

# The Goldman Sachs Group, Inc. (GS) CEO David Solomon on Q3 2019 Results - Earnings Call Transcript

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Q3: 10-15-19 Earnings Summary

 10-Q  Slides

EPS of \$4.79 misses by \$-0.10 | Revenue of \$8.32B (-3.74% Y/Y) misses by \$-3.06M

## Earning Call Audio

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The Goldman Sachs Group, Inc. (NYSE:GS) Q3 2019 Earnings Conference Call October 15, 2019 11:00 AM ET

## Company Participants

Heather Miner - Head of Investor Relations

David Solomon - Chairman and Chief Executive Officer

Stephen Scherr - Executive Vice President and Chief Financial Officer

## Conference Call Participants

Glenn Schorr - Evercore

Christian Bolu - Autonomous Research

Michael Carrier - Bank of America

Steven Chubak - Wolfe Research

Betsy Graseck - Morgan Stanley

Mike Mayo - Wells Fargo Securities

Brennan Hawken - UBS

Jim Mitchell - Buckingham Research

Chris Kotowski - Oppenheimer

Devin Ryan - JMP Securities

Gerard Cassidy - RBC Capital

Brian Kleinhanzl - KBW

Marty Mosby - Vining Sparks

## **Operator**

Good morning. My name is Dennis, and I will be your conference facilitator today. I would like to welcome everyone to the Goldman Sachs Third Quarter 2019 Earnings Conference Call. This call is being recorded today, October 15, 2019. Thank you.

Ms. Miner, you may begin your conference.

## **Heather Miner**

Good morning. This is Heather Kennedy Miner, Head of Investor Relations at Goldman Sachs. Welcome to our third quarter earnings conference call. Today, we will reference our earnings presentation, which can be found on the Investor Relations page of our website at [www.gs.com](http://www.gs.com). No information on forward-looking statements and non-GAAP measures appear on the earnings release and presentation. This audiocast is copyrighted material of The Goldman Sachs Group, Inc. and may not be duplicated, reproduced, or rebroadcast without our consent.

Today, I'm joined by our Chairman and Chief Executive Officer, David Solomon; and our Chief Financial Officer, Stephen Scherr. David will start with a high-level review of our financial performance and the operating environment, he'll then provide a brief update on several strategy items including key investments we are making to drive future growth, the significance of the Applecard launch, specifically, as it relates to other technology innovation at the firm and recent personnel changes to align with our longer-term strategic priorities. Stephen will then cover third quarter results across each of our businesses. They'll be happy to take your questions after that.

I'll now pass the call over to David. David?

### **David Solomon**

Thanks, Heather. And thanks to everyone for joining us this morning. I'm happy to be here with you. Let me begin on Page 1. We reported third quarter 2019 revenues of \$8.3 billion, down 6% versus last year. Net earnings were \$1.9 billion, resulting in an earnings per share of \$4.79. Year-to-date, we produced an ROE of 10.4% and an ROTE of 11%. Our business performed well against an uncertain geopolitical backdrop characterized by increased volatility and shifting client's sentiment.

A few highlights worth mentioning. In investment banking despite lower results versus a strong third quarter in 2018, we continue to have the world's leading franchise, ranking Number 1 in global announced and completed M&A and Number 1 in equity underwriting year-to-date. In ICS, we generated year-over-year growth demonstrating the breadth of our client footprint, including progress across both fixed income and equities.

We produced record net interest income in debt investing and lending, which annualizes to \$3.6 billion. In Investment Management, our assets under supervision increased by over \$100 billion to another record of \$1.8 trillion, and we generated record quarterly management and other fees. Lastly, we successfully launched a new and innovative credit card with Apple.

Turning to Page 2, the operating environment in the third quarter remained mixed and slowed the pace of activity by many of our corporate clients. During the quarter, trade war concerns contributed to a risk-off sentiment and sharply lower global interest rates, particularly in

August. Markets were also impacted by turmoil in Argentina, Brexit headlines in Europe, and a temporary spike in oil prices in September.

Throughout the quarter, responses from central banks, including the Federal Reserve and ECB, remained accommodative supporting both capital markets and the sustainability of global economic growth. Looking forward, our economists continue to expect global GDP growth in excess of 3% for this year and next. That said, global growth is not without risk as trade issues remain challenging.

In Europe, growth is decelerating in part due to trade and manufacturing weakness with notable challenges in Germany. In China, while trade has been a headwind, both monetary and fiscal stimulus support growth estimates of roughly 6%.

Here in the U.S., growth continues to run at about 2% with strong labor markets, low inflation and healthy wage growth. Economic conditions have also been bolstered by the Fed's two mid-cycle rate cuts. Importantly, in monitoring the data, consumers continue to show resilience and remain a meaningful source of strength in the U.S. economy. That said, recent data suggest slowing manufacturing and industrial production. Mindful of that, we remain vigilant of where we are in the economic cycle and conscious of it as we manage risk across our firm.

In my regular conversations with CEOs, there is considerable focus on the duration of the current economic cycle. While most CEOs remain focused on growing their businesses and capturing opportunities amid the disruptive forces of new technologies, geopolitical issues continue to give rise to some caution. That said, equity valuations remain relatively high. Financing markets are generally open and attractive to issuers, particularly given the low-rate environment and historically low borrowing costs. In addition to corporates, financial sponsors remain active with significant capital to deploy.

Switching gears, I'd like to spend a moment discussing our ongoing strategic investments; a topic Stephen has covered in prior calls and will expand on in a moment. These investments reflect our deliberate and disciplined approach in building new scalable businesses to serve a broader set of clients, including our markets consumer business, the recently launched Apple Card and a new transaction banking platform.

Our broader consumer business – on our broader consumer business, we are very pleased with our progress in building a modern digital consumer bank. Our competitive advantage is that we have no legacy, branch or technology infrastructