Up Costs
Costs incurred in connection with the start-up of new plants and other facilities are amortized over periods not exceeding 12 months following commencement of operations.

Income Taxes
Investment tax credits are accounted for by the flow-through method, under which the tax benefits are recognized as a reduction of income tax expense in the year the assets are placed in service

No provision is made for deferred income taxes on the undistributed earnings of foreign subsidiaries ($255.1 million at September 30, 1985), primarily because retention of these earnings is considered essential for their continuing operations. In those cases where distributions have been made, additional income taxes, if any, have been minimal due to offsets by available foreign tax credits.

Realization of benefits from the investment in tax leases results in a reduction of income tax payments with no effect on income tax expense Interest was capitalized on the investment until such time as tax benefits received exceeded the original investment Such capitalized interest plus the excess of the original investment over cumulative tax savings is amortized to expense using the interest method during the period, when the Company's cash savings through tax deferral exceed the original investment

Retirement Plans
The Company and its subsidiaries have defined benefit and defined contribution retirement plans covering substantially all employees. Pension expense includes current costs, amortization of unfunded prior service costs, primarily over 30 years, and amortization of actuarial gains and losses over 10 to15 years Funding equals or exceeds minimum funding standards required by the Employee Retirement Income Security Act.

Long-Term Contracts
Income on long-term contracts, principally government and defense contracts, is recognized on the percentage-of-completion or unit-of-delivery basis On contracts where the percentage-of-completion method is used, costs and estimated earnings in excess of progress billings are shown as a current asset Unbilled costs on unit-of-delivery contracts are included in inventory Payments received in excess of costs incurred on long-term contracts are shown as a current liability

Earnings Per Common Share.
Earnings per common share are computed by dividing net earnings by the weighted average number of common shares outstanding during the applicable periods.

Common Stock Plans
Estimated compensation related to the Performance Shares Bonus Plans is charged to expense over the term of the Plans. The tax effect of differences between the amount expensed and the amount deductible for income tax purposes is recorded as an adjustment to additional paid-in capital in the year the stock is issued

(2) BUSINESS COMBINATIONS
During 1985, the Company issued 5,396,554 shares in two business combinations accounted for as poolings of interests. The most significant combination was with Automatic Switch Company for 5,336,417 shares The accounts of pooled companies have been restated to conform to Emerson's accounting policies and fiscal year. The financial statements for periods prior to combination have been restated to include Automatic Switch Company, while there has been no restatement for the smaller acquisition due to immateriality Stockholders' equity at October 1, 1982 was restated as follows (millions of dollars).

	Balance at October 1, 1982		
	As Previously Reported	Adjustment for Pooling of Interests	As Restated
Common stock	$ 68 9	5.3	74 2
Additional paid-in capital	77 1	14 9	92 0
Retained earnings	1,472 2	102 5	1,574 7
Cumulative translation adjustments	(48 2)	(1 4)	(49 6)
Treasury stock	(11 3)	—	(11.3)
Total stockholders' equity	$1,558 7	121.3	1,680 0

Sales and net earnings of pooled companies were not significant to consolidated results of operations in the year of combination

In 1984, the Company acquired the industrial businesses of SmithKline Beckman Corporation for $208 6 million in a business combination accounted for as a purchase The Company also purchased the net assets of several smaller businesses in 1985, 1984 and 1983 for $4 0 million, $170 0 million and $85 7 million, respectively The results of operations of the purchased businesses have been included in the Company's consolidated results of operations since the respective dates of acquisition On an unaudited pro forma basis, assuming the businesses purchased in 1984 had been acquired at the beginning of the prior year, net sales would have been $4,544 4 million and $4,013 3 million for 1984 and 1983, respectively Net earnings and earnings per share would not have been significantly different than reported amounts The results of operations of the businesses purchased in 1985 and 1983 were not material to consolidated results of operations

(3) NONCAPITALIZED LEASE OBLIGATIONS
The Company leases computers transportation equipment and various other property under noncapitalized lease agreements Total rent expense for all such leases was $79 3 million in 1985, $70 8 million in 1984 and $56.7 million in 1983

The minimum annual rentals of noncancellable long-term leases, exclusive of maintenance, taxes, insurance and other operating costs, will approximate $33.5 million in 1986 and decline substantially thereafter

(4) SHORT-TERM BORROWINGS AND LINES OF CREDIT

Short-term borrowings consist primarily of commercial paper and foreign bank borrowings. The following table summarizes such borrowings during 1985, 1984 and 1983:

	Dollars in Millions					
	Domestic			Foreign		
	1985	1984	1983	1985	1984	1983
Borrowings at year end	$172.5	159.4	–	69.8	33.9	31.6
Weighted average interest rate at year end	8.0%	11.2%	–	10.0%	14.9%	15.2%
Month-end average borrowings during the year	$140.4	68.1	–	45.3	33.8	34.4
Month-end weighted average interest rate during the year	8.9%	10.5%	–	13.2%	15.1%	13.0%
Highest month-end level of borrowings during the year	$220.0	159.4	–	69.8	41.7	38.3

A revolving line of credit amounting to $300 million was maintained with various banks at September 30, 1985 to assure availability of funds, to support commercial paper borrowings and for other general corporate purposes. This credit agreement is effective through September 1992 and does not require the Company to maintain compensating balances. There were no borrowings against domestic lines of credit in 1985, 1984 or 1983.

The Company's foreign subsidiaries maintained bank credit facilities in various currencies approximating $155 million at September 30, 1985. In most instances, borrowings against these facilities have been guaranteed by the parent company to assure the availability of funds at favorable interest rates.

(5) LONG-TERM DEBT

Long-term debt is summarized as follows:

	Millions of Dollars	
	1985	1984
Notes payable in installments through 2004 at a weighted average interest rate of 8.72% at September 30, 1985	$ 31.9	37.1
Lease obligations payable in installments through 2014 at a weighted average interest rate of 6.97% at September 30, 1985	88.1	95.1
5% convertible subordinated debentures with annual sinking fund requirements to 1992	1.8	2.1
Other	6.5	10.5
	128.3	144.8
Less current maturities	13.7	14.3
	$114.6	130.5

Long-term debt maturing during each of the four years ending September 30, 1990 is $8.8 million, $9.7 million, $8.5 million and $8.0 million, respectively. The Company is in compliance with the covenants of its debt agreements and believes that the covenants will not restrict its future operations.

(6) COMMON STOCK

The Company has various stock option plans which permit certain officers and employees to purchase common stock. Changes in the number of shares subject to option are summarized as follows (shares in thousands):

	1985		1984	
	Average Price	Shares Subject to Option	Average Price	Shares Subject to Option
Beginning of year	$55.73	606.7	$38.72	473.4
Options granted	71.98	10.5	65.13	320.1
Assumed options of acquired company	50.06	5.4	–	–
Options exercised	40.78	(75.3)	26.66	(169.6)
Options cancelled	63.07	(11.1)	49.21	(17.2)
End of year	57.94	536.2	55.73	606.7
Exercisable at year end		281.1		154.1

The Company has granted units to key management personnel under two Performance Shares Bonus Plans. Each unit is equivalent to one share of common stock payable at least 50 per cent in common stock and the remainder in cash. Under the 1981 Plan, participants will receive in January 1986 an aggregate maximum of 381,474 units. The 1985 Plan provides that, upon accomplishing specific performance objectives in fiscal 1989, participants shall receive an aggregate maximum of 350,000 units. As of September 30, 1985, 270,965 units have been granted under the 1985 Plan. The Company has adopted a systematic pattern of purchasing treasury shares for issuance under these Plans which would generally require purchases over the life of the Plans assuming 80 per cent of the units will be paid in common stock.

At September 30, 1985, 1,153,124 shares of common stock, including 599,533 treasury shares, are reserved for issuance under the Company's stock plans. An additional 41,963 shares of common stock are reserved for conversion of outstanding convertible debentures of Skil Corporation, a subsidiary of the Company, at a price of $44.68 per share (22.38 shares for each $1,000 debenture).

(7) INCOME TAXES

Following is a summary of the principal components of income tax expense:

	Millions of Dollars		
	1985	1984	1983
Federal:			
Current	$221.4	227.5	192.2
Deferred–Tax over book depreciation	16.1	13.9	8.9
Deferred–Other	(7.8)	(8.6)	2.0
State and local	30.3	28.9	26.1
Foreign	33.0	25.4	19.9
	$293.0	287.1	249.1

Deferred taxes relating to state and local and foreign timing differences are not material and are included in the appropriate category above.

The following table reconciles the differences between the Company's effective income tax rate and the federal corporate statutory rate:

	1985	1984	1983
Federal corporate statutory rate	46.0%	46.0%	46.0%
State and local taxes, less federal tax benefit	2.4	2.4	2.5
Investment and research and development tax credits	(2.3)	(2.2)	(2.2)
Benefits from DISC/FSC and United States Possession Corporations	(1.2)	(1.5)	(1.9)
Other	(2.7)	(0.9)	(0.6)
Effective income tax rate	42.2%	43.8%	43.8%

(8) RETIREMENT PLANS

Pension and profit-sharing expense was $31.5 million in 1985, $35.2 million in 1984 and $30.7 million in 1983. A comparison of the present value of accumulated plan benefits and net assets for the Company's domestic defined benefit plans as of the most recent actuarial valuation dates (generally October 1, 1984 and January 1, 1984, respectively) is set forth in the following table.

	Millions of Dollars	
	1985	1984
Actuarial present value of accumulated plan benefits:		
Vested	$215.7	230.0
Nonvested	23.0	24.5
Total	$248.7	254.5
Net assets available for plan benefits	$403.0	392.8

The assumed rates of return used to determine the present value of plan benefits were primarily the rates published by the Pension Benefit Guaranty Corporation as of the respective valuation dates. For 1985, the weighted average rate was 9.2 per cent and for 1984 it was 8.8 per cent.

Retirement benefits for employees in foreign locations are funded primarily through either annuity or government programs. Assets and liabilities of the Company's foreign plans are not significant.

(9) OTHER FINANCIAL DATA

Accrued expenses at September 30, 1985 and 1984 are as follows:

	Millions of Dollars	
	1985	1984
Employee compensation	$121.0	101.8
Insurance, including self-insurance	33.4	34.8
Pension and profit-sharing plans	25.4	20.8
Taxes other than income taxes	22.7	25.5
Warranty expenses	23.3	22.8
Other	75.4	86.7
	$301.2	292.4

The following items were charged or credited to earnings during the years ended September 30, 1985, 1984 and 1983:

	Millions of Dollars		
	1985	1984	1983
Research, new product development and product improvement costs	$140.0	120.3	96.8
Maintenance and repairs	74.1	73.1	59.6
Advertising costs	55.1	50.2	37.8
Foreign transaction losses	5.8	4.1	6.3
Foreign translation (gains) losses	(2.0)	(.3)	.9

(10) CONTINGENT LIABILITIES

Contingent liabilities, which consist of guarantees, taxes, pending litigation and various other claims occurring in the normal course of business, are not expected by management to result in actual liabilities which will have a material effect on the consolidated financial position of the Company.

(11) INDUSTRY SEGMENT INFORMATION

The products manufactured by the Company are classified into three general industry segments: Commercial and Industrial Components and Systems, Consumer Products and Government and Defense Systems. Summarized information about the Company's operations in each industry segment and geographic area is as follows:

Industry Segments
(Millions of Dollars)

	Net Sales to Unaffiliated Customers			Earnings Before Income Taxes		
	1985	1984	1983	1985	1984	1983
Commercial and Industrial	$2,944	2,698	2,135	494	420	319
Consumer Products	1,150	1,170	1,072	154	185	175
Government and Defense	555	487	429	86	72	69
	4,649	4,355	3,636	734	677	563
Corporate items	–	–	–	(3)	7	23
Interest expense	–	–	–	(37)	(28)	(17)
Total	$4,649	4,355	3,636	694	656	569

	Total Assets			Depreciation Expense			Capital Expenditures		
	1985	1984	1983	1985	1984	1983	1985	1984	1983
Commercial and Industrial	$2,150	2,095	1,551	96	84	71	148	120	95
Consumer Products	729	708	664	28	25	25	43	37	28
Government and Defense	241	188	150	10	9	6	14	11	6
Corporate items	146	148	305	2	2	1	2	3	2
Eliminations	(9)	(6)	(9)	–	–	–	–	–	–
Total	$3,257	3,133	2,661	136	120	103	207	171	131

Geographic Areas
(Millions of Dollars)

	Net Sales to Unaffiliated Customers			Earnings Before Income Taxes		
	1985	1984	1983	1985	1984	1983
United States	$3,951	3,816	3,172	610	590	526
Foreign	698	539	464	90	64	44
Eliminations	–	–	–	(6)	2	(1)
Total	$4,649	4,355	3,636	694	656	569

	Total Assets			Net Assets		
	1985	1984	1983	1985	1984	1983
United States	$2,715	2,746	2,341	1,938	1,788	1,645
Foreign	609	458	371	291	220	191
Eliminations	(67)	(71)	(51)	(7)	(4)	(5)
Total	$3,257	3,133	2,661	2,222	2,004	1,831

Emerson Product Lines

The Company is engaged principally in the manufacture and sale of a broad range of electrical-electronic products and systems. These products and systems are sold primarily through independent distributors and to original equipment manufacturers and, to a lesser extent, to retailers and other users. Representative products and systems by industry segment are as follows:

Commercial & Industrial Components & Systems

- Integral HP Motors & Gear Motors
- Fractional & Sub-Fractional HP Motors & Gear Motors
- Variable Speed Motor Drives
- Electronic Power Supplies
- Uninterruptible Power Systems
- Power Conditioning, Distribution & Transfer Equipment
- Custom Motor Repair Services
- Regulators & Level Controls
- Direct Mass Flow Measuring Instruments
- Telemetering & Logging Systems
- Temperature & Pressure Sensors & Controls
- Process Control Valves
- Solenoid and Pneumatic Valves
- Valve Actuation Systems
- Fluid Heat Transfer Systems
- Mechanical Power Transmission Products
- Industrial Separating & Finishing Equipment
- Ultrasonic Test & Processing Equipment
- Electrical Transmission & Distribution Tools & Equipment
- Aviation Instrumentation
- Variable Resistors & Resistor Networks
- Commercial & Industrial Electrical Heating Products
- Industrial Process Analytic Instrumentation
- Appliance Controls & Ignition Systems

Consumer Products

- Portable Power Tools & Accessories
- Stationary Power Tools & Accessories
- Power Hobby Tools
- Hand Tools
- Electric Garbage Disposers
- Instant Hot Water Dispensers
- Electric Heating & Convection Systems
- Residential Air Movement & Ventilation Products
- Chain Saws
- Ladders & Scaffolding
- Residential Security Systems
- Intercom & Chime Systems
- Residential Comfort Control Systems
- Monofilament Line Lawn Trimmers
- Lighting & Interconnect Systems
- Shop Vacuums
- Gas Welding & Cutting Equipment
- Power Plumbing Tools

Government & Defense Systems

- Radar Systems
- Electronic Warfare Systems
- Telemetry Tracking Systems
- Missile Launching Systems
- Power Conversion Equipment
- Communications Systems
- Simulator Systems for Training
- Satellite Communications Systems
- Airborne, Ground & Surface Armament Systems
- Guidance & Control Systems
- Automatic Test Equipment
- Special Tactical Vehicles
- Anechoic Chambers
- Microwave Systems
- Radar Antennas

REPORT OF MANAGEMENT

The Company's management is responsible for the integrity and accuracy of the financial information contained in this Annual Report. Management believes that the financial statements have been prepared in conformity with generally accepted accounting principles appropriate in the circumstances and that the other information in this Annual Report is consistent with those statements. In preparing the financial statements, management makes informed judgments and estimates where necessary to reflect the expected effects of events and transactions that have not been completed.

In meeting its responsibility for the reliability of the financial statements, management relies on a system of internal accounting control. This system is designed to provide reasonable assurance that assets are safeguarded and transactions are executed in accordance with management's authorization and recorded properly to permit the preparation of financial statements in accordance with generally accepted accounting principles. The design of such control procedures recognizes that errors or irregularities may occur and that estimates and judgments are required to assess the relative cost and expected benefits of the controls. Management believes that the Company's accounting controls provide reasonable assurance that errors or irregularities that could be material to the financial statements are prevented or would be detected within a timely period.

The Audit Committee of the Board of Directors, which is comprised solely of Directors who are not employees of the Company, is responsible for monitoring the Company's accounting and reporting practices. The Audit Committee meets with management and internal auditors periodically to review the work of each and to monitor the discharge by each of its responsibilities. The Audit Committee also meets periodically with the independent auditors who have free access to the Audit Committee and the Board of Directors to discuss internal accounting control, auditing and financial reporting matters.

The independent auditors are engaged to express an opinion on the Company's financial statements. Their opinion is based on procedures which they believe to be sufficient to provide reasonable assurance that the financial statements contain no material errors.

ACCOUNTANTS' REPORT

The Board of Directors and Stockholders
Emerson Electric Co.:

We have examined the consolidated balance sheets of Emerson Electric Co. and subsidiaries as of September 30, 1985 and 1984 and the related consolidated statements of earnings, stockholders' equity, and changes in financial position for each of the years in the three-year period ended September 30, 1985. Our examinations were made in accordance with generally accepted auditing standards and, accordingly, included such tests of the accounting records and such other auditing procedures as we considered necessary in the circumstances.

In our opinion, the aforementioned consolidated financial statements present fairly the financial position of Emerson Electric Co. and subsidiaries at September 30, 1985 and 1984 and the results of their operations and the changes in their financial position for each of the years in the three-year period ended September 30, 1985, in conformity with generally accepted accounting principles applied on a consistent basis.

Peat, Marwick, Mitchell & Co.

St. Louis, Missouri
November 4, 1985

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Quarterly Financial Information

Summarized quarterly data are as follows

	Millions of Dollars						Earnings Per Common Share	
	Net Sales		Gross Profit		Net Earnings			
	1985	1984	1985	1984	1985	1984	1985	1984
First Quarter	$1,124.4	977.4	410.4	336.1	98.4	85.9	1.33	1.16
Second Quarter	1,168.6	1,092.9	426.6	376.8	102.1	95.7	1.38	1.30
Third Quarter	1,192.7	1,169.5	424.5	414.7	103.3	96.9	1.40	1.31
Fourth Quarter	1,163.5	1,115.3	417.8	416.1	97.3	90.5	1.32	1.23
Fiscal Year	$4,649.2	4,355.1	1,677.3	1,545.7	401.1	369.0	5.43	5.00

The above data differs from data originally reported to stockholders because of restatement for a pooling of interests

	Dividends Per Common Share		Price Range Per Common Share			
			1985		1984	
	1985	1984	High	Low	High	Low
First Quarter	$ .65	.575	71⅛	65⅛	68⅞	59¼
Second Quarter	.65	.575	78⅛	67⅛	68¼	58¼
Third Quarter	.65	.575	73⅛	66¼	65½	58⅛
Fourth Quarter	.65	.575	75⅛	68	70½	59
Fiscal Year	$ 2.60	2.30	78¼	65⅛	70½	58⅛

Emerson Electric Co. common stock (Symbol EMR) is listed on the New York Stock Exchange and Midwest Stock Exchange.

The Effects of Inflation on Reported Results

The accompanying inflation-adjusted financial information is presented in accordance with the requirements of the Financial Accounting Standards Board (FASB). The FASB requires that certain historical financial information be adjusted for the effects of specific price changes (current cost) and other information, such as historical sales, dividends and common stock prices, be adjusted for general inflation by applying the Consumer Price Index for All Urban Consumers (CPI-U). As acknowledged by the FASB, the methods used to prepare this data are experimental and, because of necessity, are based on assumptions, estimates and subjective judgments. They should be viewed, therefore, as approximations rather than precise measurements.

The current cost method is intended by the FASB to measure the impact of specific price changes. It assumes that the Company purchased or produced, at current costs, the same inventories and acquired property, plant and equipment of the same productive efficiency as were owned at the end of the current fiscal year. The current cost of inventories and cost of sales were estimated based on a combination of internally developed and externally available indices. Current acquisition and construction costs of property, plant and equipment were estimated using externally available indices and composite indices developed by independent consultants.

The Company believes that the current cost methodology fails to reflect the actual impact of inflation on Emerson. Specifically, current cost calculations do not consider the efficiencies or cost savings that might be realized by replacing existing assets with new, more efficient or more technologically advanced assets even though this is the avenue that Emerson pursues relentlessly in its capital expenditure programs.

For financial reporting purposes, the Company employs accelerated depreciation methods, however, for current cost calculations, the straight-line depreciation method has been applied to avoid overstating the impact of inflation.

In accordance with FASB requirements, inflation-adjusted net earnings do not reflect an adjustment to historical income tax expense, because present tax laws do not allow deductions for increased depreciation and cost of sales due to inflation. As a result, the effective tax rate increases substantially as compared with the historical financial statements.

Net assets increased as a result of the revaluation of inventories, property, plant and equipment, and net monetary items. When assessing the overall impact of inflation on its operations, the Company believes that this increase should be considered a potential adjustment in the calculation of inflation-adjusted net earnings. The FASB, however, does not permit this adjustment to be included in the calculation, even though the components of the increase are required disclosures.

In our complex economic environment, it is extremely difficult to make an accurate assessment of the impact of inflation. Nonetheless, Emerson is responsive to potential effects of inflation by stressing cost reduction, productivity improvements and effective asset management in its programs and planning in order to mitigate the effects of inflation. The Company believes that its past performance record, measured in terms of earnings and dividend growth, demonstrates a proven ability to cope with inflation.

The following data should not be construed to be indicative of the impact of inflation on Emerson, but rather, as a best-estimate calculation (stated in average 1985 dollars) based on the guidelines set forth by the FASB.

Supplementary Statement of Earnings Adjusted for Changing Prices—Year Ended September 30, 1985

(Dollars in Millions Except Per Share Amounts)

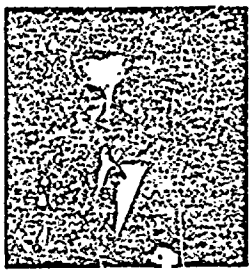
	As Reported in the Consolidated Statement of Earnings	Adjusted for Specific Price Changes (Current Cost)
Net sales	$4,649	4,649
Costs and expenses:		
Cost of sales excluding depreciation	2,855	2,870
Depreciation	136	150
Other	964	964
Total costs and expenses	3,955	3,984
Earnings before income taxes	694	665
Income taxes	293	293
Net earnings	$ 401	372
Earnings per common share	$ 5.43	5.03
Effective income tax rate	42.2%	44.1%
Translation adjustments	$ 12	13
Purchasing power gain on net monetary items		$ 2
Increase in general inflation of inventories and net property, plant and equipment during the year		$ 72
Effect of increase in specific prices		29
Excess of general inflation over specific price increases		$ 43

The current costs of inventories and net property, plant and equipment, stated in 1985 year-end dollars, were $1,178 and $1,197, respectively, at September 30, 1985.

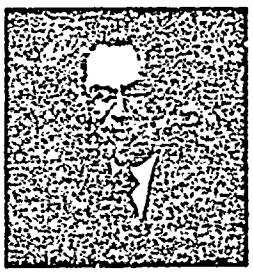
Supplementary Five-Year Information Adjusted for Effects of Changing Prices

(Dollars in Millions Except Per Share Amounts)

	Years ended September 30,				
	1985	1984	1983	1982	1981
Current cost data					
Net earnings	$ 372	335	294	302	275
Earnings per common share	$ 5.03	4.53	3.98	4.08	3.71
Net assets at year end	$2,557	2,420	2,351	2,267	2,198
Translation adjustments	$ 13	(27)	(15)		
Increase in general inflation over increase in specific prices of inventories and net property, plant and equipment	$ 43	47	3	23	92
Other information adjusted for general inflation					
Net sales	$4,649	4,515	3,923	4,088	4,487
Purchasing power gain (loss) on net monetary items	$ 2	(2)	(5)	(3)	5
Dividends paid per common share	$ 2.60	2.38	2.27	2.23	2.11
Market price of common stock at year end	$67.92	68.94	64.96	54.04	47.74
Average consumer price index	319.4	308.1	296.0	286.0	266.2

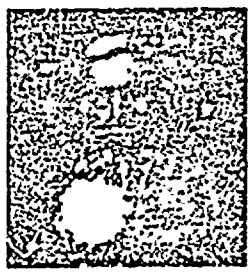


G.K. Beare

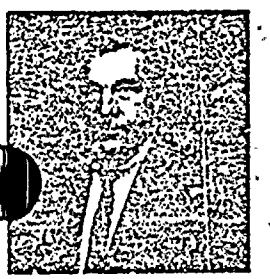


L.L. Browning, Jr.

A. A. Busch III

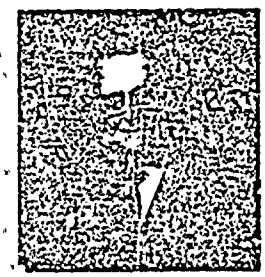


L.J. Cont:

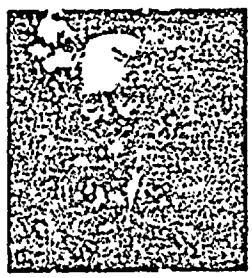


G.A. Lodge

V.R. Loucks, Jr.



W.R. Persons



R.D. Potts

Executive Committee

Conflict of Interest & Ethics Committee

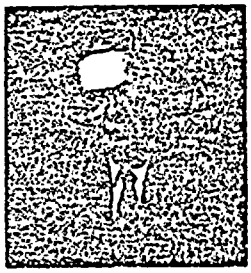
Charitable Contributions Committee

Compensation & Human Resources Committee

Audit Committee

J.A. Frates

J.J. Kelley



E.L. Keyes, Jr

C.F. Knight

W.A. Rutledge

B.A. Schnuver

W.M. Van Cleve

F.F. Williams, Jr

Finance Committee

Pension Committee

Director Emeritus
R.H. McRoberts

Advisory Members of the Board of Directors

Office of the Chief Executive

C.F. Knight
Chairman & Chief Executive Officer

W.A. Rutledge
Vice Chairman

E.L. Keyes, Jr.
President

J.J. Adorjan
Executive Vice President

J.F. Hardymon
Executive Vice President

R.W. Staley
Executive Vice President

A.E. Suter
Executive Vice President

J.K. Ver Hagen
Executive Vice President

W.C. Bousquette
Senior Vice President & Chief Financial Officer

C.A. Dill
Senior Vice President

Corporate Staff

E.L. Clary
Group Vice President-Corporate Services

R.M. Cox, Jr.
Vice President & Treasurer

D.N. Farr
Assistant Treasurer

H.F. Faught
Group Vice President-Technology

W.J. Galvin
Vice President-Financial Analysis & Systems

P.L. Gartman
Vice President-Development

A.A. Gilbert
Vice President-Manpower Development

C.W. Groennert
Vice President-Financial Services & Assistant Secretary

C. Hansen
Senior Vice President-Secretary & General Counsel

H.E. Johnson
Vice President-Planning

J.R. Marchiano
Vice President-Manufacturing

D.R. Perkins
Assistant Treasurer

C.O. Planting
Vice President-Corporate Sales

P.A. Roberts
Vice President-Public Affairs

J.C. Rohrbaugh
Senior Vice President-Industrial Relations

J.C. Wilson
Vice President of Finance & Controller

H.J. Yopp
Vice President-Tax

Operating Executives

R.F. Amter
Louisville, Kentucky

H.R. Baker
Milford, Connecticut

***T.V. Bruns**
Cincinnati, Ohio

A.P. Christenson
Birmingham, Alabama

R.W. Clancy
St. Louis, Missouri

J.F. Cole
Calabasas, California

W.L. Cook
Santa Ana, California

M.H. Damon
Rochester, New York

***W.H. Davis**
Pittsburgh, Pennsylvania

***W.L. Davis, III**
Chicago, Illinois

E.R. Ehrhard
Florham Park, New Jersey

***M.L. Engle**
St. Louis, Missouri

C.M. Frova
Fullerton, California

R.A. Geckle
Shelton, Connecticut

***D.O. Gifford**
St. Louis, Missouri

E.L. Gluck
Melville, New York

G.C. Hartman
Ithaca, New York

***V.H. Heath**
Minneapolis, Minnesota

***J.C. Janning**
Mansfield, Ohio

R.J. Jehling
Bennettsville, South Carolina

W.C. Jessen
Honeoye Falls, New York

D.L. Johnson
Brussels, Belgium

G.A. Kames
Cincinnati, Ohio

K.R. Kilpatrick
Oceanside, California

P.W. Knisely
Chicago, Illinois

H.W. Kooyman
Maysville, Kentucky

W.R. Lennartz
Carson, California

***L. Lomo**
Centralia, Missouri

E.J. Lovelady
St. Louis, Missouri

J.L. Mayfield
Hayward, California

***J.M. McConnell**
Hatfield, Pennsylvania

E.J. McGuire
St. Louis, Missouri

G.T. McKane
Elyria, Ohio

***C.L. Mikovich**
Shreveport, Louisiana

***D.J. Moore**
Brea, California

***R.J. Novello**
St. Louis, Missouri

K. Obata
Tokyo, Japan

W.W. O'Dell
Lewistown, Pennsylvania

R.V. Ogrodnik
St. Louis, Missouri

G.A. Olson
Colorado Springs, Colorado

D.G. Perkins
Boulder, Colorado

M.J. Proudfoot
Markham, Ontario Canada

R.G. Schreiner
Tupelo, Mississippi

W.L. Scroggin
Fullerton, California

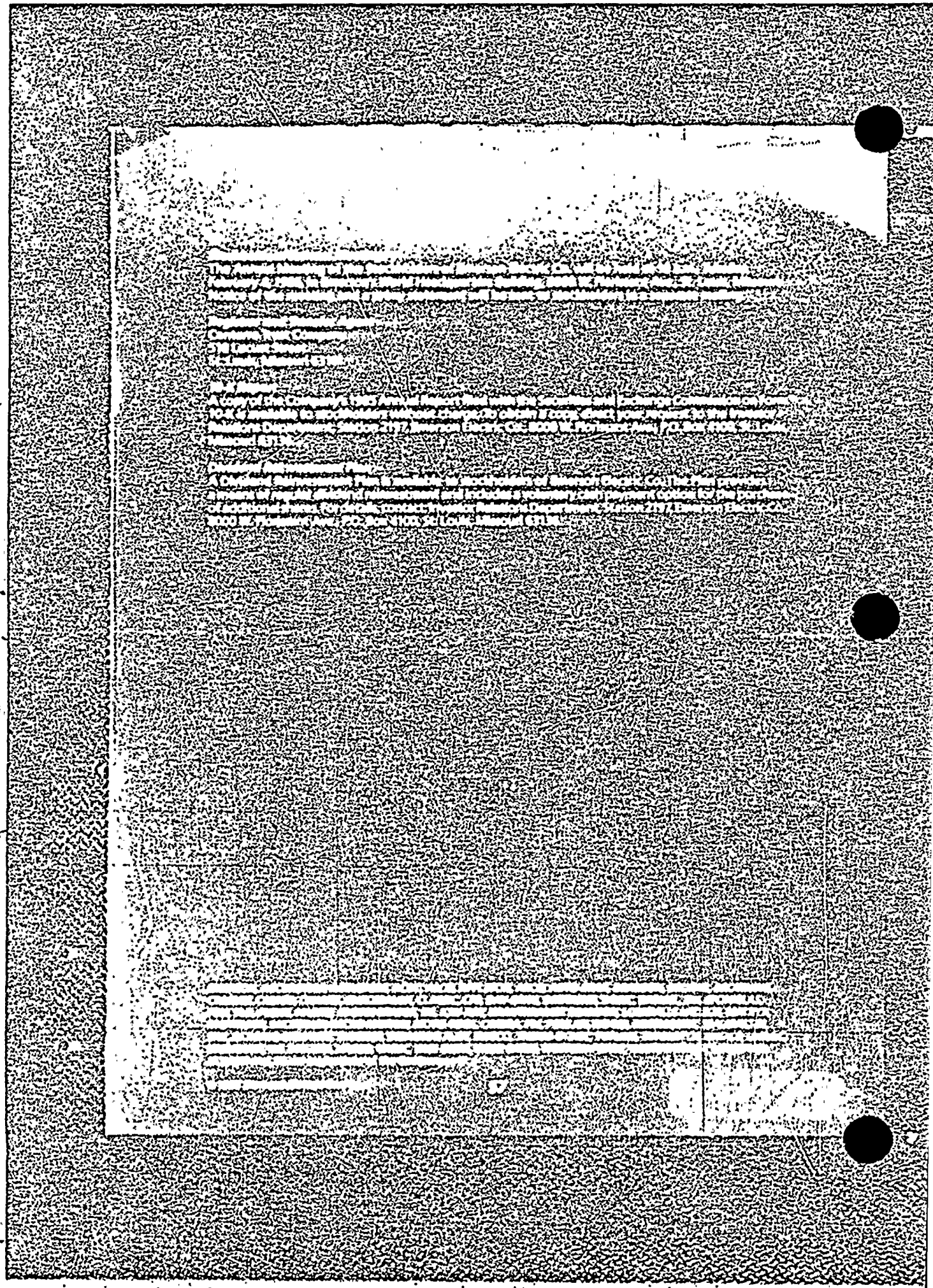
***D.L. Seals**
Racine, Wisconsin

W.K. Tolley
South El Monte, California

C.W. Totten
Los Angeles, California

A.R. Ziegler
Danbury, Connecticut

*Group Executive



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SECURITIES AND EXCHANGE COMMISSION

WASHINGTON, D.C. 20549

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DISCLOSURE INCORPORATED

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FORM 10-Q

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

For Quarter Ended December 31, 1985

Commission file number 1-278

EMERSON ELECTRIC CO.

(Exact name of registrant as specified in its charter)

Missouri	43—0259330
(State or other jurisdiction of incorporation or organization)	(I.R.S. Employer Identification No.)
8000 W. Florissant Ave., St. Louis, Missouri	63136
(Address of principal executive offices)	(Zip Code)

Registrant's telephone number, including area code (314) 553-2000

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 and (2) has been subject to such filing requirements for the past 90 days. Yes ✓ No ____

Common stock outstanding at December 31, 1985: 72,479,166 shares

PART I. FINANCIAL INFORMATION

The following unaudited consolidated financial statements, in the opinion of management, include all adjustments, consisting only of normal recurring accruals, necessary for a fair presentation of the results for the interim periods presented. The consolidated financial statements are presented in accordance with the requirements of Form 10-Q and consequently do not include all the disclosures required by generally accepted accounting principles. For further information refer to the consolidated financial statements and notes thereto included in the Company's Annual Report on Form 10-K for the year ended September 30, 1985.

EMERSON ELECTRIC CO. AND SUBSIDIARIES
CONSOLIDATED STATEMENTS OF EARNINGS
THREE MONTHS ENDED DECEMBER 31, 1985 AND 1984
(Dollars in Millions Except Per Share Data)

	Three Months Ended December 31,	
	1985	1984
Net sales	$1,154.7	1,124.4
Costs and expenses:		
Cost of sales	736.5	714.0
Selling, general and administrative	239.5	232.8
Interest expense	9.1	9.1
Other (income) deductions, net	(1.8)	.1
Total costs and expenses	983.3	956.0
Earnings before income taxes	171.4	168.4
Income taxes	72.0	70.0
Net earnings	$ 99.4	98.4
Number of shares used in computing earnings per common share (in thousands)	73,179	73,892
Per common share:		
Earnings	$1.36	1.33
Cash dividends	.69	.65

EMERSON ELECTRIC CO. AND SUBSIDIARIES
CONSOLIDATED BALANCE SHEETS

	Millions of Dollars	
	December 31, 1985	September 30, 1985
ASSETS		
CURRENT ASSETS:		
Cash	$ 11.8	9.1
Short-term investments, at cost which approximates market	83.2	79.4
Receivables, less allowances of $15.0 million and $13.7 million	679.3	723.2
Costs and estimated earnings on long-term contracts, less progress billings of $136.8 million and $123.6 million	45.2	30.8
Inventories:		
Finished products	407.2	410.6
Raw materials and work in process	767.1	745.1
Total inventories	1,174.3	1,155.7
Other current assets	114.4	87.2
TOTAL CURRENT ASSETS	2,108.2	2,085.4
PROPERTY, PLANT AND EQUIPMENT:		
Property, plant and equipment, at cost	1,606.3	1,573.2
Less accumulated depreciation	760.5	729.6
NET PROPERTY, PLANT AND EQUIPMENT	845.8	843.6
OTHER ASSETS:		
Excess of cost over net assets of purchased businesses	165.7	156.8
Other	250.4	171.0
TOTAL OTHER ASSETS	416.1	327.8
	$3,370.1	3,256.8
LIABILITIES AND STOCKHOLDERS' EQUITY		
CURRENT LIABILITIES:		
Short-term borrowings and current maturities of long-term debt	$ 237.0	156.0
Accounts payable	214.8	229.7
Advance payments on long-term contracts, less costs incurred of $15.1 million and $16.1 million	30.9	48.6
Accrued expenses	269.7	301.2
Income taxes	34.9	42.3
TOTAL CURRENT LIABILITIES	787.3	777.8
OTHER LIABILITIES	172.6	142.2
LONG-TERM DEBT, LESS CURRENT MATURITIES	228.3	114.6
STOCKHOLDERS' EQUITY:		
Preferred stock of $2.50 par value per share. Authorized 5,400,000 shares; issued - none	-	-
Common stock of $1 par value per share. Authorized 150,000,000 shares; issued 74,485,478 shares and 74,483,359 shares	74.5	74.5
Additional paid-in capital	100.2	100.4
Retained earnings	2,203.7	2,154.3
Cumulative translation adjustments	(63.9)	(73.0)
	2,314.5	2,256.2
Less common stock in treasury, 2,006,312 shares and 599,533 shares	132.6	34.0
TOTAL STOCKHOLDERS' EQUITY	2,181.9	2,222.2
	$3,370.1	3,256.8

EMERSON ELECTRIC CO. AND SUBSIDIARIES
CONSOLIDATED STATEMENTS OF CHANGES IN FINANCIAL POSITION
THREE MONTHS ENDED DECEMBER 31, 1985 AND 1984

	Millions of Dollars	
	1985	1984
Funds provided (used):		
Operations:		
Net earnings	$ 99.4	98.4
Depreciation and amortization	40.4	37.3
Changes in working capital	(80.2)	(55.6)
Other	(24.3)	.5
Total from operations	35.3	80.6
Investments:		
Capital expenditures	(41.0)	(47.1)
Realization of benefits from tax leases including amounts repayable in future years	3.3	5.0
Purchase of businesses, less cash and short-term investments acquired		
Property, plant & equipment & other assets	(10.5)	(.4)
Net working capital	(1.1)	(2.6)
Other liabilities	-	1.5
Other	(23.8)	-
Total investments	(73.1)	(43.6)
Dividends paid	(50.0)	(47.1)
Financing:		
Short-term borrowings and current maturities of long-term debt, net	80.1	7.7
Proceeds from long-term debt	117.5	-
Reduction of long-term debt	(4.5)	(.3)
Common stock transactions:		
Stock plans	.9	.9
Conversion of debentures	.1	-
Treasury stock acquired	(99.8)	(2.1)
Total financing	94.3	6.2
Increase/(decrease) in cash and short-term investments	$ 6.5	(3.9)
Funds provided by (used for) operational changes in working capital:		
Receivables and costs and estimated earnings on long-term contracts	$ 30.3	30.4
Inventories	(17.1)	(45.1)
Accounts payable and advance payments on long-term contracts	(32.8)	(35.1)
Accrued expenses	(31.8)	(19.2)
Effect of foreign currency translation on working capital	5.7	(4.4)
Other	(34.5)	17.8
	$(80.2)	(55.6)

MANAGEMENT'S DISCUSSION AND ANALYSIS OF RESULTS OF OPERATIONS AND FINANCIAL CONDITION

Results of Operations

Net sales for the quarter ended December 31, 1985 were a first quarter record of $1,154.7 million, an increase of 2.7 per cent over net sales of $1,124.4 million for the three months ended December 31, 1984. The Company's balanced diversification contributed to the sales gain despite softness in many segments of the economy. The consumer and government and defense segments showed moderate sales gains in the first quarter while commercial and industrial sales were up slightly.

Cost of sales for the current quarter was $736.5 million or 63.8 per cent of sales compared to $714.0 million or 63.5 per cent of sales for the first quarter of fiscal 1985. Selling, general and administrative expenses for the three months ended December 31, 1985 were $239.5 million or 20.7 per cent of sales compared to $232.8 million or 20.7 per cent for the same period a year ago. Profit margins remained high despite the sluggish economy and extremely competitive environment in most markets. The Company's cost reduction and productivity improvement programs had favorable impacts on these margins.

Net earnings for the first quarter of $99.4 million and earnings per share of $1.36 were the highest for any first quarter in the Company's history.

Financial Condition

A comparison of key elements of the Company's financial condition at the end of the current quarter as compared to the end of the prior fiscal year is as follows:

	December 31, 1985	September 30, 1985
Working capital (millions of dollars)	$1,320.9	$1,307.6
Current ratio	2.7 to 1	2.7 to 1
Long-term debt to long-term capital	9.5%	4.9%
Total debt to total capital	17.6%	10.9%

The level of cash and short-term investments increased by $6.5 million during the three months ended December 31, 1985. The primary sources of funds were cash flow from net earnings, depreciation and amortization totalling $139.8 million, proceeds from a $100 million Eurobond offering and an $80.1 million increase in short-term borrowings. The primary uses of funds were the acquisition of treasury stock for $99.8 million, $80.2 million for operational working capital requirements and cash dividends of $50.0 million.

PART II. OTHER INFORMATION

Item 6. Exhibits and Reports on Form 8-K

(a) Exhibits.

1. Restated Articles of Incorporation of the Company dated February 4, 1986. See page 7 of sequentially numbered copy.

2. Bylaws of the Company, as amended February 4, 1986. See page 29 of sequentially numbered copy.

3. 1986 Stock Option Plan, incorporated by reference to the Company's 1986 Proxy Statement dated December 19, 1985, Exhibit A.

(b) Reports on Form 8-K. Registrant did not file any reports on Form 8-K during the quarter ended December 31, 1985.

SIGNATURE

Pursuant to the requirements of the Securities Exchange Act of 1934, the registrant has duly caused this report to be signed on its behalf by the undersigned thereunto duly authorized.

EMERSON ELECTRIC CO.

By John C. Wilson
John C. Wilson
Vice President of Finance
and Controller
(on behalf of the registrant
and as Chief Accounting Officer)

Dated: February 7, 1986

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SECURITIES AND EXCHANGE COMMISSION
WASHINGTON, D.C. 20549

FORM 10-Q

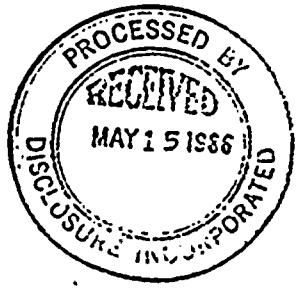
QUARTERLY REPORT UNDER SECTION 13 OR 15 (d) OF THE SECURITIES EXCHANGE ACT OF 1934

For Quarter Ended March 31, 1986

Commission file number 1-278

EMERSON ELECTRIC CO.

(Exact name of registrant as specified in its charter)



Missouri	43—0259330
(State or other jurisdiction of incorporation or organization)	(I.R.S. Employer Identification No.)
8000 W. Florissant Ave., St. Louis, Missouri	63136
(Address of principal executive offices)	(Zip Code)

Registrant's telephone number, including area code (314) 553-2000

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 and (2) has been subject to such filing requirements for the past 90 days. Yes ✓ No ____

Common stock outstanding at March 31, 1986: 72,681,276 shares

PART I. FINANCIAL INFORMATION

The following unaudited consolidated financial statements, in the opinion of management, include all adjustments, consisting only of normal recurring accruals, necessary for a fair presentation of the results for the interim periods presented. The consolidated financial statements are presented in accordance with the requirements of Form 10-Q and consequently do not include all the disclosures required by generally accepted accounting principles. For further information refer to the consolidated financial statements and notes thereto included in the Company's Annual Report on Form 10-K for the year ended September 30, 1985.

EMERSON ELECTRIC CO. AND SUBSIDIARIES
CONSOLIDATED STATEMENTS OF EARNINGS
THREE MONTHS AND SIX MONTHS ENDED MARCH 31, 1986 AND 1985
(Dollars In Millions Except Per Share Data)

	Three Months		Six Months	
	1986	1985	1986	1985
Net sales	$1,260.2	1,168.6	2,414.9	2,293.0
Costs and expenses:				
Cost of sales	816.5	744.0	1,553.0	1,458.0
Selling, general and administrative	251.1	234.6	490.6	467.4
Interest expense	14.1	9.9	23.2	19.0
Other (income) deductions, net	(2.1)	3.0	(3.9)	3.1
Total costs and expenses	1,079.6	991.5	2,062.9	1,947.5
Earnings before income taxes	180.6	177.1	352.0	345.5
Income taxes	76.8	75.0	148.8	145.0
Net earnings	$ 103.8	102.1	203.2	200.5
Number of shares used in computing earnings per common share (in thousands)	72,676	73,898	72,927	73,895
Per common share:				
Earnings	$1.43	1.38	2.79	2.71
Cash dividends	.69	.65	1.38	1.30

EMERSON ELECTRIC CO. AND SUBSIDIARIES
CONSOLIDATED BALANCE SHEETS

	Millions of Dollars	
	March 31, 1986	September 30, 1985
ASSETS		
CURRENT ASSETS:		
Cash	$ 5.8	9.1
Short-term investments, at cost which approximates market	124.4	79.4
Receivables, less allowances of $17.4 million and $13.7 million	793.6	723.2
Costs and estimated earnings on long-term contracts, less progress billings of $128.1 million and $123.6 million	61.9	30.8
Inventories:		
Finished products	418.3	410.6
Raw materials and work in process	788.9	745.1
Total inventories	1,207.2	1,155.7
Other current assets	122.3	87.2
TOTAL CURRENT ASSETS	2,315.2	2,085.4
PROPERTY, PLANT AND EQUIPMENT:		
Property, plant and equipment, at cost	1,691.2	1,573.2
Less accumulated depreciation	801.3	729.6
NET PROPERTY, PLANT AND EQUIPMENT	889.9	843.6
OTHER ASSETS:		
Excess of cost over net assets of purchased businesses	197.0	156.8
Other	245.5	171.0
TOTAL OTHER ASSETS	442.5	327.8
	$3,647.6	3,256.8
LIABILITIES AND STOCKHOLDERS' EQUITY		
CURRENT LIABILITIES:		
Short-term borrowings and current maturities of long-term debt	$ 345.3	156.0
Accounts payable	222.3	229.7
Advance payments on long-term contracts, less costs incurred of $11.1 million and $16.1 million	34.0	48.6
Accrued expenses	283.4	301.2
Income taxes	84.8	42.3
TOTAL CURRENT LIABILITIES	969.8	777.8
OTHER LIABILITIES	181.5	142.2
LONG-TERM DEBT, LESS CURRENT MATURITIES	227.8	114.6
STOCKHOLDERS' EQUITY:		
Preferred stock of $2.50 par value per share. Authorized 5,400,000 shares; issued - none	-	-
Common stock of $1 par value per share. Authorized 250,000,000 shares; issued 74,489,388 shares and 74,483,359 shares	74.5	74.5
Additional paid-in capital	101.3	100.4
Retained earnings	2,257.4	2,154.3
Cumulative translation adjustments	(41.6)	(73.0)
	2,391.6	2,256.2
Less common stock in treasury, 1,808,112 shares and 599,533 shares	123.1	34.0
TOTAL STOCKHOLDERS' EQUITY	2,268.5	2,222.2
	$3,647.6	3,256.8

EMERSON ELECTRIC CO. AND SUBSIDIARIES
CONSOLIDATED STATEMENTS OF CHANGES IN FINANCIAL POSITION
SIX MONTHS ENDED MARCH 31, 1986 AND 1985

	Millions of Dollars	
	1986	1985
Funds provided (used):		
Operations:		
Net earnings	$ 203.2	200.5
Depreciation and amortization	82.4	74.8
Changes in working capital	(167.9)	(175.0)
Other	(7.6)	(5.3)
Total from operations	110.1	95.0
Investments:		
Capital expenditures	(73.3)	(95.0)
Realization of benefits from tax leases including amounts repayable in future years	6.6	9.8
Purchase of businesses, less cash and short-term investments acquired:		
Property, plant & equipment & other assets	(85.9)	(.4)
Net working capital	(.2)	(2.6)
Other liabilities	.8	1.5
Other	(23.7)	-
Total investments	(175.7)	(86.7)
Dividends paid	(100.1)	(93.7)
Financing:		
Short-term borrowings and current maturities of long-term debt, net	188.5	63.5
Proceeds from long-term debt	117.5	.6
Reduction of long-term debt	(10.5)	(7.8)
Common stock transactions:		
Stock plans	13.3	2.2
Conversion of debentures	.3	.1
Treasury stock acquired	(101.7)	(2.5)
Total financing	207.4	56.1
Increase/(decrease) in cash and short-term investments	$ 41.7	(29.3)
Funds provided by (used for) operational changes in working capital:		
Receivables and costs and estimated earnings on long-term contracts	$ (95.5)	(40.9)
Inventories	(31.6)	(54.5)
Accounts payable and advance payments on long-term contracts	(30.7)	(37.7)
Accrued expenses	(28.0)	3.3
Effect of foreign currency translation on working capital	16.6	(14.7)
Other	1.3	(30.5)
	$(167.9)	(175.0)

MANAGEMENT'S DISCUSSION AND ANALYSIS OF RESULTS OF OPERATIONS AND FINANCIAL CONDITION

Results of Operations

Net sales for the quarter ended March 31, 1986 were $1,260.2 million, an increase of 7.8 per cent over net sales of $1,168.6 million for the second quarter of fiscal 1985. For the six months ended March 31, 1986, net sales were $2,414.9 million compared to $2,293.0 million for the same period a year ago, reflecting a 5.3 per cent increase. The Company registered sales gains in the second quarter in all segments despite the mixed domestic economic environment. The consumer segment showed solid increases in the second quarter, while commercial and industrial sales were up moderately. Sales comparisons in these segments were further enhanced by the results of purchase acquisitions. Government and defense sales were above the prior year's level, but comparisons are difficult due to an exceptionally strong quarter last year.

The current quarter's cost of sales was $816.5 million or 64.8 per cent of sales compared to $744.0 million or 63.7 per cent of sales in the second quarter of fiscal 1985. Cost of sales for the first six months of fiscal 1986 was $1,553.0 million or 64.3 per cent of sales compared to $1,458.0 million or 63.6 per cent for the first half of fiscal 1985. Selling, general and administrative expenses in the most recent quarter were $251.1 million or 19.9 per cent of sales compared to $234.6 million or 20.1 per cent of sales for the same quarter a year ago. For the first six months of fiscal 1986, selling, general and administrative expenses were $490.6 million or 20.3 per cent of sales compared to $467.4 million or 20.4 per cent of sales for the first half of fiscal 1985. Sales have grown faster than profits due to near-term price/cost pressures in a challenging price environment.

Net earnings and earnings per share for the second quarter were $103.8 million and $1.43, respectively. For the first six months of fiscal 1986 net earnings were $203.2 million or $2.79 per share. Net earnings and earnings per share for the second quarter and first six months of fiscal 1986 were the highest for any quarter and first six-month period in the Company's history.

Financial Condition

A comparison of key elements of the Company's financial condition at the end of the current quarter as compared to the end of the prior fiscal year is as follows:

	March 31, 1986	September 30, 1985
Working capital (millions of dollars)	$1,345.4	$1,307.6
Current ratio	2.4 to 1	2.7 to 1
Long-term debt to long-term capital	9.1%	4.9%
Total debt to total capital	20.2%	10.9%

The level of cash and short-term investments increased by $41.7 million during the six months ended March 31, 1986. The primary sources of funds were cash flow from net earnings, depreciation and amortization totalling $285.6 million, a $188.5 million increase in short-term borrowings and proceeds from a $100 million Eurobond offering. The primary uses of funds were $167.9 million for operational working capital requirements, the acquisition of treasury stock for $101.7 million and cash dividends of $100.1 million.

PART II. OTHER INFORMATION

Item 4. Submission of Matters to a Vote of Security Holders

At the Annual Meeting of Stockholders on February 4, 1986, four proposals described in the notice of such meeting were voted upon. The "Proposal to Approve the 1986 Stock Option Plan" was approved by a vote of 56,382,832 in favor to 1,1[illegible],284 against, with 513,131 abstaining. The "Proposal to Amend Article 4 of the Restated Articles to Increase the Authorized Common Stock" was approved by a vote of 52,412,098 in favor to 5,273,214 against, with 373,935 abstaining. The "Proposal to Amend the Restated Articles to Add Article 9, a 'Fair Price Amendment' Concerning Certain Business Combinations" was approved by a vote of 39,639,092 in favor to 14,869,991 against, with 3,550,164 abstaining. The "Proposal to Amend Article 5 of the Restated Articles Concerning Classification of the Board and Certain Other Matters" was approved by a vote of 40,160,305 in favor to 14,386,984 against, with 3,511,958 abstaining.

Item 6. Exhibits and Reports on Form 8-K

(a) Exhibits. None

(b) Reports on Form 8-K. Registrant did not file any reports on Form 8-K during the quarter ended March 31, 1986.

SIGNATURE

Pursuant to the requirements of the Securities and Exchange Act of 1934, the registrant has duly caused this report to be signed on its behalf by the undersigned thereunto duly authorized.

EMERSON ELECTRIC CO.

By _____
John C. Wilson
Vice President of Finance
and Controller
(on behalf of the registrant
and as Chief Accounting Officer)

Dated: May 12, 1986

END

M.395250 87499

SECURITIES AND EXCHANGE COMMISSION
Washington, D.C. 20549

FORM 10-K
ANNUAL REPORT PURSUANT TO SECTION 13 OR 15(d) OF
THE SECURITIES EXCHANGE ACT OF 1934

For the fiscal year ended
December 31, 1985

0-6772
Commission File No.

165
36

MELLON BANK CORPORATION
(Exact name of registrant as specified in its charter)

Pennsylvania	25-1233834
(State or other jurisdiction of incorporation or organization)	(I.R.S. Employer Identification No.)

One Mellon Bank Center
Pittsburgh, Pennsylvania 15258
(Address of principal executive offices)(Zip Code)

Registrant's telephone number, including area code -- (412) 787-5534

PROCESSED BY
DISCLOSURE INCORPORATED
MAR 3 1986

Securities registered pursuant to Section 12(b) of the Act:

Title of Each Class	Name of Each Exchange on Which Registered
Common Stock $0.50 Par Value	New York Stock Exchange
Series A Preferred Stock $1.00 Par Value	New York Stock Exchange
Floating Rate Notes Due 1989	New York Stock Exchange
Convertible Floating Rate Notes Due 1989	New York Stock Exchange

Securities registered pursuant to Section 12(g) of the Act:

5-3/8% Convertible Capital Notes Due 1993
(Title of class)

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 the filing requirements for the past 90 days.

Yes ✓ No ___

As of March 3, 1986, there were 27,132,700 shares of the Registrant's outstanding voting common stock having a market value of $1,651,703,113 held by nonaffiliates.

DOCUMENTS INCORPORATED BY REFERENCE

Portions of the following documents are incorporated by reference in the following parts of this Annual Report.

Mellon Bank Corporation 1986 Proxy Statement -- Part III
Mellon Bank Corporation 1985 Annual Report to Shareholders -- Parts I, II, and IV

The Form 10-K filed with the Securities and Exchange Commission contains the Exhibits listed on the Index to Exhibits beginning on page 33 including the Registrant's 1985 Annual Report to Shareholders. Copies of the Registrant's 1985 Annual Report to Shareholders and the Proxy Statement for its 1986 Annual Meeting may be obtained free of charge by writing to:

Mellon Bank Corporation
Corporate Secretary
3045 One Mellon Bank Center
Pittsburgh, Pennsylvania 15258

MELLON BANK CORPORATION
Form 10-K Index

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PART I

ITEM 1. BUSINESS

Description of Business

Mellon Bank Corporation (the "Corporation") is a multi-bank holding company which was incorporated under the laws of Pennsylvania in August 1971. At December 31, 1985, it was the eleventh largest bank holding company in the United States in terms of assets and common shareholders' equity and the thirteenth largest in terms of deposits. Its principal wholly-owned subsidiaries are Mellon Bank N.A., Mellon Bank (East) National Association, Mellon Bank (DE) National Association, Mellon Bank (Central) National Association, Mellon Bank (North) National Association and the companies known as Mellon Financial Services Corporation. The Corporation's banking subsidiaries provide domestic retail banking, worldwide commercial banking, and trust banking and investment management services. The Corporation's subsidiaries known as Mellon Financial Services Corporation provide commercial and consumer financial services, engage in leasing and residential real estate financing, originate commercial and consumer real estate loans and provide real estate and equity investment management services at 147 branch offices in 19 states.

Mellon Bank, N.A. ("Mellon Bank"), with its executive office in Pittsburgh, Pennsylvania, became a subsidiary of the Corporation in November 1972. With its predecessors, Mellon Bank has been in business since 1869. At December 31, 1985, it was the eleventh largest U.S. commercial bank in terms of total assets and the sixteenth largest in terms of total deposits. Mellon Bank has 124 domestic banking offices; 13 domestic representative offices; international branches in Grand Cayman, Hong Kong, London and Tokyo; 12 international representative offices in 11 countries; and a banking subsidiary, Mellon Bank Canada, in Toronto. Mellon Bank's Edge Act subsidiary, Mellon Bank International, is headquartered in New York.

Mellon Bank (East) National Association ("Mellon Bank (East)") and Mellon Bank (DE) National Association ("Mellon Bank (DE)") became subsidiaries of the Corporation in April 1983 upon the merger of The Girard Company ("Girard") into the Corporation. Mellon Bank (East) (formerly Girard Bank), which has its executive office in Philadelphia, Pennsylvania, was granted a national bank charter in 1984, having previously been chartered as a Pennsylvania bank and a member of the Federal Reserve System. Together with its predecessors, Mellon Bank (East) has been in business since 1836. Mellon Bank (DE) (originally Farmers Bank of the State of Delaware), a national banking association which has its executive office in Wilmington, Delaware, was established by an act of the Delaware legislature and originally was owned in part by that state. It has been in business since 1807.

Mellon Bank (Central) National Association ("Mellon Bank (Central)") became a subsidiary of the Corporation in September 1983 upon the merger of CCB Bancorp, Inc., the holding company for Central Counties Bank, into the Corporation. Mellon Bank (Central), which has its executive office in State College, Pennsylvania, was granted a national bank charter in 1984. The predecessor of Mellon Bank (Central), Central Counties Bank, was chartered as a Pennsylvania bank and was the result of a 1971 merger of the First National Bank of State College with Lock Haven Trust Company. In November 1985, The

Description of Business (continued)

First National Bank of Mapleton, Mapleton Depot, Pennsylvania merged with Mellon Bank (Central), adding six offices to the Corporation's community banking network, and the registered head office of Mellon Bank (Central) was moved to Mapleton Depot, Pennsylvania.

Mellon Bank (North) National Association ("Mellon Bank (North)") became a subsidiary of the Corporation in April 1984 upon the merger of Northwest Pennsylvania Corp., the holding company for Northwest Bank (the predecessor of Mellon Bank (North)), into the Corporation. Mellon Bank (North), which has its executive office in Oil City, Pennsylvania, was granted a national bank charter in 1984. Northwest Bank was chartered as a Pennsylvania bank and was the result of a 1984 merger of Northwest Bank and Union Bank & Trust Co., Erie. Together with its predecessors, Mellon Bank (North) has been in business since 1900.

The deposits of Mellon Bank, Mellon Bank (East), Mellon Bank (DE), Mellon Bank (Central) and Mellon Bank (North) (the "Banking Subisidiaries") are insured by the Federal Deposit Insurance Corporation to the extent provided by law.

The Corporation provides community financial services through the Community Banking Departments of the Banking Subsidiaries and the Commerical and Consumer Finance and Mortgage Banking Groups of the companies known as Mellon Financial Services Corporation.

The Community Banking Departments of the Banking Subsidiaries provide a broad range of financial services to individuals, small and middle market businesses, communities and institutions. These services are delivered through 316 community banking offices located in 24 counties in Pennsylvania and throughout Delaware, as well as through automated teller machines in branch locations and off-premise sites. The Banking Subsidiaries' automated teller machines are affiliated with the CashStream and CIRRUS networks. The Banking Subsidiaries' credit card programs are affiliated with both the Mastercard and Visa card systems. In March 1985, Mellon Bank (DE) acquired substantially all of the credit card loan portfolio of Mellon Bank and currently operates the credit card business previously operated by Mellon Bank and Mellon Bank (East).

The Commercial and Consumer Finance Group of Mellon Financial Services Corporation, headquartered in Oak Brook, Illinois, specializes in commercial and industrial loans to small businesses and resort time-sharing developers. Through 121 offices in 17 states, this group also provides direct loans to individuals and purchases dealer sales finance contracts. In January 1986, Mellon Financial Services Corporation purchased from AVCO Financial Services, Inc. the assets of its Diversified Sales Division, which provides financing of various residential housing units, primarily in the southern United States. Through Mellon Life Insurance Company, it engages in the underwriting, as reinsurer, of credit life and credit accident and health insurance directly related to extensions of credit by the Corporation's Commerical and Consumer Finance Group and its Banking Subsidiaries. Three wholly-owned industrial banks located in Colorado make consumer and

Description of Business (continued)

commercial loans and accept savings and time deposits; however, they cannot accept those deposit accounts which the Federal Reserve Board considers to be transaction accounts.

The Mortgage Banking Group of Mellon Financial Services Corporation originates and services residential and commercial mortgages for institutional investors and makes residential land acquisition, development and construction loans. Active subsidiaries of Mellon Financial Services Corporation, operated by the Mortgage Banking Group, are headquartered in New Orleans, Louisiana; Cleveland, Ohio; Denver, Colorado; and Houston, Texas.

Institutional financial services are provided by the Banking Subsidiaries through the Corporate Banking, Technology Products, Financial Institutions, International Banking and Real Estate Finance Departments, international branches and representative offices of Mellon Bank and Mellon Bank (East), as well as Edge Act and other banking subsidiaries of Mellon Bank and the Corporation's leasing subsidiaries.

The Corporate Banking Department services large domestic commercial and industrial customers. The Financial Institutions Department services domestic financial institutions, including domestic banks, major thrift institutions, broker/dealers and insurance companies, finance companies and equity syndicators. The Technology Products Department provides money management services to commercial customers and data processing services to financial institutions. Mellon Financial Services Corporation operates representative offices on behalf of the Banking Subsidiaries. These offices are located in Atlanta, Georgia; Chicago, Illinois; Dallas and Houston, Texas; Denver, Colorado; New York, New York; Boston, Massachusetts; and Los Angeles and San Francisco, California.

The International Banking Department provides financial and trade services to corporations, financial institutions and governments worldwide through offices and subsidiaries in the U.S. and abroad. The offices in Pittsburgh, Philadelphia, New York and Toronto and the other international branches are active in commercial and interbank lending and deposit and loan operations. The Corporation's Edge Act subsidiary, Mellon Bank International, provides correspondent banking services to foreign banks and international trade financing and holds foreign investments. Mellon Bank Canada provides full service commercial banking in Canada. A discussion of the Corporation's international operations is presented on pages 37 through 39 of the Corporation's 1985 Annual Report to Shareholders (the "1985 Annual Report"). Selected financial data for international operations are presented in Note 18 in the Notes to Financial Statements on pages 61 through 63 of the 1985 Annual Report. These sections of the 1985 Annual Report are incorporated herein by reference.

The Real Estate Finance Department originates and obtains financing for commercial, multi-family and other income-producing real estate projects.

Description of Business (continued)

The Leasing Group of the Corporation provides worldwide equipment leasing and financing specifically designed to coincide with a company's financial needs. Allomon Corporation, a wholly-owned subsidiary of Mellon Financial Services Corporation #1, makes loans and investments for its own account.

The Trust and Investment Departments of the Banking Subsidiaries as well as Mellon Real Estate Investment Management Corporation, Mellon Bank (FL) National Association, Franklin Portfolio Associates, Mellon Financial Services Corporation #6, Mellon-Pictet International Management ("Mellon-Pictet"), Mellon Securities Trust Company and the Capital Markets Department provide a wide variety of trust, investment, portfolio and funds management services.

The Trust and Investment Departments of the Banking Subsidiaries provide fiduciary services, investment management services, custody services and other financial services to individuals, corporations, institutions and governments throughout the world. Such services include corporate trust, master trust, personal trust and account management, management of employee benefit funds and international investment management. Mellon Real Estate Investment Management Corporation provides real estate investment advisory services to employee benefit funds, institutions and individuals from its offices in New York City and Detroit, Michigan and also acts as a sponsor of and investment advisor to Mellon Participating Real Estate Investment Trust, a closed-end investment company registered under the Investment Company Act of 1940. Mellon Bank (FL) National Association, a wholly-owned subsidiary of the Corporation located in Boca Raton, Florida, is a bank that offers trust services to Florida residents, and the Corporation has obtained preliminary regulatory approval to establish another trust bank in Sarasota, Florida. Franklin Portfolio Associates, Inc., a wholly-owned subsidiary of Mellon Financial Services Corporation #1, provides equity portfolio management services to institutional customers from its Boston, Massachusetts office. Mellon Financial Services Corporation #6, also a wholly-owned subsidiary of Mellon Financial Services Corporation #1, provides passive equity management services from its office in San Francisco, California. Mellon-Pictet, a joint venture between the Corporation and Pictet & Cie, a private Swiss bank, is engaged in international investment management services for pension funds and other organizations. Mellon Securities Trust Company provides custody and processing capabilities for certain specialized securities transactions related to master trust business from its New York City site.

The Capital Markets Department is responsible for funding assets and maintaining liquidity to meet financing requirements. This Department manages the investment securities portfolios of the Banking Subsidiaries, consisting primarily of bonds and notes issued by the United States Treasury, state and political subdivisions and other governmental agencies. The Department also engages in money market, foreign exchange and bank eligible securities transactions on behalf of bank customers and for the Bank's own trading account. Options and financial futures are also traded and used for hedging purposes.

Description of Business (continued)

Other subsidiaries of the Corporation and of Mellon Bank and Mellon Bank (East) are engaged in the issuance of commercial paper and long-term debt, data processing and trust operations services and the operation of bank premises.

The Corporation and Commonwealth National Financial Corporaton of Harrisburg, Pennsylvania ("Commonwealth") entered into a Plan of Merger dated as of October 8, 1985 pursuant to which Commonwealth will be merged with the Corporation. On December 30, 1985, Commonwealth's shareholders approved the merger, which has also been approved by the Pennsylvania Department of Banking and the Federal Reserve Board. Two shareholders of Commonwealth have brought an action in the U.S. Federal District Court for the Middle District of Pennsylvania seeking to enjoin the merger and claiming damages in an unspecified amount. Subject to this litigation, the merger is presently scheduled to be consummated on April 2, 1986. Upon consummation of the merger, the Corporation will expand its community banking network by becoming the sole shareholder of Commonwealth National Bank, which has 43 offices throughout Cumberland, Dauphin, Lancaster and York counties in Pennsylvania.

In February 1986 the Corporation purchased Carleton Financial Computations, Inc. of South Bend, Indiana. With its subsidiaries, Data-Link Systems, Inc. and M-Data, Inc., Carleton provides various data-processing and data transmission services to financial institutions in the United States and Canada.

Agreements in principle were reached in late 1985 and in January 1986 to acquire the stock or certain assets and liabilities of five subsidiaries of Pidata Corporation of New York, New York. One of these subsidiaries, Pidata Services Incorporated of Pittsburgh, Pennsylvania, was acquired by the Corporation in December 1985 and provides trust, cash management, retail marketing and other accounting services to more than 115 financial institutions throughout the United States. The four Pidata subsidiaries to be acquired in 1986 provide transfer agency services to securities issuers and recordkeeping and shareholder services to mutual funds.

On March 24, 1986, the Corporation entered into an agreement for the purchase of certain assets and the assumption of certain deposit liabilities of Community Savings & Loan, Inc. of Bethesda, Maryland ("Community"). As of December 31, 1985, Community had deposits of approximately $332 million and operated eight branches in the three-county area north of Washington, D.C.

The Corporation and the Banking Subsidiaries will continue to evaluate potential business acquisitions afforded by liberalization of the laws restricting bank and bank holding company acquisitions and expansions that, under evolving legal standards, may be in the best interests of the Corporation.

Supervision and Regulation

The Corporation, as a bank holding company, is regulated under the Bank Holding Company Act of 1956, as amended (the "Act"), and, with its subsidiaries, is subject to the supervision of the Board of Governors of the Federal Reserve System (the "Federal Reserve Board"). Generally, the Act limits the business of bank holding companies to banking or managing or controlling banks, performing certain servicing activities for subsidiaries and engaging in such other activities as the Federal Reserve Board may determine to be so closely related to banking or managing or controlling banks as to be a proper incident thereto. The Act requires the approval of the Federal Reserve Board for the acquisition, directly or indirectly, by a bank holding company of another bank and prohibits the Corporation from acquiring a commercial bank outside Pennsylvania except in those states which by statute specifically authorize such an acquisition and except in certain situations involving financially distressed banks or bank holding companies. The Act also prohibits a bank holding company from acquiring ownership or control of more than 5 percent of any class of voting shares of a company which is not a bank or engaged in permissible activities under the Act.

The Corporation is among the U.S. bank holding companies that received preliminary approval in 1985 from the Office of the Comptroller of the Currency and final approval from the Federal Reserve Board to open consumer banks. The Comptroller of the Currency's approval was for 16 consumer banks, and the Federal Reserve Board approved four. Before any consumer banks were opened, the United States District Court for the Southern District of Florida issued a stay prohibiting the Comptroller of the Currency from issuing final charters while the permissibility of operating consumer banks was under judicial review. The United States Supreme Court recently handed down a decision supporting the interpretation of the law which formed the basis of the regulatory approvals. However, it is unlikely that this decision will have an immediate effect upon the Corporation's ability to open consumer banks.

The Banking Subsidiaries and Mellon Bank (FL) National Association, as national banking associations, are subject to supervision, regulation and examination by the office of the Comptroller of the Currency as well as the Federal Reserve Board and the Federal Deposit Insurance Corporation. These agencies and federal laws extensively regulate various aspects of the banking business, including permissible types and amounts of loans, investments and other activities, interest rates on deposits and loans, branching and reserve requirements. In addition, Mellon Bank, Mellon Bank (East), Mellon Bank (Central) and Mellon Bank (North) are subject to Pennsylvania laws and Mellon Bank (DE) is subject to Delaware laws, which, among other things, limit interest rates on loans. These regulations and laws are intended primarily for the protection of the banks' depositors and customers rather than holders of the Corporation's securities.

Franklin Portfolio Associates, Inc., Mellon Real Estate Investment Management Corporation, Mellon Financial Services Corporation #6 and Mellon-Pictet are registered investment advisors under the Investment Advisors Act of 1940 and, as such, are supervised by the Securities and Exchange Commission (the "SEC") as well as banking regulators.

Supervision and Regulation (continued)

There are certain restrictions on the ability of the Corporation and certain of its nonbank affiliates to borrow from its Banking Subsidiaries and on the ability of such Banking Subsidiaries to pay dividends to the Corporation, as explained in Note 15 of the Notes to Financial Statements set forth on pages 60 and 61 of the 1985 Annual Report, which Note is incorporated herein by reference.

The Office of the Comptroller of the Currency has authority under the Financial Institutions Supervisory Act to prohibit national banks such as the Banking Subsidiaries from engaging in any activity which, in the Comptroller's opinion, constitutes an unsafe or unsound practice in conducting their businesses. The Federal Reserve Board has similar authority with respect to the Corporation and its non-banking subsidiaries.

Under new regulations promulgated by the Securities and Exchange Commission ("SEC") and effective January 1, 1986, various securities - related activities of banks are subject to regulation by the SEC. The Corporation received an extension until June 1, 1986 to bring its activities into full compliance with the new rule.

Under the terms of banking legislation enacted in Pennsylvania in 1982, the Corporation may acquire four additional banking subsidiaries in Pennsylvania between March 1986 and March 1990 and may own and operate an unlimited number of banking subsidiaries in Pennsylvania after March 1990. Such legislation does not prohibit the Corporation's Banking Subsidiaries or other bank subsidiaries of the Corporation which are headquartered in Pennsylvania from acquiring additional banks in Pennsylvania. The 1982 legislation, among other things, also permits Pennsylvania banks to establish branches in counties contiguous to those in which they were previously allowed to branch and in Allegheny, Philadelphia, Delaware and Montgomery Counties and will permit banks to establish branches anywhere in Pennsylvania after March 4, 1990. Prior to 1982, Pennsylvania law prohibited the Corporation from owning an interest of 25 percent or more in more than one bank located in Pennsylvania, and banks were limited to establishing and maintaining branches in the county of their principal office and in contiguous counties. The Corporation has taken advantage of the opportunities created by the 1982 legislation by merging with The Girard Company, CCB Bancorp, Inc. and Northwest Pennsylvania Corp., by the January 1985 merger of The Citizens National Bank of New Castle with Mellon Bank, by the November 1985 merger of the First National Bank of Mapleton, Mapleton Depot, with Mellon Bank (Central) and by the proposed merger of the Corporation with Commonwealth. The Corporation's Banking Subsidiaries currently maintain branches in 24 counties in Pennsylvania and throughout Delaware, and the Corporation and its Banking Subsidiaries continuously evaluate further opportunities resulting from the passage of the 1982 legislation and any future legislation which would permit further expansion.

Other subsidiaries of the Corporation are subject to the laws and regulations of the states in which they conduct their business, as well as the Federal law described below.

Supervision and Regulation (continued)

Federal legislation with respect to international lending by domestic banks, among other things, instructs the Federal bank regulatory agencies to require special reserves when, in the judgment of the agencies, the quality of a bank's assets has been impaired by a protracted inability of foreign public or private borrowers to make payment of external indebtedness or no definite prospects exist for the orderly restoration of debt service. At December 31, 1985, the Corporation had charged off loans to these borrowers in amounts at least equal to the prescribed amounts of the special reserves and, pursuant to these regulations, special reserves were not required.

Competition

The Corporation and its banking and nonbanking subsidiaries are subject to intense competition in all aspects and areas of their businesses from banks, other domestic and foreign financial institutions, including savings and loan associations, savings banks, finance companies, credit unions and other providers of financial services, such as money market funds, brokerage firms, investment companies, credit companies and insurance companies. The Corporation also competes with nonfinancial institutions including retail stores that maintain their own credit programs and governmental agencies that make available loans to certain borrowers.

Although Mellon Bank is the largest banking institution headquartered in the nineteen county area of Western Pennsylvania in which it is currently permitted to maintain branches, it competes with approximately 150 commercial banks, mutual savings banks and savings and loan associations and numerous credit unions and consumer finance institutions. Mellon Bank (East) is the fourth largest banking institution headquartered in the Philadelphia Metropolitan Statistical Area, the fourth largest metropolitan area in the United States, in which approximately 60 commercial banks and 100 thrifts with a total of over 1,300 offices are located. In most of the markets in which the Corporation's Banking Subsidiaries operate, they compete with large regional and other banking organizations in the making of commercial, industrial and consumer loans and in the provision of other products and services.

Competition has increased in recent years in many areas in which the Corporation and its subsidiaries operate, in substantial part because other types of financial institutions and other entities have begun to engage in activities traditionally engaged in by commercial banks. Commercial banks face significant competition (a) in acquiring assets due to such factors as the increase in commercial paper issued by industrial companies, increased activities by foreign banks and credit unions and the increased lending powers granted to and employed by many types of thrift institutions and credit unions and (b) in attracting deposits at reasonable prices due to the activities of money market funds, increased activities of nonbank deposit takers, including brokerage firms, alternatives presented by foreign banks and the increased availability of demand deposit-type accounts at thrift institutions and credit unions. Unlike the Corporation, many of these nonbank institutions are not subject to as extensive regulation as that described above under "Supervision and Regulation" and, thus, may have a competitive advantage over the Corporation in certain respects.

As a result of the enactment of the 1982 Pennsylvania banking legislation and in the event of additional legislation permitting further expansion described above under "Supervision and Regulation," the Corporation can be expected to face additional competition from (a) financial institutions located in areas in which the Corporation may seek to expand and (b) financial institutions expanding into those areas in which the Corporation maintains offices.

Employees

At December 31, 1985, the Corporation and its subsidiaries employed 15,188 people.

Statistical Disclosure for Bank Holding Companies

I. Distribution of Assets, Liabilities and Stockholders' Equity; Interest Rates and Interest Differential

Information required by this section of Securities Act Industry Guide 3 ("Guide 3") is presented in the Rate/Volume Variance Analyses on the following pages 14 through 16 and in Net Credit Revenue, International Operations and Average Balances and Interest Rates on pages 24, 61 through 63 and 66 through 69 of the 1985 Annual Report, which portions are incorporated herein by reference.

MELLON BANK CORPORATION

Rate/Volume Variance Analysis
Consolidated

(in millions)	Year ended December 31, 1984 over/(under) 1983 Due to change in Rate	Volume	Net change	1985 over/(under) 1984 Due to change in Rate	Volume	Net change
Increase/(decrease) in credit revenue from:						
Interest-earning assets:						
Money market investments:						
Interest-bearing deposits with banks	$ 15	$(80)	$ (65)	$ (25)	$ (27)	$ (52)
Federal funds sold and securities purchased under agreements to resell	11	12	23	(20)	(26)	(46)
Other	2	-	2	-	1	1
Trading account securities	6	2	8	(8)	(7)	(15)
Investment securities:						
U.S. Treasury and agency securities	(2)	(35)	(37)	(4)	72	68
Obligations of states and political subdivisions	1	-	1	5	5	10
Other	1	4	5	(1)	(2)	(3)
Loans (includes fees on loans)	113	436	549	(294)	329	35
Lease finance assets	2	6	8	(1)	6	5
Total	149	345	494	(348)	351	3
Increase/(decrease) in interest expense on:						
Interest-paying liabilities:						
Deposits in domestic offices:						
Demand	-	7	7	3	(4)	(1)
Savings accounts	2	4	6	-	(3)	(3)
Money market deposit accounts	(11)	59	80	(52)	72	20
Retail savings certificates	(1)	84	83	(35)	10	(25)
Negotiable certificates of deposit	36	4	40	(63)	22	(41)
Other time deposits	1	60	61	(7)	-	(7)
Deposits in foreign offices	20	(25)	(5)	(26)	(1)	(27)
Federal funds purchased and securities sold under agreements to repurchase	46	(27)	19	(107)	113	6
Commercial paper	18	25	43	(33)	(6)	(39)
Other funds borrowed	5	2	7	(18)	(18)	(26)
Notes and debentures (with original maturities over one year)	5	7	12	(10)	43	33
Total	143	210	353	(338)	228	(110)
Increase/(decrease) in net credit revenue	$ 6	$ 135	$ 141	$ (10)	$ 123	$ 113

Amounts are calculated on a fully taxable equivalent basis where applicable and are before reserve requirements; changes in credit revenue or interest expense not arising solely as a result of rate or volume variances are allocated proportionally to rate and volume based on their relative absolute magnitudes.

MELLON BANK CORPORATION

Rate/Volume Variance Analysis
Domestic Operations

(in millions)	Year ended December 31, 1984 over/(under) 1983 Due to change in Rate	Volume	Net change	1985 over/(under) 1984 Due to change in Rate	Volume	Net change
Increase/(decrease) in credit revenue from:						
Interest-earning assets:						
Money market investments:						
Interest-bearing deposits with banks	$ -	$ -	$ -	$ -	$ (1)	$ (1)
Federal funds sold and securities purchased under agreements to resell	11	12	23	(20)	(26)	(46)
Other	-	3	3	(1)	(2)	(3)
Trading account securities	6	3	9	(8)	(7)	(15)
Investment securities:						
U.S. Treasury and agency securities	(2)	(35)	(37)	(4)	72	68
Obligations of states and political subdivisions	1	-	1	5	5	10
Other	-	1	1	-	-	-
Loans and lease finance assets (includes fees on loans)	98	386	484	(256)	330	74
Total	114	370	484	(284)	371	87
Increase/(decrease) in interest expense on:						
Interest-paying liabilities:						
Deposits in domestic offices:						
Demand deposits	-	7	7	3	(4)	(1)
Savings accounts	2	4	6	-	(3)	(3)
Money market deposit accounts	11	69	80	(52)	72	20
Retail savings certificates	(1)	84	83	(35)	10	(25)
Negotiable certificates of deposit	36	8	44	(62)	25	(37)
Other time deposits	(1)	47	46	(19)	(2)	(21)
Federal funds purchased and securities sold under agreements to repurchase	46	(27)	19	(107)	113	6
Other funds borrowed	22	19	41	(39)	(23)	(62)
Funds provided to international operations	(18)	12	(6)	54	43	97
Notes and debentures (with original maturities over one year)	5	7	12	(10)	43	33
Total	102	230	332	(267)	274	7
Increase/(decrease) in net credit revenue	$ 12	$ 140	$ 152	$ (17)	$ 97	$ 80

Amounts are calculated on a fully taxable equivalent basis where applicable and are before reserve requirements; changes in credit revenue or interest expense not arising solely as a result of rate or volume variances are allocated proportionally to rate and volume based on their relative absolute magnitudes.

MELLON BANK CORPORATION

Rate/Volume Variance Analysis
International Operations

(in millions)	Year ended December 31, 1984 over/(under) 1983 Due to change in Rate	Volume	Net change	1985 over/(under) 1984 Due to change in Rate	Volume	Net change
Increase/(decrease) in credit revenue from:						
Interest-earning assets:						
Money market investments:						
Interest-bearing deposits with banks	$ 15	$ (80)	$ (65)	$ (25)	$ (26)	$(51)
Other	2	(3)	(1)	1	3	4
Trading account securities	-	(1)	(1)	-	-	-
Investment securities	1	3	4	(1)	(2)	(3)
Loans (includes fees on loans)	17	56	73	(39)	5	(34)
Total	35	(25)	10	(64)	(20)	(84)
Increase/(decrease) in interest expense on:						
Interest-paying liabilities:						
Deposits	22	(16)	6	(15)	(2)	(17)
Other funds borrowed	1	8	9	(2)	(1)	(3)
Funds provided by domestic operations	18	(12)	6	(54)	(43)	(97)
Total	41	(20)	21	(71)	(46)	(117)
Increase/(decrease) in net credit revenue	$ (6)	$ (5)	$ (11)	$ 7	$ 26	$ 33

Amounts are calculated on a fully taxable equivalent basis where applicable and are before reserve requirements; changes in credit revenue or interest expense not arising solely as a result of rate or volume variances are allocated proportionally to rate and volume based on their relative absolute magnitudes.

Statistical Disclosure for Bank Holding Companies (continued)

II. Investment Portfolio

A. Investment securities year-end book values:

(in millions)	December 31, 1983	1984	1985
U.S. Treasury and agency securities	$ 1,307	$ 1,255	$ 1,849
Obligations of states and political subdivisions	300	296	1,119
Other securities:			
Bonds, notes and debentures	115	128	67
Stock of Federal Reserve Bank	17	20	20
Other	3	7	5
Total Other	135	155	92
Total Investment Securities	$ 1,742	$ 1,706	$ 3,060

B. Maturity Distribution of Investment Securities

Information required by this section of Guide 3 is presented in Balance Sheet Review on page 29 of the 1985 Annual Report and is incorporated herein by reference.

Statistical Disclosure for Bank Holding Companies (continued)

III. Loan Portfolio

A. Types of Loans

Information required by this section of Guide 3 is presented in Credit Risk and Asset Quality on page 32 of the 1985 Annual Report and is incorporated herein by reference.

B. Maturities and Sensitivities of Loans to Changes in Interest Rates

Information on loan maturities required by this section of Guide 3 is set forth in Balance Sheet Review on page 29 of the 1985 Annual Report and is incorporated herein by reference.

Sensitivity to changes in interest rates of loans at December 31, 1985 (excluding consumer credit and consumer mortgages):

(In millions)	Domestic operations	International operations	Total
Loans due in one year or less*	$ 8,843	$2,149	$10,992
Loans due after one year:			
Variable rates	2,630	1,250	3,880
Fixed rates	3,045	410	3,455
Total loans	$14,518	$3,809	$18,327

*Includes demand loans and loans with no stated maturity.

C. Risk Elements

Information required by this section of Guide 3 is set forth in Credit Risk and Asset Quality and International Operations on pages 32 through 39 of the 1985 Annual Report and is incorporated herein by reference.

Statistical Disclosure for Bank Holding Companies (continued)

IV. Summary of Loan Loss Experience

Reserve for Possible Credit Losses

A reserve is maintained for each operating subsidiary which has loans or leases at an amount which, in management's judgment, constitutes an adequate reserve to absorb losses on specific known risks and other risks in the portfolio which have not been specifically identified.

The reserve against domestic and international loans maintained by each applicable entity is not allocated or restricted to any individual loan, group of loans or geographic area. The reserve is available to absorb all credit losses in the entity's loan and lease portfolio, whether they arise domestically or internationally. In computing profitability for purposes or internal management analysis, however, certain subjective assumptions are made which may be revised as management's criteria for evaluating profit center profitability evolve or change in response to changing conditions. The allocation of this reserve between domestic and international loans and leases is based on these assumptions.

In domestic and international commercial lending, the level of credit losses relative to outstanding loans can vary widely from period to period due to the large size of individual credits that may require charge-off and to the effects of changing economic conditions. Sudden changes in risk can occur in the international portfolio due to world economic and political events. It is not possible to identify specifically all the potential losses that exist in the portfolio at a given point in time. Management believes, however, that all material risks have been considered in establishing the level of the reserve for possible credit losses.

The discussion required by this section of Guide 3 is set forth in Credit Risk and Asset Quality on pages 32 through 36 of the 1985 Annual Report and is incorporated herein by reference. The allocation of the Corporation's reserve for possible credit losses on loans and lease finance assets and the ratio of loans and leases to total corporate loans and leases, as required by this section of Guide 3, appears on the following pages 20 and 21.

Statistical Disclosure for Bank Holding Companies (continued)

IV. Summary of Loan Loss Experience (continued)

Assignment of the corporate reserve for possible credit losses on loans and lease finance assets:

(in thousands)	December 31, 1981	1982	1983	1984	1985
Banking:					
Domestic banking:					
Commercial and financial (excluding real estate); (includes loans to commercial and industrial borrowers, loans to financial institutions and other commercial loans)	$ 63,411	$ 79,670	$111,793	$128,432	$143,313
Consumer loans (includes all consumer installment, charge card and other personal type loans and consumer mortgages)	8,114	7,935	22,110	25,205	29,891
Real estate (includes commercial construction and commercial mortgage loans)	15,679	26,403	32,252	34,354	40,718
Total reserve applicable to domestic banking	87,204	114,008	166,155	188,051	213,922
International banking	28,925	35,903	50,525	84,103	110,933
Total Banking	116,129	149,911	216,680	272,154	324,855
Nonbanking:					
Mortgage and real estate (real estate loans)	8,053	8,878	14,020	17,936	21,359
Commercial/Consumer finance (direct installment loans, retail installment notes and second mortgages, commercial and industrial loans and commercial mortgages)	6,226	6,668	7,057	8,934	9,612
Total nonbanking	14,279	15,546	21,077	26,870	30,971
Total reserve for possible credit losses on loans	130,408	165,457	237,757	299,024	355,826
Lease finance assets	3,693	3,721	3,747	4,669	5,659
Total reserve for possible credit losses	$134,101	$169,178	$241,504	$303,693	$361,485

Statistical Disclosure for Bank Holding Companies (continued)

IV. Summary of Loan Loss Experience (continued)

For each category on page 20, the ratio of loans and leases to total corporate loans and leases is as follows:

	Percent of Loans and Leases to Corporate Total December 31,				
	1981	1982	1983	1984	1985
Banking:					
Domestic banking:					
Commercial and financial (excluding real estate): (includes loans to commercial and industrial borrowers, loans to financial institutions and other commercial loans)	47.6%	49.4%	46.1%	49.3%	51.0%
Consumer loans (includes all consumer installment, charge card and other personal type loans and consumer mortgages)	16.8	14.1	16.0	15.0	14.1
Real estate (includes commercial construction and commercial mortgage loans)	5.4	6.8	8.2	8.3	8.9
Total domestic banking	69.8	70.3	70.3	72.6	74.0
International banking	23.5	23.2	22.9	19.6	17.1
Total Banking	93.3	93.5	93.2	92.2	91.1
Nonbanking:					
Mortgage and real estate (real estate loans)	2.9	2.8	3.3	4.4	5.3
Commercial/Consumer finance (direct installment loans, retail installment notes and second mortgages, commercial and industrial loans and commercial mortgages)	2.0	2.0	2.0	1.9	1.9
Total nonbanking	4.9	4.8	5.3	6.3	7.2
Lease finance assets	1.8	1.7	1.5	1.5	1.7
Total Corporation	100.0%	100.0%	100.0%	100.0%	100.0%

Reserve and Credit Loss Ratios

Information required by this section of the Guide is set forth in Credit Risk and Asset Quality on pages 32 through 36 of the 1985 Annual Report and is incorporated herein by reference.

Statistical Disclosure for Bank Holding Companies (continued)

V. Deposits

Information required by this section of Guide 3 is set forth on pages 29, 61 through 63, 66 and 67 of the 1985 Annual Report and is incorporated herein by reference.

VI. Return on Equity and Assets

	Year ended December 31,		
	1983	1984	1985
Common shareholders' equity as a percent of total assets*	5.2 %	5.2 %	5.2 %
Common shareholders' equity and preferred stock as a percent of total assets*	5.5	5.5	5.5
Net income as a percent of:			
Total assets*	.76	.57	.67
Common shareholders' equity*	14.7	11.0	12.9
Common shareholders' equity and preferred stock*	14.1	10.4	12.2
Net income applicable to common stock as a percent of:			
Total assets*	.74	.54	.63
Common shareholders' equity*	14.3	10.3	12.3
Dividends per common share as a percent of:			
Net income per common share	32.8	46.1	37.6

*Based on Balance Sheet averages

VII. Short-Term Borrowings

Information required by this section of Guide 3 is contained on page 45 and in Notes 8 and 9 of the Notes to Financial Statements on page 55 of the 1985 Annual Report and is incorporated herein by reference.

ITEM 2. PROPERTIES

In February 1983, Mellon Bank entered into a long-term lease of a 54-story office building in Pittsburgh, Pennsylvania, which is known as One Mellon Bank Center. Mellon Bank has the option to purchase the building at its fair market value at the end of the 25-year primary lease term and at other times during the lease renewal periods at the then market value subject to the lease. At December 31, 1985, Mellon occupied approximately 82% of the building's 1,450,000 square feet of rentable space. The remaining space has been or will be subleased to third parties.

During 1984, Mellon Bank entered into a sale/leaseback arrangement of the former Union Trust Building in Pittsburgh, Pennsylvania, known as Two Mellon Bank Center. At December 31, 1985, Mellon Bank occupied 23% of this building's approximately 530,000 square feet of rentable space. The remainder of the facility is either subleased to others or under renovation for the Corporation's own use and sublease to third parties.

Mellon Bank owns the 41-story building in Pittsburgh, Pennsylvania known as Three Mellon Bank Center. Of the approximately 943,000 square feet of rentable space, 88% is occupied by Mellon Bank and the remainder is subleased.

At December 31, 1985, Mellon Bank owned 83 of its 125 banking offices and leased the remainder. The leases expire at various times through the year 2011. Mellon Bank also holds beneficial ownership in fee of approximately 20 acres of land located in North Fayette Township, Pennsylvania. A plan is currently being developed for the use of this land.

Mellon Bank (East) occupies approximately 71% of the 513,300 square feet of space in three buildings owned by it in Mellon Bank Center, a complex of four buildings in Center City Philadelphia, Pennsylvania. Within the fourth building, Mellon Bank (East) leases approximately 341,000 square feet of space for terms varying from five to ten years. During 1985, Mellon Bank (East) entered into a 25-year lease of the former Lit Brothers Building in Philadelphia, Pennsylvania, known as Mellon Independence Center. The lease provides Mellon Bank (East) with various options to acquire additional space and extend the term of the lease. Mellon Bank (East) also has the right, under certain circumstances, to participate in the sale of the building. Mellon Bank (East) will initially occupy approximately 60% of the total 791,000 square feet premise. In addition, Mellon Bank (East) leases approximately 171,500 square feet at various locations within Philadelphia County. Leases expire at various times through the year 1993. In January 1986, Mellon Bank (East) sold a 22,000 square foot commercial building located in Feasterville, Bucks County, Pennsylvania. At December 31, 1985, Mellon Bank (East) owned 13 of its 99 banking offices and leased the remainder. These leases expire at various times through the year 2003.

Properties (continued)

Mellon Bank (DE) owns a three story office building known as the Pike Creek Building in New Castle County, Delaware and currently occupies the building's entire 80,000 square feet of rentable space. In 1984, Mellon Bank (DE) sold an 18-story office building in Wilmington, Delaware but it continues to lease approximately 34,300 square feet of the total 212,400 usable square feet. Mellon Bank (DE) leases approximately 55,700 square feet in an office building at Concord Mall in Wilmington, Delaware. At December 31, 1985, Mellon Bank (DE) owned 14 of its 29 banking offices and leased the remainder. Leases expire at various times through the year 2003.

Mellon Bank (Central) owns its main office building in State College, Pennsylvania and occupies all of the approximately 55,000 square feet of available space. Of its 33 offices located in the six county area in central Pennsylvania, 25 are owned and 7 are leased; another office consists of one building which is owned and space in an adjacent building which is leased.

Mellon Bank (North) owns its headquarters office buildi g in Oil City, Pennsylvania, which also includes its main banking office. The bank occupies all of the approximately 59,000 square feet of floor space available. Of the remaining 38 banking facilities located in a five-county area, including one off-premise automated teller machine, 24 are owned and 14 are leased under lease agreements expiring at various dates through the year 2007. Mellon Bank (North) also owns a maintenance supply facility and an operations center.

Subsidiaries of the Corporation lease office space primarily for their operations at the other domestic and international locations listed on pages 70 and 71 of the 1985 Annual Report, which pages are incorporated herein by reference. The leases expire at various dates through the year 2055.

ITEM 3. LEGAL PROCEEDINGS

NONE

ITEM 4. SUBMISSION OF MATTERS TO A VOTE OF SECURITY HOLDERS

NONE

Executive Officers of the Registrant

Information relating to executive officers of the Corporation as of December 31, 1985, is as follows:

	Age	Position and Year Elected	
J. David Barnes	56	Chairman and Chief Executive Officer of the Corporation and Chairman and Chief Executive Officer of Mellon Bank	1985 (1) 1981
George T. Farrell	54	President of the Corporation and of Mellon Bank	1985 (2) 1981
G. Christian Lantzsch	60	Vice Chairman and Treasurer of the Corporation and Vice Chairman of Mellon Bank	1980 1971 1980
Norman M. Steere	54	Vice Chairman of the Corporation and of Mellon Bank	1984 (3)
Elmer G. Grant	60	Vice Chairman of the Corporation and of Mellon Bank	1985 (4)
Edward A. Montgomery, Jr.	51	Vice Chairman of the Corporation and Chairman and Chief Executive Officer of Mellon Bank (East)	1985 (5)
Vincent E. Furey, Jr.	46	President of Mellon Bank (East)	1985 (6)
Frederick K. Beard	44	Executive Vice President of Mellon Bank	1985 (7)
Brendan J. Carroll	52	Executive Vice President of Mellon Bank	1981 (8)
T. Ronald Casper	42	Executive Vice President of Mellon Bank	1985 (9)
E. Michael Caulfield	39	Executive Vice President of Mellon Bank	1985 (10)
George P. DiNardo	48	Executive Vice President of Mellon Bank	1985 (11)

Executive Officers of the Registrant (continued)

Robert L. Pletcher	55	Executive Vice President of Mellon Bank	1985 (12)
Craig G. Ford	56	Executive Vice President of Mellon Bank	1981 (13)
Gary R. Frauenholz	50	Executive Vice President of Mellon Bank	1985 (14)
Richard A. Gaugh	45	Executive Vice President of Mellon Bank	1985 (15)
Ralph B. Hurlbutt	43	Executive Vice President of Mellon Bank	1985 (16)
David L. Johns	42	Executive Vice President of Mellon Bank	1985 (17)
Donald A. McMullen, Jr.	36	Executive Vice President of Mellon Bank	1985 (18)
Theodore C. Miller	47	Executive Vice President of Mellon Bank	1985 (19)
William J. Stallkamp	46	Executive Vice President of Mellon Bank	1985 (20)
P. William Bonito	40	Assistant Treasurer of the Corporation and Senior Vice President and Controller of Mellon Bank	1985 (21) 1982
Martin G. McGuinn	43	Vice President, General Counsel and Secretary of the Corporation and Senior Vice President and General Counsel of Mellon Bank	1981
James D. Roy	45	Assistant Treasurer of the Corporation and Senior Vice President of Mellon Bank	1981 1979

(1) From 1981 until April 6, 1983, the date on which Girard was merged with and into the Corporation, Mr. Barnes was Chairman and Chief Executive Officer of the Corporation. From April 1983 to April 1985, Mr. Barnes was President and Chief Executive Officer of the Corporation.

Executive Officers of the Registrant (continued)

(2) From 1981 until April 1983, the date on which Girard was merged with and into the Corporation, Mr. Farrell was President of the Corporation. From April 1983 to April 1985, Mr. Farrell was Vice Chairman of the Corporation.

(3) Prior to 1984, Mr. Steere had been an Executive Vice President of Mellon Bank since 1981, before which he had been a Senior Vice President of Mellon Bank since 1979.

(4) Prior to the September 1983 merger of CCB Bancorp, Inc. with and into the Corporation, Mr. Grant was Chairman and President of CCB Bancorp, Inc. and Central Counties Bank. Following the merger, Mr. Grant continued as Chairman and President of Central Counties Bank until March 1984, at which time he was elected an Executive Vice President of Mellon Bank. In 1985, Mr. Grant was elected to his present position as Vice Chairman of the Corporation and of Mellon Bank.

(5) Prior to 1985, Mr. Montgomery had been in charge of the Real Estate Department of Mellon Bank and had overall management responsibility for the Corporation's mortgage banking companies in Ohio, Colorado, Louisiana and Texas.

(6) Prior to 1985, Mr. Purey had been an Executive Vice President of Mellon Bank (East) in charge of its Community Banking Department, before which he had been in charge of the corporate and commercial banking activities of Girard Bank.

(7) Prior to 1985, Mr. Beard had been a Senior Vice President of Mellon Bank since 1979.

(8) Prior to 1981, Mr. Carroll had been a Senior Vice President of Mellon Bank since 1979.

(9) Prior to 1985, Mr Casper had been an Executive Vice President of Mellon Bank (East) since March 1983. Prior thereto, he had been a Senior Vice President of Mellon Bank (East) since 1983, before which he had been a Senior Vice President of Mellon Bank since 1982. From 1975 to 1982 Mr. Casper was a Vice President of Mellon Bank.

(10) Prior to 1985, Mr. Caulfield had been a Senior Vice President of Mellon Bank since 1981, before which he had been a Vice President of Mellon Bank since 1978.

(11) Prior to 1985, Mr. DiNardo had been a Senior Vice President of Mellon Bank since 1979.

(12) Prior to 1985, Mr. Fletcher had been a Senior Vice President of Mellon Bank since 1979.

(13) Prior to 1981, Mr. Pord had been a Senior Vice President of Mellon Bank since 1975.

(14) Prior to 1985, Mr. Frauenholz had been a Senior Vice President of Mellon Bank since 1981, before which he had been the Mortgage Corporation's Chief Operating Officer since 1978.

Executive Officers of the Registrant (continued)

(15) Prior to 1985, Mr. Gaugh had been a Senior Vice President of Mellon Bank since 1980.

(16) Prior to 1985, Mr. Hurlbutt had been a Senior Vice President of Mellon Bank since 1981, before which he had been Vice President and General Manager of Mellon Bank International since 1975.

(17) Prior to 1985, Mr. Johns had been a Senior Vice President of Mellon Bank since 1984, before which he had been a Vice President and Division Head of Mellon Bank since 1981. From 1977 to 1981 Mr. Johns was a Vice President of Mellon Bank.

(18) Prior to 1985, Mr. McMullen had been a Senior Vice President of Mellon Bank since 1983, before which he had been a Vice President and Division Head of Mellon Bank since 1980.

(19) Prior to 1985, Mr. Miller had been a Senior Vice President and Group Head of Mellon Bank since 1981, before which he had been a Vice President and Division Head of Mellon Bank since 1976.

(20) Prior to 1985, Mr. Stallkamp had been a Senior Vice President of Mellon Bank since 1978.

(21) Prior to 1985, Mr. Bonito had been a Senior Vice President of Mellon Bank since 1982 and was Controller of Mellon Bank from 1978 to 1982.

Messrs. Barnes, Farrell, Grant, Lantzsch, Montgomery and Steere were elected for a one-year term; all other executive officers serve at the pleasure of their appointing authority. Each executive officer of the Corporation has held his office since the date shown and, unless otherwise indicated, all have been executive officers of the Corporation of Mellon Bank for more than five years.

There are no family relationships between any directors or executive officers of the Corporation.

PART II

ITEM 5. MARKET FOR THE REGISTRANT'S COMMON EQUITY AND RELATED STOCKHOLDER MATTERS

The information required by this Item is set forth on pages 42, 60, 61 and 76 of the 1985 Annual Report and is incorporated herein by reference.

ITEM 6. SELECTED FINANCIAL DATA

The information required by this Item is set forth on pages 22, 43, 66 and 67 of the 1985 Annual Report and is incorporated herein by reference.

ITEM 7. MANAGEMENT'S DISCUSSION AND ANALYSIS OF FINANCIAL CONDITION AND RESULTS OF OPERATIONS

The information required by this Item is set forth on pages 22 through 43 and pages 60 and 61 of the 1985 Annual Report and is incorporated herein by reference.

ITEM 8. FINANCIAL STATEMENTS AND SUPPLEMENTARY DATA

Reference is made to Item 14 on page 31 hereof for a detailed listing of the items incorporated herein by reference.

ITEM 9. DISAGREEMENTS ON ACCOUNTING AND FINANCIAL DISCLOSURE

NONE

PART III

ITEM 10. DIRECTORS AND EXECUTIVE OFFICERS OF THE REGISTRANT

The information required by this Item pertaining to directors of the Corporation is included in the Corporation's proxy statement for its 1986 annual meeting of shareholders (the "1986 Proxy Statement") under the subcaption "Biographical Summaries of Nominees" under the caption ELECTION OF DIRECTORS and is incorporated herein by reference. The information required by this Item pertaining to executive officers of the Corporation has been included in Part I of this Form 10-K under the caption "Executive Officers of the Registrant."

ITEM 11. EXECUTIVE COMPENSATION

The information required by this Item is included in the 1986 Proxy Statement under the following captions: EXECUTIVE COMPENSATION AND BENEFIT PLANS; STOCK OPTIONS, STOCK APPRECIATION RIGHTS AND PERFORMANCE UNITS; AND RATIFICATION OF THE 1981 AMENDMENT TO THE CORPORATION'S INCENTIVE STOCK OPTION PLAN (1972). These portions of the 1986 Proxy Statement are incorporated herein by reference.

ITEM 12. SECURITY OWNERSHIP OF CERTAIN BENEFICIAL OWNERS AND MANAGEMENT

The information required by this Item is included in the 1986 Proxy Statement under the caption BENEFICIAL OWNERSHIP OF STOCK and is incorporated herein by reference.

ITEM 13. CERTAIN RELATIONSHIPS AND RELATED TRANSACTIONS

The information required by this Item is included in the 1986 Proxy Statement under the caption BUSINESS RELATIONSHIPS AND RELATED TRANSACTONS and is incorporated herein by reference.

PART IV

ITEM 14. EXHIBITS, FINANCIAL STATEMENT SCHEDULES AND REPORTS ON FORM 8-K

a) The financial statements and schedules required for the Annual Report of the Corporation on Form 10-K are included, attached or incorporated by reference as indicated in the following index. Page numbers followed by an asterisk(*) refer to pages of the 1985 Annual Report; other page numbers refer to the pages which follow.

Financial Statements	Page No.
Mellon Bank Corporation (and its subsidiaries):	
Consolidated Income Statement	44*
Consolidated Balance Sheet	45*
Consolidated Statement of Changes in Financial Position	46*
Consolidated Statement of Changes in Common Shareholders' Equity	47*
Mellon Bank Corporation (Parent Corporation)	
Income Statement	48*
Balance Sheet	49*
Statement of Changes in Financial Position	50*
Statement of Changes in Common Shareholders' Equity	47*
Notes to Financial Statements	51* through 63*
Report of Independent Accountants	64*

Financial Statement Schedules

Schedules I, II, III and all other schedules are omitted either because they are not required or not applicable or because the required information is shown in the financial statements or notes thereto.

Other Financial Data

Selected Quarterly Data	40*

b) Reports on Form 8-K.

The Corporation was not required to file a Form 8-K during the quarter ended December 31, 1985.

c) Exhibits

The exhibits listed on the Index to Exhibits on pages 33 through 36 are filed herewith in response to this item.

SIGNATURE

Pursuant to the requirements of Section 13 or 15(d) of the Securities Exchange Act of 1934, the Corporation has duly caused this Annual Report to be signed on its behalf by the undersigned, thereunto duly authorized.

Mellon Bank Corporation
(the Corporation)

By _____
J. David Barnes
Chairman and Chief
Executive Officer

DATED: March 27, 1986

Pursuant to the requirements of the Securities Exchange Act of 1934, this Annual Report has been signed below by the following persons on behalf of the Corporation and in the capacities and on the date indicated:

Signature	Capacities
J. David Barnes	Director, Chairman and Principal Executive Officer
G. Christian Lantzsch	Director, Vice Chairman, Treasurer, Principal Financial Officer and Principal Accounting Officer
John M. Arthur, Howard O. Beaver, Jr., Robert J. Buckley, A. W. Calder, Edward Donley, William B. Eagleson, Jr., George T. Farrell, C. Frederick Fetterolf, W. H. Krome George, Thomas C. Graham, Elmer G. Grant, Bryce Jordan, Robert E. Kirby, Andrew W. Mathieson, Seward Prosser Mellon, Nathan W. Pearson, Robert R. Price, Gerald G. Probst, H. Robert Sharbaugh, Richard M. Smith, William P. Snyder III, Norman M. Steere, Leon H. Sullivan, James W. Wilcock, L. Stanton Williams, William S. Woodside, William J. Young	Directors

By _____
Martin G. McGuinn
Attorney-in-fact

DATED: March 27, 1986

Index to Exhibits

Exhibit No.	Description	Prior Filing or Sequential Page No. Herein
3.1	Restated Articles of Incorporation of Mellon Bank Corporation, as amended.	Previously filed as Exhibit 3.1 to Annual Report on Form 10-K for the year ended December 31, 1984 and incorporated herein by reference.
3.2	By-Laws of Mellon Bank Corporation, as amended.	Previously filed as Exhibit 3.2 to Annual Report on Form 10-K for the year ended December 31, 1984 and incorporated herein by reference.
10.1	Lease dated as of February 1, 1983 between 500 Grant Street Associates Limited Partnership and Mellon Bank, N.A. with respect to One Mellon Bank Center.	Previously filed as Exhibit 10.2 to Annual Report on Form 10-K for the year ended December 31, 1982 and incorporated herein by reference.
10.2	First Amendment to Lease Agreement dated as of November 1, 1983, between 500 Grant Street Associates Limited Partnership and Mellon Bank, N.A.	Previously filed as Exhibit 10.1 to Registration Statement on Form S-15 (Registration No. 2-88266) and incorporated herein by reference.
10.3	Construction Management Agreement dated as of February 16, 1983 between Mellon Bank, N.A. and United States Steel Corporation with respect to One Mellon Bank Center.	Previously filed as Exhibit 10.4 to Annual Report on Form 10-K for the year ended December 31, 1982 and incorporated herein by reference.
10.4	Construction Agreement dated as of February 1, 1983 between Mellon Bank, N.A. and 500 Grant Street Associates Limited Partnership with respect to One Mellon Bank Center.	Previously filed as Exhibit 10.5 to Annual Report on Form 10-K for the year ended December 31, 1982 and incorporated herein by reference.
10.5	Mellon Bank Corporation Profit Bonus Plan.	Previously filed as Exhibit 10.1 to Annual Report on Form 10-K for the year ended December 31, 1981 and incorporated herein by reference.

Index to Exhibits

Exhibit No.	Description	Prior Filing or Sequential Page No. Herein
10.6	Mellon Bank Corporation Supplemental Retirement Benefits Plan	Previously filed as Exhibit 10.10 to Annual Report on Form 10-K for the year ended December 31, 1983 and incorporated herein by reference.
10.7	Mellon Bank Corporation Long-Term Profit Incentive Plan, as amended.	Previously filed as Exhibit 10.11 to Annual Report on Form 10-K for the year ended December 31, 1983 and incorporated herein by reference.
10.8	Mellon Bank (East) Supplemental Income and Benefit Plan.	Previously filed as Exhibit 10.12 to Annual Report on Form 10-K for the year ended December 31, 1983 and incorporated herein by reference.
10.9	Employment Contract dated March 23, 1984, between Mellon Bank and Elmer G. Grant.	Previously filed as Exhibit 10.14 to Annual Report on Form 10-K for the year ended December 31, 1983 and incorporated herein by reference.
11.1	Computation of Primary and Fully-Diluted Earnings Per Share	37
12.1	Computation of Ratios of Earnings to Fixed Charges and Ratios of Earnings to Fixed Charges and Preferred Stock Dividends-Parent Corporation	39
12.2	Computation of Ratios of Earnings to Fixed Charges and Ratios of Earnings to Fixed Charges and Preferred Stock Dividends-Consolidated	40
13.1*	Mellon Bank Corporation 1985 Annual Report to Shareholders	43
22.1	List of Subsidiaries of the Corporation	123
24.1	Consent of Independent Accountants	131
25.1	Power of Attorney	133
28.1	Form 11-K	145

* This document shall be deemed to have been "filed" only to the extent of the materia" incorporated herein by reference.

Index to Exhibits
-3-

The documents identified below which define the rights of holders of long-term debt of the Corporation are not filed herewith as the total amount of securities authorized thereunder do not exceed 10% of the total assets of the Corporation and its subsidiaries on a consolidated basis. The Corporation hereby agrees to furnish a copy of such documents to the Securities and Exchange Commission upon request.

1 Indenture dated as of September 1, 1974 between the Corporation and First National City Bank, Trustee, with respect to Floating Rate Notes Due 1989.

2 Indenture dated as of June 15, 1979 between the Corporation and Manufacturers Hanover Trust Company, Trustee, with respect to Floating Rate Notes Due 1989 (Convertible by Holder prior to June 15, 1988 into 8 1/2% Debentures Due 2009; Convertible by Mellon Bank Corporation after June 15, 1980 and prior to June 15, 1988 into Fixed Rate Debentures Due 2009).

3 Indenture dated as of May 1, 1982 between the Corporation and Bankers Trust Company, Trustee, providing for the issuance of debt securities in series from time to time, as supplemented.

4 Indenture dated as of June 1, 1968, between Girard Trust Bank (now Mellon Bank (East)) and First Pennsylvania Bank, N.A., Trustee, with respect to 5 3/8% Convertible Capital Notes due June 1, 1993, as supplemented by the First Supplemental Indenture dated as of June 30, 1969 among The Girard Company (now the Corporation), Mellon Bank (East) and the Trustee, and as supplemented by the Second Supplemental Indenture dated as of April 6, 1983 among Mellon Bank (East), the Corporation and the Trustee.

5 Indenture dated as of May 15, 1979, between The Girard Company (now the Corporation) and The Philadelphia National Bank, Trustee, with respect to Floating Rate Notes due May 15, 1978 (convertible prior to May 15, 1986 into 9% Debentures due 1999), as supplemented by the First Supplemental Indenture, dated as of April 6, 1983 between the Corporation and the Trustee.

6 Indenture dated as of May 15, 1979, between The Girard Company (now the Corporation) and The Philadelphia National Bank, Trustee, with respect to Debentures due May 15, 1999, as supplemented by the First Supplemental Indenture, dated as of April 6, 1983, between the Corporation and the Trustee.

7	Note Purchase Agreement dated July 6, 1977 (the "Purchase Agreement") in connection with 8.95% Notes Due September 1, 1997 between The Girard Company (now the Corporation) and several institutional purchasers listed in Schedule I of the Purchase Agreement, and the Assumption Agreement dated April 6, 1983 of the Corporation in connection with the assumption by the Corporation of all obligations under the Purchase Agreement.
8	Fiscal and Paying Agency Agreement dated as of November 29, 1984 among Mellon Bank, N.A., as Issuer, Mellon Bank Corporation and Chemical Bank, as Fiscal and Paying Agent, relating to U.S. $250 Million Floating Rate Subordinated Capital Notes due November 1996.
9	Fiscal and Paying Agency Agreement dated as of March 7, 1985 among Mellon Financial Company, as Issuer, Mellon Bank Corporation, as Guarantor, and Chemical Bank, as Fiscal and Paying Agent, relating to U.S. $100 Million 11 3/4% Guaranteed Debentures due 1995.

Exhibit 11.1

Mellon Bank Corporation

Computation of Primary and Fully-Diluted Earnings Per Share

	Year Ended December 31,		
	1983	1984	1985
Primary earnings per common share			
Stock and Stock Equivalents (average shares):			
Common shares outstanding	23,986,591	26,373,880	26,863,972
Common stock equivalents (a)	366,308	370,755	554,298
Shares assumed to be repurchased under the treasury stock method at average annual market prices	(276,262)	(293,999)	(417,778)
Total	24,076,637	26,450,636	27,000,492
Net income applicable to common stock	$178,552,000	$148,822,000	$191,471,000
Primary earnings per common share	$7.42	$5.63	$7.09
Reported earnings per common share (b)	$7.14	$5.64	$7.13
Fully-diluted earnings per common share			
Stock, Stock Equivalents and Dilutive Items (average shares):			
Common shares outstanding	23,986,591	26,373,880	26,863,972
Common stock equivalents (a)	366,308	370,755	554,298
Shares assumed to be repurchased under the treasury stock method at the greater of the year-end closing or average annual market prices	(257,296)	(257,633)	(404,264)
Shares issuable upon assumed conversion of 5 3/8% Convertible Capital Notes	52,939	33,757	25,808
Total	24,148,542	26,520,759	27,039,814
Net income applicable to common stock	$178,552,000	$148,822,000	$191,471,000
Add: After-tax benefit of interest expense saved on assumed conversion of 5 3/8% Convertible Capital Notes	22,000	24,000	21,000
Adjusted net income	$178,574,000	$148,846,000	$191,492,000
Fully-diluted earnings per common share	$7.39	$5.61	$7.08

(a) Common stock equivalents consist of stock options.

(b) Earnings per share presented in the Annual Reports to Shareholders are computed by dividing net income, after deducting dividends on preferred stock, by the weighted average number of common shares outstanding during the periods. The effect of common stock equivalents on primary earnings per share was less than one percent for each of the years 1983-1985.

Exhibit 12.1

COMPUTATION OF RATIOS OF EARNINGS TO FIXED CHARGES AND RATIOS OF EARNINGS TO COMBINED FIXED CHARGES AND PREFERRED STOCK DIVIDENDS
(dollar amounts in thousands)

Mellon Bank Corporation (parent Corporation)(1)

	Year ended December 31,				
	1981	1982	1983	1984	1985
1. Income before income taxes and before undistributed income/ (losses) of subsidiaries	$ 88,827	$ 63,944	$ 75,774	$ 72,006	$ 80,483
2. Fixed charges-interest expense, one-third of rental expense, and amortization of debt issuance costs	202,504	164,975	147,212	186,139	167,979
3. Preferred stock dividend requirements	-	-	9,440	16,540	18,260
4. Income before income taxes and before undistributed income/ (losses) of subsidiaries, plus fixed charges (Line 1 + Line 2)	$291,331	$228,919	$222,986	$258,145	$248,462
5. Ratio of earnings (as defined) to fixed charges (Line 4 ÷ Line 2)	1.44	1.39	1.51	1.39	1.48
6. Ratio of earnings (as defined) to combined fixed charges and preferred stock dividends (Line 4 ÷ [Line 2 + Line 3])	1.44	1.39	1.42	1.27	1.33

(1) The parent Corporation ratios include the accounts of Mellon Bank Corporation (the "Corporation"), Mellon Financial Company and Girard Financial Corporation, wholly-owned subsidiaries of the Corporation that function as financing entities for the Corporation and its subsidiaries by issuing commercial paper and other debt guaranteed by the Corporation. For purposes of computing these ratios, earnings represent parent Corporation income before income taxes and before undistributed income/(losses) of subsidiaries, plus the fixed charges of the parent Corporation. Fixed charges represent interest expense, one-third (the proportion deemed representative of the interest factor) of rental expense and amortization of debt issuance costs. Preferred stock dividend requirements represent the pre-tax earnings which would be required to cover the Corporation's preferred stock dividends. Preferred stock was not issued until April 1983; accordingly, no preferred stock dividends were accrued in the three-month period ending March 31, 1983. Because the ratio excludes from earnings the undistributed net income of subsidiaries, the ratio varies with the payments of dividends by such subsidiaries.

Exhibit 12.2

COMPUTATION OF RATIOS OF EARNINGS TO FIXED CHARGES AND RATIOS OF EARNINGS TO COMBINED FIXED CHARGES AND PREFERRED STOCK DIVIDENDS
(dollar amounts in thousands)

Mellon Bank Corporation and its Subsidiaries(1)

	Year ended December 31,				
	1981	1982	1983	1984	1985
1. Net income	$ 115,511	$ 134,372	$ 183,815	$ 158,544	$ 201,695
2. Total U.S. and foreign income taxes provided (benefit)	8,767	9,517	34,530	(6,689)	49,407
3. Net income before income taxes (Line 1 + Line 2)	$ 124,278	$ 143,889	$ 218,345	$ 151,855	$ 251,102
4. Fixed charges:					
a. Interest expense (excluding interest on deposits)	$ 564,716	$ 585,957	$ 581,808	$ 662,141	$ 636,947
b. One-third of rental expense, net of income from subleases, and amortization of debt issuance costs	7,208	6,968	11,244	22,324	24,447
c. Total fixed charges (excluding interest on deposits) (Line 4a + Line 4b)	571,924	592,925	593,052	684,465	661,394
d. Interest on deposits	1,213,301	1,156,997	1,031,712	1,303,931	1,220,055
e. Total fixed charges (Line 4c + Line 4d)	$1,785,225	$1,749,922	$1,624,764	$1,988,396	$1,881,449
5. Preferred stock dividend requirements	$ -	$ -	$ 9,440	$ 16,940	$ 18,260
6. Net income before income taxes plus total fixed charges:					
a. Excluding interest on deposits (Line 3 + Line 4c)	$ 696,202	$ 736,814	$ 811,397	$ 836,320	$ 912,496
b. Including interest on deposits (Line 3 + Line 4e)	$1,909,503	$1,893,811	$1,843,109	$2,140,251	$2,132,551

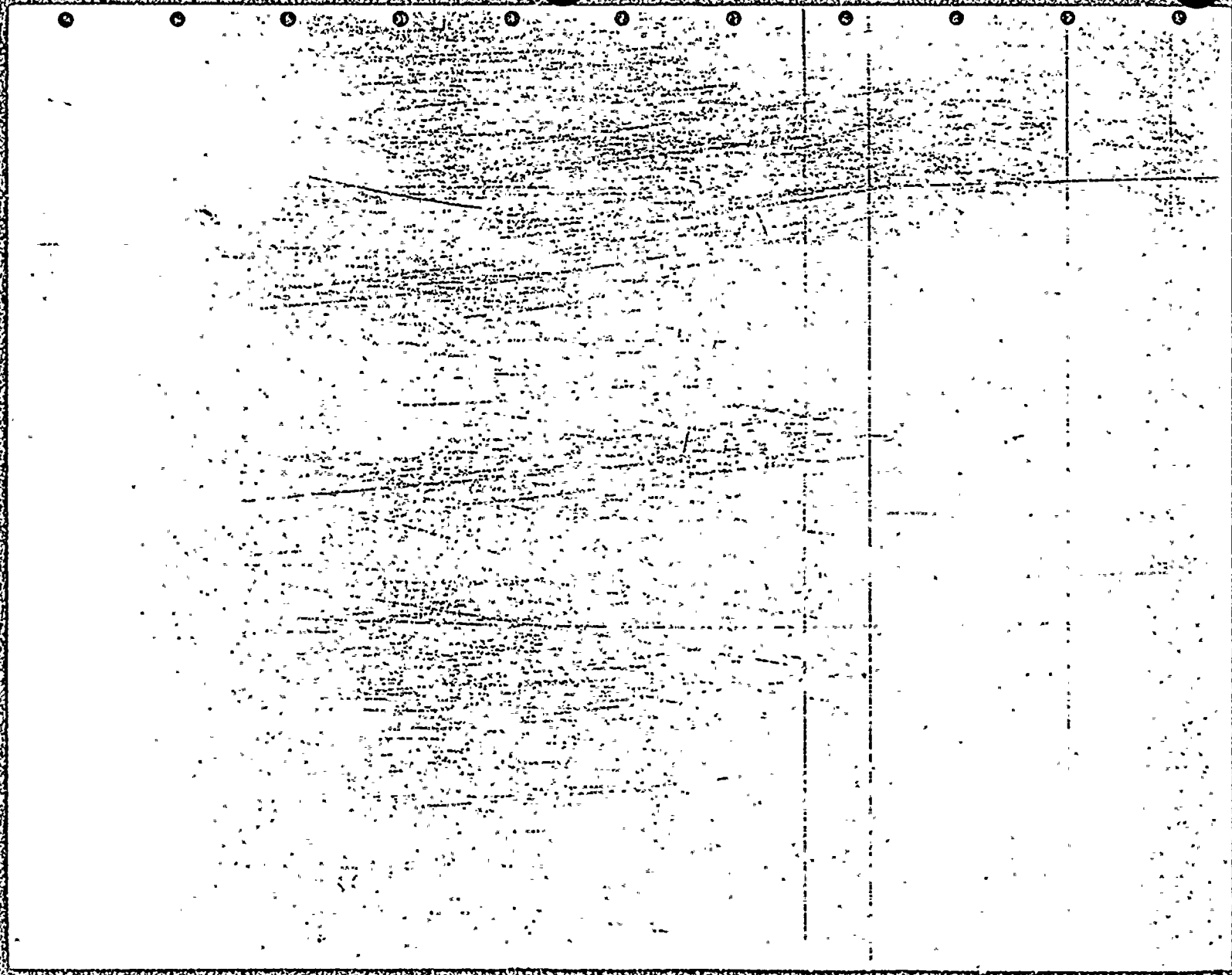
Exhibit 12.2
(continued)

COMPUTATION OF RATIOS OF EARNINGS TO FIXED CHARGES AND RATIOS OF EARNINGS TO COMBINED FIXED CHARGES AND PREFERRED STOCK DIVIDENDS
(Dollar amounts in thousands)

Mellon Bank Corporation and its Subsidiaries(1)

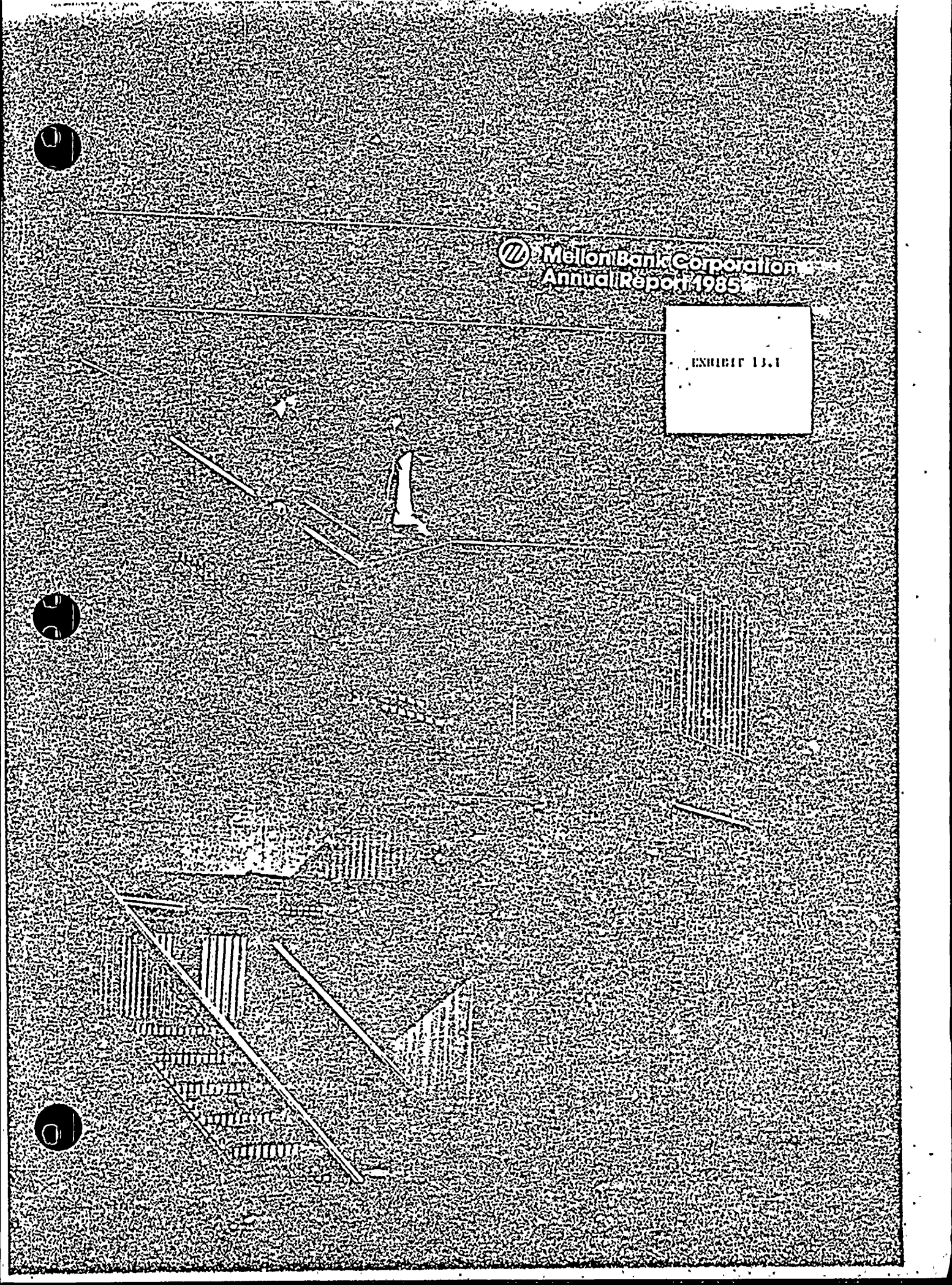
	Year ended December 31,				
	1981	1982	1983	1984	1985
7. Ratios of earnings (as defined) to fixed charges:					
a. Excluding interest on deposits (Line 6a ÷ Line 4c)	1.22	1.24	1.37	1.22	1.38
b. Including interest on deposits (Line 6b ÷ Line 4e)	1.07	1.08	1.13	1.08	1.13
8. Ratios of earnings (as defined) to combined fixed charges and preferred stock dividends					
a. Excluding interest on deposits (Line 6a ÷ [Line 4c + Line 5])	1.22	1.24	1.35	1.19	1.34
b. Including interest on deposits (Line 6b ÷ [Line 4e + Line 5])	1.07	1.08	1.13	1.07	1.12

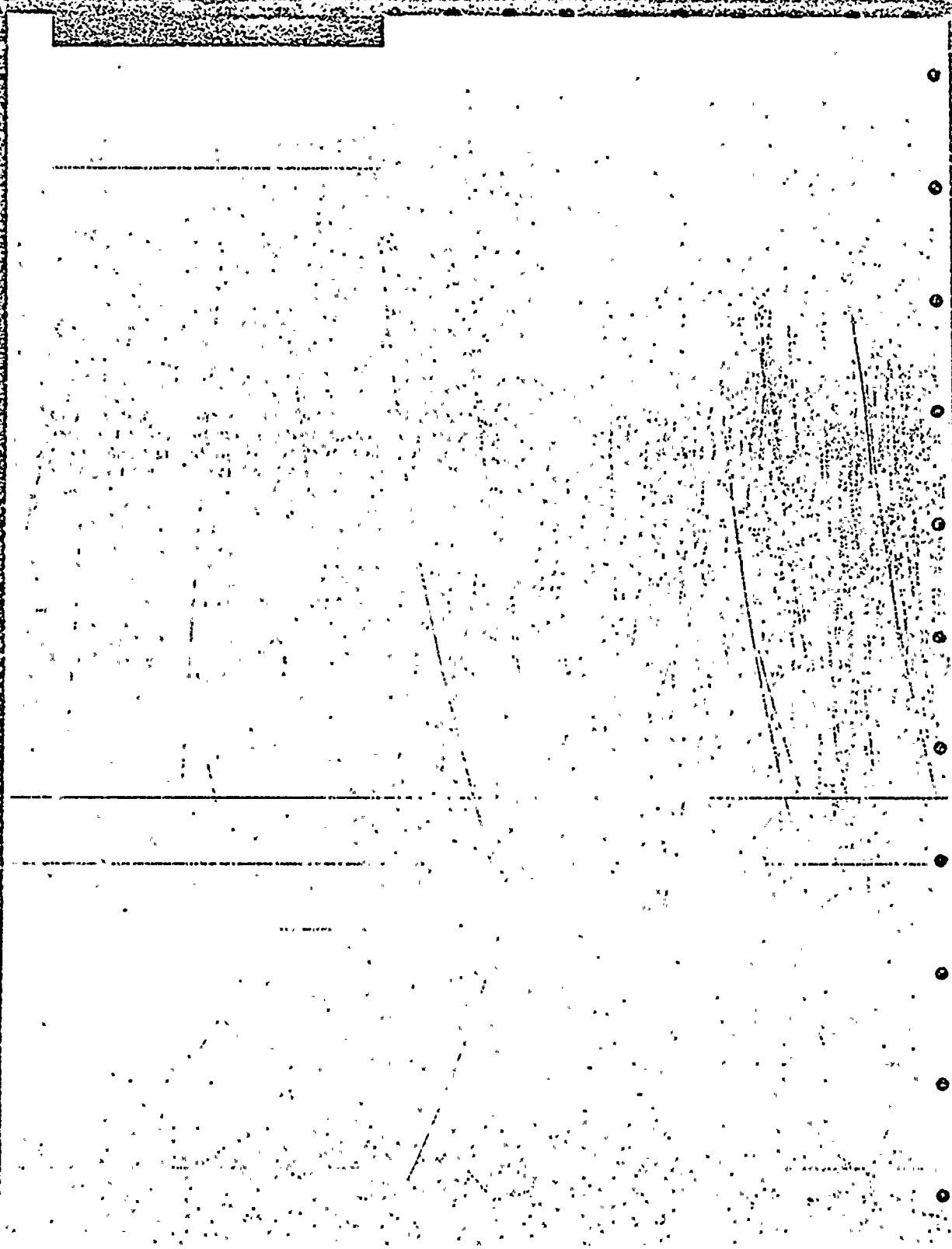
(1) For purposes of computing these ratios, earnings represent consolidated net income, plus total U.S. and foreign income taxes provided in computing consolidated net income, plus consolidated fixed charges. Fixed charges, excluding interest on deposits, include interest expense (other than on deposits), one-third (the proportion deemed representative of the interest factor) of rental expense net of income from subleases, and amortization of debt issuance costs. Fixed charges, including interest on deposits, include all interest expense, one-third (the proportion deemed representative of the interest factor) of rental expense net of income from subleases, and amortization of debt issuance costs. Preferred stock dividend requirements represent the pre-tax earnings which would be required to cover the Corporation's preferred stock dividends. Preferred stock was not issued until April 1983; accordingly, no preferred stock dividends were accrued in the three-month period ending March 31, 1983.



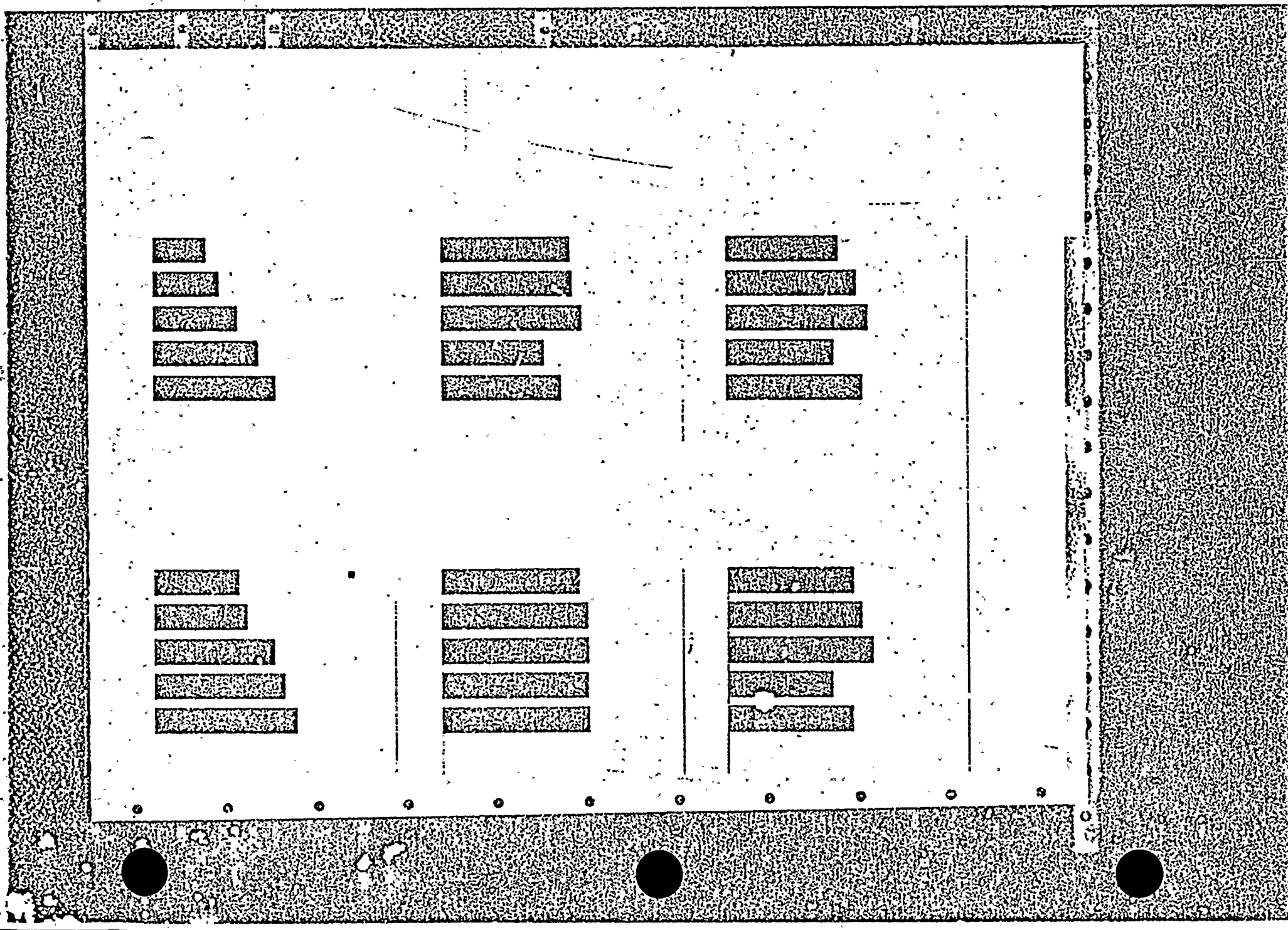
Mellon Bank Corporation
Annual Report 1985

EXHIBIT 13.1





Mellon Bank Corporation is a multinational financial services organization and the 11th largest bank holding company in the United States. Through its banking subsidiaries located principally in Delaware and Pennsylvania, the Corporation provides domestic retail banking as well as worldwide commercial banking and trust and investment management services. In addition, Mellon Financial Services provides consumer and mortgage banking, leasing, commercial real estate financing and investment management services.



In The Year 1985

- Net income increased 27% to $201.7 million, a record level; net income per common share increased 26% to $7.13.
- Total assets increased by 9% to $33.4 billion; loans and leases increased by 13% to $22.3 billion.
- Service revenue increased by 21% to $365 million.
- The Corporation agreed to merge with Commonwealth National Financial Corporation and to acquire Carleton Financial Computations, Inc. and portions of Fidata Corporation.

(dollar amounts in millions, except per share amounts)	1984	1985	Increase/(decrease)	
For the year				
Net income	$ 158.5	$ 201.7	$ 43.2	27 %
Net income applicable to common stock	148.8	191.5	42.7	29
Dividends on common stock	68.6	71.9	3.3	5
Per common share				
Net income	$ 5.64	$ 7.13	$ 1.49	26 %
Dividends	2.60	2.68	.08	3
At year-end				
Total assets	$30,603	$33,406	$2,803	9 %
Loans and lease finance assets	19,687	22,319	2,632	13
Deposits	18,997	18,583	(414)	(2)
Common shareholders' equity	1,499	1,637	138	9
Ratios				
Return on assets	.54%	.63%		
Assets to common shareholders' equity	19.2	19.4		
Return on common shareholders' equity	10.3 %	12.3 %		
Primary capital as a percentage of total assets	6.64%	6.62%		

To Our Shareholders

At Mellon Bank Corporation, we seek to achieve favorable levels of short term profitability while focusing on those actions that will ensure a solid, profitable future. Our 1985 results reflect success in these efforts. Net income rose to $201.7 million—the highest level in the Corporation's history—from $158.5 million in 1984. Net income per common share increased to $7.13 from $5.64 per common share in 1984. This 26 percent increase in net income per common share was attributable to strong increases in revenues from our core credit and service businesses, and substantial securities gains. Return on common shareholders' equity increased to 12.3 percent from 10.3 percent in 1984, and return on assets improved to .63 percent from .54 percent. These results point to important progress as we position our Corporation for the realities of a rapidly-evolving financial services industry. We are building on our strengths and cultivating those businesses that promise to provide durable long-term earnings.

For example, we continue to make substantial progress in developing our capital markets business. In 1985, this paid off in the form of unusually large increases in trading revenue and securities gains. As we build our capital markets expertise, we are enhancing our already strong position in the domestic corporate marketplace. Our decade-long effort to broaden the scope of the high-quality financial services we offer to this market has included the establishment of a nationwide network of representative offices, the quadrupling of our staff of relationship officers, and the development of specialized financing products and services. As a result, we have substantially increased our market share of commercial and industrial loans while maintaining a level of charge-offs below that of most major bank holding companies.

We are also positioning Mellon for the future by pursuing our historical commitment to being a leading provider of technology-based financial services, by developing products internally and by acquiring companies that have well-established products and solid market reputations. This philosophy was a driving force behind our decisions in 1985 to acquire Carleton Financial Computations, Inc. of South Bend, Indiana and three subsidiaries of Fidata Corporation of New York, and to form Mellon Securities Trust Company in New York. The Carleton acquisition will expand our business of providing data processing services to financial institutions across the country; the acquisition of the Fidata units will broaden the array of fiduciary operational/processing services that we offer; and the formation of Mellon Securities Trust Company enables us to provide processing and custody capabilities for certain specialized securities transactions.

Another key element of our long-term strategy is the building of a strong community banking presence throughout the Central Atlantic region. This strategy is reflected in our 1985 agreement to merge with Commonwealth National Financial Corporation of Harrisburg, Pennsylvania, and our opening of a middle market representative office in Edison, New Jersey. Commonwealth, a $1.4 billion bank holding company, offers a full range of banking and trust services through 43 offices in south central Pennsylvania. Upon consummation of the Commonwealth merger, we will have community banking

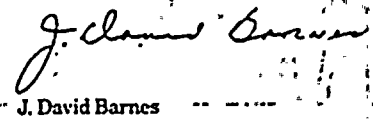
Members of the Corporate Office (left to right): Edward A. Montgomery, Jr., Vice Chairman; George T. Farrell, President; J. David Barnes, Chairman and Chief Executive Officer; Elmer G. Grant, Vice Chairman; G. Christian Lantzsch, Vice Chairman and Treasurer; and Norman M. Steere, Jr., Vice Chairman.

locations in most of Pennsylvania's largest population centers. This and other bank mergers expand our market presence, strengthen our base of stable core deposits and prepare the Corporation for the onset of interstate banking.

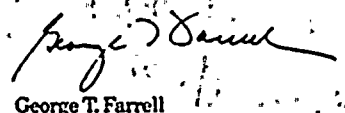
We still face profitability challenges, particularly in international banking and some aspects of community banking. Our international loan portfolio has been affected adversely by the economic difficulties of some lesser developed countries, although these loans amount to a relatively modest portion of our generally high-quality loan and lease portfolio. Reexamination of our international markets and services led us to conclude that we will provide international financial services on a more selective basis and in markets that we believe we can serve profitably. In 1985, we closed our Athens and Frankfurt offices and, at the same time, applied for establishment of a financial services subsidiary in Australia. Going forward, we will concentrate on providing credit and operating services to foreign financial institutions and multinational companies, and global trade banking to customers in our Central Atlantic market.

We are committed to serving our community markets more effectively and profitably. We are implementing a strategy that includes increasing our lending to individuals and businesses, enhancing productivity, lowering costs and improving service quality. Intertwined with this effort is the continuing evolution of a customer-driven spirit in our banks, with each Mellon Bank making its own decisions on how best to respond to local market needs.

In all aspects of our business, we strive to implement ideas that can bring results, both now and for the future. We made solid progress in 1985—progress that resulted from our market orientation, which makes the customer the focus of our activities, and the talent and dedication of the more than 15,000 Mellon associates whose efforts enable us to be regarded as a premier financial services organization.



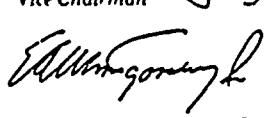
J. David Barnes
Chairman and Chief Executive Officer



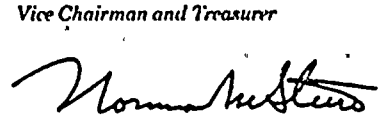
George T. Farrell
President

Elmer G. Grant
Vice Chairman

G. Christian Lantzsch
Vice Chairman and Treasurer



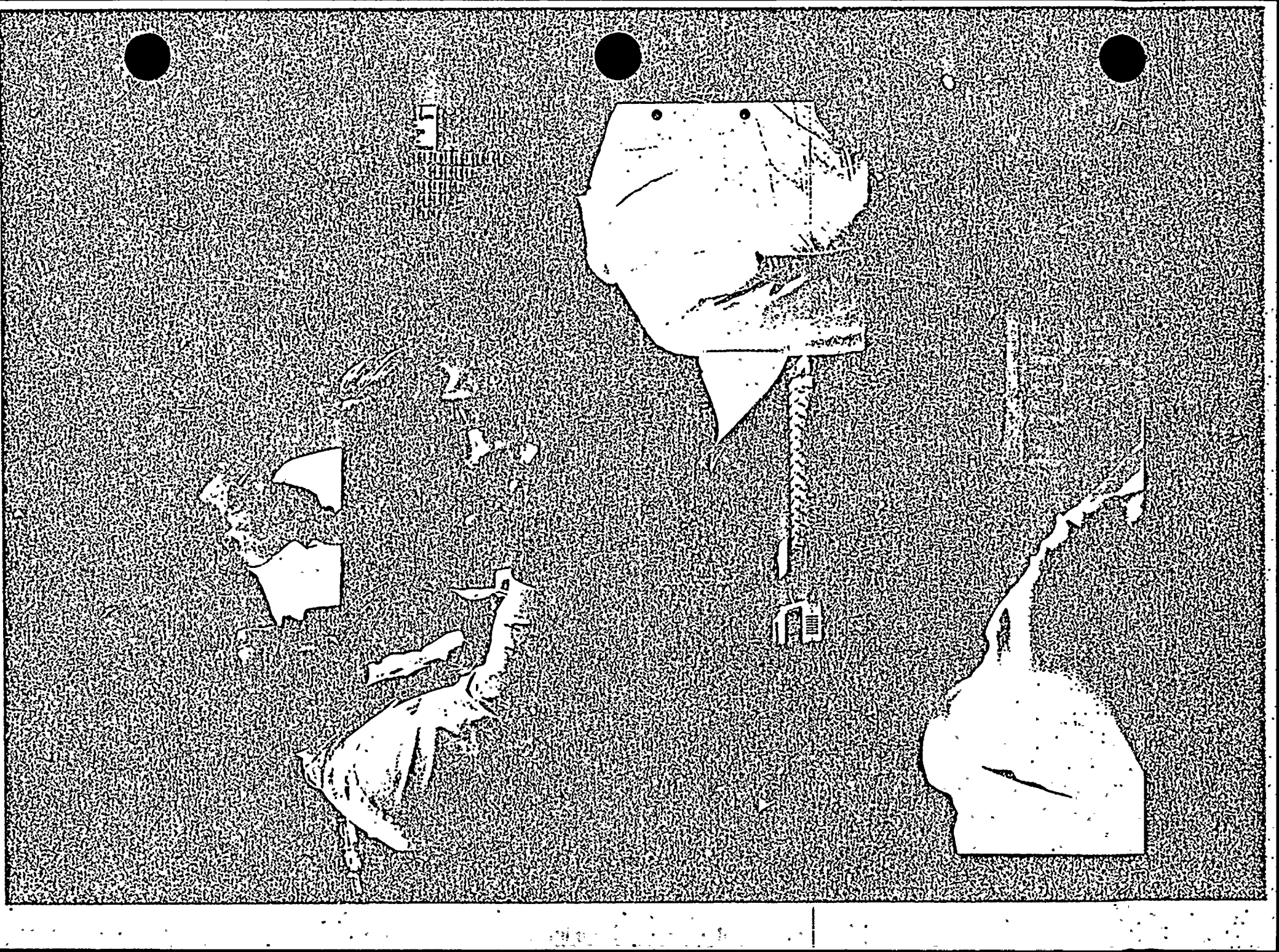
Edward A. Montgomery, Jr.
Vice Chairman



Norman M. Steere
Vice Chairman

Mellon Bank Corporation realized significant progress on many fronts in 1985. It was a year in which our net income increased substantially, in which we built upon our reputation of meeting the financial services needs of our customers, and in which we affirmed our commitment to attract, retain and build the skills of outstanding people who enable Mellon to be a premier financial services organization.

In short, 1985 was a year of progress. Progress in financial performance, progress in serving our customers and progress through our associates.



In Review

Progress in Financial Performance

In 1985, Mellon Bank Corporation made substantial progress towards attainment of its long-term financial objectives. We achieved marked improvement in net income from our core businesses—principally the provision of credit products and operating services—as well as substantial gains on the sale of investment securities; we registered sharp increases in return on assets and return on common shareholders' equity; and we enhanced our financial strength through the continued building of reserves and capital.

Profitability Measures. Net income increased by 27 percent from 1984. Core net income increased by $17.2 million, or 11 percent, while gains on the sale of investment securities increased by $89 million. We also improved in two other key profitability measures: return on common shareholders' equity and return on assets. Return on common shareholders' equity, which compares earnings to common shareholders' ownership interest in the Corporation, rose to 12.3 percent from 10.3 percent in 1984. Return on assets, which compares earnings to the Corporation's assets, improved to .63 percent from .54 percent in 1984.

Net Credit Revenue. Net credit revenue (the difference between interest that we pay for funds and the interest earned on loans and other assets, plus related fees) increased in 1985 by $125 million, or 17 percent, due to increased loans and leases, wider interest rate spreads on investment securities, and a substantially higher level of loan fees. Loans and leases increased on average by $2.7 billion, or 16 percent, $2.1 billion of which was due to growth in our commercial loan portfolio. Continuing a pattern of strong and steady growth, Mellon's share of the commercial and industrial market increased sharply during 1985, reflecting loan growth among large corporations and financial institutions, middle market firms and small businesses. Lease financing revenue increased 19 percent over the prior year, reflecting our ongoing response to customer demand for cost-effective financing of capital equipment. Our commitments in the commercial real estate markets grew prudently while real estate loans outstanding increased significantly as a result of prior years' commitments. We emphasize high credit quality lending to large and experienced developers. We continued to experience strong loan growth in the health care industry, where we are a leading provider of financial products and services to high-quality health care institutions nationwide. Among consumers, loan growth, which increased $572 million, or 17 percent on average, was spurred by the introduction of our Personal Credit Line revolving credit product, increased demand for residential mortgages, and our broadened geographical reach in consumer markets.

Service Revenue. We continue to stress the development of high-quality services to generate fee revenue and income. In 1985, total service revenue increased by 21 percent. Strong revenue increases were registered in numerous fee-generating products

Progress in financial performance: Financial strength has been enhanced by the development of expertise in an increasing number of financial services businesses.

Outstanding results from our capital markets activities were important to Mellon's financial performance in 1985. We are developing our capital markets business into a third Mellon core strength, complementing our traditional strengths in credit management and operating skills. Shown in the trading room in One Mellon Bank Center, Pittsburgh, are Capital Markets Department associates (clockwise from bottom left: Jonathan Bakker, R. T. Crystian, Jr., Thomas Myers, Julie Jenkins, Rosalie Barsotti and Leo Au.

and services. Revenue from data processing for other financial institutions increased by 17 percent, as we expanded transaction volume and added customers. Cash management fees and deposit transaction charges increased by 32 percent, due to expansion of both our product line and our customer base. Revenue from mortgage servicing fees increased by 18 percent as our servicing portfolio grew to $8.7 billion, ranking us among the top mortgage banking companies in the United States. Trust and investment revenue, including trustee, custody, record-keeping and investment advisory services for corporations, pension plans and financial institutions, increased by 22 percent. Brokerage and advisory fees for equipment leasing services increased by 52 percent. In 1985, we also centralized the Corporation's credit cardholder service activities at Mellon Bank (DE). Total charge service fee revenue increased by 9 percent from 1984.

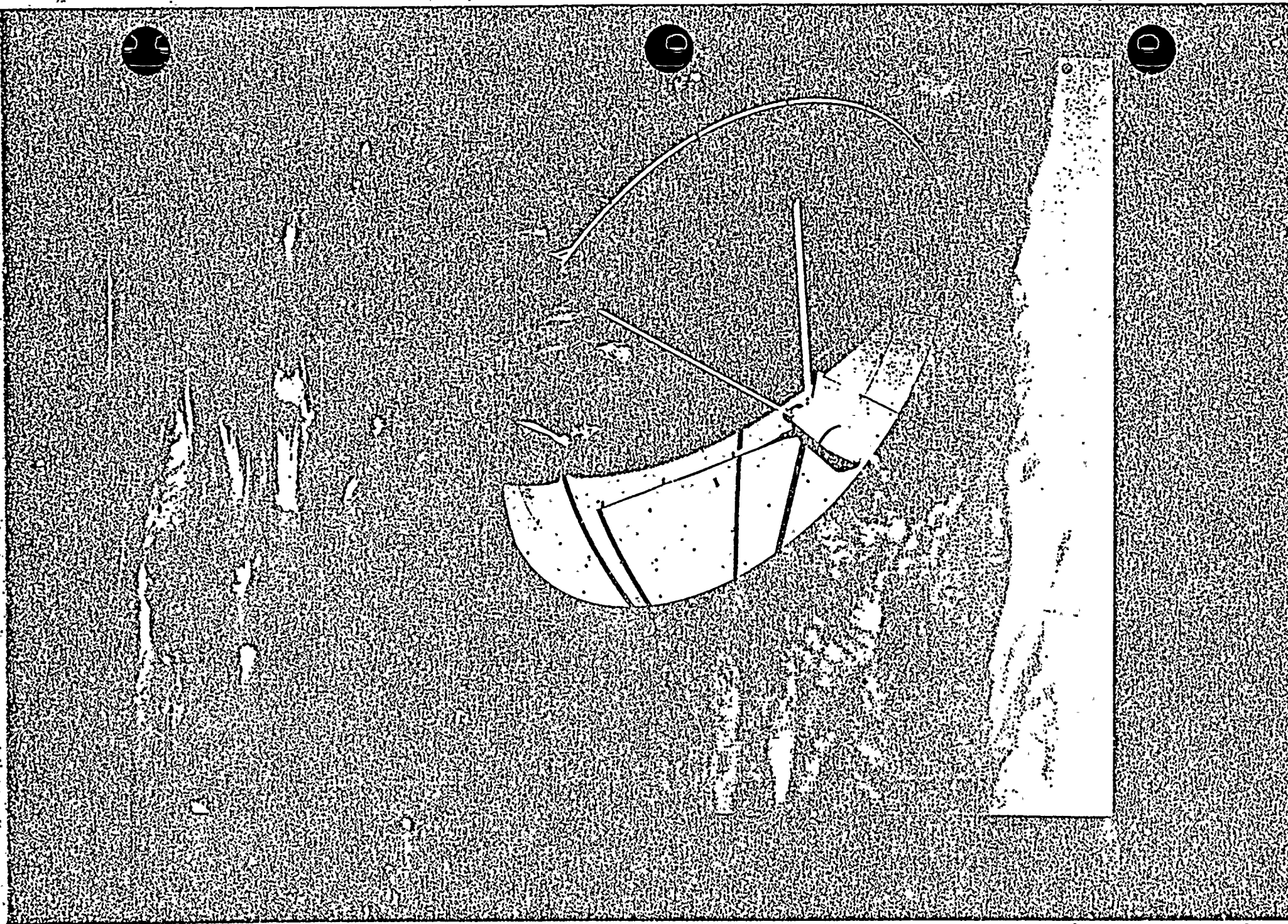
Securities Gains and Trading Profits. Gains on the sale of investment securities increased dramatically, to $92.5 million in 1985 from $3.6 million in 1984. Trading account profits and commissions also increased significantly, to $15.9 million from $6 million in 1984. These increases result from our continued development of expertise in capital markets activities and a declining interest rate environment that provided the opportunity to excel in both the securities and trading businesses. While obviously welcomed, gains of this magnitude may not be repeated frequently. Our goal in developing our capital markets expertise is to produce recurring income consistent with Corporate objectives and to capitalize fully on extraordinary market opportunities such as may occur from time to time.

Reserve Strength and Credit Quality. In fostering asset growth, we maintain our traditional emphases on credit quality and sound loan loss reserves. At year-end, Mellon's loan loss reserve (maintained to absorb losses in the loan and lease portfolios) amounted to $361.5 million, up from $303.7 million in 1984. In relation to asset quality, our reserves rank among the highest of major bank holding companies. In terms of credit quality, our percentage of nonperforming (cash-basis, past due and restructured) assets to total loans and leases decreased in 1985 to 2.72 percent from 2.81 percent in 1984. As a percent of average loans and leases, Mellon's loan losses increased to .45 percent in 1985 from .34 percent a year earlier, principally as a result of higher consumer and domestic commercial credit losses. While we are not satisfied with this increase, our credit loss ratio remains one of the lowest among major bank holding companies.

Funding. A strong funding position is especially desirable in this period of rapid change in the financial services industry. The Corporation has built a strong base of core funds—essentially deposits generated through our community banking activities and other funds with maturities of more than one year—with which to lend, invest, and build the Corporation. These core funds are attractive for their stability, and provide an important base upon which to manage the liquidity of the Corpora-

Progress in financial performance: Mellon has developed specialized knowledge in meeting the financial services needs of companies in numerous growth industries, including communications.

We are a leading lender to the cable television industry. Many cable firms—including Denver-based TCI, the largest cable company in the United States—do business with Mellon. The Mellon/TCI relationship has spanned 15 years, from shortly after TCI's incorporation in 1968 to its current position atop the industry, with some 3.9 million subscribers. Pictured at a TCI satellite dish in Denver are company founder and Chairman Bob Magness (c.), Barney Schotters, TCI's vice president of finance and Cynthia Townsend of Mellon's Denver office, relationship officer for TCI.



tion. During 1985, our core deposits increased by 7 percent, to $11.5 billion. Because of our emphasis on core deposits, our reliance on "purchased" funds—such as certain negotiable certificates of deposit, federal funds and commercial paper—has decreased markedly. Our domestic purchased funds ratio (a comparison of purchased funds to assets) declined to 36 percent during 1985 from as much as 56 percent just three years ago.

Capital. Our primary and total capital ratios (capital compared to total assets), which at year-end 1985 stood at 6.6 percent and 7.9 percent, respectively, were well above the Federal Reserve Board's minimum capital adequacy ratios of 5.5 percent for primary capital and 6.0 percent for total capital. Our capacity to make loans has expanded in step with increases in our capital. With primary capital at $2.2 billion, Mellon's combined legal lending limit grew to more than $330 million at year-end 1985 from more than $290 million a year earlier.

Financial Strength. We believe that it is of paramount importance that Mellon Bank Corporation maintain its profitability and financial strength. By doing both in 1985, we enhanced our capacity to meet our obligations to our major constituencies: shareholders, customers, associates, creditors and communities.

Progress in Serving Our Customers

As a sales and service organization in an industry with few unique products, we recognize that it is the quality of our service to customers that sets us apart from our competitors. At all times, we strive for a level of quality that exceeds our customers' highest expectations for precise, timely and responsive service. Our continuing focus on quality is particularly important in a financial services industry characterized by greater economic uncertainty, heightened innovation in financial markets, deregulation and broadening competition. We infuse quality into the total customer relationship—by providing a comprehensive array of financial and operating services; by anticipating customers' needs and developing new and sophisticated products and services to meet those needs; and by dealing with our customers on a relationship basis, a point of view that considers transactions not as single, unrelated events, but as steps in building long-term customer relationships.

This approach has enabled us to excel in meeting the total financial services needs of both the institutional and community markets.

Institutional Financial Services

The institutional market consists primarily of large corporations (those with annual sales of more than $125 million) and financial institutions.

Credit Products. Mellon ranks among the 10 largest institutional market lenders in the United States. Our share of the vast domestic commercial and industrial loan business exceeded 3 percent, a record level, towards the close of 1985. With our national

Progress in serving our customers: Meeting customer needs means supplying customers with a full array of high-quality financial products and services.

New York City-based NYNEX Corporation, which provides communication and information products and services for the Northeast region of the United States, uses Mellon's Master Trust product to administer its multibillion dollar pension fund. In addition, NYNEX utilizes Mellon's cash management products, including a lockbox for collecting payments to its New England Telephone subsidiary. Overlooking Manhattan from Brooklyn Heights are John Geistl, Mellon's Master Trust relationship officer for NYNEX, Joe Clines, NYNEX assistant director and Henry Voorhees of Mellon's Global Cash Management Division.

distribution system now largely in place, we are devoting substantial resources to building the skills of our relationship officers and pursuing additional attractive customer and product segments in the institutional market.

Trust and Investment Products. One of our flagship trust and investment products is Master Trust/Custody, through which we help institutional sponsors to administer employee benefit plans, endowments and foundations and to monitor the investment performance of their investment advisors. Master Trust/Custody assets continued to expand rapidly, to $53 billion. We added to our base of Master Trust customers and, during 1985, opened a Master Trust representative office in San Francisco.

The highly disciplined investment approach we have been following in our equity and actively managed fixed income investments continued to produce exceptional investment performance in 1985. In the passively managed fixed income area, the financial markets expressed an increased interest in bond-indexed portfolios and, at year-end, Mellon's was one of the larger pools of bond-indexed funds in the country.

The investment services provided by our four specialized investment entities continued to be received favorably. Assets under management at Mellon-Pictet International Management, Limited, our London-based joint venture that provides international investment expertise to pension funds, increased sharply. Assets at Mellon Capital Management, our San Francisco affiliate that provides passive equity management services, more than tripled. Assets under management at Mellon Real Estate Investment Management Corporation in New York grew significantly. Boston-based Franklin Portfolio Associates, Inc., which has produced excellent investment results in its active investment management services, doubled its number of pension fund clients.

Cash Management Products. We are consistently ranked as a premier supplier of cash management products and services—a particularly important element in reinforcing our long-term relationships with customers. We are a long-time provider of lockbox services, one of 50 cash management products we offer. By the end of 1985, the number of sites for our new national lockbox network had expanded to eight Mellon owned and operated facilities, and volume had increased significantly. Cash management has evolved to the point where the need for analytical tools has become increasingly important. Among the products we have developed to meet this need is a microcomputer system that enables customers to perform analyses of cash management information from all of their banks. This product has been received enthusiastically by the marketplace.

Capital Markets Products. There are several dimensions to our capital markets business. A traditional emphasis has been to provide funding for a significant portion of the Corporation's loans and investments. A newer focus is to offer corporate treasurers the new and sophisticated techniques, such as interest rate swaps, that are increasingly required in managing financing costs. We also market securities to individual and institutional investors. We originate some of these securities—certain housing and

Progress in serving our customers: Mellon provides a wide range of electronically-based products, including CashStream, one of the largest shared electronic banking machine systems in the United States.

In 1985, CashStream cardholders were able to begin using their cards to pay for purchases at many Mobil gas stations in Delaware, New Jersey and Pennsylvania. The benefit is twofold: Mobil receives payment in a timely manner with reduced processing costs, and customers enjoy the convenience of another payment alternative. "Filling up" at a Mobil station in Green Tree, Pa., are Harry Hritsko of Mellon's Technology Products Department (L) and Ronald Cook, Pennsylvania area manager for Mobil.

other tax-free municipal bond issues—as part of bond underwriting groups in which we at times act as lead underwriter. During the year, we increased significantly our participation in these transactions.

Community Financial Services

The community financial services market includes consumers, small businesses and middle market companies.

Serving the Middle Market. We serve the large and expanding middle market (generally firms with annual sales between $5 million and $125 million) through banking offices in Delaware and Pennsylvania, and through a nationwide network of representative offices. In 1985, we added middle market representative offices in San Francisco and northern New Jersey to this network, which also includes offices in Atlanta, Baltimore, Chicago, Dallas, Los Angeles and New York.

Serving Small Business. We have long been a major supplier of financial products and services to small businesses in Delaware and Pennsylvania. At times, we apply our lending expertise to making possible the completion of transactions that might not match traditional lending criteria but may be solid, creditworthy opportunities if government or other sources of support can be worked into the transaction. We are a leading lender under Small Business Administration programs and, during 1985, Mellon was appointed a "preferred" lender of SBA loans.

Serving Consumers. We are committed to meeting the total financial services needs of the individual. We offer a complete line of banking, personal trust, mortgage and consumer finance products, and at all times strive to provide high-quality service that is caring, precise, efficient and convenient. We serve individuals through 316 banking offices in Delaware and Pennsylvania, and 147 consumer finance, mortgage, and trust and investment offices in 19 states. In an effort to make our services available to as many people as possible, we are building our presence throughout Delaware and Pennsylvania. In 1985, Mellon Bank (Central) completed its merger with The First National Bank of Mapleton, Mapleton Depot, and Mellon Bank (North) signed an agreement to purchase a branch of a savings and loan association in Erie County.

We continue to broaden the scope of products we offer to consumers. In 1985, we introduced our Personal Credit Line product, a revolving line of credit that can be accessed through checking and used for whatever purpose the borrower chooses. Other products introduced in 1985 include a precious metals trading account that allows customers to either invest in bullion or purchase gold and silver coins, and a self-directed Individual Retirement Account through which customers can choose among numerous investment options.

We are a leader in providing high-quality electronic banking products and services. We are a principal member and part owner of CIRRUS, a national electronic banking machine network with more than 11,000 automated teller machines throughout the United States and Canada. Our CashStream™ network is among the largest regional shared electronic banking machine systems in the United States, with 166 member financial institutions and more than 1,600 electronic banking machines in Delaware,

Progress through our associates: We combine the skills of our associates with technology to increase productivity and service quality.

Branch office automation was one of many systems integrations completed in 1985 at Mellon Bank (DE) and Mellon Bank (East). It has led to more efficient data entry and faster availability of information on customers' accounts. Branch office automation involved a major training effort, as tellers learned to use new computer terminals for the automated processing of customer transactions. At a teller training facility in Mellon's new human resources development center, teller trainer Jim Mulkerin instructs teller Jennifer Fulton in the use of an automated teller station.

Maryland, New Jersey, Pennsylvania and West Virginia. Cardholders can withdraw cash at any CashStream banking machine and make deposits at many of them. Through CashStream retail payment terminals—known as point-of-sale or POS terminals—CashStream cards can be used to pay for retail purchases. In 1985, Mobil Oil installed CashStream POS terminals at many of its gasoline stations in Delaware, New Jersey and Pennsylvania. About 350 Mobil stations will participate in this program by the end of 1986. Other POS devices were installed in retail and food stores, and additional Pennsylvania state liquor stores were added to a pilot POS program.

Serving Our Communities. We continue to take a strong interest in the ongoing economic, social and cultural vitality of communities we serve. In 1985, for example, we signed a long-term agreement to lease Philadelphia's historic Lit Brothers Building, capping a lengthy effort by Philadelphians to preserve the popular 19th century structure. This is but a single example among hundreds of actions undertaken to better our communities.

A Top Priority. At Mellon, the customer is the focus of our efforts, the starting point for our decisions and actions. Meeting the needs of all our customers—from the largest corporation to the individual depositor—remains a top priority.

Progress Through Our Associates

We recognize that our potential for success rests with—actually within—each Mellon associate. A mutual commitment exists between the Corporation and Mellon associates: we strive to be an outstanding employer in every way and, in turn, expect each associate to provide Mellon with his or her best effort. The Corporation and its associates have built a workplace that encourages ideas and communication, rewards performance, emphasizes fair and equal treatment, and builds confidence and competence.

Development. In 1985, we completed construction of a new human resources development center. We have based in this facility the full scope of our training activities, which we believe are indispensable to the growth of our people and our organization. We offer more than 100 in-house training programs designed to provide all associates with the skills required to meet the needs of our customers and to advance in their careers.

We have set in motion a new performance planning and appraisal system whereby associates and their managers work together to develop specific, mutually agreed-upon goals. Through this program—which was implemented in many areas of the Corporation in 1985 and will be in place Corporate-wide by the end of 1987—associates better understand their roles, and managers and associates commit themselves to meeting clearly-defined objectives.

Compensation. We continue an aggressive compensation program that enables us to attract and retain the caliber of individual necessary to maintain Mellon's strength. We regularly examine our compensation program to ensure competitiveness with the

Progress through our associates: The ideas of people are critical to our success.

Mellon values the ideas of its associates. One way we put those ideas to use is through associates' participation in Quality Circles, a program in which they meet regularly to identify and resolve work-related problems. The efforts of 900 participating associates have resulted in a savings of more than $1 million over the past four years. Pictured are (clockwise from bottom left) members of the "PLUS" Quality Circle: Stewart Emore, Lisa Donovan, Arthur Weeks, Maria Balouris, John Shope, Dennis Bucher and Carolyn Byrne.

financial services marketplace. We also offer excellent benefits, with many associates enjoying participation in a flexible compensation program that is recognized as being among the most comprehensive in the United States.

Communication. We are careful to take our associates' views into account in running our businesses, and seek open communication and cooperation between manager and associate. We also seek associates' input on a formal basis through attitude surveys aimed at uncovering what our associates feel is wrong—and right—about Mellon. We react promptly to the surveys' findings, implementing associates' suggestions and addressing their concerns.

It is our firm belief that the talent and creativity of our associates is as important to enhancing profit as are market penetration and product profitability. About 900 Mellon associates participate in Quality Circles—small groups of associates meeting regularly on work time to identify and solve work-related problems. Quality Circles' suggestions resulted in approximately $400,000 in savings in 1985, for a cumulative savings of over $1 million since the program began four years ago. The program's other benefits include improved service quality, increasingly efficient operations and forestalling of future problems. Also in 1985, many associates at Mellon Bank (East) and Mellon Bank (DE) participated in a quality assurance program that led to improvements in customer service in these banks' markets.

Productivity. We give our people the tools they need to perform tasks productively and to make their jobs as fulfilling as possible. For example, this year's completion of the integration of many of the operating systems of Mellon Bank (DE) and Mellon Bank (East) with those of the rest of the Corporation's domestic banks put new automation at the hands of associates. The automation of many teller functions makes tellers' work easier and allows them to better meet customers' needs for quick and accurate information and personal service. Similar productivity benefits have evolved in many other areas in which systems integration has taken place. At Mellon Bank in Pittsburgh, we have shifted certain time-consuming functions—such as loan processing and administration—from branches to specialized offices so that branch associates can focus on sales and service. We are also testing an information system for customer representatives, complementing the automation of our teller stations.

Community Involvement. An aspect of associate dedication that does not appear on the balance sheet is our associates' involvement in their communities—an involvement we heartily encourage. Each year, associates contribute more than 200,000 hours of volunteer time to community activities.

Focus on Associates. Our focus on associates—their needs, their capabilities—is integral to the Mellon business philosophy. In 1985, as in years past, Mellon's commitment to its people was matched by a like commitment to the organization by our associates, who distinguished themselves with consistently outstanding performance. As we go forward, such effort will be critical to successfully negotiating the challenging course that lies ahead.

Mellon Bank Corporation (and its subsidiaries)

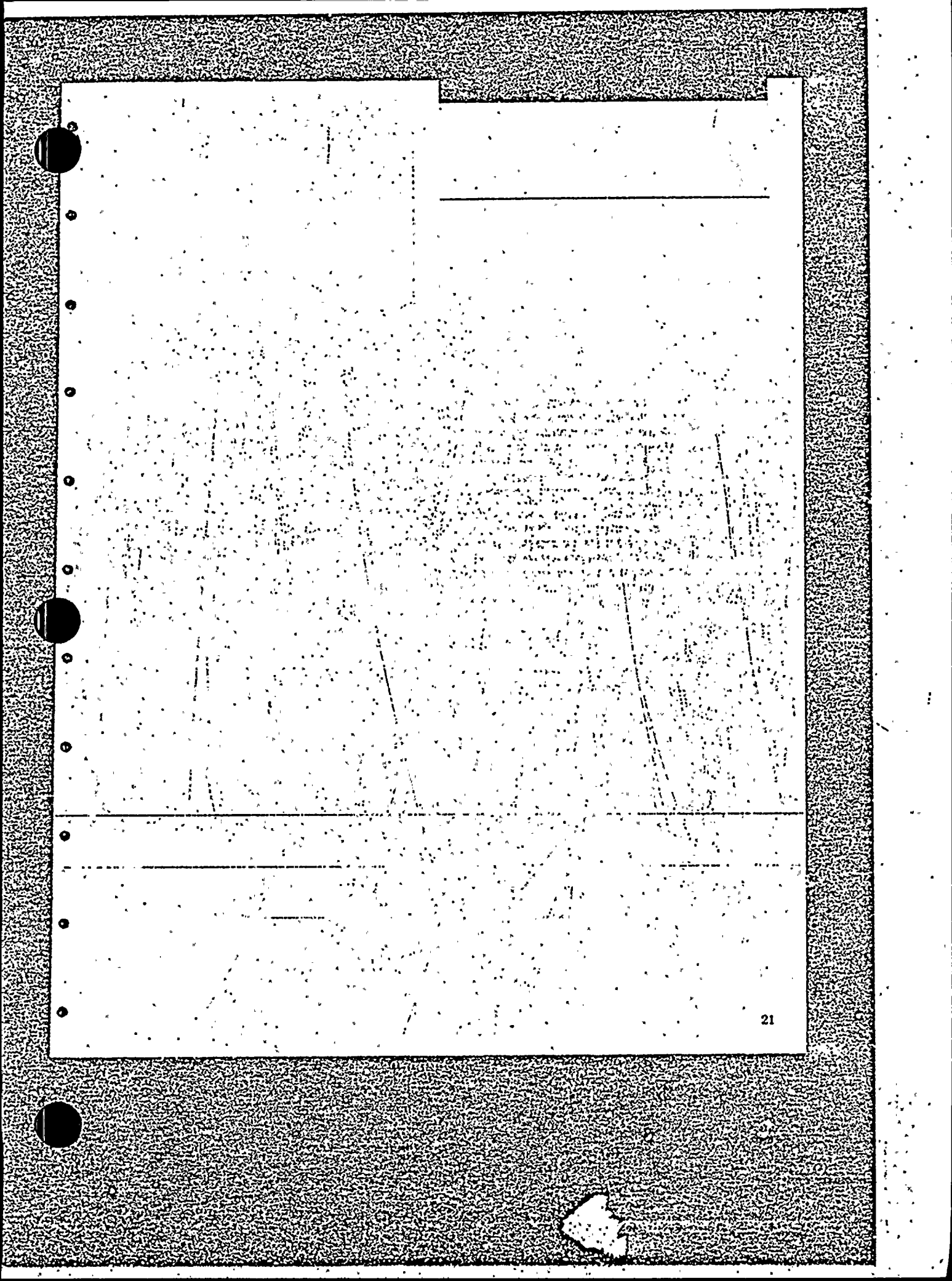
Financial Summary

(dollar amounts in millions, except per share amounts)	1980	1981	1982	1983	1984	1985
Year ended December 31						
Net credit revenue	$ 327.1	$ 366.4	$ 445.6	$ 614.9	$ 747.1	$ 872.4
Service revenue	84.4	103.0	130.7	230.5	302.1	365.1
Trading revenue	7.2	1.3	20.7	11.8	5.5	22.6
Gains on sale of investment securities*	(3.2)	(19.4)	(15.4)	10.8	3.6	92.5
Other revenue	10.7	10.8	12.3	34.3	25.7	12.4
Provision for possible credit losses	28.5	37.0	68.1	52.2	116.7	148.3
Operating expense	257.6	300.9	381.9	631.8	815.4	965.6
Net income	$ 112.5	$ 115.5	$ 134.4	$ 183.8	$ 158.5	$ 201.7
Net income:						
Domestic	$ 81.6	$ 68.6	$ 91.3	$ 150.7	$ 159.2	$ 197.6
International	30.9	46.9	43.1	33.1	(.7)	4.1
Per common share						
Net income	$ 5.73	$ 5.88	$ 6.83	$ 7.44	$ 5.64	$ 7.13
Dividends	1.89	2.09	2.24	2.44	2.60	2.68
Average balances						
Money market investments	$ 3,435	$ 4,355	$ 4,183	$ 4,298	$ 3,634	$ 3,073
Investment securities	974	946	1,298	1,672	1,378	2,113
Loans and lease finance assets	7,573	8,759	10,886	13,935	17,347	20,083
Interest-earning assets	12,066	14,218	16,653	20,345	22,821	25,687
Reserve for possible credit losses	124	123	154	220	273	331
Total assets	14,625	16,890	19,539	24,232	27,601	30,246
Deposits	9,770	11,166	12,280	14,579	17,009	18,250
Notes and debentures	426	428	417	565	613	1,038
Preferred stock	—	—	—	48	89	93
Common shareholders' equity	860	932	1,018	1,253	1,438	1,562
Ratios *(based on balance sheet averages)*						
Return on assets**	.77%	.68%	.69%	.74%	.54%	.63%
Assets to common shareholders' equity	17.0	18.1	19.2	19.3	19.2	19.4
Return on common shareholders' equity**	13.1 %	12.4 %	13.2 %	14.3 %	10.3 %	12.3 %
Net rate on interest-earning assets computed on a fully taxable equivalent basis	3.24%	3.19%	3.29%	3.57%	3.30%	3.81%
Ratios *(based on year-end amounts)*						
Primary capital as a percentage of total assets	6.27%	5.98%	6.04%	6.09%	6.64%	6.62%
Total capital as a percentage of total assets	8.42%	7.54%	6.83%	7.28%	7.71%	7.92%

**Income tax (benefit) expense applicable to gains on sale of investment securities were as follows: 1980-($1.5) million; 1981-($8.9) million; 1982-$7.1 million; 1983-$5.0 million; 1984-$1.3 million; and 1985-$42.5 million.*

***Net of dividends on preferred stock.*

The Corporation acquired through merger: The Girard Company and Mortgage & Trust, Inc. in April 1983, CCB Bancorp, Inc. in September 1983 and Northwest Pennsylvania Corp. in April 1984 ("the mergers"). The mergers were accounted for under the purchase accounting method. The results of operations, assets and liabilities of these companies were included in the Corporation's results from their respective dates of acquisition. To provide comparability, the effect of significant mergers in 1983 and 1984 is shown separately in the following tables.



Earnings Performance

Overview

Mellon Bank Corporation achieved record net income of $261.7 million for 1985, an increase of $43.2 million, or 27%, from 1984. Net income per common share rose to $7.13, a 26% increase from the $5.64 earned in 1984. Return on assets improved to .63%, up 9 basis points from 1984. Return on common shareholders' equity increased to 12.3%, up from 10.3% in 1984.

For analytical purposes, net income has been segregated into three components—net income from core businesses, trading revenue and gains on the sale of investment securities, and nonrecurring items. Net income from core businesses has been defined to include net credit revenue, service revenue, recurring operating expense and the portion of the credit loss provision necessary to cover net credit losses and loan growth during the period. Trading revenue consists of trading account profits and commissions, foreign exchange trading gains and gains on the sale of mortgages and mortgage-backed securities, net of market revaluation. Nonrecurring items include the effect of cash-basis loans, the portion of the credit loss provision that resulted in an increase in the reserve ratio, and other specified items of revenue and expense. This presentation, in management's judgment, improves the analysis of changes in net income from the Corporation's core businesses. It should be recognized, however, that there are no clear guidelines for separating nonrecurring from recurring items. Accordingly, other bank holding companies that provide a similar division may utilize somewhat different classifications.

The impact of these items on the increase in net income per common share in 1985 from the prior year has been summarized in the table below.

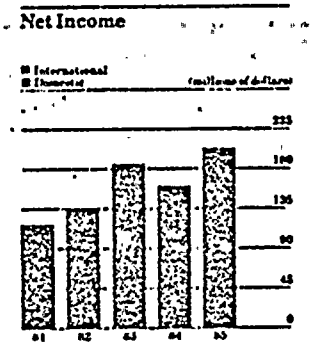
Net income from core businesses increased by $17.2 million, or [illegible]%, in 1985. Core net credit revenue rose $118.9 million, or 15%, while service revenue increased by $63.0 million, or 21%. In order to support this revenue growth, recurring operating expense increased by $126.2 million, or 15%. Core earnings also reflected a 16% increase in the provision for possible credit losses compared with 1984.

Higher trading revenue resulted in an increase in net income of $9.2 million, or $.34 per common share, while gains on the sale of investment securities contributed $47.7 million, or $1.78 per common share, to the rise in earnings. These favorable effects were partially offset by significant changes in nonrecurring revenue and expense. Nonrecurring expense increased significantly in 1985 while nonrecurring revenue was lower than in 1984. The Corporation also increased its reserve ratio during 1985.

As shown in the chart below, net income from international operations for 1985 increased by $4.8 million, compared with 1984, but continues to be down considerably from 1983 and prior years. The decrease in earnings and return on assets in 1984, as compared with 1983, was primarily attributable to a substantial increase in the provision for possible credit losses and lower earnings from international operations in 1984.

Changes in net income per common share

1984 Net income per common share		$ 5.64
Increase/(decrease) attributable to:		
Core businesses:		
Net credit revenue	2.13	
Service revenue	1.27	
Provision for possible credit losses	(.36)	
Operating expense and other	(2.51)	
Total		.53
Trading revenue and gains on sale of investment securities		2.12
Nonrecurring items:		
Effect of cash-basis loans	.13	
Nonrecurring revenue	(.38)	
Provision for possible credit losses	(.27)	
Nonrecurring operating expense	(.64)	
Total		(1.16)
1985 Net income per common share		$ 7.13



Net credit revenue

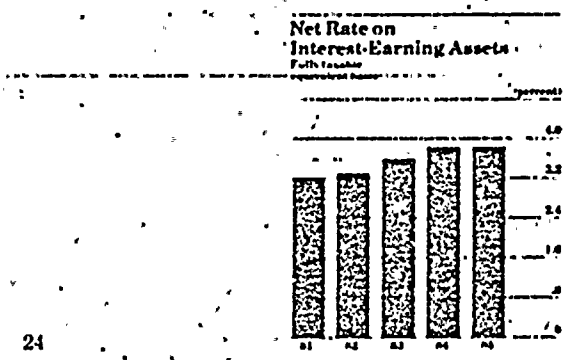
(dollar amounts in millions)	1983	1984/1983 Increase/(decrease) From mergers	1984/1983 Increase/(decrease) Excluding mergers	1984	1985/1984 Increase/ (decrease)	1985
Interest revenue	$2,170.2	$209.5	$270.3	$2,650.0	$ (7.7)	$2,642.3
Loan fees	58.2	4.4	.6	63.2	23.9	87.1
Interest expense	1,613.5	140.6	212.0	1,966.1	(109.1)	1,857.0
Net credit revenue	614.9	73.3	58.9	747.1	125.3	872.4
Taxable equivalent increments to net credit revenue	110.4	15.6	(6.6)	119.4	(13.1)	106.3
Net credit revenue (fully taxable equivalent basis)	$ 725.3	$ 88.9	$ 52.3	$ 866.5	$ 112.2	$ 978.7
Net rate on interest-earning assets	3.57%			3.80%		3.81%

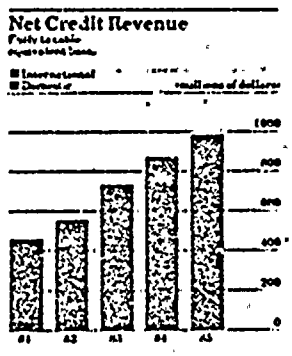
Net credit revenue increased in 1985 primarily as a result of average earning asset growth of 12%. Loans and leases increased on average by $2.7 billion, or 16%, from the prior year, primarily reflecting growth in the Corporation's domestic loan portfolio. Net credit revenue in 1985 was also enhanced by higher core fund levels and significant purchases of U.S. Treasury and agency securities that were funded principally by repurchase agreements. Spreads on these securities were significantly wider during 1985, reflecting a sharp decline in the cost of supporting funds.

These favorable effects were offset partially by the decreased benefit of low cost core deposits in the lower interest rate environment of 1985 as well as a shift in the mix of the commercial loan portfolio from prime-sensitive loans to cost-plus loans which typically have narrower spreads. Spreads on prime-sensitive loans were also narrower in 1985.

Cash-basis loans and leases resulted in a reduction in net credit revenue of $22.8 million in 1985. This compared favorably with 1984 when net credit revenue was reduced by $29.2 million as a result of cash-basis loans and leases. This improvement was due to the receipt of interest payments on international cash-basis loans.

As shown in the chart below, net credit revenue from domestic operations increased $78.9 million, or 10%, from 1984, while net credit revenue from international operations increased $33.3 million, or 30%, for the same period. A discussion of international net credit revenue appears on page 37. Domestic and international net credit revenue, average balances and rates are presented on pages 68 and 69. Additional information on interest-earning assets, sources of funds, maturities of loans, investment securities and deposits, and the repricing and interest rate sensitivity of assets and liabilities begins on page 28





Service and other revenue

(in thousands)	1983	1984/1983 Increase/(decrease) From mergers	1984/1983 Increase/(decrease) Excluding mergers	1984	1985/1984 Increase/ (decrease)	1985
Service revenue:						
Letters of credit and acceptance financing fees	$ 19,423	$ 818	$ 3,862	$ 24,103	$ 5,976	$ 30,079
Charge service fees	21,487	3,207	6,233	30,930	2,812	33,742
Data processing fees	38,058	1,192	3,789	43,049	7,290	50,339
Cash management fees and deposit transaction charges	30,186	5,762	13,864	49,812	15,872	65,684
Mortgage servicing fees	20,682	3,229	1,896	25,807	4,734	30,541
Trust and Investment Department fees	73,831	10,585	11,347	95,763	21,032	116,795
Other	26,813	2,927	2,906	32,646	5,290	37,936
Total service revenue	230,480	27,720	43,810	302,110	63,006	365,116
Trading revenue:						
Trading account profits and commissions	7,826	—	(1,840)	5,986	9,951	15,937
Gains on sale of mortgages and mortgage-backed securities (net of market revaluation)	(325)	(543)	(701)	(1,569)	2,795	1,226
Foreign exchange gains	4,300	855	(4,076)	1,079	4,353	5,432
Total trading revenue	11,801	312	(6,637)	5,476	17,099	22,575
Gains on sale of investment securities	10,797	1,355	(9,196)	3,956	88,555	92,511
Other revenue	34,318	2,279	(10,907)	25,690	(13,268)	12,422
Total service and other revenue	$287,396	$32,266	$ 17,170	$336,832	$155,792	$492,624

Service revenue for 1985 rose $63.0 million, or 21%, from the prior year. The growth in Trust and Investment Department fees was due primarily to a higher volume of services provided to employee benefit funds and institutions, as well as increases in Master Trust/Custody and related services. Service revenue also grew as a result of increased data processing services to a greater number of financial institutions in a wider geographic region, an increase in the volume of standby letters of credit and higher cash management fees and deposit transaction charges. In 1985, cash management and other commercial fees amounted to $45.2 million, up $14.1 million, or 45%, from 1984. This increase resulted from growth in the volume of regional lockbox and other cash management services, an increase in the prices charged for these services, as well as an increase in the number of customers who paid fees in lieu of maintaining interest-free balances for cash management services. Transaction charges on consumer deposit accounts amounted to $29.5 million in 1985, compared with $18.7 million in 1984.

Trading revenue contributed $12.2 million after-tax, or $.45 per common share, to net income in 1985 compared with $3.0 million after-tax, or $.11 per common share, in 1984. Market conditions provided trading opportunities on which the Corporation capitalized during 1985. Gains on the sale of investment securities contributed $50.0 million after-tax, or $1.86 per common share, to net income in 1985 compared with $2.3 million after-tax, or $.08 per common share, in 1984. These gains were primarily attributable to the sharp decline in interest rates during 1985.

Nonrecurring revenue in 1985, principally gains on the sale of securities previously acquired in connection with loan settlements and other equity securities, amounted to $7.7 million after-tax, or $.29 per common share. Nonrecurring revenue items in 1984 included a $2.5 million after-tax gain on the sale of an office building in Delaware, a $2.8 million after-tax settlement of claims with the government of Iran, and other items of nonrecurring revenue which collectively totalled $18.0 million after-tax, or $.67 per common share.

Operating expense and employment data

(dollar amounts in thousands)	1983	1984/1983 Increase(decrease) From mergers	1984/1983 Increase(decrease) Excluding mergers	1984	1985/1984 Increase/ (decrease)	1985
Staff expense	$349,772	$43,842	$ 48,242	$441,856	$ 67,499	$509,355
Equipment expense	48,091	6,599	3,782	58,472	9,733	68,205
Net occupancy expense	46,484	7,556	43,495	97,535	12,391	109,926
Shares, capital and franchise taxes	13,374	1,404	(1,147)	13,631	852	14,483
Other expense	174,078	22,839	6,969	203,886	59,754	263,640
Total operating expense	$631,799	$82,240	$101,341	$815,380	$150,229	$965,609
Average equivalent employees	11,939	1,847	974	14,760	1,047	15,807

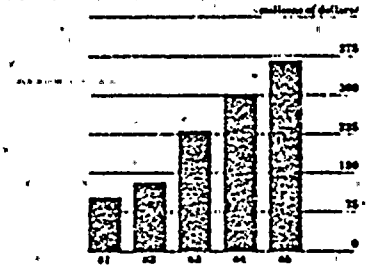
Operating expense increased $150.2 million in 1985 from the prior year. Excluding the effect of nonrecurring expense and the effect of the April 1984 merger with Northwest Pennsylvania Corp., the increase was $120.2 million, or 15%. The increase in staff expense reflected higher salary levels and, excluding the effect of the Northwest merger, an increase of 889 average full-time equivalent employees from the prior year. Staff has been expanded to support a greater volume of revenue-producing activities and to increase business development efforts related principally to regional lockbox and other cash management services, Master Trust/Custody and related services, and mortgage banking operations. The increase in net occupancy expense in 1985 primarily reflects additional leased space at a number of locations and higher real estate taxes. The rise in other expense included certain nonrecurring expense, higher amortization of intangibles, as well as increases in various categories of expense including supplies, telephone, professional, consulting and other purchased services.

Goodwill, amounting to $89 million at December 31, 1985, is being amortized over the remaining estimated benefit period which approximates 16 years on a weighted average basis. Goodwill amortization, which has no tax effect, amounted to $5.5 million in 1985, compared with $5.1 million in 1984 and $2.9 million in 1983.

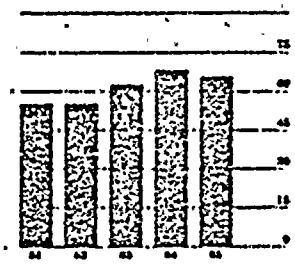
Capitalized mortgage servicing portfolio costs, which represent the value of mortgage servicing rights acquired through mergers and other acquisitions of mortgage servicing portfolios, amounted to $71 million at December 31, 1985. These costs are amortized over the remaining estimated benefit period which approximates six years on a weighted average basis. Amortization of these costs amounted to $10.3 million in 1985, compared with $6.7 million in 1984 and $5.3 million in 1983.

Nonrecurring expense in 1985 was $23.3 million. On an after-tax basis, this amounted to $15.3 million, or $.57 per common share. This amount consisted principally of write-downs in the carrying value of certain equity investments and other real estate acquired, as well as expense incurred in connection with an early retirement program which was partially offset by the favorable effects of changes in pension plan actuarial assumptions. The early retirement program was adopted to reduce staff expense in future years.

Service Revenue



Operating Expense Ratio



Organizational Performance

In order to provide additional analytical insight into the Corporation's financial performance for 1985, we present the following organizational performance review. The data and discussion that follow have been prepared on a management reporting basis and include certain allocations among business units that have been made to make the information and discussion more meaningful.

	1984			1985		
(dollar amounts in millions)	Average assets	Net income	Return on assets*	Average assets	Net income	Return on assets*
Mellon Bank	$21,702	$ 92	.42%	$23,311	$161	.69%
Mellon Bank (East):						
Mellon Bank (East)	3,762	7	.19	3,997	(3)	(.07)
Purchase accounting effect	(23)	15	—	(13)	13	—
Total Mellon Bank (East)	3,739	22	.59	3,984	10	.24
Community banks:**						
Community banks	1,665	14	.85	2,211	11	.50
Purchase accounting effect	3	5	—	9	2	—
Total community banks	1,668	19	1.16	2,220	13	.59
Total banking subsidiaries	27,109	133	.49	29,515	184	.62
Mortgage Banking	805	11	1.39	1,193	3	.29
Leasing	255	6	2.49	368	6	1.61
Commercial and Consumer Finance	363	4	1.21	413	6	1.50
Parent and other	(931)	5	—	(1,135)	4	—
Total Mellon Bank Corporation (and its subsidiaries)	$27,601	$159	.54%	$30,246	$202	.63%

*Calculated using dollar amounts in thousands and net income applicable to common stock.
**Includes Mellon Bank (Central), Mellon Bank (North) and Mellon Bank (DE).

The increase in the Corporation's net income in 1985 was primarily the result of growth in the earnings of Mellon Bank. Improvement in core earnings and higher gains on the sale of investment securities in 1985 were partially offset by decreases in nonrecurring revenue, increases in nonrecurring expense and an increase in the bank's credit loss reserve ratio compared with the prior year.

Net income for Mellon Bank (East) in 1985 reflected only nominal growth in net credit revenue. A 17% increase in average loan levels was almost completely offset by narrower spreads on interest-earning assets as yields on variable-rate assets fell more quickly than the cost of supporting funds during 1985. Service revenue showed modest improvement in 1985. The rise in net credit and service revenue was more than offset by the effect of higher credit losses, an increase in the reserve ratio and higher operating expense.

Net income for the Corporation's community banks included modest increases in net income at Mellon Bank (Central) and Mellon Bank (North) during 1985. This improvement was more than offset by a decline in net income at Mellon Bank (DE) in 1985 as a result of operating expense associated with the transfer of the Corporation's credit card operations, higher credit losses and a significant increase in the reserve ratio at Mellon Bank (DE).

The decrease in the earnings of the mortgage banking subsidiaries in 1985 was primarily attributable to higher credit losses on loans to residential builders, a nonrecurring write-off of capitalized mortgage servicing portfolio costs and a decline in nonrecurring revenue compared with 1984.

Balance Sheet Review

Average balances (dollar amounts in millions)	1983	1984/1983 Increase/(decrease) From mergers	1984/1983 Increase/(decrease) Excluding mergers	1984	1985/1984 Increase/ (decrease)	1985
Interest-earning assets						
Money market investments	$ 4,298	$ 76	$ (740)	$ 3,634	$ (562)	$ 3,072
Trading account securities	440	—	22	462	(62)	400
Investment securities	1,672	252	(546)	1,378	735	2,113
Loans and lease finance assets	13,935	1,154	2,258	17,347	2,735	20,082
Total	$20,345	$1,482	$ 994	$22,821	$2,846	$25,667
Funds supporting interest-earning assets (available basis)						
Core deposits:						
Demand	$ 1,956	$ 310	$ 6	$ 2,272	$ 178	$ 2,450
Savings accounts	877	182	(107)	952	(64)	888
Money market deposit accounts	1,615	308	505	2,428	913	3,341
Retail savings certificates	2,058	535	220	2,813	92	2,905
Negotiable certificates of deposit with maturities in excess of one year	543	7	962	1,512	(376)	1,136
Other time deposits	308	24	511	843	(26)	817
Total core deposits	7,357	1,366	2,097	10,820	717	11,537
Purchased funds:						
Negotiable certificates of deposit with maturities less than or equal to one year	2,428	64	(969)	1,523	631	2,154
Foreign office deposits	3,275	12	(303)	2,984	(12)	2,972
Short-term borrowed funds	5,716	181	(199)	5,698	1,038	6,736
Total purchased funds	11,419	257	(1,471)	10,205	1,657	11,862
Notes and debentures	565	46	2	613	445	1,058
All other	1,004	(187)	366	1,183	27	1,210
Total	$20,345	$1,482	$ 994	$22,821	$2,846	$25,667
Average domestic purchased funds ratio	39.8%			29.0%		35.8%

Average earning assets grew by $2.8 billion, or 12%, during 1985. Average levels of loans and lease finance assets rose by $2.7 billion, or 16%. Mellon added significantly to its holdings of investment securities in 1985, principally U.S. Treasury and agency securities which increased on average by $716 million. These securities purchases were funded primarily by overnight repurchase agreements.

The growth in average loans was supported by purchased funds, core deposits and a reduction in money market investments.

The increase in average notes and debentures was primarily attributable to the issuance by a subsidiary of the Corporation of $100 million in 11.75% Guaranteed Debentures and $150 million in Floating Rate Extendible Notes in the first half of 1985 and the issuance in November 1984 by Mellon Bank of $250 million in Floating Rate Subordinated Capital Notes.

Since 1983, the Corporation's liquidity has been enhanced by increases in core deposit levels as a result of mergers and growth in money market deposit accounts and retail savings certificates. In 1984, the lengthening of the maturities of negotiable certificates of deposit also contributed to the higher core deposit levels. The growth in money market deposit accounts continued during 1985 but was partially offset as many of the negotiable certificates of deposit that were issued during 1984 approached maturity. The Corporation's domestic purchased funds ratio, which indicates reliance on purchased funds, has decreased since 1983 and continues to compare favorably to other major bank holding companies.

Maturity distribution of investment securities

(dollar amounts in millions)	December 31, 1985 Book value: Within 1 year Amt.	Yld.	1-5 years Amt.	Yld.	5-10 years Amt.	Yld.	After 10 years Amt.	Yld.	Total	Total market value	Average maturity at year-end (in years)
U.S. Treasury and agency securities	$ 71	8.98%	$786	9.29%	$ 985	9.15%	$ 7	8.91%	$1,849	$1,890	4.41
Obligations of states and political subdivisions	415	12.33	71	11.31	184	12.90	449	15.42	1,119	1,108	9.24
Other securities:											
Bonds, notes and debentures	3	8.23%	30	9.90%	8	11.69%	26	10.66%	67	64	9.81
Stock of Federal Reserve Bank	—		—		—		—		20	20	
Other	—		—		—		—		5	8	
Total	$489		$887		$1,177		$482		$3,060	$3,088	

Note: Rates for obligations of states and political subdivisions, and bonds, notes and debentures, are calculated on a fully taxable equivalent basis using a 46% federal income tax rate. Fully taxable equivalent increments to interest revenue are $24.0 million for maturity due within one year; $4.5 million for maturity after one but within five years; $11.6 million for maturity after five but within 10 years; and $32.3 million for maturity after 10 years.

Maturity distribution of loans

(in millions)	December 31, 1985 Within 1 year**	1-5 years	After 5 years	Total
Domestic:*				
Commercial and financial	$ 7,340	$2,642	$1,611	$11,593
Real estate	1,503	915	507	2,925
Total domestic	8,843	3,557	2,118	14,518
International	2,149	1,206	454	3,809
Total	$10,992	$4,763	$2,572	$18,327

*Excludes consumer credit and consumer mortgages.
**Includes demand loans and loans with no stated maturity.

Maturity distribution of domestic time deposits

(in millions)	December 31, 1985 Within 3 months	3-6 months	6-12 months	After 1 year	Total
Negotiable certificates of deposit in denominations of $100,000 or greater	$1,472	$486	$401	$1,036	$3,395
Negotiable certificates of deposit in denominations of less than $100,000	2	—	—	—	2
Total negotiable certificates of deposit	1,474	486	401	1,036	3,397
Other time deposits in denominations of $100,000 or greater	123	106	96	180	505
Other time deposits in denominations of less than $100,000	14	—	11	—	25
Total other time deposits	137	106	107	180	530
Total	$1,611	$592	$508	$1,216	$3,927

Interest rate sensitivity

An important factor in the management of the Corporation's balance sheet is interest rate sensitivity. Mellon actively manages its interest rate sensitivity position in order to maintain an appropriate balance between the maturity and the repricing characteristics of its assets and liabilities and to maximize net credit revenue during periods of stable as well as volatile interest rates. It is the Corporation's policy that the cumulative gap position at the one year level, as a percentage of total assets, should not exceed plus or minus 5%. This percentage did not exceed plus or minus 3.50% at the end of any month during 1985.

The interest rate sensitivity table below shows the repricing characteristics of the major categories of Mellon's earning assets and supporting funds at December 31, 1985. The data is based upon contractual maturities and, where applicable, management's assumptions as to the repricing characteristics of certain assets and supporting funds, and includes the impact of financial futures contracts and interest rate swaps.

	December 31, 1985				
(dollar amounts in millions)	0-90 days	91-180 days	181-365 days	Over 1 year and fixed rate	Total
Interest-earning assets					
Money market investments	$ 1,816	$ 170	$ 63	$ 3	$ 2,052
Trading account securities	947	10	—	—	957
Investment securities	37	238	240	2,545	3,060
Loans and lease finance assets	15,453	1,289	575	5,002	22,319
Total	$18,253	$ 1,707	$ 878	$7,550	$28,388
Funds supporting interest-earning assets					
Interest-paying deposits (available basis):					
Demand deposits	$ —	$ —	$ —	$ 524	$ 524
Savings accounts	6	6	11	667	690
Money market deposit accounts	3,773	—	—	—	3,773
Retail savings certificates	818	751	434	897	2,900
Negotiable certificates of deposit	2,287	238	144	630	3,299
Other time deposits	382	103	6	22	513
Foreign office deposits	1,919	171	192	151	2,433
Total interest-paying deposits	9,185	1,269	787	3,091	14,332
Short-term borrowed funds	8,965	102	15	55	9,137
Notes and debentures	620	193	5	327	1,145
Available interest-free demand deposits	—	—	—	2,323	2,323
All other	1,234	(418)	(11)	646	1,451
Total	$20,004	$ 1,146	$ 796	$6,442	$28,388
Interest sensitivity gap	$(1,751)	$ 561	$ 82	$1,108	$ —
Cumulative gap	$ (1,751)	$(1,190)	$(1,108)	$ —	$ —
Cumulative gap as a percentage of total assets			(3.32)%		

Capital and dividends

The maintenance of an adequate level of capital to support business growth is an important element in the Corporation's ability to add to future earnings. Common shareholders' equity increased to $1.6 billion at December 31, 1985, from $1.5 billion at December 31, 1984, and $1.4 billion at December 31, 1983. Earnings retention was primarily responsible for this growth. The Corporation's internal capital growth rate in 1985 was 7.7%, compared with 5.6% in 1984.

The quarterly dividend on common stock was increased to $.67 in 1985, an increase of 3% over 1984. The common stock dividend payout ratio was 38% in 1985, compared with 46% in 1984. The Corporation's long-term targeted payout ratio is 30%.

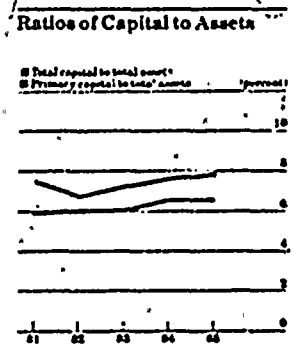
The Corporation's primary and total capital, as defined by the Federal Reserve Board, were strengthened during 1985 by the growth in shareholders' equity and by the substantial increase in the reserve for possible credit losses. Total capital was also improved as a result of the issuance of $100 million in 11.75% Guaranteed Debentures in the first quarter of 1985. The increases in the Corporation's primary and total capital ratios in 1984 reflect the issuance in November 1984 by Mellon Bank of $250 million in Floating Rate Subordinated Capital Notes.

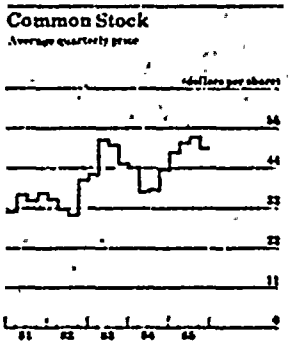
The Federal Reserve Board reviews the level of a bank holding company's intangible assets in assessing its capital adequacy. Federal Reserve Board guidelines state that a bank holding company's aggregate intangible assets may be excessive if they exceed 25% of tangible primary capital. The Corporation's goodwill as a percent of tangible primary capital was 4.28% at December 31, 1985, 4.75% at December 31, 1984, and 4.95% at December 31, 1983. Goodwill plus capitalized mortgage servicing portfolio costs as a percent of tangible primary capital was 7.71% at December 31, 1985, 7.35% at December 31, 1984, and 8.10% at December 31, 1983.

Mellon's primary and total capital ratios, which appear in the following table, were substantially higher than the target ratios of 5.50% for primary capital and 6.00% for total capital that are used by the federal bank regulatory agencies to measure capital adequacy at December 31, 1985.

	1983	1984	1985
Primary capital as a percentage of total assets	6.09%	6.64%	6.62%
Total capital as a percentage of total assets	7.28	7.71	7.92

Note: Primary capital, as defined by the Federal Reserve Board, includes common shareholders' equity, perpetual preferred stock, the reserve for possible credit losses, mandatory convertible debt and minority interest in equity of consolidated subsidiaries. Total capital includes primary capital, limited life preferred stock and long-term debt with an original maturity of at least seven years. The ratios are computed based upon total assets at year-end, as reported, plus the year-end reserve for possible credit losses. Ratios for 1984 and 1983 have been restated to conform with this definition.





Credit Risk and Asset Quality

Credit policy

The Corporation manages credit risk through the establishment and implementation of prudent credit policies and the diversification of the loan and lease portfolios. The credit policies are adopted by the Asset/Liability Committee based upon its evaluation of developments in the political, economic and social environments that could affect lending risks.

Extensions of credit in excess of certain dollar amounts are approved by credit committees staffed by senior officers from the Credit Policy Department and the Corporation's lending and other relationship departments. Other credit extensions are approved either jointly by individual lending officers and Credit Policy officers or by the individual lending officer.

The Corporation assesses the quality of its risk assets and assigns a quality rating to domestic customers and their borrowings, where the Corporation has significant credit exposure, and to commercial borrowers in selected foreign countries. Quality ratings are reviewed at least annually.

The Country Review Committee approves country exposure limits for all foreign countries in which the Corporation's exposure is greater than $10 million.

The Auditing Department, through its Credit Review Division, provides an independent assessment of credit policy and the quality of portfolio assets.

Composition of loan and lease portfolio at year-end

	December 31,				
(In millions)	1981	1982	1983	1984	1985
Domestic operations					
Commercial and industrial	$ 4,134	$ 4,619	$ 5,904	$ 7,676	$ 8,993
Financial institutions	409	768	909	1,331	1,485
Other	291	357	402	870	1,115
Total commercial and financial	4,834	5,744	7,215	9,877	11,593
Commercial construction	431	602	1,137	1,702	2,045
Commercial mortgage	321	420	570	683	880
Consumer mortgage	1,013	1,011	1,288	1,266	1,378
Total real estate	1,765	2,033	2,995	3,651	4,303
Consumer credit	955	907	1,500	2,014	2,227
Lease finance assets	184	198	237	289	387
Total domestic operations	7,738	8,882	11,947	15,831	19,510
International operations					
Commercial and industrial	1,379	1,488	1,915	2,133	2,025
Financial institutions	757	909	1,092	1,203	1,245
Governments and official institutions	190	225	528	453	517
Other	44	59	7	67	22
Total international operations	2,370	2,681	3,542	3,856	3,809
Total loans and lease finance assets, net of unearned discount	$10,108	$11,563	$15,489	$19,687	$22,319

Note: No other concentrations of loans to borrowers engaged in similar activities exceeded 10% of total consolidated loans and lease finance assets at December 31, 1985.

The majority of domestic commercial and financial loans were made to corporate borrowers in the manufacturing, financial services, energy extraction and refining, wholesale and retail trade, service and public utility industries. Loans to companies in the energy extraction business are based upon proven oil and gas or other mineral reserves.

The commercial construction loan portfolio is diversified geographically and by type of project, and generally consists of loans to large and experienced professional developers.

A discussion of the Corporation's international outstandings is presented on pages 38 and 39.

Cash-basis, past due and restructured loans and lease finance assets at year-end

Cash-basis loans and lease finance assets are those where, in the opinion of management, collection of interest is doubtful. Interest accruals are generally discontinued whenever the payment of interest is more than 60 days past due or payment of principal is past due 90 days or more, or sooner in situations where management believes it is appropriate. Bank regulatory agencies generally require that interest accruals be discontinued on commercial loans and lease finance assets when interest or principal is past due 90 days or more. Most large commercial banks follow this practice. If the Corporation were to have adhered strictly to this 90-day requirement, the total of cash-basis, past due and restructured loans and lease finance assets of the Corporation would have been reduced from actual levels by the amounts shown as less than 90 days past due and not restructured in the table below.

Past due loans and lease finance assets are those which are contractually past due 90 days or more but are not on cash-basis. Due to regulatory reporting changes adopted in 1983, included in the past due category are past due consumer loans of $24 million in 1985, $23 million in 1984 and $22 million in 1983. In prior years, these loans were excluded from this category. Restructured loans and lease finance assets include those on which a portion of interest or principal has been forgiven and those made at less than market rates.

(dollar amounts in millions)	December 31, 1981	1982	1983	1984	1985
Domestic operations:					
Cash-basis	$ 63	$195	$246	$310	$382
Past due	—	7	43	24	24
Restructured	63	11	10	—	4
Total	126	213	299	334	410
International operations:					
Cash-basis	46	115	162	213	190
Past due	—	1	42	5	6
Restructured	1	1	36	1	1
Total	47	117	240	219	197
Total cash-basis, past due and restructured	$173	$330	$539	$553	$607
Cash-basis loans and lease finance assets less than 90 days past due and not restructured	$ 11	$ 87	$ 72	$139	$197
Total excluding loans and lease finance assets less than 90 days past due and not restructured	$162	$243	$467	$414	$410
As a percentage of total loans and lease finance assets:					
Total cash-basis, past due and restructured	1.72%	2.85%	3.48%	2.81%	2.72%
Total excluding loans and lease finance assets less than 90 days past due and not restructured	1.61	2.10	3.01	2.10	1.84

Domestic cash-basis loans and leases at December 31, 1985, compared with December 31, 1984, reflect the addition of a large diversified national credit that amounted to $44 million. Loans to commercial and residential builders accounted for the rest of the increase. The Corporation had no significant industry concentrations of domestic cash-basis loans.

Subsequent to the end of 1985, a sharp decline occurred in the price of oil. This could adversely affect the ability of certain domestic and international borrowers to service their obligations to the Corporation.

Foregone interest on cash-basis and restructured loans and lease finance assets at year-end

(in thousands)	Domestic			International		
	Cash-basis	Restructured	Total	Cash-basis	Restructured	Total
1981						
Interest revenue foregone	$ 9,452	$1,275	$10,727	$ 7,771	$ —	$ 7,771
1982						
Interest revenue foregone	$10,835	$ 136	$10,971	$ 6,737	$ —	$ 6,737
1983						
Contractual interest due	$26,616	$ 710	$27,326	$20,870	$2,973	$23,843
Interest revenue recognized	16,500	648	17,148	12,856	2,919	15,775
Interest revenue foregone	$10,116	$ 62	$10,178	$ 8,014	$ 54	$ 8,068
1984						
Contractual interest due	$36,670	$ 78	$36,748	$30,274	$ 64	$30,338
Interest revenue recognized	19,512	49	19,561	11,417	48	11,465
Interest revenue foregone	$17,158	$ 29	$17,187	$18,857	$ 16	$18,873
1985						
Contractual interest due	$42,273	$ 450	$42,723	$21,990	$ 38	$22,028
Interest revenue recognized	16,552	344	16,896	24,074	33	24,107
Interest revenue foregone	$25,721	$ 106	$25,827	$ (2,084)	$ 5	$ (2,079)

Note: The data in the table above includes interest revenue foregone on loans that were included as "cash-basis and restructured" at the end of each year. Not included is the effect of interest received on loans that were restored to accrual status during the year.

Real estate acquired

Real estate acquired in connection with loan settlements, included in other assets, amounted to $55.5 million at December 31, 1985, compared with $26.8 million at December 31, 1984. Foreclosures on loans to residential builders were primarily responsible for this increase. The after-tax impact of these assets on the Corporation's net income, which consists of interest cost of carry, gains and losses on disposition, net operating costs and write-downs in carrying value, was a decrease of $4.9 million in 1985, compared with a decrease of $597,000 in 1984.

It is the Corporation's policy to liquidate acquired real estate as soon as it can be done profitably. In certain cases the Corporation may elect to hold these properties in order to complete construction and to enhance their disposition.

Summary of credit losses and recoveries

(in thousands)	1981	1982	1983	1984	1985
Balance at beginning of year	$118,641	$134,101	$169,178	$241,504	$303,693
Reserves acquired in mergers	—	—	50,207	4,612	652
Credit losses:					
Domestic operations:					
Commercial and industrial	(13,436)	(16,999)	(16,419)	(22,099)	(44,724)
Financial institutions	—	(2,200)	(4,298)	(4,214)	(10,091)
Other	(306)	(720)	(458)	(474)	(212)
Total commercial and financial	(13,742)	(19,919)	(21,175)	(26,787)	(55,027)
Commercial construction	(89)	(13)	(220)	(1,307)	(6,428)
Commercial mortgage	(3,271)	(154)	(89)	(1,824)	(3,548)
Consumer mortgage	(84)	(456)	(1,123)	(1,126)	(1,379)
Total real estate	(3,444)	(628)	(1,432)	(4,257)	(11,355)
Consumer credit	(13,252)	(11,881)	(12,874)	(24,570)	(35,446)
Lease finance assets	—	—	—	(1,433)	(1,397)
Total domestic operations	(30,438)	(32,428)	(35,481)	(57,047)	(103,225)
International operations:					
Commercial and industrial	(1,623)	(8,098)	(11,229)	(11,410)	(8,363)
Governments and official institutions	—	—	(5,035)	(4,519)	(8,984)
Financial institutions	—	—	—	(2,186)	(4,280)
Total international operations	(1,623)	(8,098)	(16,264)	(18,115)	(21,627)
Total credit losses	(32,061)	(40,526)	(51,745)	(75,162)	(124,852)
Credit recoveries:					
Domestic operations:					
Commercial and industrial	4,128	2,818	14,579	8,593	12,196
Financial institutions	188	263	1	—	8,921
Other	36	55	1,018	355	13
Total commercial and financial	4,352	3,136	15,598	8,948	21,130
Commercial construction	200	—	2	166	126
Commercial mortgage	—	1,077	628	431	840
Consumer mortgage	3	4	27	48	254
Total real estate	203	1,081	657	645	1,220
Consumer credit	3,001	3,142	4,002	5,894	7,684
Lease finance assets	—	17	26	—	—
Total domestic operations	7,556	7,376	20,283	15,487	30,032
International operations:					
Commercial and industrial	2,994	142	1,382	576	3,637
Governments and official institutions	—	—	—	—	2
Total international operations	2,994	142	1,382	576	3,639
Total credit recoveries	10,550	7,518	21,665	16,063	33,671
Net credit losses	(21,511)	(33,008)	(30,080)	(59,099)	(91,181)
Provision charged to expense:					
Domestic operations	36,503	53,151	31,069	65,559	103,502
International operations	468	14,934	21,130	51,117	44,819
Total provision charged to expense	36,971	68,085	52,199	116,676	148,321
Net addition to reserve	15,460	35,077	22,119	57,577	57,140
Balance at year-end	$134,101	$169,178	$241,504	$303,693	$361,485

Reserve and credit loss ratios

	1981	1982	1983	1984	1985
Reserve for possible credit losses to average December loans and leases	1.37%	1.46%	1.58%	1.61%	1.70%
Net credit losses to average loans and leases	.25	.30	.22	.34	.45

Credit losses

The Corporation's net credit loss ratio has historically been among the lowest of major bank holding companies. The increase in the ratio of net credit losses to average loans and leases in 1985 was principally the result of higher domestic commercial credit losses and higher consumer credit losses.

The increase in domestic commercial credit losses in 1985 was primarily attributable to higher losses on loans to a large national diversified credit, as well as higher losses on loans to middle market companies in a variety of industries. The increase in consumer credit losses was primarily a result of an increase in losses on credit card loans made in 1983 and 1984 through a direct mail marketing program, and increases in losses on installment loans.

The 1983 ratio of net credit losses to average loans and leases, which was the Corporation's lowest in the last five years, reflected the addition of loans acquired in the merger with The Girard Company, which were recorded at their market value net of credit quality write-downs of $42 million. Consequently, the Corporation incurred nominal credit losses on these acquired loans in 1983.

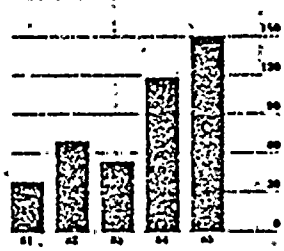
From time to time, the bank regulatory agencies determine that credits to certain countries have been impaired to varying degrees. These agencies direct banks to reflect this impairment by either establishing allocated transfer risk reserves or by electing to take credit losses. The Corporation has recognized losses on credits related to these countries in amounts equal to or greater than those specified by the regulators.

Reserve for possible credit losses

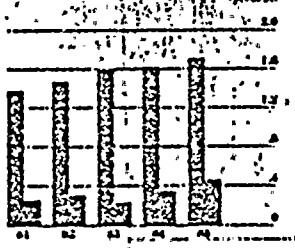
A reserve for possible credit losses is maintained at each operating subsidiary in an amount which, in management's judgment, is adequate to absorb losses in the loan and lease finance asset portfolios. On the basis of December 1985 average loans and leases, the Corporation's ratio of the reserve to total loans and leases was 1.70%, up from the December 1984 ratio of 1.61%. As illustrated in the chart below, this reserve ratio is relatively high compared to the Corporation's net credit loss ratio. The Corporation believes it to be prudent to maintain a reserve ratio of this magnitude.

The components of the provision for possible credit losses are shown in the chart below. In absolute terms, the reserve was increased by $57.1 million during 1985 to a level exceeding $361 million, compared with a reserve of $303.7 million at December 31, 1984. The provision in 1985 included a net addition of $27 million in the reserve assigned to international operations, which rose to 2.91% of international loans at December 31, 1985, from 2.18% at the prior year-end. The Corporation's reserve was increased to cover loan growth and to achieve a higher reserve ratio as a result of management's view of international economic uncertainties.

Components of Provision for Possible Credit Losses



Reserve and Credit Loss Ratios



International Operations

Selected financial data

(dollar amounts in millions)	1981	1982	1983	1984	1985
Net income from international operations	$46.9	$43.1	$33.1	$(4.7)	$4.1
Net income from international operations as a percent of consolidated net income	41%	32%	18%	—%	2%

International operations include international banking activities conducted through the International Banking Department and the global funding activities of the Capital Markets Department. For earnings and related information on international operations and geographic distribution of selected data see note 18 of notes to financial statements.

International operations for 1985 and 1984 included on average $311 million and $396 million of interest-bearing deposits with foreign domiciled institutions that are purchased as part of the Corporation's global funding activities. Net income generated from these activities was $1.1 million and $567,000 in 1985 and 1984.

Net income from international operations for 1985 increased by $4.8 million compared with 1984 but continues to be down considerably from 1983 and prior years. Net credit revenue on a fully taxable equivalent basis increased by $33.3 million primarily as a result of the recovery of interest receipts on cash-basis loans. Foreign exchange trading revenue increased by $4.4 million from the prior year. These favorable effects were offset considerably by lower acceptance revenue, the write-down in the value of certain foreign equity investments and the expense of closing the Frankfurt, West Germany office. Additionally, net income in 1984 included a $2.8 million after-tax settlement with the government of Iran.

As previously mentioned, the Corporation increased its reserve for possible credit losses assigned to international operations during 1985. The reserve rose to 2.91% of international loans at December 31, 1985, compared with 2.18% at the end of 1984.

Assets by International Monetary Fund classification at year-end

(dollar amounts in millions)	1984 Amount	1984 Percent of total international assets	1985 Amount	1985 Percent of total international assets
Industrial countries	$6,370	67%	$4,958	65%
OPEC countries	326	3	229	3
Centrally planned economies	61	1	156	2
Developing countries:				
Emerging exporters of manufactured goods	1,343	14	1,063	14
Net oil exporters	737	8	689	9
Other middle income	678	7	425	6
Other low income	42	—	56	1
Total	$9,557	100%	$7,556	100%

Note: Distributions are based on location of obligor or investment except for assets guaranteed by a third party where location is that of the guarantor. Country economic classification is based on data published by the International Monetary Fund. See note 18 of notes to financial statements for additional information.

International outstandings

Loans in the international portfolio represented 17% of total loans and lease finance assets at December 31, 1985.

At December 31, 1983, 1984 and 1985, the Corporation's total public and private sector outstandings (loans, acceptances, interest-bearing deposits with other banks, other investments and related accrued interest) related to each of the countries shown below exceeded .75% of total consolidated assets. Country distributions are based on the location of the obligor or investment, except for assets guaranteed by a third party, where the location is that of the guarantor.

(in millions)	Commercial and industrial		Financial institutions		Governments and official institutions	Other	Total
	Public	Private	Public	Private			
December 31, 1983							
United Kingdom	$ 50	$189	$ 27	$ 543	$ 10	$ 5	$ 824
Japan	—	93	2	637	12	2	746
France	54	—	137	433	—	—	624
West Germany	27	134	36	370	5	2	574
Mexico	139	228	106	11	80	1	565
Brazil	142	30	76	197	58	1	504
Canada	—	178	—	261	10	1	450
Republic of Korea	—	26	74	252	70	—	422
Australia	1	335	11	61	—	1	409
Sweden	—	3	—	246	40	—	289
Italy	83	5	57	130	14	—	289
December 31, 1984							
Japan	$ —	$ 88	$ 35	$1,002	$ 12	$ 2	$1,139
United Kingdom	14	129	3	514	25	11	696
Mexico	150	223	126	—	91	1	591
Brazil	196	38	63	186	50	1	534
France	52	—	45	329	105	—	531
Australia	1	318	—	150	—	1	470
Canada	—	233	—	205	14	1	453
Republic of Korea	3	15	179	158	—	1	356
West Germany	17	123	6	188	19	1	354
Italy	50	33	126	78	62	1	350
Spain	13	49	7	149	29	—	247
December 31, 1985							
Japan	$ —	$ 79	$ —	$ 862	$ 14	$ 6	$ 961
United [illegible]	27	213	68	330	9	24	671
Mexico	141	184	131	—	123	—	579
Brazil	197	47	52	[illegible]	64	—	489
Australia	30	227	14	[illegible]	[illegible]	5	363
France	57	1	156	106	[illegible]	—	320

International outstandings continued

The following discussion summarizes recent developments concerning refinancings of obligations of borrowers in Mexico and Brazil.

Mexico

At December 31, 1985, the Corporation had approximately $395.0 million in outstandings to Mexican public sector borrowers.

In connection with an agreement completed in early 1984, the Corporation made $8.5 million in new loans during 1985 to the Mexican government at current market rates with maturities of ten years.

During 1985, the Corporation agreed to refinance $267.7 million in obligations of public sector borrowers that mature between 1985 and 1990. Included in this agreement is $110.6 million which remains subject to the satisfaction by the Mexican government of the conditions contained therein. This agreement provides for the rescheduling of the maturities of these loans for periods of up to 14 years and for changes in the rates of interest. The weighted average interest rates for those loans which mature between 1985 and 1990 are as shown in the following table.

(dollar amounts in millions)	Before refinancing	After refinancing
$31.3*	2.125% over Prime	1.125% over Prime
36.3	1.875% over LIBOR	**
89.5	1.750% over Prime	**
30.8	0.847% over LIBOR	**
79.8	0.824% over Prime	**

*This amount is net of approximately $8.3 million that is expected to be prepaid in 1986 as well as a $2.1 million prepayment that was received in the first quarter of 1985.

**Weighted average interest rates after refinancing will be 0.875% over LIBOR (London Interbank Offered Rate) or a comparable domestic interest rate for the period 1985-1986. Interest rate margins will increase to 1.125% for the period 1987-1991 and 1.250% for the period 1992-1998. At December 31, 1985, the Mellon Bank, N.A. Prime Rate exceeded the three-month LIBOR by approximately 1.5%.

During 1985, the Corporation received $43.2 million in interest payments and $10.3 million in principal payments, including prepayments, on Mexican public sector outstandings. The Corporation's consolidated income statement for 1985 included $41.9 million in interest revenue on Mexican public sector outstandings. None of the Corporation's total outstandings to public sector borrowers in Mexico at December 31, 1985, was classified as cash-basis.

The government of Mexico has implemented a program that makes U.S. dollars available to private sector borrowers to make payments on debts contracted prior to December 1982. Borrowers must first have obtained extensions of the maturities of their loans for at least six years with minimum grace periods on principal payments of at least three years. Under this program, the Corporation has refinanced $118.8 million of its $184.4 million in Mexican private sector outstandings and anticipates that an additional $19.4 million will be refinanced. Of the Corporation's total outstandings to private sector borrowers in Mexico at December 31, 1985, $16.2 million was classified as cash-basis.

Brazil

The Corporation is represented in negotiations with the government of Brazil to refinance certain obligations of public and private sector borrowers that mature after 1984. In connection with these negotiations, the Corporation agreed to an extension of the refinancing agreement completed in 1984 to include $40.8 million in Brazilian public and private sector outstandings that matured during 1985. The Corporation is also considering the maintenance of short-term trade loans of approximately $135.1 million and interbank deposits of up to approximately $46.6 million.

During 1985, the Corporation received $73.5 million in interest payments on Brazilian outstandings. The Corporation's consolidated income statement for 1985 included $71.1 million in interest revenue on Brazilian outstandings. Of the Corporation's total outstandings to public and private sector borrowers in Brazil at December 31, 1985, $1.8 million was classified as cash-basis.

Selected Quarterly Data

(dollar amounts in millions, except per share amounts)	1984 March 31	1984 June 30	1984 Sept. 30	1984 Dec. 31	1985 March 31	1985 June 30	1985 Sept. 30	1985 Dec. 31
Quarterly consolidated income statement								
Net credit revenue	$ 159.9	$ 185.1	$ 197.4	$ 204.7	$ 199.3	$ 219.5	$ 226.2	$ 227.4
Service revenue	69.8	76.4	72.8	83.1	85.1	88.7	91.4	99.8
Trading revenue	(1.9)	.3	2.0	5.1	3.3	14.7	2.6	2.0
Gains on sale of investment securities	2.1	—	—	1.5	5.3	73.1	3.7	10.5
Other revenue	3.5	7.3	6.5	8.4	1.8	3.3	3.7	3.7
Provision for possible credit losses	17.2	30.4	31.9	37.1	20.3	45.3	29.2	53.6
Operating expense	187.5	202.7	207.7	217.5	224.0	249.2	236.7	255.7
Income before income taxes	28.7	36.0	39.1	48.2	50.5	104.8	61.7	34.1
Provision for income taxes	(4.3)	(3.4)	(3.5)	4.8	9.0	36.7	14.7	(10.9)
Net income	33.0	39.4	42.6	43.4	41.5	68.1	47.0	45.0
Dividends on preferred stock	2.1	2.4	2.5	2.6	2.5	2.6	2.5	2.5
Net income applicable to common stock	$ 30.9	$ 37.0	$ 40.1	$ 40.8	$ 39.0	$ 65.5	$ 44.5	$ 42.5
Net income per common share	$ 1.20	$ 1.40	$ 1.51	$ 1.53	$ 1.46	$ 2.45	$ 1.65	$ 1.57
Quarterly average balances								
Money market investments	$ 4,017	$ 4,146	$ 2,992	$ 3,392	$ 3,605	$ 3,471	$ 2,835	$ 2,396
Investment securities	1,342	1,405	1,368	1,397	1,505	1,893	2,584	2,368
Loans and lease finance assets	15,706	17,042	17,948	18,671	19,350	19,881	20,229	20,848
Interest-earning assets	21,516	23,032	22,816	23,910	24,917	25,668	25,994	26,074
Reserve for possible credit losses	247	261	285	299	312	315	340	354
Total assets	25,824	27,851	27,715	28,999	29,797	30,473	30,454	30,253
Deposits	15,703	17,083	17,349	17,888	18,564	18,416	18,025	18,006
Notes and debentures	586	592	589	683	883	1,083	1,135	1,128
Preferred stock	77	91	93	93	93	93	94	84
Common shareholders' equity	1,382	1,430	1,457	1,463	1,507	1,541	1,585	1,614
Rate analysis								
Yield on total interest-earning assets	11.66%	12.34%	13.09%	12.50%	11.43%	11.17%	10.78%	10.84%
Cost of funds supporting interest-earning assets	8.14	8.57	9.12	8.61	7.77	7.33	6.95	6.93
Net rate on interest-earning assets	3.52%	3.77%	3.97%	3.89%	3.66%	3.84%	3.83%	3.91%

Note: Rates are calculated on a fully taxable equivalent basis using actual number of days in quarter and year and are before effect of reserve requirements. Fees on loans are included in the calculation of rates.

Fourth Quarter Review

Net income for the fourth quarter of 1985 was $45.0 million compared with $43.4 million for the fourth quarter of 1984. On a per common share basis, net income for the fourth quarter of 1985 increased to $1.57 from the $1.53 reported in the fourth quarter of the prior year.

Net credit revenue for the fourth quarter of 1985 increased to $227.4 million from $204.7 million in the fourth quarter of 1984, principally reflecting higher loan and lease levels, up $2.2 billion, or 12%, on average. The improvement in net credit revenue also reflected higher levels of investment securities, which increased on average by $1.0 billion in the fourth quarter of 1985 compared with the fourth quarter of the prior year.

Service revenue for the fourth quarter increased 20% from the fourth quarter of 1984, principally due to growth in Trust and Investment Department fees, cash management fees and data processing fees.

The provision for possible credit losses for the fourth quarter of 1985 totalled $53.6 million, while net credit losses amounted to $33.7 million. This compares with a provision of $37.1 million and net credit losses of $23.8 million for the fourth quarter of 1984.

Operating expense for the fourth quarter of 1985 increased to $255.7 million from $217.5 million in the fourth quarter of 1984, due primarily to the same factors which were responsible for the year-to-year increase.

The income tax provision for the fourth quarter of 1985 reflected investment tax credits and other tax credits that totalled $10.0 million. Similar credits amounted to $1.3 million in the fourth quarter of 1984.

Pending Acquisitions

The Corporation announced in October 1985 the signing of a definitive agreement to merge with Commonwealth National Financial Corporation, a bank holding company based in Harrisburg, Pennsylvania, with 43 branch offices and approximately $1.4 billion of assets at December 31, 1985. The agreement to merge has been approved by the boards of directors of both corporations. Commonwealth National's shareholders, the Pennsylvania Department of Banking and the Federal Reserve Board. As a result of the merger, Commonwealth National's shareholders may elect to receive for each share of Commonwealth National stock either $40 in cash or 1.6 shares of a new issue of Mellon Bank Corporation convertible preferred stock which will be priced to approximate a $25 market value. The election is subject to the restriction that 55% of Commonwealth National's shares will be exchanged for the new preferred stock and 45% for cash.

A class action and derivative action have been brought by two shareholders of Commonwealth National seeking to enjoin the merger and claiming damages in an unspecified amount because of alleged violations of securities laws by the Corporation and Commonwealth National, and an alleged breach of fiduciary duty by the directors of Commonwealth National. The Corporation is vigorously defending this suit and believes that its defense will be successful.

At December 31, 1985, the Corporation had several acquisitions pending with an aggregate cash purchase consideration of less than $50 million.

Common and Preferred Stock

Common stock

(dollars per share)	Quarter ended 1984 March 31	June 30	Sept. 30	Dec. 31	1985 March 31	June 30	Sept. 30	Dec. 31
Market price range:								
High	$ 52	$ 41⅛	$ 42¼	$ 46¾	$ 51⅛	$ 55	$ 56⅛	$ 54⅛
Low	38⅞	33½	33¾	40⅜	44½	47	47¾	46⅞
Average	44.27	37.72	38.27	43.61	48.47	51.10	52.57	49.58
Dividends	.65	.65	.65	.65	.67	.67	.67	.67

	1983	1984	1985
Common share data:			
Shareholders' equity per share at year-end	$53.62	$56.21	$60.39
Shareholders at year-end	17,227	19,185	18,528
Shares outstanding at year-end	25,792,971	26,675,747	27,109,370
Average shares outstanding	23,986,591	26,373,880	26,863,972

Series A preferred stock

(dollars per share)	Quarter ended 1984 March 31	June 30	Sept. 30	Dec. 31	1985 March 31	June 30	Sept. 30	Dec. 31
Market price range:								
High	$ 26¾	$ 25⅞	$ 24⅛	$ 25¼	$ 27	$ 28⅛	$ 30¼	$ 29
Low	25	22⅛	23½	24	24⅛	26⅛	27¾	27⅛
Average	25.59	24.66	24.19	24.75	26.09	26.96	28.55	28.26
Dividends	.70	.70	.70	.70	.70	.70	.70	.70

	1983	1984	1985
Preferred share data:			
Shareholders at year-end	8,378	10,230	9,844
Shares outstanding at year-end	3,031,581	3,643,895	3,653,886

Changing Prices

Financial disclosures prepared in accordance with generally accepted accounting principles report the actual dollar amounts received or expended without giving consideration to changes in the purchasing power of money. The following table presents selected financial data adjusted for the effects of changing prices as required by the Financial Accounting Standards Board. These inflation-adjusted data, which are restated in constant 1985 dollars, are referred to as constant dollar amounts and were computed by adjusting the reported data by the U.S. Consumer Price Index for all Urban Consumers to reflect changes in general purchasing power.

Constant dollar net income and common shareholders' equity amounts have been further adjusted to reflect depreciation expense on fixed assets on a constant dollar basis. It should be noted that this index may not be appropriate because it does not necessarily bear any direct relationship to all of the assets, liabilities, common shareholders' equity, revenue or expense of financial institutions.

(dollar amounts in millions, except per share amounts)	Year ended December 31, 1981	1982	1983	1984	1985
Net credit revenue:					
As reported	$ 366.4	$ 445.6	$ 614.9	$ 747.1	$ 872.4
Inflation adjusted	433.3	496.5	663.8	773.5	872.4
Net income:					
As reported	$ 115.5	$ 134.4	$ 183.8	$ 158.5	$ 201.7
Inflation adjusted	127.1	138.5	187.0	152.9	192.4
Net income per common share:					
As reported	$ 5.88	$ 6.83	$ 7.44	$ 5.64	$ 7.13
Inflation adjusted	6.47	7.04	7.56	5.42	6.78
Dividends per common share:					
As reported	$ 2.09	$ 2.24	$ 2.44	$ 2.60	$ 2.68
Inflation adjusted	2.47	2.50	2.63	2.69	2.68
Market price per common share at year-end:					
As reported	$ 36¾	$ 37⅛	$ 51	$ 46¾	$ 52⅛
Inflation adjusted	43⅛	42¼	55	48⅜	52⅛
Purchasing power loss on net monetary assets	$ 78.7	$ 34.5	$ 34.6	$ 38.5	$ 36.3
Common shareholders' equity	1,062.5	1,037.5	1,379.1	1,450.3	1,555.4
Average Consumer Price Index	272.4	289.1	298.4	311.1	322.2

Note: Because the Corporation does not have significant amounts of property, plant and equipment, constant dollar data has been substituted for current cost information.

Consolidated Income Statement

Mellon Bank Corporation (and its subsidiaries)

	(In thousands, except per share amounts)	Year ended December 31, 1983	1984	1985
Credit revenue	Loans	$1,542,906	$2,076,652	$2,105,758
	Money market investments:			
	Interest-bearing deposits with banks	306,714	242,191	189,641
	Federal funds sold and securities purchased under agreements to resell	86,966	110,909	63,985
	Other	15,648	18,019	16,928
	Trading account securities	42,352	51,366	36,146
	Investment securities:			
	U.S. Treasury and agency securities	131,409	94,178	162,283
	Obligations of states and political subdivisions	17,920	18,708	24,648
	Other	9,363	13,553	10,893
	Fees on loans	58,240	63,190	87,072
	Lease financing revenue	16,949	25,285	30,058
	Total credit revenue	2,228,467	2,713,151	2,729,410
Interest expense	Deposits:			
	Domestic offices	743,300	1,020,291	963,561
	Foreign offices	288,412	283,640	256,494
	Federal funds purchased and securities sold under agreements to repurchase	363,260	381,883	388,360
	Commercial paper	114,267	156,747	117,468
	Other funds borrowed	49,574	56,954	30,960
	Notes and debentures (with original maturities over one year)	54,707	66,557	100,159
	Total interest expense	1,613,520	1,966,072	1,857,002
Net credit revenue	Net credit revenue	614,947	747,079	872,408
	Provision for possible credit losses	52,199	116,676	148,321
	Net credit revenue after provision for possible credit losses	562,748	630,403	724,087
Service and other revenue	Service revenue	230,480	302,110	365,116
	Trading revenue	11,801	5,476	22,575
	Gains on sale of investment securities	10,797	3,556	92,511
	Other revenue	34,318	25,690	12,422
	Total service and other revenue	287,396	336,832	492,624
Operating expense	Salaries and wages	271,032	347,599	392,637
	Pension, incentive and other employee benefits	78,740	94,257	116,718
	Equipment expense	48,091	58,472	68,205
	Net occupancy expense	46,484	97,535	109,926
	Shares, capital and franchise taxes	13,374	13,631	14,483
	Other expense	174,078	203,686	263,640
	Total operating expense	631,799	815,380	965,609
Income	Income before income taxes	218,345	151,855	251,102
	Provision for income taxes	34,530	(6,689)	49,407
	Net income	183,815	158,544	201,695
	Dividends on preferred stock	5,263	9,722	10,224
	Net income applicable to common stock	$ 178,552	$ 148,822	$ 191,471
Per common share	(Based on 23,986,591; 26,373,880 and 26,863,972 average shares of common stock outstanding) Net income	$7.44	$5.64	$7.13

See accompanying notes to financial statements.

Consolidated Balance Sheet

Mellon Bank Corporation (and its subsidiaries)

	(in thousands)	December 31, 1984	1985
Assets	Cash and due from banks	$ 1,822,114	$ 1,609,791
	Money market investments:		
	Interest-bearing deposits with banks	2,579,364	1,173,474
	Federal funds sold and securities purchased under agreements to resell	695,019	710,450
	Other	184,744	168,565
	Trading account securities	316,219	956,865
	Investment securities:		
	U.S. Treasury and agency securities	1,254,782	1,848,894
	Obligations of states and political subdivisions	296,644	1,118,765
	Other	155,052	91,990
	Total investment securities	1,706,478	3,059,649
	Loans, net of unearned discount of $169,977 and $157,956	19,397,654	21,931,246
	Lease finance assets	288,896	387,429
	Total loans and lease finance assets	19,686,550	22,318,675
	Less: Reserve for possible credit losses	(303,693)	(361,485)
	Net loans and lease finance assets	19,382,857	21,957,190
	Customers' acceptance liability	2,671,401	2,235,659
	Premises and equipment	333,721	390,878
	Other assets	900,898	1,137,674
	Total assets	$30,602,815	$33,406,195
Liabilities	Deposits in domestic offices:		
	Interest-free	$ 4,077,172	$ 3,872,983
	Interest-bearing	11,919,339	12,265,603
	Deposits in foreign offices:		
	Interest-free	7,948	11,107
	Interest-bearing	2,992,850	2,432,932
	Total deposits	18,997,309	18,582,625
	Federal funds purchased and securities sold under agreements to repurchase	4,218,117	7,372,910
	Commercial paper	1,518,670	1,357,164
	Other funds borrowed	375,484	406,628
	Acceptances outstanding	2,671,401	2,235,693
	Other liabilities	377,003	575,060
	Notes and debentures (with original maturities over one year)	852,016	1,145,383
	Total liabilities	29,010,000	31,675,463
Preferred stock	Preferred stock—$1.00 par value		
	Authorized—10,000,000 shares		
	Issued—3,643,895 and 3,653,886 shares Series A	93,329	93,550
Common shareholders' equity	Common stock—$.50 par value		
	Authorized—60,000,000 shares		
	Issued—27,219,222 and 27,659,959 shares	13,612	13,831
	Surplus	585,464	605,164
	Undivided profits	913,165	1,031,301
	Less: Treasury stock—543,475 and 550,589 shares at cost	(12,755)	(13,114)
	Total common shareholders' equity	1,499,486	1,637,182
	Total liabilities, preferred stock and common shareholders' equity	$30,602,815	$33,406,195

See accompanying notes to financial statements.

Consolidated Statement of Changes in Financial Position

Mellon Bank Corporation (and its subsidiaries)

	(in thousands)	Year ended December 31, 1983	1984	1985
Increase(decrease) in financial resources invested in interest-earning assets	**Financial resources derived from/(applied to):**			
	Operations:			
	Net income	$ 183,815	$ 158,544	$ 201,695
	Provision for possible credit losses	52,199	116,676	148,321
	Deferred taxes, depreciation and other nonfund items	65,328	31,649	86,476
	Financial resources derived from operations	301,342	306,869	436,492
	Dividends on common and preferred stock	(60,476)	(78,299)	(82,171)
		240,866	228,570	354,321
	Deposits and other financing activities:			
	Deposits	(100,311)	2,631,152	(519,275)
	Borrowed funds	208,490	(7,219)	3,024,431
	Notes and debentures	(71,138)	268,944	203,367
	Deposits and other funds acquired in mergers	4,853,651	679,211	104,591
	Floating Rate Notes issued in merger	47,500	—	—
	Common stock issued in mergers	187,784	29,348	5,167
	Preferred stock issued in mergers	76,371	15,997	—
		5,202,356	3,617,403	2,908,281
	Other activities:			
	Cash and due from banks	(343,721)	(21,676)	219,654
	Premises and equipment	(9,912)	(97,149)	(105,924)
	Assets and liabilities acquired in mergers, net	(627,712)	(64,830)	(13,204)
	Other, net	(134,519)	(111,432)	(153,824)
		(1,115,864)	(295,087)	(53,298)
	Increase in financial resources invested in interest-earning assets	$ 4,327,358	$3,550,886	$ 3,209,304
Increase (decrease) in interest-earning assets	Money market investments	$ (667,892)	$ (612,118)	$(1,427,747)
	Money market investments acquired in mergers	723,667	156,449	11,109
	Investment and trading account securities	(200,962)	(372,340)	1,955,763
	Investment securities acquired in mergers	547,036	181,234	38,034
	Loans and lease finance assets	610,941	3,844,866	2,577,512
	Loans and lease finance assets acquired in mergers	3,314,568	352,795	54,613
	Increase in interest-earning assets	$4,327,358	$3,550,886	$ 3,209,304

See accompanying notes to financial statements.

Statement of Changes in Common Shareholders' Equity

Mellon Bank Corporation (consolidated and parent Corporation)

(in thousands)	Common stock	Surplus	Undivided profits	Treasury stock	Total common shareholders' equity
Balance at January 1, 1983	$10,122	$359,225	$ 710,877	$(12,610)	$1,067,614
1983 additions/(deductions):					
Net income			183,815		183,815
Dividends on preferred stock at $2.06 per share			(5,263)		(5,263)
Dividends on common stock at $2.44 per share			(55,213)		(55,213)
Common stock issued in mergers	2,962	184,822			187,784
Issuance of stock under option plans, net, dividend reinvestment plan and conversion of 5.375% Convertible Capital Notes	85	4,746		(76)	4,755
Foreign currency translation			(419)		(419)
Balance at December 31, 1983	13,169	548,793	833,797	(12,686)	1,383,073
1984 additions/(deductions):					
Net income			158,544		158,544
Dividends on preferred stock at $2.80 per share			(9,722)		(9,722)
Dividends on common stock at $2.60 per share			(68,577)		(68,577)
Common stock issued in merger	337	29,075		(64)	29,348
Issuance of stock under option plans, net, dividend reinvestment plan and conversion of 5.375% Convertible Capital Notes	106	7,596		(5)	7,697
Foreign currency translation			(877)		(877)
Balance at December 31, 1984	13,612	585,464	913,165	(12,755)	1,499,486
1985 additions/(deductions):					
Net income			201,695		201,695
Dividends on preferred stock at $2.80 per share			(10,224)		(10,224)
Dividends on common stock at $2.68 per share			(71,947)		(71,947)
Common stock issued in merger	58	5,109			5,167
Issuance of stock under option plans, net, dividend reinvestment plan and conversion of 5.375% Convertible Capital Notes	161	14,591		(359)	14,393
Foreign currency translation			(1,388)		(1,388)
Balance at December 31, 1985	$13,831	$605,164	$1,031,301	$(13,114)	$1,637,182

See accompanying notes to financial statements.

Income Statement

Mellon Bank Corporation (parent Corporation)

	(in thousands)	Year ended December 31, 1983	1984	1985
Revenue	Dividends from subsidiaries:			
	Banks	$ 74,462	$ 75,116	$ 81,803
	Other	5,600	7,670	8,289
	Interest from subsidiaries:			
	Banks	82,544	83,028	44,695
	Other	70,589	107,588	126,358
	Other revenue	6,970	3,163	4,898
	Total revenue	239,365	276,563	266,043
Expense	Interest expense:			
	Commercial paper	114,267	147,617	109,576
	Notes and debentures (with original maturities over one year)	32,678	38,212	57,709
	Shares, capital and franchise taxes	9,926	9,056	9,209
	Other expense	6,720	9,672	9,066
	Total expense	163,591	204,557	185,560
Income	Income before income taxes, undistributed income of subsidiaries	75,774	72,006	80,483
	Provision for income taxes	(646)	(2,968)	(2,655)
	Income before undistributed income	76,420	74,974	83,138
	Equity in undistributed income of subsidiaries:			
	Banks	97,000	71,179	112,272
	Other	10,395	12,391	6,285
	Net income	183,815	158,544	201,695
	Dividends on preferred stock	5,263	9,722	10,224
	Net income applicable to common stock	$178,552	$148,822	$191,471

See accompanying notes to financial statements.

Balance Sheet

Mellon Bank Corporation (parent Corporation)

	(in thousands)	December 31, 1984	1985
Assets	Due from subsidiary bank	$ 335	$ 378
	Money market investments with subsidiaries	532,871	151,708
	Advances and other receivables due from subsidiaries:		
	Banks	91,067	199,760
	Other	1,213,322	1,639,341
	Investments in subsidiaries:		
	Banks	1,388,235	1,504,540
	Other	151,374	162,875
	Other assets	18,292	38,382
	Total assets	$3,395,496	$3,697,374
Liabilities	Commercial paper	$1,438,307	$1,286,489
	Other funds borrowed	—	17,327
	Other liabilities	2,246	5,477
	Notes and debentures (with original maturities over one year)	362,128	657,349
	Total liabilities	1,802,681	1,966,642
Preferred stock	Preferred stock—$1.00 par value		
	Authorized—10,000,000 shares		
	Issued—3,643,895 and 3,653,886 shares Series A	93,321	92,550
Common shareholders' equity	Common stock—$.50 par value		
	Authorized—60,000,000 shares		
	Issued—27,219,222 and 27,659,959 shares	13,613	13,831
	Surplus	585,464	605,164
	Undivided profits	913,165	1,031,301
	Less: Treasury stock—543,475 and 550,589 shares at cost	(12,758)	(13,114)
	Total common shareholders' equity	1,499,486	1,637,182
	Total liabilities, preferred stock and common shareholders' equity	$3,395,496	$3,697,374

See accompanying notes to financial statements.

Statement of Changes in Financial Position

Mellon Bank Corporation (parent Corporation)

	(in thousands)	Year ended December 31, 1983	1984	1985
Increase (decrease) in financial resources invested in subsidiaries and interest-earning assets	Financial resources derived from/(applied to):			
	Operations:			
	Net income	$ 183,815	$ 158,544	$ 201,695
	Less: Equity in undistributed net income of subsidiaries and other nonfund items	(104,212)	(78,124)	(112,448)
	Financial resources derived from operations	79,603	80,420	89,247
	Dividends on common and preferred stock	(60,476)	(78,299)	(82,171)
		19,127	2,121	7,076
	Financing activities:			
	Commercial paper	325,731	205,903	(151,818)
	Commercial paper acquired in merger	36,337	—	—
	Borrowed funds	—	—	17,327
	Notes and debentures	(2,704)	24,373	295,221
	Notes and debentures acquired in merger	72,229	—	—
	Common stock issued in mergers	187,784	29,348	5,167
	Preferred stock issued in mergers	76,371	15,997	—
		695,748	275,621	165,897
	Other, net	7,050	(13,003)	(16,608)
	Increase in financial resources invested in subsidiaries and interest-earning assets	$ 721,925	$ 264,739	$ 156,365
Increase (decrease) in investment in subsidiaries and interest-earning assets	Money market investments with subsidiaries	$ 90,453	$(153,013)	$(331,073)
	Investment in subsidiaries	33,842	908	10,832
	Investment in subsidiaries acquired in mergers	289,192	75,941	5,17
	U.S. Treasury securities	(59,365)	—	—
	Advances to subsidiaries	286,008	340,903	521,430
	Advances to subsidiaries acquired in merger	81,795	—	—
	Increase in investment in subsidiaries and interest-earning assets	$ 721,925	$ 264,739	$ 156,365

See accompanying notes to financial statements.

Notes to Financial Statements

1. Accounting policies

Basis of presentation. The consolidated financial statements of Mellon Bank Corporation (Corporation), a multibank holding company, include the accounts of the Corporation and its wholly-owned subsidiaries. Investments in companies 20–50% owned are carried at equity. Investments in companies less than 20% owned are carried at cost. Intra-corporate transactions are not reflected in the consolidated financial statements. The consolidated income statement includes results of acquired subsidiaries only from the dates of acquisition. Goodwill is being amortized over the remaining estimated benefit period which approximates 16 years on a weighted average basis at December 31, 1985.

The parent Corporation financial statements include the accounts of the Corporation and those of two wholly-owned financing subsidiaries that function as financing entities for the Corporation and its subsidiaries and affiliates by issuing commercial paper and other debt guaranteed by the Corporation. Financial data for the Corporation and the financing subsidiaries are combined for financial reporting due to this limited function of the financing subsidiaries and the unconditional guarantee of all the financing subsidiaries' obligations by the Corporation.

Investment and trading account securities. Investment securities are stated at cost, adjusted for amortization of premium and accretion of discount on a level earnings rate basis. Gains and losses on sales of investment securities, other than U.S. Treasury bills, are reported as securities gains/(losses) and are included in service and other revenue. Gains and losses on sales of U.S. Treasury bills are included in interest revenue. Cost of investment securities sold is calculated on a specific identification basis.

Trading account securities are stated at market value. Trading account profits and commissions include both realized gains and losses and unrealized gains and losses to reflect market value. The liability incurred on short-sale transactions, representing the obligation to deliver securities, is included in other funds borrowed at market value.

Loans. Loans are reported at the principal amount outstanding, net of any unearned discount. Interest revenue on nondiscounted loans is recognized based on the principal amount outstanding. Interest revenue on discounted loans is recognized based on methods that approximate a level yield. Loans on which the accrual of interest has been discontinued are designated as cash-basis loans. Loans are generally placed on cash-basis when principal is past due 90 days or more or where interest is more than 60 days past due and the loan is not well secured and is not in the process of collection. Loans may be placed on cash-basis sooner where management believes that it is appropriate. When a loan is placed on cash-basis, previously accrued and uncollected interest is reversed against current period interest revenue. Cash-basis loans are restored to an accrual basis when interest and principal payments become current or the loan becomes well secured and in the process of collection. Consumer loans generally are charged-off on a formula basis upon reaching varying stages of delinquency.

Lease financing. Revenue on direct financing leases is recognized on a basis to achieve a constant periodic rate of return on the outstanding net receivable balance. Revenue on leveraged leases is recognized on a basis to achieve a constant rate of return on the outstanding investment in the lease, net of related deferred tax liability, in the years in which the net investment is positive.

Reserve for possible credit losses. The reserve for possible credit losses on loans and lease finance assets is based on management's judgment. Factors considered in determining an adequate reserve include industry concentrations, specific known risks, adequacy of collateral on specific higher risk loans, past experience, the status and amount of cash-basis, past due and restructured loans and lease finance assets, the ratio of the reserve to loans and lease finance

1. Accounting policies continued

assets outstanding, and current as well as anticipated economic and political conditions that may impact certain borrowers. Losses, net of recoveries, are charged against the reserve. Assets acquired in settlement of indebtedness are included in other assets at the lower of estimated fair value or carrying amount of the indebtedness; subsequent write-downs and net direct operating expenses attributable to such assets are included in other expense.

Premises and equipment. Premises and equipment are stated at cost less accumulated depreciation and amortization. Depreciation and amortization are calculated over the estimated useful life of the asset, limited in the case of leasehold improvements to the lease term, using the straight-line method.

Taxes. The deferred federal income tax provision results from recog ng certain items of revenue and expense in the consolidated financial statements in different years than they are recognized for income tax purposes.

Investment tax credits, other than those applicable to lease financing transactions, reduce the provision for income taxes in the year such credits become available. Investment tax credits on lease financing transactions reduce the provision for income taxes over the life of the lease.

The Corporation and its domestic subsidiaries (except life insurance subsidiaries) file a consolidated U.S. income tax return. The provision for U.S. income taxes of the Corporation and each subsidiary is calculated as if each subsidiary filed a separate return except that tax benefits of losses are allocated to the subsidiaries incurring such losses to the extent they reduce consolidated taxable income.

Foreign currency translation. Assets and liabilities denominated in foreign currencies are translated principally at current rates of exchange. Revenue and expense accounts are translated monthly at month-end rates of exchange. Net currency exchange positions are valued at rates of exchange, spot or future as appropriate, prevailing at the end of the period. Resulting gains or losses are included in the consolidated income statement. Premiums and discounts on contracts hedged are accrued over the periods of the contracts. Translation gains and losses and related hedging gains and losses on investments in foreign entities whose functional currency is not the U.S. dollar are included in common shareholders' equity.

Pension plans. Most Corporation subsidiaries have trusteed, noncontributory pension plans covering substantially all salaried employees. Annual pension expense includes normal cost as actuarially computed, amortization of unfunded prior service cost, where applicable, and the interest thereon. Actuarial gains and losses and the cost of plan changes are spread over periods less than or equal to the average remaining career service lives of active plan participants.

Interest rate futures. Gains and losses on futures contracts used to hedge certain assets and liabilities are deferred and are either recognized in income in the period of disposition of the assets or liabilities being hedged or are amortized over the life of the hedged transaction as an adjustment to interest expense or interest revenue. Gains and losses on futures contracts used to hedge trading account activities are recognized currently in trading account profits and commissions.

Net income per common share. Net income per common share is computed by dividing net income, after deducting dividends on preferred stock, by the weighted average number of common shares outstanding during each of the years presented.

Reclassification. Prior year amounts have been reclassified to conform to the presentation for 1985.

2. Cash and due from banks

The subsidiary banks of the Corporation are required to maintain reserve balances with a Federal Reserve bank based principally on deposits outstanding. Balances maintained are included in cash and due from banks. At December 31, 1985, the required reserves were approximately $432,310,000 and for the year averaged approximately $416,815,000.

3. Investment securities

Book and market values are as follows:

	December 31, 1984		1985	
(in thousands)	Book value	Market value	Book value	Market value
U.S. Treasury and agency securities	$1,254,782	$1,251,094	$1,848,894	$1,889,847
Obligations of states and political subdivisions	296,644	259,329	1,118,765	1,108,238
Other securities	155,052	147,668	91,990	89,697
Total investment securities	$1,706,478	$1,658,091	$3,059,649	$3,087,782

4. Pledged assets

Investment securities, loans, money market investments, trading account securities and equipment carried at $3,210,840,000 on December 31, 1985, were pledged as required to secure repurchase agreements, deposits of public funds and for other purposes.

5. Loans and lease finance assets

Loans and lease finance assets outstanding, net of unearned discount, are as follows:

	December 31,	
(in millions)	1984	1985
Domestic operations:		
Loans:		
Commercial and industrial	$ 7,676	$ 8,993
Financial institutions	1,331	1,485
Other	870	1,115
Total commercial and financial	9,877	11,593
Commercial construction	1,702	2,045
Commercial mortgage	683	660
Consumer mortgage	1,266	1,378
Total real estate	3,651	4,303
Consumer credit	2,014	2,227
Total loans	15,542	18,123
Lease finance assets:		
Direct lease finance assets	154	177
Leveraged lease finance assets	40	40
Assets on interim rent and other lease assets	95	170
Total lease finance assets	289	387
Total domestic operations	15,831	18,510
International operations (see note 18 for details)	3,856	3,809
Total loans and lease finance assets, net of unearned discount	$19,687	$22,319

5. Loans and lease finance assets continued

Information on cash-basis, past due and restructured loans and lease finance assets at year-end is as follows:

(in thousands)	December 31, 1984	1985
Outstanding amounts at year-end:		
Cash-basis	$522,843	$571,729
Past due	28,785	29,947
Restructured	1,278	5,003
Total	$552,906	$606,679

6. Reserve for possible credit losses

Activity is as follows:

(in thousands)	1983	1984	1985
Balance at January 1	$169,178	$241,504	$ 303,693
Reserves acquired in mergers	50,207	4,612	652
Additions/(deductions):			
Credit losses	(51,745)	(75,162)	(124,852)
Recoveries	21,665	16,063	33,071
Net credit losses	(30,080)	(59,099)	(91,181)
Provision charged to expense	52,199	116,676	118,321
Balance at December 31	$241,504	$303,693	$ 331,485

7. Premises and equipment

A summary of year-end balances is as follows:

(in thousands)	December 31, 1984	1985
Land	$ 23,401	$ 21,583
Buildings	135,574	170,196
Equipment	266,967	325,417
Leasehold improvements	41,666	43,251
Subtotal	467,608	560,452
Less: Accumulated depreciation and amortization	133,887	169,574
Total premises and equipment	$333,721	$390,878

Included in the above data are capital leases for premises and equipment at a net book value of $4,773,000 and $3,949,000 at December 31, 1984 and 1985.

Rental expense was $32,940,000, $66,044,000 and $71,158,000 net of related sublease revenue of $446,000, $1,952,000 and $4,127,000 in 1983, 1984 and 1985. Depreciation and amortization expense totalled $28,439,000, $38,026,000 and $44,960,000 in 1983, 1984 and 1985. Maintenance and repairs expense amounted to $32,005,000, $43,533,000 and $49,228,000 in 1983, 1984 and 1985.

As of December 31, 1985, the Corporation and its subsidiaries are obligated under non-cancelable leases (principally for banking premises) with expiration dates through 2055. A summary of the future minimum rental commitments under noncancelable leases, net of related sublease revenue totalling $56.3 million is as follows:

1986	$49,106,000	1989	$ 63,504,000	1996-2000	$273,207,000
1987	51,459,000	1990	59,442,000	2001-2005	329,240,000
1988	48,867,000	1991-1995	272,163,000	2006-2055	234,399,000

8. Federal funds purchased and securities sold under agreements to repurchase

Federal funds purchased and securities sold under agreements to repurchase represent funds acquired for portfolio acquisitions, arbitrage activities and other funding requirements. Although funds purchased may extend for periods longer than one day, the majority of such transactions mature on the business day after execution.

Selected balances and rates are as follows:

(dollar amounts in thousands)	1984	1985
Funds purchased:		
Maximum month-end balance	$4,218,117	$7,372,910
Average daily balance	3,694,003	4,972,512
Average rate during year	10.3%	7.8%
Average rate at December 31	9.0	9.1
Funds purchased, net of funds sold:		
Maximum month-end balance	$3,523,098	$3,662,460
Average daily balance	2,638,699	4,197,397

9. Commercial paper

Commercial paper borrowings principally represent obligations of two financing subsidiaries, the repayment of which is guaranteed by the Corporation. Commercial paper also includes obligations of a foreign bank subsidiary, the repayment of which is guaranteed by Mellon Bank, N.A. (Mellon Bank). Maximum maturities are nine months; average maturity at December 31, 1985, was approximately 29 days.

Selected balances and rates are as follows:

(dollar amounts in thousands)	1984	1985
Maximum month-end balance	$1,583,603	$1,589,452
Average daily balance	1,474,779	1,411,813
Average rate during year	10.6%	8.3%
Average rate at December 31	9.2	8.0

Commercial paper backup lines of credit extended to the Corporation by various nonaffiliated banks were $200,000,000 at December 31, 1984 and 1985. Certain lines are for a one-year term. Others are subject to periodic review or 60 days notice of cancellation. Lines of credit were supported by compensating balances of $500,000 at December 31, 1984. No compensating balances were maintained at December 31, 1985. Lines of credit extended to subsidiaries of the Corporation by various nonaffiliated banks to support short-term borrowings were $15,000,000 and $10,000,000 at December 31, 1984 and 1985. The majority of the lines are for a one-year term and were supported by compensating balances of $700,000 and $200,000 at December 31, 1984 and 1985. No borrowings were made under any line of credit in either year.

10. Notes and debentures (with original maturities over one year)

(in thousands)	December 31, 1984	1985
Parent Corporation:		
Convertible Floating Rate Notes Due May 15, 1987 (10.85% and 8.30% at December 31, 1984 and 1985)	$ 50,000	$ 50,000
Floating Rate Notes Due June 1, 1989 (10.00% and 8.40% at December 31, 1984 and 1985)	19,953	18,470
Convertible Floating Rate Notes Due June 15, 1989 (9.50% and 8.05% at December 31, 1984 and 1985)	120,225	120,225
Floating Rate Extendible Notes Due April 30, 2000 (7.92% at December 31, 1985)	—	149,854
13.50% Notes Due August 15, 1987	24,946	24,963
10.60% Notes Due December 15, 1987	74,690	74,782
5.375% Convertible Capital Notes Due June 1, 1993	[illegible]	705
11.75% Guaranteed Debentures Due March 7, 1995		100,000
8.95% Promissory Notes Due September 1, 1997	18,650	17,200
Various notes—8.65% to 14.125% due 1985-1990	52,900	101,150
Banking subsidiaries:		
Variable-rate notes due 1993-1996 (10.28% and 8.39% at December 31, 1984 and 1985)	155,000	155,000
Floating Rate Subordinated Capital Notes Due November 1996 (9.44% and 8.31% at December 31, 1984 and 1985)	250,000	250,000
Obligations under capital leases—7.00% to 15.00% due 1985-1997	5,510	4,863
Various notes—7.25% to 9.16% due 1985-2005	31,008	30,053
Nonbanking subsidiaries:		
Floating Rate Notes Due 1988 (9.21% and 7.93% at December 31, 1984 and 1985)	47,500	47,500
Obligations under capital leases—10.20% to 11.00% due 1985-1989	624	473
Various notes—5.00% to 10.75% due 1985-1986	246	145
Total notes and debentures	$852,016	$1,145,383

The unsecured Convertible Floating Rate Notes Due May 15, 1987, are convertible at the option of the holder prior to May 15, 1986, into 9% debentures due 1999. The interest rate is reset semiannually at .65% above the then current interest yield equivalent of the market discount rate of six-month U.S. Treasury bills, subject to a minimum rate of 6.50%. The notes are not redeemable prior to May 15, 1986, but are redeemable thereafter at the option of the Corporation at par plus accrued interest. The 9% debentures due 1999 are not redeemable prior to May 15, 1989, but are redeemable thereafter at the option of the Corporation at prices declining to par by 1995, plus accrued interest. Equal mandatory sinking fund payments are to be made in each of the years 1989 through 1998 in amounts sufficient to retire, at par, 91% of the aggregate principal amount of debentures issued.

The unsecured Floating Rate Notes Due June 1, 1989, are repayable semiannually at par plus accrued interest on any June 1 or December 1, at the option of the holder; the notes are subject to redemption at par plus accrued interest at the option of the Corporation. Interest is payable semiannually at a rate 1% above the yield on certain three-month U.S. Treasury bills. The Corporation may not make any payment or other distribution on its stock in shares of capital stock of Mellon Bank unless Mellon Bank guarantees payment of the principal and interest on these notes.

The unsecured Convertible Floating Rate Notes Due June 15, 1989, are redeemable at par plus accrued interest on and after June 30, 1986, at the option of the Corporation. Interest is payable

10. Notes and debentures (with original maturities over one year) continued

semiannually on June 15 and December 15, at a rate .50% above the yield on certain six-month U.S. Treasury bills. The notes are convertible at the option of the holder at any time prior to June 15, 1988, into 8.5% debentures due 2009; and at the option of the Corporation prior to June 15, 1988, into fixed-rate debentures due 2009 at an interest rate equal to the higher of 8.5% or .65% over the yield on certain 30-year U.S. Treasury securities.

The unsecured Floating Rate Extendible Notes Due April 30, 2000, are repayable in whole or in part on April 30, 1988, and on each subsequent election date at the option of the holder at 100% of their principal amount together with interest to the date of repayment. The extendible notes are subject to redemption by the Corporation in whole or in part on April 30, 1988, and on each subsequent election date and each subsequent redemption date at 100% of their principal amount together with interest to the date of redemption. The interest rate is subject to adjustment on the business day following each weekly auction of 91-day Treasury bills and will be .65% above the interest yield equivalent of the average 91-day Treasury bill auction rate. Interest is payable quarterly on January 30, April 30, July 30 and October 30 of each year.

The 5.375% Convertible Capital Notes Due June 1, 1993, are convertible at the option of the holder into a combination of common and preferred stock of the Corporation. The notes may be redeemed at the option of the Corporation, at a declining rate of premium (.75% and .50% at December 31, 1985 and 1986) and at par after May 31, 1988. Conversions resulted in the issuance of 7,937 and 3,477 common shares and 3,168 and 1,387 preferred shares in 1984 and 1985. Annual sinking fund payments are required in an amount sufficient to redeem $1,000,000 principal amount of the notes. Notes repurchased and notes converted may be used to satisfy sinking fund requirements. Sinking fund requirements were satisfied for 1984 and 1985 through the application of principal amounts of notes converted to date. The Corporation has assumed joint and several liability with Mellon Bank (East) National Association—Mellon Bank (East)—formerly Girard Bank, for payment of principal and interest on the notes. The notes are subordinated to obligations to other creditors of the Corporation and to obligations to depositors and other creditors of Mellon Bank (East).

The unsecured 11.75% Guaranteed Debentures Due March 7, 1995, are subject to redemption on or after March 7, 1992, at the option of the Corporation at a redemption price equal to 100.5% of their principal amount if redeemed during the twelve-month period beginning March 7, 1992, and at a redemption price equal to 100% of their principal amount if redeemed on or after March 7, 1993, in each case plus accrued interest. Interest payments are made annually in arrears commencing March 7, 1986, at an annual rate of 11.75%.

The Floating Rate Subordinated Capital Notes Due November 1996, bear interest, payable quarterly, at a rate equal to 1/8th of 1% above the arithmetic mean of the London Interbank Offered Rates for three-month Eurodollar deposits quoted by certain leading banks. Thirty days prior to maturity, the Corporation will purchase the notes for a purchase price equal to the principal amount plus accrued interest for consideration consisting of cash, capital securities (common stock, perpetual preferred stock or other primary capital securities) or a combination thereof. The Corporation will sell such capital securities on behalf of note holders who elect to receive cash in exchange for their notes. The notes may be purchased, at the option of the

10. Notes and debentures (with original maturities over one year) continued

Corporation, or redeemed, at the option of Mellon Bank, any time after November 1985 in whole or in part for cash. The notes are subordinated to obligations to depositors and other creditors of Mellon Bank.

The capital note agreements of Mellon Bank (East) included in various notes under banking subsidiaries above require the transfer from Mellon Bank (East)'s "retained earnings" to "retained earnings appropriated for capital note retirement" of a monthly amount equaling 1/120th of the principal outstanding on each of the note issues, up to an aggregate of 50% of the outstanding principal. Transfers commenced in July 1980 and 1982 for the notes due in 1985 and 1987 respectively, and commenced in July 1984 for the issue due in 1989. As of December 31, 1984 and 1985, $1,283,050 and $2,518,125 have been transferred for capital note retirement. The notes are subordinated to obligations to depositors and other creditors of Mellon Bank (East), except other capital note holders of Mellon Bank (East) with which they rank equally.

11. Preferred stock

The preferred stock outstanding at December 31, 1985, bears an annual, cumulative dividend of $2.80 per share. The preferred stock will not be redeemed for at least five years from April 12, 1984. From such date until April 30, 1993, the preferred stock will be redeemable at prices declining from $26.40 to $25.28, plus accrued dividends. On April 30, 1994, and on each April 30 thereafter until and including April 30, 2003, the Corporation will be required to redeem 10% of the total number of shares of preferred stock outstanding at the close of business on April 30, 1993, at a price of $25 per share plus accrued dividends, so that the issue will be completely retired by April 30, 2003. The Corporation may, however, elect to satisfy this requirement by crediting shares of preferred stock optionally redeemed or otherwise acquired by the Corporation. In any 12-month period beginning after April 30, 1993, the Corporation has the noncumulative right to retire an additional 10% of the preferred stock outstanding at the close of business on April 30, 1993, at the same price applicable to a mandatory redemption. In the event that the Corporation is liquidated, and after creditors have been paid but before any payments are made with respect to the Corporation's common stock, holders of each share of preferred stock will be entitled to receive $25 per share plus accrued dividends plus a premium if the liquidation is voluntary and occurs before April 30, 1993. Any excess of the redemption amount over the carrying amount will be charged to expense in the year of redemption.

12. Service and trading revenue

Components of service and trading revenue are as follows:

(in thousands)	Year ended December 31, 1983	1984	1985
Service revenue:			
Service charges, fees and commissions	$147,307	$194,070	$232,372
Trust and Investment Department fees	73,831	95,763	116,795
Other service revenue	9,342	12,277	15,949
Total service revenue	$230,480	$302,110	$365,116
Trading revenue:			
Trading account profits and commissions	$ 7,826	$ 5,966	$ 15,917
Gains on sale of mortgages and mortgage-backed securities net of market revaluation	(325)	(1,569)	1,226
Foreign exchange gains	4,300	1,079	5,432
Total trading revenue	$ 11,801	$ 5,476	$ 22,575

13. Taxes

Components of income tax provisions in the consolidated financial statements are presented below. The current and deferred components of the income tax provision for 1983 and 1984 have been restated to reflect tax returns as actually filed.

(in thousands)	Year ended December 31, 1983	1984	1985
Current taxes:			
Federal (after reduction for investment tax credits of $207 in 1983 and $34,054 in 1985)	$ 2,991	$ 2,082	$19,957
State	478	2,800	2,608
Foreign	16,753	18,501	18,278
Subtotal	20,222	23,383	40,843
Deferred taxes:			
Federal	13,025	(30,335)	5,955
State	1,283	263	(391)
Subtotal	14,308	(30,072)	5,564
Total	$34,530	$ (6,689)	$49,407

The principal items of income and expense which give rise to deferred federal income taxes are shown below:

(in thousands)	Year ended December 31, 1983	1984	1985
Provision for possible credit losses	$ 9,044	$(26,231)	$(24,409)
Occupancy expense	(442)	(5,823)	(6,225)
Employee benefits	(2,227)	(1,059)	(2,637)
Investment tax credit	(4,642)	(6,934)	19,689
Lease financing income	7,421	8,376	16,463
Depreciation and amortization	(73)	7,880	7,500
Interest income	4,611	(676)	442
Other, net	(637)	(5,838)	(1,848)
Deferred federal taxes	$13,025	$(30,335)	$ 5,955

A reconciliation of the federal statutory tax rate to the tax rate based on consolidated income before income taxes is as follows:

	1983	1984	1985
Federal statutory tax rate	46.0 %	46.0 %	46.0 %
Statutory tax adjustments:			
Tax-exempt income from loans and securities	(23.7)	(36.3)	(18.7)
Investment tax credit	(2.2)	(4.6)	(5.9)
Tax-exempt income from purchase accounting adjustments	(2.4)	(6.9)	(3.4)
Other, net	(1.9)	(2.6)	1.7
Tax rate based on reported income	15.8 %	(4.4)%	19.7 %

Income before income taxes generated from locations domiciled outside of the United States was $23,565,000, $9,198,000 and $10,424,000 for the years ended December 31, 1983, 1984 and 1985.

14. Employee benefits

Pension plans. Pension expense for 1983, 1984 and 1985 was $13,603,000, $16,500,000 and $16,314,000. In 1985, certain actuarial changes were made relating to the principal salaried pension plan as follows: the actuarial method was changed from the aggregate cost method to the projected unit credit method and the assumed interest rate used to discount the benefit obligation was changed from 7% to 9%. These changes reduced pension expense by $6,843,000 in 1985. Additionally, an Enhanced Early Retirement Plan was offered to certain employees covered by the principal plan. This plan increased pension expense by $6,934,000 in 1985.

14. Employee benefits continued

At January 1, 1984 and 1985, the latest valuation dates, the market value of the plans' assets was $254,569,000 and $282,482,000; the present value of projected benefits payable at retirement was $336,506,000 and $373,674,000; and the present value of accumulated plan benefits was $137,815,000 and $138,370,000 vested, and $12,147,000 and $11,373,000 nonvested. Present values are computed using the plans' actuarial assumptions including weighted average rates of return of 8% for 1984 and 9% for 1985.

Long Term Profit Incentive Plan. The Long Term Profit Incentive Plan (the Plan) provides for the issuance of stock options, stock appreciation rights and performance units to officers and key employees of the Corporation and its subsidiaries. Stock options may be granted at prices not less than the fair market value of the common stock on the date of grant. Options may be exercised during fixed periods of time not to exceed ten years from date of grant.

As of December 31, 1985, options for 777,850 shares are available for grant under the current Plan. No shares are available for grant under prior plans of the Corporation. During 1983, 1984 and 1985 options for 207,500; 249,650 and 284,000 shares were granted and became exercisable. During 1983, 1984 and 1985 options for 47,182; 18,954 and 132,259 shares were exercised.

Additional information concerning options under this Plan is as follows:

		Number of shares	Option price	
			Per share	Aggregate
				(in thousands)
Shares under option at December 31:				
	1983	333,093	$26.50–47.63	$14,011
	1984	553,039	26.50–47.06	21,773
	1985	696,830	26.50–54.81	32,246

In connection with the mergers of Mellon Bank Corporation with The Girard Company and CCB Bancorp, Inc., options to purchase the common stock of those companies and stock appreciation rights outstanding at the respective dates of the mergers were converted into options to purchase a combination of common and preferred shares of the Corporation. The resulting stock of the Corporation under option at December 31, 1985, was 78,555 shares of common and 32,622 shares of preferred stock at option prices ranging from $18.04 to $33.05 for common stock and from $9.86 to $18.22 for preferred stock. No further options or stock appreciation rights have been or will be granted under these plans.

Profit Bonus Plan. At the discretion of the Human Resources Committee of the Board of Directors of the Corporation, awards are made to key employees, payable at the election of the participants in cash or in shares of common stock of the Corporation. Awards are generally payable over a period of three years subject to continued employment of the participants. Amounts awarded were $5,498,000 for 1983, $5,712,000 for 1984 and $8,298,000 for 1985.

15. Restrictions on dividends and regulatory limitations

The Corporation is subject to certain restrictions on the payment of dividends under indentures relating to long-term debt that it acquired in the merger with The Girard Company. Under the most restrictive of these indentures, the Corporation has agreed not to pay dividends or to make any distribution upon any of its capital stock or to purchase or otherwise acquire its own capital stock or to make investments, loans or advances to certain subsidiaries, if the aggregate of all amounts used for such purposes after December 31, 1976 (by The Girard Company up to April 6, 1983, and by the Corporation thereafter), would exceed the sum of 75% of the consolidated net income (of The Girard Company and the Corporation for the respective periods stated) from January 1, 1977, to the close of the most recent fiscal quarter, plus the net proceeds from the issuance of capital stock and the conversion of convertible debt into capital stock after December 31, 1976, plus $10,000,000. As of December 31, 1985, the Corporation had $176,769,000 available for the declaration of dividends under the foregoing restriction.

15. Restrictions on dividends and regulatory limitations continued

The approval of the Office of the Comptroller of the Currency is required if the total of all dividends declared by a national bank in any calendar year exceeds the bank's net profits, as defined, for that year combined with its retained net profits for the preceding two calendar years. Under this dividend limitation formula, the Corporation's bank subsidiaries can, without prior regulatory approval, declare dividends in 1986 of approximately $191,750,000 of their total undivided profits of $830,599,000 at December 31, 1985, plus an additional amount equal to the net profits, as defined, for 1986 up to the date of any such dividend declaration.

The Federal Reserve Act limits extensions of credit by the Corporation's bank subsidiaries to the Corporation and to certain other affiliates of the Corporation, requires borrowings to such companies to be collateralized and limits the amount of investments by the banks in these entities. At December 31, 1985, such extensions of credit and investments were limited in amount to $222,733,000 as to the Corporation and any other affiliate and to $445,466,000 as to the Corporation and all of its other affiliates.

16. Legal proceedings

Various legal proceedings are pending against the Corporation and its subsidiaries. Management believes that the aggregate liability, if any, arising from such proceedings will not have a material adverse effect on the Corporation and its subsidiaries.

17. Commitments and guarantees

In the normal course of business, the Corporation extends commitments and guarantees, which are not included in the financial statements in accordance with generally accepted accounting principles. Management does not anticipate a material loss as a result of the commitments and guarantees.

At December 31, 1985, commitments supported by letters of credit, for which fees are recognized over the commitment period, amounted to $2,845,788,000, net of $900,969,000 that had been conveyed to investors through participation. These commitments consisted of $2,359,030,000 for customer debt obligations and $486,758,000 for customer contract performance obligations. Commitments expiring within one year amounted to $272,976,000, from one to five years amounted to $1,479,355,000, and after five years amounted to $494,355,000.

18. International operations

Selected financial data for international operations are as follows:

In millions	Year ended December 31, 1983	1984	1985
Income statement:			
Interest revenue	$700	$713	$630
Loan fees	9	6	4
Interest expense	590	611	494
Net credit revenue	119	107	140
Provision for possible credit losses	21	51	45
Net credit revenue after provision for possible credit losses	98	56	95
Service and other revenue	22	26	24
Operating expense	71	90	109
Income (loss) before income taxes	49	(8)	10
Provision for income taxes	16	(7)	6
Net income (loss)	$ 33	$ (1)	$ 4

18. International operations continued

(in millions)	December 31, 1984	1983
Balance sheet:		
Assets		
Money market investments:		
Interest-bearing deposits	$2,579	$1,168
Other, principally corporate placements	195	169
Investment securities	87	33
Trading account securities	14	36
Loans, net of unearned discount:		
Commercial and industrial	2,133	2,025
Financial institutions	1,203	1,245
Governments and official institutions	453	517
Other	67	22
Total loans	3,856	3,809
Less: Reserve for possible credit losses	(84)	(111)
Net loans	3,772	3,698
Customers' acceptance liability	2,537	2,125
Other assets	289	216
Total assets	$9,473	$7,445
Liabilities and Capital		
Deposits:		
Demand:		
Banks in foreign countries including foreign branches of U.S. banks	$ 142	$ 89
Foreign governments, official institutions, central banks and international institutions	1	—
Other	130	114
Total demand deposits	273	203
Time:		
Banks in foreign countries including foreign branches of U.S. banks	1,258	761
Foreign governments, official institutions, central banks and international institutions	634	439
Other	1,396	1,437
Total time deposits	3,288	2,637
Total deposits	3,561	2,840
Commercial paper	60	71
Other funds borrowed	62	59
Acceptances outstanding	2,537	2,125
Other liabilities	21	24
Funds provided from domestic operations and capital	3,212	2,326
Total liabilities and capital	$9,473	$7,445

Note: Time deposits include $3,270,000,000 and $2,635,000,000 at December 31, 1984 and 1983, in denominations of $100,000 or greater.

18. International operations continued

Percent of international operations to consolidated amounts:

	1983	1984	1985
Net credit revenue	19%	14%	16%
Income before income taxes	22	—	4
Net income	16	—	2
Net income applicable to common stock	19	—	2
Average total assets	35	32	27
Average total liabilities	36	33	27

Geographic distribution of net credit revenue, service and other revenue, income before income taxes and net income is as follows:

	Net credit revenue			Service and other revenue			Income before income taxes			Net income		
(in millions)	1983	1984	1985	1983	1984	1985	1983	1984	1985	1983	1984	1985
Europe	$ 32	$ 29	$ 30	$ 5	$ 4	$ 5	$ 8	$(1)	$(3)	$ 5	$ 1	$(1)
North America	20	10	21	6	7	6	13	(1)	7	12	—	3
Asia Pacific	12	12	19	7	7	8	4	(4)	(2)	2	(2)	(1)
Latin America	54	53	67	3	4	4	24	(6)	6	14	(2)	2
Middle East and Africa	1	3	3	1	4	1	—	4	2	—	2	1
Total	$119	$107	$140	$22	$26	$24	$49	$(8)	$10	$33	$(1)	$ 4

Geographic distribution of assets at year-end is as follows:

(in millions)	1984	1985
Europe	$3,120	$2,015
North America	1,796	1,744
Asia Pacific	2,632	2,063
Latin America	1,718	1,612
Middle East and Africa	291	122
Total	$9,557	$7,556

Note: Amounts shown are before deducting the reserve for possible credit losses. Geographic distributions of assets and income are based on location of obligor or investment except for assets guaranteed by a third party where location is that of the guarantor.

Income from international operations and the related geographic distribution is determined after internal allocations for taxes, expenses, provision and reserve for possible credit losses, capital and borrowed funds. Such allocations and the underlying assumptions are subjective and may change as management's criteria for evaluating business segment profitability evolve or are revised in response to changing conditions and risks. Expenses charged to international operations include those directly incurred in connection with such activities plus an allocable share of general support and overhead charges.

Report of Independent Accountants

To the Board of Directors and Shareholders of Mellon Bank Corporation:

We have examined the balance sheet of Mellon Bank Corporation (parent Corporation) and the consolidated balance sheet of Mellon Bank Corporation and its subsidiaries as of December 31, 1985 and 1984, and the related statements of income, changes in common shareholders' equity and changes in financial position for each of the years in the three-year period ended December 31, 1985. Our examinations were made in accordance with generally accepted auditing standards and, accordingly, included such tests of the accounting records and such other auditing procedures as we considered necessary in the circumstances.

In our opinion, the aforementioned financial statements present fairly the financial position of Mellon Bank Corporation (parent Corporation) and Mellon Bank Corporation and its subsidiaries at December 31, 1985 and 1984, and the results of their operations and changes in financial position for each of the years in the three-year period ended December 31, 1985, in conformity with generally accepted accounting principles applied on a consistent basis.

Peat, Marwick, Mitchell & Co.

Peat, Marwick, Mitchell & Co.

Pittsburgh, Pennsylvania
January 20, 1986

Five-Year Condensed Income Statement

Mellon Bank Corporation (and its subsidiaries)

	(in thousands)	1981	1982	1983	1984	1985
Net credit revenue	Net credit revenue*	$453,736	$548,355	$725,334	$866,473	$978,678
Service and other revenue	Service revenue:					
	Letters of credit and acceptance financing fees	10,233	14,085	19,423	24,103	30,079
	Charge service fees	5,872	6,604	21,487	30,930	33,742
	Data processing fees	20,541	28,748	38,058	43,049	50,339
	Cash management fees and deposit transaction charges	8,658	13,157	30,156	49,812	65,684
	Mortgage servicing fees	8,562	9,612	20,682	25,807	30,541
	Trust and investment Department fees	31,492	36,638	73,831	95,763	116,795
	Other	17,590	21,040	26,813	32,646	37,936
	Total service revenue	102,948	130,684	230,480	302,110	365,116
	Trading revenue:					
	Trading account profits and commissions	3,897	9,922	7,[illegible]	5,966	15,917
	Gains on sale of mortgages and mortgage-backed securities (net of market revaluation)	(8,657)	5,183	(325)	(1,569)	1,223
	Foreign exchange gains	6,057	5,555	4,300	1,079	5,433
	Total trading revenue	1,297	20,660	11,801	5,476	22,573
	Gains on sale of investment securities	(19,362)	(15,420)	10,797	3,556	92,611
	Other revenue	10,803	12,314	34,318	25,690	12,422
	Total service and other revenue	95,686	148,238	287,396	336,832	492,724
Provision for possible credit losses	Provision for possible credit losses	36,971	68,065	92,199	116,676	143,221
Operating expense	Staff expense	170,941	215,166	349,772	441,866	569,335
	Equipment expense	23,452	31,443	49,091	58,472	68,205
	Net occupancy expense	19,337	22,954	46,484	97,535	109,920
	Shares, capital and franchise taxes	8,737	5,070	13,374	13,631	14,483
	Other expense	78,397	107,224	174,078	203,686	263,640
	Total operating expense	300,864	381,677	631,799	815,350	965,609
Income	Income before income taxes*	211,587	246,331	328,732	271,249	357,372
	Provision for income taxes*	96,076	111,959	144,917	112,705	155,677
	Net income	115,511	134,372	183,815	158,544	201,695
	Dividends on preferred stock	—	—	5,263	9,722	10,224
	Net income applicable to common stock	$115,511	$134,372	$178,552	$148,822	$191,471

*Includes fully taxable equivalent adjustments to net credit revenue.

Consolidated Balance Sheet—
Average Balances and Interest Rates

Mellon Bank Corporation (and its subsidiaries)

	(dollar amounts in millions)	1981 Average balance	1981 Average rate
Assets	**Interest-earning assets:**		
	Money market investments:		
	Interest-bearing deposits with banks	$ 3,603	16.30%
	Federal funds sold and securities purchased under agreements to resell	542	16.75
	Other	210	13.51
	Trading account securities	158	14.19
	Investment securities:		
	U.S. Treasury and agency securities	490	9.81
	Obligations of states and political subdivisions	386	10.11
	Other	70	9.83
	Loans, net of unearned discount	8,585	16.20
	Lease finance assets	174	10.28
	Total loans and lease finance assets	8,759	16.08
	Total interest-earning assets	14,218	15.70%
	Cash and due from banks	1,451	
	Customers' acceptance liability	871	
	Premises and equipment	91	
	Other assets	382	
	Reserve for possible credit losses	(123)	
	Total assets	$16,890	
Liabilities, preferred stock and common shareholders' equity	**Interest-paying liabilities:**		
	Deposits in domestic offices:		
	Demand	$ 218	5.17%
	Savings accounts	774	4.92
	Money market deposit accounts	—	—
	Retail savings certificates	1,304	12.66
	Negotiable certificates of deposit	3,491	16.13
	Other time deposits	94	14.90
	Deposits in foreign offices	2,866	14.72
	Total interest-paying deposits	8,747	13.97
	Federal funds purchased and securities sold under agreements to repurchase	1,908	15.83
	Commercial paper	979	16.59
	Other funds borrowed	323	13.40
	Notes and debentures (with original maturities over one year)	428	13.09
	Total interest-paying liabilities	12,385	14.36%
	Deposits in domestic offices—interest-free	2,404	
	Deposits in foreign offices—interest-free	15	
	Total interest-free deposits	2,419	
	Acceptances outstanding	871	
	Other liabilities	283	
	Total liabilities	15,958	
	Preferred stock	—	
	Common shareholders' equity	932	
	Total liabilities, preferred stock and common shareholders' equity	$16,890	
Rates	Yield on total interest-earning assets		15.70%
	Cost of funds supporting interest-earning assets		12.51
	Net rate on interest-earning assets		3.19%

Note: Rates are calculated on a fully taxable equivalent basis at a rate approximating 46% using actual number of days in year and are before effect of reserve requirements. Fees on loans are included in the calculation of rates. Cash-basis loans and the related income effect have been included in the calculation

1982		1983		1984		1985	
Average balance	Average rate	Average balance	Average rate	Average balance	Average rate	Average balance	Average rate
$ 3,305	13.63%	$ 3,160	9.71%	$ 2,371	10.21%	$ 2,091	9.07%
663	12.17	931	9.34	1,055	10.42	775	8.25
215	11.00	207	7.55	208	8.68	206	9.19
286	12.71	440	10.25	462	11.47	400	9.49
877	11.90	1,250	10.59	917	10.39	1,633	10.00
343	10.20	299	10.99	301	11.41	345	12.82
78	9.82	123	8.75	160	9.55	135	9.27
10,704	14.33	13,729	12.29	17,094	13.08	19,773	11.49
182	10.49	206	10.23	253	11.29	309	10.90
10,886	14.27	13,935	12.26	17,347	13.05	20,082	11.48
16,653	13.76%	20,345	11.50%	22,821	12.41%	25,687	11.05%
1,315		1,529		1,634		1,547	
1,094		1,741		2,347		2,078	
173		241		298		366	
458		596		774		921	
(154)		(220)		(273)		(331)	
$19,539		$24,232		$27,601		$30,246	
$ 308	5.16%	$ 565	4.81%	$ 699	4.81%	$ 621	5.31%
752	5.00	900	4.84	983	5.13	914	5.15
13	9.75	1,649	8.55	2,405	9.21	3,309	7.28
1,698	12.06	2,068	10.64	2,863	10.58	2,956	9.39
4,247	12.43	3,019	9.57	3,060	10.74	3,282	8.80
55	10.89	233	9.63	834	10.00	832	9.16
2,969	12.24	3,239	8.90	2,973	9.54	2,962	8.66
10,042	11.52	11,673	8.84	13,817	9.44	14,876	8.20
2,925	12.00	3,984	9.12	3,694	10.34	4,973	7.81
1,080	12.98	1,225	9.32	1,475	10.63	1,412	8.32
422	11.93	507	9.77	529	10.77	351	8.83
417	12.09	565	10.05	613	10.89	1,058	9.48
14,886	11.71%	17,954	8.99%	20,128	9.77%	22,670	8.19%
2,220		2,870		3,181		3,364	
18		36		11		10	
2,238		2,906		3,192		3,374	
1,096		1,742		2,349		2,077	
301		329		405		470	
18,521		22,931		26,074		28,591	
—		48		89		93	
1,018		1,253		1,438		1,562	
$19,539		$24,232		$27,601		$30,246	
	13.76%		11.50%		12.41%		11.05%
	10.47		7.93		8.61		7.24
	3.29%		3.57%		3.80%		3.81%

of rates. Rates for notes and debentures and total interest paying liabilities are computed net of obligations under purchase option pr premises on which interest was capitalized in 1982 and 1983.

Domestic and International Balance Sheet—Average Balances and Interest Rates

Mellon Bank Corporation (and its subsidiaries)

	(dollar amounts in millions)	1983 Average balance	1983 Interest revenue/ expense	1983 Average rate
Domestic operations	**Interest-earning assets:**			
	Interest-bearing deposits with banks	$ 8	$ 1	10.53%
	Federal funds sold and securities purchased under agreements to resell	931	87	9.34
	Other money market investments	—	—	—
	Trading account securities	418	43	10.28
	U.S. Treasury and agency securities	1,250	132	10.59
	Obligations of states and political subdivisions	299	33	10.99
	Other investment securities	63	6	9.13
	Loans and lease finance assets	10,642	1,325	12.45
	Total interest-earning assets	13,611	$1,627	11.95%
	Other assets	2,033		
	Total assets	$15,644		
	Interest-paying liabilities:			
	Deposits in domestic offices:			
	Demand deposits	$ 563	$ 27	4.81%
	Savings accounts	900	44	4.84
	Money market deposit accounts	1,649	141	8.55
	Retail savings certificates	2,068	220	10.64
	Negotiable certificates of deposit	2,969	282	9.50
	Other time deposits	108	11	9.61
	Total interest-paying deposits	8,259	725	8.77
	Federal funds purchased and securities sold under agreements to repurchase	3,984	363	9.12
	Other funds borrowed	1,667	158	9.51
	Funds provided to international operations	(2,810)	(277)	9.86
	Notes and debentures	565	55	10.00
	Total interest-paying liabilities	11,665	1,024	8.80
	Other funds supporting earning assets	1,946	—	—
	Total funds supporting earning assets	13,611	$1,024	7.52%
	All other funds	2,033		
	Total liabilities and capital	$15,644		
	Domestic net credit revenue and net rate		$ 603	4.43%
International operations	**Interest-earning assets:**			
	Interest-bearing deposits with banks	$ 3,152	$ 306	9.71%
	Other money market investments	207	16	7.55
	Trading account securities	22	2	9.66
	Other investment securities	60	5	8.36
	Loans	3,293	383	11.64
	Total interest-earning assets	6,734	$ 712	10.57%
	Other assets	1,854		
	Total assets	$ 8,588		
	Interest-paying liabilities:			
	Deposits	$ 3,417	$ 307	9.00%
	Other funds borrowed	6	6	8.03
	Funds provided by domestic operations	2,810	277	9.86
	Total interest-paying liabilities	6,289	590	9.37
	Other funds supporting earning assets	445	—	—
	Total funds supporting earning assets	6,734	$ 590	8.75%
	All other funds	1,854		
	Total liabilities and capital	$ 8,588		
	International net credit revenue and net rate		$ 122	1.82%

Note: Interest revenue and expense amounts are presented on a fully taxable equivalent basis at a rate approximating 46%. Rates are calculated using dollar amounts in thousands and actual number of days in

1984 Average balance	1984 Interest revenue/ expense	1984 Average rate	1985 Average balance	1985 Interest revenue/ expense	1985 Average rate
$ 5	$ 1	10.90%	$ —	$ —	—%
1,075	110	10.42	775	64	8.25
34	3	9.51	—	—	—
449	52	11.53	387	37	9.52
917	95	10.39	1,633	163	10.00
301	34	11.41	345	44	12.82
67	7	9.93	65	7	10.18
13,599	1,809	13.31	16,289	1,883	11.56
16,427	$2,111	12.85%	19,494	$2,198	11.27%
2,370			2,573		
$18,797			$22,067		
$ 699	$ 34	4.81%	$ 621	$ 33	5.31%
983	50	5.13	914	47	5.15
2,405	221	9.21	3,309	241	7.28
2,863	303	10.58	2,958	278	9.39
3,038	326	10.72	3,282	289	8.80
588	57	9.65	570	36	6.36
10,576	991	9.37	11,652	924	7.93
3,694	382	10.34	4,973	388	7.81
1,856	199	10.73	1,620	137	8.41
(2,684)	(283)	10.53	(2,239)	(186)	8.28
613	67	10.89	1,058	100	9.48
14,055	1,356	9.65	17,064	1,363	7.99
2,372	—	—	2,430	—	—
16,427	$1,356	8.25%	19,494	$1,363	6.99%
2,370			2,573		
$18,797			$22,067		
	$ 755	4.60%		$ 835	4.28%
$ 2,366	$ 241	10.21%	$ 2,091	$ 190	9.07%
174	15	8.52	206	19	9.19
13	1	9.42	13	1	8.72
93	9	9.27	70	6	8.42
3,748	456	12.14	3,793	422	11.14
6,394	$ 722	11.29%	6,173	$ 638	10.34%
2,410			2,006		
$ 8,804			$ 8,179		
$ 3,241	$ 313	9.67%	$ 3,224	$ 296	9.19%
148	15	9.92	143	12	8.57
2,684	283	10.53	2,239	186	8.29
6,073	611	10.05	5,606	494	8.82
321	—	—	567	—	—
6,394	$ 611	9.55%	6,173	$ 494	8.01%
2,410			2,006		
$ 8,804			$ 8,179		
	$ 111	1.73%		$ 144	2.33%

year and are before effect of reserve requirements. Fees on loans are included in the calculation of rates. Cash basis loans and the related income effect have been included in the calculation of rates.

Principal Locations

Domestic

California
Los Angeles
555 South Flower Street
Los Angeles, California 90071
Telephone: 213-624-0913

San Francisco
595 Market Street
San Francisco, California 94105
Telephone: 415-495-5180

Colorado
Denver
1775 Sherman Street
Denver, Colorado 80203
Telephone: 303-837-2180

Delaware
Wilmington
10th & Market Streets
Wilmington, Delaware 19801
Telephone: 302-429-4600

Florida
Boca Raton
5550 Glades Road
Boca Raton, Florida 33431
Telephone: 305-368-6080

Georgia
Atlanta
225 Peachtree Street, N.E.
Atlanta, Georgia 30303
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Illinois
Chicago
55 West Monroe Street
Chicago, Illinois 60603
Telephone: 312-341-6666

55 East Jackson Boulevard
Chicago, Illinois 60604
Telephone: 312-341-6600

Oak Brook
1415 West 22nd Street
Oak Brook, Illinois 60521
Telephone: 312-986-2000

Louisiana
New Orleans
3850 North Causeway Boulevard
Metairie, Louisiana 70002
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551 Madison Avenue
New York, New York 10022
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88 Pine Street
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100 Seneca Street
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Philadelphia, Pennsylvania 19102
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Pittsburgh
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Pittsburgh, Pennsylvania 15258
Telephone: 412-234-5000

Commerce Court
4 Station Square
Pittsburgh, Pennsylvania 15219
Telephone: 412-391-5210

State College
341 North Science Park Road
State College, Pennsylvania 16803
Telephone: 814-234-6300

Texas
Dallas
2121 San Jacinto Tower
Dallas, Texas 75201
Telephone: 214-979-0053

Houston
1100 Louisiana Street
Houston, Texas 77002
Telephone: 713-659-6066

3100 Travis Street
Houston, Texas 77006
Telephone: 713-525-8000

Additional Locations
The Mellon Banks operate 652 domestic banking locations, including 316 community banking offices. Mellon Financial Services operates 147 branch offices in 19 states.

Abroad

Argentina
Buenos Aires
25 de Mayo 555
1002 Buenos Aires, Argentina
Telephone: 313-0798

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BHP House, 140 William Street
Melbourne, Victoria 3000,
Australia
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Sydney
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19 Martin Place
Sydney, N.S.W. 2000, Australia
Telephone: 232-7744

Brazil
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Av. Rio Branco, 138, Andar 17
Rio de Janeiro, Brazil
Telephone: 221-1445

Canada
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One First Canadian Place
Toronto, Ontario, M5X 1A4,
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Telephone: 416-362-6051

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P.O. Box 710
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3701 Edinburgh Tower
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Chiyoda-ku, Tokyo 100, Japan
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1725, Daewoo Center Building
541, 5-ka, Namdaemun-ro,
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Edificio Omega
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11560 Mexico, D.F.
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Republic of Singapore
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Cutlers Gardens
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Multicentro Empresarial del Este
Torre Libertador Nucleo A
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Directors

Mellon Bank Corporation

John M. Arthur
Chairman
Duquesne Light Company
Electric utility

J. David Barnes
Chairman and Chief Executive Officer
Mellon Bank Corporation and
Mellon Bank

Howard O. Beaver, Jr.
Retired Chairman and Chief
Executive Officer
Carpenter Technology Corporation
Wrought specialty steel producer

Robert J. Buckley
Chairman and Chief Executive Officer
Allegheny International, Inc.
Multi national, multi product
specialty manufacturing

Alexander W. Calder
Chairman, President and
Chief Executive Officer
Joy Manufacturing Company
Machinery and equipment

Edward Donley
Chairman
Air Products and Chemicals, Inc.
Industrial gases, chemical products,
industrial process equipment and
construction and engineering services

William B. Eagleson, Jr.
Retired Chairman
Mellon Bank Corporation,
Mellon Bank (East)
and Mellon Bank (DE)

George T. Farrell
President
Mellon Bank Corporation and
Mellon Bank

C. Frederick Fetterolf
President and Chief Operating Officer
Aluminum Company of America
Production and sale of alumina and
chemical products, primary aluminum
and aluminum mill products

W. H. Krome George
Chairman of the Executive Committee
Aluminum Company of America
Production and sale of alumina and
chemical products, primary aluminum
and aluminum mill products

Thomas C. Graham
Vice Chairman and
Chief Operating Officer—
Steel & Related Resources
United States Steel Corporation
Diversified manufacturing and
energy-producing company

Elmer G. Grant
Vice Chairman
Mellon Bank Corporation and
Mellon Bank

Pryce Jordan
President
The Pennsylvania State University

Robert E. Kirby
Retired Chairman and
Chief Executive Officer
Westinghouse Electric Corporation
Electric equipment

G. Christian Lantzsch
Vice Chairman and Treasurer
Mellon Bank Corporation
Vice Chairman
Mellon Bank

Andrew W. Mathieson
Executive Vice President
Richard K. Mellon and Sons
Investments and philanthropy

Seward Prosser Mellon
President
Richard K. Mellon and Sons
Investments and philanthropy

Nathan W. Pearson
Financial Advisor
Paul Mellon Family Interests

Robert R. Price
Chairman and Chief Executive Officer
Mellon Bank (North)

Gerald G. Probst
Chairman and Chief Executive Officer
Sperry Corporation
Manufacturer of information
processing systems, electronics,
command and control systems
and farm machinery

H. Robert Sharbaugh
Retired Chairman
Sun Company, Inc.
Energy

Richard M. Smith
Retired Vice Chairman
Bethlehem Steel Corporation
Integrated steel producer engaged
primarily in the manufacture and
sale of steel and steel products

William P. Snyder III
President
The Shenango Furnace Company
Pig iron, coke and ingot molds

Norman M. Steere
Vice Chairman
Mellon Bank Corporation
and Mellon Bank

Leon H. Sullivan
Pastor
Zion Baptist Church of Philadelphia
Chairman of the Board
OIC International, Inc.
Manpower skills, worldwide training
for the unskilled and unemployed

James W. Wilcock
Chairman and President
PACE Industries, Inc.
A private, diversified manufacturing
and services company
Retired Chairman and
Chief Executive Officer
Joy Manufacturing Company
Machinery equipment

L. Stanton [illegible]
Retired Chairman and
Chief Executive Officer
PPG Industries, Inc.
Manufacturer of glass, chemicals,
coatings and fiber glass

William S. Woodside
Chairman and Chief Executive Officer
American Can Company
International company engaged primarily
in worldwide packaging, specialty
retailing and financial services

William J. Young
President
Portland Cement Association
Trade association for the
portland cement industry

Advisory Board

Fletcher L. Byrom

Michael D. Dingman

James H. Higgins

Chairmen Emeriti

William B. Eagleson, Jr.

James H. Higgins

John A. Mayer

Mellon Bank

John M. Arthur
J. David Barnes
Robert J. Buckley
Alexander W. Calder
Edward Donley
William B. Eagleson, Jr.
George T. Farrell
C. Frederick Fetterolf
W. P. Krome George
Thomas C. Graham
Elmer G. Grant
Robert Z. Kirby
G. Christian Lantzsch
Andrew W. Mathieson
Seward Prosser Mellon
Nathan W. Pearson
William P. Snyder III
Norman M. Steere
James W. Wilcock
Stanton Williams
William S. Woodside

Mellon Bank (East)

J. David Barnes
Howard O. Beaver, Jr.
Lewis W. Bluemle, Jr.
William B. Eagleson, Jr.
Craig G. Ford
Vincent E. Furey, Jr.
Pemberton Hutchinson
Thomas V. Lefevre
Mary Ellin Meyerson
Helen S. Meyner
Edward A. Montgomery, Jr.
Roland Morris
John R. Park
F. Markoe Rivinus
H. Robert Sharbaugh
Richard M. Smith
Francis R. Strawbridge III
Leon H. Sullivan
William J. Young

Mellon Bank (DE)

John S. Barry
James Beebe, Jr.
Courtland A. Bell, Jr.
Eugene D. Bookhammer
Robert D. Burris
Betty L. Chambers
Robert C. Cole, Jr.
Carl DeMartino
Arden B. Engebretsen
Craig G. Ford
John E. Healy II
H. Harrison Kephart, Jr.
Garrett B. Lyons
W. Charles Parndee, Jr.
Bruce M. Sturgatt
John G. Townsend II

Mellon Bank (Central)

Roswell Brayton, Sr.
Galen E. Dreibelbis
Craig G. Ford
Sidney Friedman
John Lloyd Hanson
F. Enos Harley
Robert L. Hite
Robert R. Hoover
Bryce Jordan
Edwin E. Lash
Robert F. Mattern
G. Henry McCormick
Richard L. McMaster
Harry M. Metz
Dale W. Miller
Alvin L. Snowiss
Robert M. Welham
John J. Wolf

Mellon Bank (North)

James D. Berry III
J. W. Bingham
William S. DeArment
John J. Finn
Craig G. Ford
M. Fletcher Gornall
Robin D. Hart
J. Douglas James
George A. Lang, Jr.
Richard C. Lyons
Roger A. Markle
C. J. Myron
John S. Patton
Robert R. Price
Daryl W. Rhea
Paul D. Shafer, Jr.
James A. Stranahan III
Quentin E. Wood

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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

N

For the quarter ended
March 31, 1986

0-6772
Commission File No.

30

MELLON BANK CORPORATION
(Exact name of registrant as specified in its charter)

Pennsylvania	25-1233834
(State or other jurisdiction of incorporation or organization)	(I.R.S. Employer Identification No.)

One Mellon Bank Center
Pittsburgh, Pennsylvania 15258
(Address of principal executive offices)(Zip Code)

Registrant's telephone number, including area code -- (412) 787-5534

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 the filing requirements for the past 90 days.

Yes ✓ No ___

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

Class	Outstanding as of March 31, 1986
Common Stock, $0.50 par value	27,252,336

FORM 10-Q
March 31, 1986

MELLON BANK CORPORATION
and its subsidiaries

PART I - FINANCIAL INFORMATION

Item 1. Financial Statements

All financial information, with the exception of the Computation of Primary and Fully-Diluted Earnings Per Share, the Ratios of Earnings to Fixed Charges and the Ratios of Earnings to Combined Fixed Charges and Preferred Stock Dividends, is contained in the Mellon Bank Corporation First Quarter Report 1986 which is being filed herewith as Exhibit 20.1 and such information is hereby incorporated by reference.

In the opinion of management, all adjustments necessary to a fair statement of the results of the periods presented have been included.

	Three months ended March 31,	
	1985	1986
RATIOS OF EARNINGS TO FIXED CHARGES:		
Mellon Bank Corporation (parent Corporation) (1)	1.34	1.43
Mellon Bank Corporation and its Subsidiaries (2):		
Excluding interest on deposits	1.32	1.37
Including interest on deposits	1.10	1.15
RATIOS OF EARNINGS TO COMBINED FIXED CHARGES AND PREFERRED STOCK DIVIDENDS:		
Mellon Bank Corporation (parent Corporation) (1)	1.20	1.30
Mellon Bank Corporation and its Subsidiaries (2):		
Excluding interest on deposits	1.28	1.33
Including interest on deposits	1.09	1.14

PART I - FINANCIAL INFORMATION

(1) Parent Corporation-The parent Corporation ratios include the accounts of Mellon Bank Corporation (the "Corporation") and Mellon Financial Company, a wholly-owned subsidiary of the Corporation that functions as a financing entity for the Corporation and its subsidiaries by issuing commercial paper and other debt guaranteed by the Corporation. For purposes of computing these ratios, earnings represent parent Corporation income before income taxes and before undistributed income/(losses) of subsidiaries, plus the fixed charges of the parent Corporation. Fixed charges represent interest expense, one-third (the proportion deemed representative of the interest factor) of rental expense and amortization of debt issuance costs. Preferred stock dividend requirements represent the pre-tax earnings that would be required to cover the Corporation's preferred stock dividends. Because the ratio excludes from earnings the undistributed net income of subsidiaries, the ratio varies with the payments of dividends by such subsidiaries.

(2) Consolidated-For purpoces of computing these ratios, earnings represent consolidated net income, plus total U.S. and foreign income taxes provided in computing consolidated net income, plus consolidated fixed charges. Fixed charges, excluding interest on deposits, include interest expense (other than on deposits), one-third (the proportion deemed representative of the interest factor) of rental expense net of income from subleases, and amortization of debt issuance costs. Fixed charges, including interest on deposits, include all interest expense, one-third (the proportion deemed representative of the interest factor) of rental expense net of income from subleases, and amortization of debt issuance costs. Preferred stock dividend requirements represent the pre-tax earnings that would be required to cover the Corporation's preferred stock dividends.

PART II - OTHER INFORMATION

Item 6. Exhibits

(a) Exhibits

11.1 Computation of Primary and Fully-Diluted Earnings Per Share.

12.1 Computation of Ratios of Earnings to Fixed Charges and Ratios of Earnings to Combined Fixed Charges and Preferred Stock Dividends (parent Corporation).

12.2 Computation of Ratios of Earnings to Fixed Charges and Ratios of Earnings to Combined Fixed Charges and Preferred Stock Dividends (Consolidated).

20.1 Mellon Bank Corporation First Quarter Report 1986.

PART II - OTHER INFORMATION (Continued)

(b) Reports on Form 8-K

During the first quarter of 1986, the Corporation filed the following Current Reports on Form 8-K:

(1) A report dated January 21, 1986 for the purpose of filing the Corporation's press release of 1985 financial statements and supplemental information.

(2) A report dated February 3, 1986 for the purpose of filing the Second Supplemental Indenture dated February 3, 1986 to Registration Statement Nos. 2-83530 and 33-01628 pertaining to certain debt securities of Mellon Financial Company and related guarantees of the Corporation.

(3) A report dated February 4, 1986 relating to the issuance and sale of Australian Dollar Notes Due February 14, 1989.

(4) A report dated February 21, 1986 relating to the issuance and sale of 9% Notes Due March 1, 1996.

(5) A report dated March 4, 1986 for the purpose of filing audited excerpts of the Corporation's 1985 Annual Report to Shareholders and filing Commonwealth National Financial Corporation's audited 1985 Annual Report, information included in a Prospectus Supplement to Registration Statement File No. 33-01397 relating to the merger of Commonwealth into the Corporation.

The Corporation also filed a report on Form 8-K dated April 2, 1986 for the purpose of filing the press release of Mellon Bank Corporation announcing consummation of the merger of Commonwealth National Financial Corporation with and into the Corporation. No financial statements were filed as part of such report.

SIGNATURE

Pursuant to the requirements of the Securities Exchange Act of 1934, the Registrant has duly caused this Report to be signed on its behalf by the undersigned thereunto duly authorized.

MELLON BANK CORPORATION
(Registrant)

Date: May 12, 1986

By: G. C. Lantzsch
G. Christian Lantzsch
Vice Chairman and Treasurer
(Duly Authorized Officer of
Registrant and Principal
Financial Officer of Registrant)

Exhibit 11.1

Mellon Bank Corporation

Computation of Primary and Fully-Diluted Earnings Per Share

	Three months ended March 31, 1985	1986
Primary earnings per common share		
Stock and Stock Equivalents (average shares):		
Common shares outstanding	26,717,259	27,167,912
Common stock equivalents (a)	624,448	715,623
Shares assumed to be repurchased under the treasury stock method at quarter average market prices	(485,454)	(538,379)
Total	26,856,253	27,345,156
Net income applicable to common stock	$ 39,007,000	$ 57,909,000
Primary earnings per common share	$1.45	$2.12
Reported earnings per common share (b)	$1.46	$2.13
Fully-diluted earnings per common share		
Stock, Stock Equivalents and Dilutive Items (average shares):		
Common shares outstanding	26,717,259	27,167,912
Common stock equivalents (a)	624,448	715,623
Shares assumed to be repurchased under the treasury stock method at the greater of the quarter-end closing or quarter average market prices	(485,454)	(447,750)
Shares issuable upon assumed conversion of 5 3/8% Convertible Capital Notes	25,808	22,325
Total	26,882,061	27,458,110
Net income applicable to common stock	$ 39,007,000	$ 57,909,000
Add: After-tax benefit of interest expense saved on assumed conversion of 5 3/8% Convertible Capital Notes	6,000	5,000
Adjusted net income	$ 39,013,000	$ 57,914,000
Fully-diluted earnings per common share	$1.45	$2.11

(a) Common stock equivalents consist of stock options.

(b) Earnings per share presented in the First Quarter Reports to Shareholders are computed by dividing net income, after deducting dividends on preferred stock, by the weighted average number of common shares outstanding during the periods. The effect of common stock equivalents on primary earnings per share was less than one percent for each of the above periods presented.

Exhibit 12.1

COMPUTATION OF RATIOS OF EARNINGS TO FIXED CHARGES AND RATIOS OF EARNINGS TO COMBINED FIXED CHARGES AND PREFERRED STOCK DIVIDENDS

Mellon Bank Corporation
(parent Corporation)

		Three months ended March 31,	
		1985	1986
		(dollar amounts in thousands)	
1.	Income before income taxes and before undistributed income/ (losses) of subsidiaries	$14,138	$19,152
2.	Fixed charges-interest expense, one-third of rental expense, and amortization of debt issuance costs	41,676	44,039
3.	Preferred stock dividend requirements	4,652	4,623
4.	Income before income taxes and before undistributed income/ (losses) of subsidiaries, plus fixed charges (Line 1 + Line 2)	$55,814	$63,191
5.	Ratio of earnings (as defined) to fixed charges (Line 4 ÷ Line 2)	1.34	1.43
6.	Ratio of earnings (as defined) to combined fixed charges and preferred stock dividends (Line 4 ÷ [Line 2 + Line 3])	1.20	1.30

Exhibit 12.2

COMPUTATION OF RATIOS OF EARNINGS TO FIXED CHARGES AND RATIOS OF EARNINGS TO COMBINED FIXED CHARGES AND PREFERRED STOCK DIVIDENDS

Mellon Bank Corporation
and its Subsidiaries

	Three months ended March 31, 1985	1986
	(dollar amounts in thousands)	
1. Net income	$ 41,523	$ 60,432
2. Total U.S. and foreign income taxes provided	8,967	11,652
3. Net income before income taxes (Line 1 + Line 2)	$ 50,490	$ 72,084
4. Fixed charges:		
a. Interest expense (excluding interest on deposits)	$150,562	$190,791
b. One-third of rental expense net of income from subleases, and amortization of debt issuance costs	5,941	6,265
c. Total fixed charges (excluding interest on deposits) (Line 4a + Line 4b)	156,503	197,056
d. Interest on deposits	325,778	286,369
e. Total fixed charges (Line 4c + Line 4d)	$482,281	$483,425
5. Preferred stock dividend requirements	$ 4,652	$ 4,623
6. Net income before income taxes plus total fixed charges:		
a. Excluding interest on deposits (Line 3 + Line 4c)	$206,993	$269,140
b. Including interest on deposits (Line 3 + Line 4e)	$532,771	$555,509

Exhibit 12.2
(continued)

COMPUTATION OF RATIOS OF EARNINGS TO FIXED CHARGES AND RATIOS OF EARNINGS TO COMBINED FIXED CHARGES AND PREFERRED STOCK DIVIDENDS

Mellon Bank Corporation
and its Subsidiaries

	Three months ended March 31, 1985	1986
7. Ratios of earnings (as defined) to fixed charges:		
a. Excluding interest on deposits (Line 6a ÷ Line 4c)	1.32	1.37
b. Including interest on deposits (Line 6b ÷ Line 4e)	1.10	1.15
8. Ratios of earnings (as defined) to combined fixed charges and preferred stock dividends:		
a. Excluding interest on deposits (Line 6a ÷ [Line 4c + Line 5])	1.28	1.33
Including interest on deposits deposits (Line 6b ÷ [Line 4e + Line 5])	1.09	1.14

Mellon Bank Corporation
First Quarter Report 1984

Exhibit 20.1

1

In The First Quarter 1986

- Net income increased 46% to $60.4 million; net income per common share increased 46% to $2.13.
- Total assets increased by 11% to $34.1 billion; loans and leases increased by 15% to $22.5 billion.
- Service revenue increased by 26% to $107.0 million.
- The Corporation's financial position was strengthened by a $62.0 million addition to the reserve for possible credit losses.
- The Corporation finalized its merger with Commonwealth National Financial Corporation, which was completed on April 2.

(dollar amounts in millions, except per share amounts)	1985	1986	Increase/(decrease)	
For the three months ended March 31				
Net income	$ 41.5	$ 60.4	$ 18.9	46%
Net income applicable to common stock	39.0	57.9	18.9	48
Dividends on common stock	17.9	18.7	.8	4
Per common share:				
Net income	$ 1.46	$ 2.13	$ .67	46%
Dividends	.67	.69	.02	3
Balances at March 31				
Total assets	$30,657	$34,063	$3,406	11%
Loans and lease finance assets	19,656	22,517	2,861	15
Deposits	18,523	18,752	229	1
Common shareholders' equity	1,523	1,683	160	11
First quarter ratios				
Return on assets *(annualized)*	.53%	.71%		
Assets to common shareholders' equity	19.8	19.8		
Return on common shareholders' equity *(annualized)*	10.5 %	14.1 %		
Primary capital as a percentage of total assets	6.71%	6.78%		

To Our Shareholders

Mellon Bank Corporation achieved strong earnings growth in the first quarter of 1986. Net income increased 46 percent, to $60.4 million, or $2.13 per common share, from $41.5 million, or $1.46 per common share, in the first quarter of 1985. These results primarily reflect good performance in our credit and operating services businesses. We also realized improved trading profits as well as substantial gains on the sale of investment securities, and further strengthened the balance sheet by a $62 million increase in the reserve for possible credit losses.

Our first quarter performance indicates that many of the strategies we have been pursuing —including the continuous building of our core businesses, increased operating efficiency, development of new revenue sources, and maintenance of our financial strength—have begun to deliver positive results.

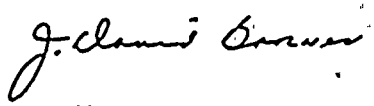
Mellon's core businesses continue to perform well. During the quarter, we achieved sizable increases in net credit revenue and service revenue. We are stressing quality customer service and the development of sophisticated credit and service revenue products.

Operating efficiency has been increased dramatically through integration of the systems of our domestic banks. We have put in place sophisticated operating systems that support the full array of products and services offered by all our banks. Completion of this effort was partly responsible for the significant slowing in operating expenses we experienced in the first quarter.

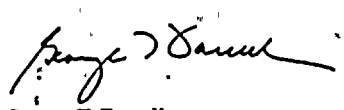
We continue to achieve outstanding performance in capital markets activities. Our capabilities in this area enabled us to take full advantage of the falling interest rate environment that existed in the first quarter, resulting in substantial trading profits and securities gains. Recent history has proven that our capital markets skills enhance the Corporation's earnings capacity and complement our core businesses.

Our ongoing emphasis on financial strength is especially important in today's financial services marketplace. For example, as we had anticipated in view of several factors present in the market—including the potential effects of depressed energy prices and renewed economic pressure on some Latin American nations—the Corporation experienced an increased level of nonperforming assets during the first quarter. Asset quality will likely be a concern for major bank holding companies throughout the balance of the year. Our long-standing credit management expertise, high-quality loan portfolio, and strong loan loss reserve place the Corporation in a position to prosper in the challenging year ahead.

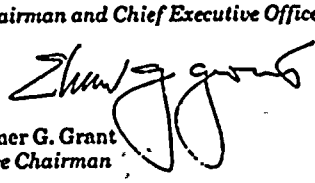
With an encouraging first quarter behind us and a solid strategy in place, we face the balance of 1986 with confidence and enthusiasm.



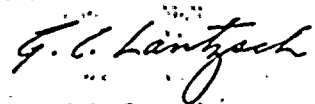
J. David Barnes
Chairman and Chief Executive Officer



George T. Farrell
President



Elmer G. Grant
Vice Chairman



G. Christian Lantzsch
Vice Chairman and Treasurer

Edward A. Montgomery, Jr.
Vice Chairman

Norman M. Steere
Vice Chairman

News Briefs

New Directors Elected

Shareholders have elected six new members to Mellon Bank Corporation's board of directors. Joining the board are:

- Donna R. Ecton, vice president-administration of Campbell Soup Company, a position she has held since joining Campbell in 1983. Previously, Ms. Ecton had been president of a New York executive recruiting firm and had spent nearly 10 years in banking. She is a 1969 graduate of Wellesley College and earned an M.B.A. from Harvard University in 1971.

- Charles F. Merrill, chairman, president and chief executive officer of The Commonwealth National Bank. Mr. Merrill joined Commonwealth in 1982. Previously, he held executive positions at two other banks. He is a 1955 graduate of Amherst College.

- Edward A. Montgomery, Jr., chairman and chief executive officer of Mellon Bank (East) and vice chairman of Mellon Bank Corporation. Mr. Montgomery, who joined Mellon in 1959, has held his current position since 1985. He was previously senior vice president and head of the Real Estate Department. He is a 1956 graduate of Trinity College and earned his M.B.A. at Harvard University in 1959.

- Vincent A. Sarni, chairman and chief executive officer of PPG Industries, Inc. Mr. Sarni spent 12 years with Olin Corporation before joining PPG in 1968. He held various executive positions at PPG before being elected to his current post in 1984. He is a graduate of the University of Rhode Island and did graduate work at New York University and Harvard University.

- David S. Shapira, president and chief executive officer of Giant Eagle, Inc. Mr. Shapira joined Giant Eagle, the largest chain of grocery stores in western Pennsylvania, in 1970. He has held his current position since 1980. Mr. Shapira earned his undergraduate degree at Oberlin College in 1963 and his M.A. at Stanford University in 1964.

- Quentin E. Wood, chairman and chief executive officer of Quaker State Oil Refining Corporation. Mr. Wood, who joined the company in 1948, has held his current position since 1982. He is a 1948 graduate of The Pennsylvania State University.

Retiring from the board are William B. Eagleson, Jr., W. H. Krome George, Robert R. Price, William P. Snyder III and James W. Wilcock. The Corporation appreciates their dedicated service throughout their terms as directors.

Commonwealth Merger Completed

Mellon Bank Corporation's merger with Commonwealth National Financial Corporation of Harrisburg, Pennsylvania, was completed on April 2, increasing to 28 the number of counties in Pennsylvania in which Mellon has on-site presence.

Commonwealth, with assets of $1.5 billion at March 31, 1986, has 43 branch offices and 31 CashStream/CIRRUS automated teller machine locations in four south central Pennsylvania counties.

Under the terms of the merger, The Commonwealth National Bank and Commonwealth National Life Insurance Company become wholly-owned subsidiaries of the Corporation. The Commonwealth National Bank provides consumer and commercial banking and personal and corporate trust services throughout its market.

Mellon Plans to Open Bank in Maryland

Mellon Bank Corporation plans to open a new banking subsidiary, Mellon Bank (MD), in the second quarter of 1986.

Mellon Bank (MD) will be a federally-insured, state-chartered institution operating eight branch offices in three Maryland counties. At its opening, it will have assets of approximately $347 million and deposits of about $323 million.

Mellon was invited in February by the state of Maryland to consider acquiring the business of the former Community Savings and Loan, Inc. of Bethesda, which had been closed and placed in state-controlled conservatorship in September 1985.

The Corporation has reached definitive agreements with the Maryland Deposit Insurance Fund to purchase certain assets and assume certain deposit liabilities of Community. Mellon will make an investment of $37.5 million—a $14 million premium for Community's core deposits and $23.5 million for capitalization of the newly-organized Mellon Bank (MD).

The transaction requires the approvals of the Federal Reserve Board, the Maryland Commissioner of Banking and the Maryland Circuit Court.

Carleton, Fidata Acquisitions Bring New Markets to Mellon

Mellon will enter new markets in mutual fund and mortgage loan processing, and the sale and licensing of financial data processing services as a result of three acquisitions completed in the first quarter.

On March 14, Mellon completed the purchase of Fidata Systems Incorporated, and the purchase of certain assets and the assumption of certain liabilities of Fidata Trust Company Massachusetts. The Boston-based companies, which provide mutual fund accounting and record-keeping services, were combined into a new entity known as the Mutual Fund Services Group of Mellon Financial Services Corporation.

Carleton Financial Computations, Inc., based in South Bend, Indiana, became a subsidiary of the Corporation on February 28. Carleton and its primary subsidiary, Data-Link Systems, Inc., provide financial data processing services to financial institutions throughout the United States and Canada. In addition to its expertise in providing data processing services to mortgage banking companies and thrift institutions, Data-Link will continue to sell and license computer software.

Financial Review

Earnings performance

(in millions, except per share amounts)	Three months ended March 31, 1985	1986
Net income	$41.5	$60.4
Net income applicable to common stock	39.0	57.9
Net income per common share	1.46	2.13

In the first quarter of 1986, the Corporation recorded a 46% increase in net income from the prior year. The higher earnings reflected continued growth in net income from our core businesses—our recurring credit and operating services businesses—which increased by $13.8 million, or 37%. The quarter also reflected higher trading revenue and large gains on the sale of investment securities, substantially offset by a $62.0 million addition to the reserve for possible credit losses. Return on assets improved to .71%, up 18 basis points from a year ago. Return on common shareholders' equity increased to 14.1%, up from 10.5% for the first quarter of 1985.

The growth in net income from core businesses for the first quarter of 1986 resulted from an increase in net credit revenue, up $23.5 million, or 11%, and a sharp rise in service revenue, up $21.8 million, or 26%. These favorable effects were offset partially by a higher credit loss provision and higher operating expense, although the rate of growth in operating expense has slowed considerably compared with recent years.

The effect of various factors on net income per common share has been summarized in the table to the right. Although there are no generally accepted guidelines for separating nonrecurring from recurring items, it is management's judgment that this presentation improves the analysis of changes in the Corporation's net income.

Changes in net income per common share

First quarter 1985 net income per common share		$1.46
Increase/(decrease) attributable to:		
Core businesses:		
Net credit revenue	.63	
Service revenue	.41	
Net credit losses and provision to cover loan growth	(.34)	
Operating expense and other	(.22)	
Total		.48
Trading revenue and gains on sale of investment securities		1.15
Nonrecurring items:		
Effect of cash-basis loans	.07	
Nonrecurring revenue	.05	
Provision to increase reserve ratio	(1.05)	
Nonrecurring operating expense	(.03)	
Total		(.96)
First quarter 1986 net income per common share		$2.13

Net credit revenue

(dollar amounts in millions)	Three months ended March 31, 1985	1986
Interest revenue	$636.1	$674.6
Loan fees	19.5	28.6
Interest expense	476.3	477.2
Net credit revenue	199.3	226.0
Taxable equivalent increments to net credit revenue	25.7	37.9
Net credit revenue (fully taxable equivalent basis)	$225.0	$263.9
Net rate on interest-earning assets	3.66%	3.78%

Net credit revenue increased in the first quarter of 1986 primarily as a result of average earning asset growth of 14% over the first quarter of 1985. Loans and leases increased on average by $2.7 billion, or 14%, primarily reflecting growth in the Corporation's domestic commercial loan portfolio.

Investment securities increased on average by $1.4 billion, or 91%. Interest rate spreads on these securities were substantially wider during the first quarter of 1986 compared with a year ago.

Net credit revenue (continued)

Cash-basis and restructured loans and leases resulted in a reduction in net credit revenue of $4.0 million in the first quarter of 1986, compared with $7.3 million in the first quarter of 1985.

At March 31, 1986, and reflecting average demand deposit levels, the cumulative excess of interest-sensitive funds over interest-sensitive assets for funds and assets that reprice within three months, six months and one year was $1.6 billion, $1.4 billion and $1.4 billion.

Service and other revenue

(in thousands)	Three months ended March 31, 1985	1986
Service revenue:		
Trust and Investment Department fees	$25,606	$ 36,581
Cash management fees and deposit transaction charges	17,008	18,916
Data processing fees	11,519	14,597
Mortgage servicing fees	6,940	9,033
Letters of credit and acceptance financing fees	7,304	8,724
Charge service fees	7,229	8,217
Other	9,551	10,930
Total service revenue	85,157	106,998
Trading revenue:		
Trading account profits and commissions	1,474	9,262
Gains on sale of mortgages and mortgage-backed securities (net of market revaluation)	408	5,111
Foreign exchange gains	1,393	2,060
Total trading revenue	3,275	16,433
Gains on sale of investment securities	5,297	50,229
Other revenue	1,797	4,208
Total service and other revenue	$95,526	$177,868

Service revenue rose $21.8 million, or 26%, during the first quarter of 1986. The growth in Trust and Investment Department fees was due primarily to the improved markets for equity and fixed income securities, a higher volume of services provided to employee benefit funds and institutions, as well as increases in Master Trust/Custody and related services. Fees from institutional customers also reflected an increase in revenue from new products. Service revenue also grew as a result of increased data processing services provided to a greater number of financial institutions as well as a rise in the level of services provided to existing customers.

Trading revenue contributed $8.9 million after-tax, or $.33 per common share, to net income in the first quarter of 1986, compared with $1.8 million after-tax, or $.07 per common share, in the first quarter of 1985. Gains on the sale of investment securities contributed $27.1 million after-tax, or $1.00 per common share, to net income in 1986, compared with $2.9 million after-tax, or $.11 per common share, a year ago. These gains were realized primarily as a result of the Corporation's ability to capitalize on opportunities created by the decline in interest rates.

Nonrecurring revenue, principally gains on the sale of securities previously acquired in connection with loan settlements and other equity securities, amounted to $2.1 million after-tax, or $.08 per common share, in the first quarter of 1986. Nonrecurring revenue items in 1985 amounted to $848,000 after-tax, or $.03 per common share.

Provision for possible credit losses

The provision for possible credit losses for the first quarter of 1986 totaled $90.4 million, while net credit losses amounted to $28.4 million. In the first quarter of 1985, the provision amounted to $20.3 million and net credit losses amounted to $16.8 million. Higher losses were incurred in 1986 on loans to domestic and international commercial borrowers. Credit losses in the first quarter of 1986 included $7.0 million in credit losses to energy-related credits. The reserve for possible credit losses was increased by $62.0 million during the first quarter of 1986 to achieve higher reserves in view of domestic and international economic uncertainties and to cover loan growth. The reserve as a percentage of average loans and leases for the last month of the quarter was 1.91% at March 31, 1986, compared with 1.70% at December 31, 1985, and 1.58% at March 31, 1985.

Operating expense and employment data

(dollar amounts in thousands)	Three months ended March 31, 1985	1986
Staff expense	$119,477	$126,159
Equipment expense	15,752	19,518
Net occupancy expense	28,255	29,035
Shares, capital and franchise taxes	3,945	4,106
Other expense	56,588	62,615
Total operating expense	$224,017	$241,433
Average full-time equivalent employment	15,387	15,997

Operating expense increased by $17.4 million during the first quarter of 1986. The rate of growth in the Corporation's operating expense slowed to 8%, in part reflecting completion of many of the projects undertaken in recent years to unify the operating systems of our domestic banks. Staff expense for the first quarter reflected higher salary levels and an increase in average full-time equivalent employment from the first quarter of 1985. Nonrecurring expense, included in equipment expense, for the first quarter of 1986 was $1.0 million on an after-tax basis, or $.04 per common share.

Organizational performance

(in millions)	Three months ended March 31, 1985	1986
Net income:		
Mellon Bank, N.A.	$33.2	$47.1
Mellon Bank (East)*	1.9	7.4
Community banks**	3.2	3.4
Total banking subsidiaries	38.3	57.9
Mortgage Banking	1.5	2.6
Leasing	1.3	—
Commercial and Consumer Finance	1.0	1.3
Parent and other	(.6)	(1.4)
Total Mellon Bank Corporation (and its subsidiaries)	$41.5	$60.4

*Includes purchase accounting effect.
**Includes Mellon Bank (Central), Mellon Bank (North) and Mellon Bank (DE) and related purchase accounting effect.
Note: Data has been prepared on a management reporting basis.

The increase in the Corporation's net income during the first quarter of 1986 was primarily the result of growth in the earnings of Mellon Bank, N.A. The bank's higher earnings resulted from growth in revenues from core businesses, as well as increased trading revenue. Mellon Bank, N.A.'s net income also reflected large gains on the sale of investment securities, substantially offset by a significant increase in the reserve for possible credit losses.

Net income for Mellon Bank (East) reflected an increase in gains on the sale of investment securities and an improvement in core earnings. The improvement in core earnings was attributable to wider spreads on higher levels of investment securities, growth in the domestic middle market commercial loan portfolio, and operating expense levels that were essentially unchanged from a year ago.

Net income from Leasing declined during the first quarter due to a $3.2 million credit loss attributable to a single credit.

Notes and debentures/Capital

At March 31, 1986, notes and debentures were $1.3 billion, an increase of $192.4 million from December 31, 1985. This increase resulted from the issuance by a subsidiary of the Corporation of $125 million in 9% Notes Due March 1, 1996, and the issuance of Australian dollar-denominated notes due February 14, 1989. The effective U.S. dollar rate paid on the Australian dollar-denominated notes, as a result of an interest rate swap, was 7.675% during the first quarter of 1986.

The Corporation's total capital, as defined under regulations of the Federal Reserve Board, was $2.9 billion at March 31, 1986, and resulted in a total capital ratio of 8.43% compared with 7.92% at December 31, 1985. The Corporation's primary capital at March 31, 1986, was $2.3 billion and resulted in a primary capital ratio of 6.78% compared with 6.62% at year-end 1985.

Cash-basis, past due and restructured loans and lease finance assets

Cash-basis loans and lease finance assets are those on which, in the opinion of management, collection of interest is doubtful. Interest accruals are generally discontinued whenever the payment of interest is more than 60 days past due or payment of principal is past due 90 days or more, or sooner in situations in which management believes it appropriate. Bank regulatory agencies generally require that interest accruals be discontinued on commercial loans and lease finance assets when interest or principal is past due 90 days or more. Most large commercial banks follow this practice. If the Corporation were to have adhered strictly to this 90-day requirement, its total cash-basis, past due and restructured loans and lease finance assets would have been reduced from actual levels by the amounts shown as less than 90 days past due and not restructured in the table below.

Past due loans and lease finance assets are those that are contractually past due 90 days or more but are not on cash-basis. Restructured loans and lease finance assets include those on which a portion of interest or principal has been forgiven and those made at less than market rates.

	December 31, 1985			March 31, 1986		
(dollar amounts in millions)	Domestic	International	Total	Domestic	International	Total
-basis	$382	$190	$572	$488	$170	$658
lue	24	6	30	22	11	33
ructured	4	1	5	57	1	58
Total	$410	$197	$607	$567	$182	$749
Cash-basis loans and lease finance assets less than 90 days past due and not restructured	$ 95	$102	$197	$145	$ 90	$235
Total excluding loans and lease finance assets less than 90 days past due and not restructured	$315	$ 95	$410	$422	$ 92	$514
As a percentage of total loans and lease finance assets:						
Total cash-basis, past due and restructured			2.72%			3.33%
Total excluding loans and lease finance assets less than 90 days past due and not restructured			1.84			2.28

The increase in domestic cash-basis loans at March 31, 1986, compared with December 31, 1985, principally reflected the addition of a loan to a cement manufacturer and a loan to an on-shore oil and gas exploration and production firm. The increase in the domestic restructured category reflected the addition of a loan to a developer of an office building complex.

During the first quarter of 1986, a sharp decline occurred in the price of oil that could adversely affect the ability of certain domestic and international borrowers to service their obligations to the Corporation.

International outstandings

The following discussion summarizes recent developments concerning refinancings of obligations of borrowers in Mexico and Brazil.

Mexico

At March 31, 1986, the Corporation had $573.1 million in outstandings to borrowers in Mexico of which $390.6 million was to the public sector and $182.5 million was to the private sector. None of the public sector and $15.2 million of the private sector outstandings at March 31, 1986, were classified as cash-basis. There were no material changes in the status of refinancings of private sector outstandings since December 31, 1985.

During the first quarter of 1986, the Corporation completed the refinancing of $236.4 million of the $267.7 million in obligations of public sector borrowers that were originally to have matured between 1985 and 1990. Completion of the refinancing of the remaining $31.3 million is subject to the receipt of a prepayment of $8.3 million from the Mexican public sector. This agreement provides for the rescheduling of the maturities of these loans for periods of up to 14 years and for changes in the rates of interest. The weighted average interest rates for those loans that were originally to have matured between 1985 and 1990 are as shown in the following table.

During the first quarter of 1986, the Corporation received $10.9 million in interest payments and $1.6 million in principal payments on Mexican public sector outstandings. The Corporation's consolidated income statement for the first quarter of 1986 included $8.7 million in interest revenue on Mexican public sector outstandings.

(dollar amounts in millions)	Before refinancing	After refinancing
$31.3*	2.125% over Prime	1.125% over Prime
36.3	1.875% over LIBOR	**
89.5	1.750% over Prime	**
30.8	0.847% over LIBOR	**
79.8	0.824% over Prime	**

**This amount is net of an $8.3 million prepayment yet to be received.*

***Weighted average interest rates after refinancing will be 0.875% over LIBOR (London Interbank Offered Rate) or a comparable domestic interest rate for the period 1985-1986. Interest rate margins will increase to 1.125% for the period 1987-1991 and 1.250% for the period 1992-1998. At March 31, 1986, the Mellon Bank, N.A. Prime Rate exceeded the three-month LIBOR by approximately 1.7%.*

Brazil

At March 31, 1986, the Corporation had approximately $463.2 million in outstandings to public and private sector borrowers in Brazil. Of these outstandings, $1.0 million was classified as cash-basis.

The Corporation is represented in negotiations with the government of Brazil to refinance certain obligations of public and private sector borrowers that mature after 1984. In 1985, the Corporation agreed to an extension, until January 17, 1986, of the refinancing agreement completed in 1984 to include $40.8 million in Brazilian outstandings that matured in 1985. During the first quarter of 1986, the government of Brazil requested the Corporation to continue to extend the terms of the 1984 agreement to cover both 1985 maturities and $48.8 million in 1986 maturities, to reduce the interest rates on these loans and to continue the maintenance of short-term trade loans and interbank deposits. The Corporation is presently considering these requests.

During the first quarter of 1986, the Corporation received $11.1 million in interest payments on Brazilian outstandings. The Corporation's consolidated income statement for the first quarter of 1986 included $10.5 million in interest revenue on Brazilian outstandings.

Consolidated Income Statement

Mellon Bank Corporation (and its subsidiaries)

	(in thousands, except per share amounts)	Three months ended March 31, 1985	1986
Credit revenue	Loans	$519,750	$540,226
	Money market investments:		
	Interest-bearing deposits with banks	60,660	27,877
	Federal funds sold and securities purchased under agreements to resell	16,763	16,908
	Other	4,605	3,668
	Trading account securities	8,849	13,565
	Investment securities:		
	U.S. Treasury and agency securities	30,475	40,810
	Obligations of states and political subdivisions	4,913	19,781
	Other	3,142	1,883
	Fees on loans	19,501	28,619
	Lease financing revenue	6,955	9,865
	Total credit revenue	675,613	703,202
Interest expense	Deposits:		
	Domestic offices	258,446	234,990
	Foreign offices	67,332	51,379
	Federal funds purchased and securities sold under agreements to repurchase	87,477	127,028
	Commercial paper	33,789	27,525
	Other funds borrowed	7,313	9,158
	Notes and debentures (with original maturities over one year)	21,983	27,080
	Total interest expense	476,340	477,160
Net credit revenue	Net credit revenue	199,273	226,042
	Provision for possible credit losses	20,292	90,393
	Net credit revenue after provision for possible credit losses	178,981	135,649
Service and other revenue	Service revenue	85,157	106,998
	Trading revenue	3,275	16,433
	Gains on sale of investment securities	5,297	50,229
	Other revenue	1,797	4,208
	Total service and other revenue	95,526	177,868
Operating expense	Salaries and wages	92,349	102,844
	Pension, incentive and other employee benefits	27,128	23,315
	Equipment expense	15,752	19,518
	Net occupancy expense	28,255	29,055
	Shares, capital and franchise taxes	3,945	4,106
	Other expense	56,588	62,615
	Total operating expense	224,017	241,433
Income	Income before income taxes	50,490	72,084
	Provision for income taxes	8,967	11,652
	Net income	41,523	60,432
	Dividends on preferred stock	2,516	2,523
	Net income applicable to common stock	$ 39,007	$ 57,909
Per common share	(Based on 26,717,259 and 27,167,912 average shares of common stock outstanding)		
	Net income	$ 1.46	$ 2.13

See accompanying notes to financial statements.

Consolidated Balance Sheet

Mellon Bank Corporation (and its subsidiaries)

	(In thousands)	December 31, 1985	March 31, 1986
Assets	Cash and due from banks	$ 1,609,791	$ 1,907,189
	Money market investments:		
	Interest-bearing deposits with banks	1,173,474	1,685,092
	Federal funds sold and securities purchased under agreements to resell	710,450	575,964
	Other	168,565	133,508
	Trading account securities	956,865	584,643
	Investment securities:		
	U.S. Treasury and agency securities	1,848,894	2,413,489
	Obligations of states and political subdivisions	1,118,765	989,121
	Other	91,990	97,252
	Total investment securities (market value $3,087,782 and $3,633,962)	3,059,649	3,499,862
	Loans, net of unearned discount of $157,956 and $243,642	21,931,246	22,119,206
	Lease finance assets	387,429	397,741
	Total loans and lease finance assets	22,318,675	22,516,947
	Less: Reserve for possible credit losses	(361,485)	(423,463)
	Net loans and lease finance assets	21,957,190	22,093,484
	Customers' acceptance liability	2,235,659	1,971,317
	Premises and equipment	396,878	412,386
	Other assets	1,137,674	1,199,936
	Total assets	$33,406,195	$34,063,381
Liabilities	Deposits in domestic offices:		
	Interest-free	$ 3,872,983	$ 3,816,255
	Interest-bearing	12,265,603	12,358,624
	Deposits in foreign offices:		
	Interest-free	11,107	18,473
	Interest-bearing	2,432,932	2,558,855
	Total deposits	18,582,625	18,752,207
	Federal funds purchased and securities sold under agreements to repurchase	7,372,910	7,950,127
	Commercial paper	1,357,164	1,451,783
	Other funds borrowed	406,628	227,741
	Acceptances outstanding	2,235,693	1,971,317
	Other liabilities	575,060	595,476
	Notes and debentures (with original maturities over one year)	1,145,383	1,337,781
	Total liabilities	31,675,463	32,286,432
Preferred stock	Preferred stock—$1.00 par value Authorized—10,000,000 shares Issued—3,653,886 and 3,656,891 shares Series A	93,550	93,618
Common shareholders' equity	Common stock—$.50 par value Authorized—60,000,000 shares Issued—27,659,959 and 27,805,273 shares	13,831	13,904
	Surplus	605,164	612,056
	Undivided profits	1,031,301	1,070,627
	Less: Treasury stock—550,589 and 552,937 shares at cost	(13,114)	(13,256)
	Total common shareholders' equity	1,637,182	1,683,331
	Total liabilities, preferred stock and common shareholders' equity	$33,406,195	$34,063,381

See accompanying notes to financial statements.

Consolidated Statement of Changes in Financial Position

Mellon Bank Corporation (and its subsidiaries)

	(in thousands)	Three months ended March 31, 1985	1986
Increase/(decrease) in financial resources invested in interest-earning assets	**Financial resources derived from/(applied to):**		
	Operations:		
	Net income	$ 41,523	$ 60,432
	Provision for possible credit losses	20,292	90,393
	Deferred taxes, depreciation and other nonfund items	17,380	3,551
	Financial resources derived from operations	79,195	154,376
	Dividends on common and preferred stock	(20,398)	(21,240)
		58,797	133,136
	Deposits and other financing activities:		
	Deposits	(534,811)	169,582
	Borrowed funds	579,939	492,949
	Notes and debentures	106,302	190,874
	Deposits and other funds acquired in mergers	60,364	1,524
		211,794	854,929
	Other activities:		
	Cash and due from banks	(5,263)	(297,219)
	Premises and equipment	(24,526)	(21,229)
	Assets and liabilities acquired in mergers, net	(7,789)	(33,246)
	Other, net	29,575	(28,033)
		(8,003)	(379,727)
	Increase in financial resources invested in interest-earning assets	$ 262,588	$ 608,338
Increase/(decrease) in interest-earning	Money market investments	$ 153,067	$ 339,014
	Money market investments acquired in mergers	7,104	3,061
	Investment and trading account securities	102,454	67,991
	Investment securities acquired in mergers	31,013	—
	Loans and lease finance assets	(52,701)	198,272
	Loans and lease finance assets acquired in mergers	21,651	—
	Increase in interest-earning assets	$ 262,588	$ 608,338

See accompanying notes to financial statements.

Consolidated Statement of Changes in Common Shareholders' Equity

Mellon Bank Corporation (and its subsidiaries)

	(in thousands)	Three months ended March 31, 1985	1986
Common shareholders' equity	Balance at beginning of period	$1,499,486	$1,637,182
	Additions/(deductions):		
	Net income	41,523	60,432
	Dividends on preferred stock at $.70 per share	(2,516)	(2,523)
	Dividends on common stock at $.67 and $.69 per share	(17,882)	(18,717)
	Issuance of stock under option plans, net, dividend reinvestment plan and conversion of 5.375% Convertible Capital Notes	3,470	6,823
	Foreign currency translation	(1,069)	134
	Balance at end of period	$1,523,012	$1,683,331

See accompanying notes to financial statements.

Notes to Financial Statements

Reclassification

Prior year amounts have been reclassified to conform to the presentation for 1986.

Composition of loan and lease portfolio

(in millions)	December 31, 1985	March 31, 1986
Domestic operations:		
Loans:		
Commercial and industrial	$ 8,993	$ 9,323
Financial institutions	1,485	1,379
Other	1,115	1,017
Total commercial and financial	11,593	11,719
Commercial construction	2,045	2,232
Commercial mortgage	880	917
Consumer mortgage	1,378	1,421
Total real estate	4,303	4,570
Consumer credit	2,227	2,220
Total loans	18,123	18,509
Lease finance assets	387	398
Total domestic operations	18,510	18,907
International operations:		
Commercial and industrial	2,025	2,001
Financial institutions	1,245	1,076
Governments and official institutions	517	517
Other	22	16
Total international operations	3,809	3,610
Total loans and lease finance assets, net of unearned discount	$22,319	$22,517

Reserve for possible credit losses

Activity is as follows:

(In thousands)	Three months ended March 31, 1985	1986
Balance at beginning of period	$303,693	$361,485
Reserves acquired in mergers	256	—
Additions/(deductions):		
Credit losses	(31,413)	(40,680)
Recoveries	14,628	12,265
Net credit losses	(16,785)	(28,415)
Provision charged to expense	20,292	90,393
Balance at end of period	$307,456	$423,463

Pension expense

In the first quarter of 1986, the Corporation adopted the Financial Accounting Standards Board's new pension standard for all pension plans. This required the uniform adoption of the projected unit credit actuarial method and certain other actuarial changes. This change reduced pension expense by $3,146,000 for the quarter ended March 31, 1986.

Merger

On April 2, 1986, Commonwealth National Financial Corporation, a bank holding company based in Harrisburg, Pennsylvania, was merged with and into Mellon Bank Corporation. In connection with the merger, approximately 2,718,250 shares of a new issue of Mellon convertible preferred stock and $55.5 million will be exchanged for all outstanding shares of Commonwealth National common stock.

Commonwealth National Financial Corporation, with total assets of $1.5 billion and total deposits of $1.1 billion at March 31, 1986, reported a net loss for the first quarter of $957,000, compared with net income of $2.4 million a year ago. The decrease in earnings was attributable primarily to nonrecurring expense and an increase in the provision for possible credit losses in the first quarter of 1986 and nonrecurring revenue in the first quarter of 1985.

In December 1985, a class action and derivative action were brought by two shareholders of Commonwealth National seeking to enjoin the merger between Commonwealth National and Mellon and claiming damages in an unspecified amount because of alleged violations of securities laws by Mellon and Commonwealth National and an alleged breach of fiduciary duty by the directors of Commonwealth National. On April 2, 1986, the merger was completed. On April 7, 1986, the United States District Court for the Middle District of Pennsylvania issued an order denying the shareholders' request to enjoin the merger. Although the shareholders' claims for damages in an unspecified amount remain, the Corporation continues to vigorously defend this suit and believes that its defenses will be successful.

Consolidated Balance Sheet—
Average Balances and Interest Rates

Mellon Bank Corporation (and its subsidiaries)

	(dollar amounts in millions)	March 31, 1985 Average balance	Average rate
Assets	**Interest-earning assets:**		
	Money market investments:		
	Interest-bearing deposits with banks	$ 2,647	9.30%
	Federal funds sold and securities purchased under agreements to resell	744	9.14
	Other	214	8.72
	Trading account securities	367	10.04
	Investment securities:		
	U.S. Treasury and agency securities	1,147	10.86
	Obligations of states and political subdivisions	291	12.41
	Other	157	9.26
	Loans, net of unearned discount	19,061	11.91
	Lease finance assets	289	10.93
	Total loans and lease finance assets	19,350	11.90
	Total interest-earning assets	24,917	11.43%
	Cash and due from banks	1,654	
	Customers' acceptance liability	2,361	
	Premises and equipment	341	
	Other assets	836	
	Reserve for possible credit losses	(312)	
	Total assets	$29,797	
Liabilities, preferred stock and common shareholders' equity	**Interest-paying liabilities:**		
	Deposits in domestic offices:		
	Demand	$ 598	5.51%
	Savings accounts	919	5.26
	Money market deposit accounts	2,945	7.92
	Retail savings certificates	2,992	10.08
	Negotiable certificates of deposit	3,567	9.27
	Other time deposits	1,066	9.50
	Deposits in foreign offices	3,112	8.78
	Total interest-paying deposits	15,199	8.69
	Federal funds purchased and securities sold under agreements to repurchase	4,117	8.62
	Commercial paper	1,559	8.79
	Other funds borrowed	324	9.17
	Notes and debentures (with original maturities over one year)	883	10.43
	Total interest-paying liabilities	22,082	8.76%
	Deposits in domestic offices—interest-free	3,355	
	Deposits in foreign offices—interest-free	10	
	Total interest-free deposits	3,365	
	Acceptances outstanding	2,361	
	Other liabilities	389	
	Total liabilities	28,197	
	Preferred stock	93	
	Common shareholders' equity	1,507	
	Total liabilities, preferred stock and common shareholders' equity	$29,797	
Rates	**Yield on total interest-earning assets**		11.43%
	Cost of funds supporting interest-earning assets		7.77
	Net rate on interest-earning assets		3.66%

Note: Rates are calculated on a fully taxable equivalent basis at a rate approximating 46% using actual number of days in year and are before effect of reserve requirements. Fees on loans are included in the calculation of rates. Cash-basis loans and the related income effect have been included in the calculation of rates.

Three months ended,							
June 30, 1985		September 30, 1985		December 31, 1985		March 31, 1986	
Average balance	Average rate	Average balance	Average rate	Average balance	Average rate	Average balance	Average rate
$ 2,516	9.21%	$ 1,815	8.97%	$ 1,405	8.52%	$ 1,347	8.39%
724	8.58	823	7.55	809	7.89	928	7.39
231	9.04	197	9.11	182	10.02	168	8.86
423	9.63	346	8.69	464	9.54	758	9.30
1,446	10.56	2,128	9.74	1,799	9.31	1,857	8.96
289	12.38	324	12.88	474	13.30	1,090	12.80
158	9.26	132	9.14	93	9.50	95	9.46
19,583	11.63	19,920	11.21	20,509	11.24	21,653	10.99
298	10.95	309	11.25	339	10.50	396	11.22
19,881	11.62	20,229	11.21	20,848	11.23	22,049	10.99
25,668	11.17%	25,994	10.78%	26,074	10.84%	28,290	10.62%
1,548		1,480		1,508		1,434	
2,318		2,016		1,616		2,031	
359		375		387		411	
895		929		1,022		1,108	
(315)		(340)		(354)		(377)	
$30,473		$30,454		$30,253		$32,897	
$ 601	5.37%	$ 629	5.21%	$ 657	5.18%	$ 685	5.27%
909	5.18	898	5.16	929	5.01	920	5.07
3,089	7.43	3,454	6.92	3,739	7.00	3,767	6.87
2,968	9.54	2,936	9.15	2,931	8.81	2,947	8.65
3,296	8.91	3,128	8.40	3,142	8.55	3,699	8.23
919	9.08	803	8.77	545	9.19	605	8.63
3,284	8.69	2,822	8.75	2,635	8.40	2,517	8.28
15,066	8.33	14,670	7.95	14,578	7.82	15,140	7.67
4,835	7.77	5,412	7.37	5,506	7.68	7,006	7.35
1,429	8.52	1,316	7.88	1,347	8.01	1,417	7.88
312	9.33	386	8.30	379	8.67	451	8.23
1,083	9.40	1,135	9.22	1,127	9.10	1,221	9.01
22,725	8.29%	22,919	7.88%	22,937	7.88%	25,235	7.67%
3,340		3,345		3,419		3,289	
10		10		9		10	
3,350		3,355		3,428		3,299	
2,321		2,017		1,616		2,031	
443		484		564		575	
28,839		28,775		28,545		31,140	
93		94		94		94	
1,541		1,585		1,614		1,663	
$30,473		$30,454		$30,253		$32,897	
	11.17%		10.78%		10.84%		10.62%
	7.33		6.95		6.93		6.84
	3.84%		3.83%		3.91%		3.78%

Principal Locations

Domestic

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Mellon Bank Center
Philadelphia, Pennsylvania 19102
Telephone: 215-585-2000

Pittsburgh
Mellon Bank Center
Pittsburgh, Pennsylvania 15258
Telephone: 412-234-5000

Commerce Court
4 Station Square
Pittsburgh, Pennsylvania 15219
Telephone: 412-391-5210

State College
341 North Science Park Road
State College, Pennsylvania 16803
Telephone: 814-234-6300

Texas
Dallas
2121 San Jacinto Tower
Dallas, Texas 75201
Telephone: 214-979-0053

Houston
1100 Louisiana Street
Houston, Texas 77002
Telephone: 713-650-6066

3100 Travis Street
Houston, Texas 77006
Telephone: 713-525-8000

Additional Locations
The Corporation's banking subsidiaries—The Commonwealth National Bank, Mellon Bank (Central), Mellon Bank (DE), Mellon Bank (East), Mellon Bank, N.A. and Mellon Bank (North)— operate 692 domestic banking locations, including 359 community banking offices. Mellon Financial Services operates 154 branch offices in 23 states.

April 2, 1986

Abroad

Argentina
Buenos Aires
Av. Corrientes 311
1043 Buenos Aires, Argentina
Telephone: 312-5702

Australia
Melbourne
Level 44, Rialto
525 Collins Street
Melbourne, Victoria 3000,
Australia
Telephone: 6144211

Sydney
Level 60, MLC Centre
19 Martin Place
Sydney, N.S.W. 2000, Australia
Telephone: 232-7744

Brazil
Rio de Janeiro
Av. Rio Branco, 138, Andar 17
Rio de Janeiro, Brazil
Telephone: 221-1445

Canada
Toronto
One First Canadian Place
Toronto, Ontario, M5X 1A4,
Canada
Telephone: 416-362-6051

Cayman Islands
Grand Cayman
P.O. Box 710
Grand Cayman, British West
Indies

Hong Kong
Hong Kong
3701 Edinburgh Tower
15 Queens Road Central,
Hong Kong
Telephone: 252-353

Italy
Milan
Via Gabrio Casati 1
20123 Milan, Italy
Telephone: 804-846

Japan
Tokyo
New Yurakucho Building 424
1-12-1, Yurakucho
Chiyoda-ku, Tokyo 100, Japan
Telephone: 216-5861

Korea
Seoul
1725, Daewoo Center Building
541, 5-ka, Namdaemun-ro,
Chung-ku
Seoul, Korea
Telephone: 776-7881

Mexico
Mexico City
Edificio Omega
Campos Eliseos 345
Colonia Polanco
11560 Mexico, D.F.
Telephone: 596-8722

Philippines
Manila
Solidbank Building
777 Paseo de Roxas Avenue
Makati, Metro Manila, Philippines
Telephone: 817-9681

Singapore
Singapore
50 Raffles Place 28-01
Shell Tower
Singapore 0104
Republic of Singapore
Telephone: 225-2929

Spain
Madrid
Paseo de La Castellana, 42,
Segundo
28046 Madrid, Spain
Telephone: 435-86-77

Taiwan
Taipei
Worldwide House
683 Minsheng East Road
Taipei, Taiwan
Telephone: 712-6183

United Kingdom
London
6 Devonshire Square
London, EC2M 4LB, England
Telephone: 626-9828

Cutlers Gardens
5 Devonshire Square
London, EC2M 4LD, England
Telephone: 283-7471

Venezuela
Caracas
Multicentro Empresarial del Este
Edificio Libertador, Nucleo C
Caracas, Venezuela
Telephone: 987-8311

Directors and Management

Mellon Bank Corporation Directors

John M. Arthur
Chairman
Duquesne Light Company

J. David Barnes
Chairman and Chief Executive Officer
Mellon Bank Corporation and Mellon Bank, N.A.

Howard O. Beaver, Jr.
Retired Chairman and Chief Executive Officer
Carpenter Technology Corporation

Robert J. Buckley
Chairman and Chief Executive Officer
Allegheny International, Inc.

Alexander W. Calder
Chairman, President and Chief Executive Officer
Joy Manufacturing Company

Edward Donley
Chairman
Air Products and Chemicals, Inc.

Donna R. Ecton
Vice President—Administration
Campbell Soup Company

George T. Farrell
President
Mellon Bank Corporation and Mellon Bank, N.A.

C. Frederick Fetterolf
President and Chief Operating Officer
Aluminum Company of America

Thomas C. Graham
Vice Chairman and Chief Operating Officer—Steel & Related Resources
United States Steel Corporation

Elmer G. Grant
Vice Chairman
Mellon Bank Corporation and Mellon Bank, N.A.

Bryce Jordan
President
The Pennsylvania State University

Robert E. Kirby
Retired Chairman and Chief Executive Officer
Westinghouse Electric Corporation

G. Christian Lantzsch
Vice Chairman and Treasurer
Mellon Bank Corporation
Vice Chairman
Mellon Bank, N.A.

Andrew W. Mathieson
Executive Vice President
Richard K. Mellon and Sons

Seward Prosser Mellon
President
Richard K. Mellon and Sons

Charles F. Merrill
Chairman, President and Chief Executive Officer
The Commonwealth National Bank

Edward A. Montgomery, Jr.
Vice Chairman
Mellon Bank Corporation
Chairman and Chief Executive Officer
Mellon Bank (East)

Nathan W. Pearson
Financial Advisor
Paul Mellon Family Interests

Gerald G. Probst
Chairman and Chief Executive Officer
Sperry Corporation

Vincent A. Sarni
Chairman and Chief Executive Officer
PPG Industries, Inc.

David S. Shapira
President and Chief Executive Officer
Giant Eagle, Inc.

H. Robert Sharbaugh
Retired Chairman
Sun Company, Inc.

Richard M. Smith
Retired Vice Chairman
Bethlehem Steel Corporation

Norman M. Steere
Vice Chairman
Mellon Bank Corporation and Mellon Bank, N.A.

Leon H. Sullivan
Pastor
Zion Baptist Church of Philadelphia
Chairman of the Board
OIC International, Inc.

L. Stanton Williams
Retired Chairman and Chief Executive Officer
PPG Industries, Inc.

Quentin E. Wood
Chairman and Chief Executive Officer
Quaker State Oil Refining Corporation

William S. Woodside
Chairman and Chief Executive Officer
American Can Company

William J. Young
Retired President
Portland Cement Association

Advisory Board

Fletcher L. Byrom

Michael D. Dingman

William B. Eagleson, Jr.

W. H. Krome George

William P. Snyder III

James W. Wilcock

Chairmen Emeriti

William B. Eagleson, Jr.

James H. Higgins

John A. Mayer

Corporate Office

J. David Barnes
Chairman and Chief Executive Officer

George T. Farrell
President

Elmer G. Grant
Vice Chairman

G. Christian Lantzsch
Vice Chairman and Treasurer

Edward A. Montgomery, Jr.
Vice Chairman

Norman M. Steere
Vice Chairman

April 21, 1986

Principal Operating Entities

Banking Entities

The Commonwealth National Bank
A commercial bank based in Harrisburg, Pennsylvania, serving consumer and small- to middle-sized commercial markets in south central Pennsylvania.

Mellon Bank Canada
A chartered Canadian bank in Toronto providing services to the corporate market throughout Canada.

Mellon Bank (Central) National Association
A commercial bank based in State College, Pennsylvania, serving consumer and small- to middle-sized commercial markets in central Pennsylvania.

Mellon Bank (DE) National Association
A commercial bank based in Wilmington, Delaware, serving consumer and small- to middle-sized commercial markets throughout Delaware. Also provides nationwide cardholder processing services.

Mellon Bank (East) National Association
A commercial bank based in Philadelphia serving consumer and small commercial markets in eastern Pennsylvania, and middle-sized and large commercial markets in many eastern states.

Mellon Bank (FL) National Association
A national bank based in Boca Raton, Florida, limited to trust activities.

Mellon Bank International
An Edge Act subsidiary in New York engaged in international banking services for domestic/foreign corporations and foreign correspondent banks and governments.

Mellon Bank, N.A.
A commercial bank based in Pittsburgh serving consumer and small commercial markets in western Pennsylvania, much of the national middle market, and large commercial and financial institution markets throughout most of the United States and worldwide.

Mellon Bank (North) National Association
A commercial bank based in Oil City, Pennsylvania, serving consumer and small- to middle-sized commercial markets in northwestern Pennsylvania.

Mellon Securities Trust Company
A corporation in New York providing securities processing and custody services.

Banking-Related Entities

Mellon Financial Services Corporation

Carleton Financial Computations, Inc.
An organization based in South Bend, Indiana, providing financial data processing services to financial institutions throughout the United States and Canada.

Commercial and Consumer Finance Group
A finance company based in Oak Brook, Illinois, specializing in commercial and industrial loans to smaller businesses as well as loans to individuals, dealer sales finance plans and resort time-sharing loans.

Fiduciary Services Group
An organization based in Pittsburgh providing trust accounting, cash management processing and IRA record-keeping services, data processing systems, and retail marketing products to the domestic and international financial services industry.

Leasing Group
An equipment leasing organization based in Pittsburgh, with regional offices in major cities in the United States, providing a broad range of leasing and lease-related services for corporations throughout the United States and in selected areas worldwide.

Mortgage Banking Group
Four mortgage banking subsidiaries, based in New Orleans, Cleveland, Denver and Houston, providing credit secured by real estate and related services.

Mutual Fund Services Group
An organization based in Boston providing mutual fund record-keeping and shareholder servicing.

Mellon Asset Management Services

Mellon Capital Management
An investment advisory firm in San Francisco providing portfolio and investment consulting services.

Franklin Portfolio Associates, Inc.
An investment advisory firm in Boston providing investment management services for employee benefit funds and institutional clients.

Mellon Real Estate Investment Management Corporation
An investment advisory firm based in New York providing real estate investment management and consulting services.

Mellon-Pictet International Management, Limited
A joint venture based in London engaged in international investment management services.

Corporate Information

Exchange listing	The stock of Mellon Bank Corporation is traded on the New York Stock Exchange. The trading symbols are MEL (common stock) and MEL Pr A and MEL Pr B (Series A and Series B preferred stock). The Transfer Agent and Registrar is Mellon Bank, N.A., Commerce Court, 4 Station Square, Pittsburgh, Pennsylvania 15219.
Dividend Reinvestment and Common Stock Purchase Plan	Registered holders of Mellon Bank Corporation stock may purchase Mellon common stock at a 5% discount from market value through reinvestment of common dividends, preferred dividends or both. Registered shareholders may also buy Mellon common stock at market value with optional cash payments of at least $50 for each purchase up to $5,000 per calendar quarter. There are no brokerage commissions or service fees charged on purchases made through the Plan. Plan details are contained in a Prospectus dated December 31, 1984, which may be obtained through the Secretary of the Corporation.
Dividend payments	Subject to approval of the board of directors, dividends are paid on Mellon Bank Corporation's common stock and Series A and Series B preferred stock on or about the 15th day of February, May, August and November.
Investor, broker, security analyst contact	Investors, brokers, security analysts and others desiring financial information should contact Donald W. Ebbert, Jr., director of investor relations for Mellon Bank Corporation. Telephone: 412-234-5601 or Outside Pennsylvania 800-245-1094 Inside Pennsylvania 800-872-3019
Shareholder, noteholder inquiries	Requests for information or assistance regarding stock records or notes should be directed to the Secretary of the Corporation, 3045 One Mellon Bank Center, Pittsburgh, Pennsylvania 15258.

Mellon Bank Corporation is an Equal Employment Opportunity/Affirmative Action Employer.

Mellon is committed to providing equal employment opportunities to every associate and every applicant for employment regardless of, but not limited to, such factors as race, sex, religion, national origin, age or handicap. A belief in the dignity of every individual and a sense of responsibility to the common good are the foundations of our commitment.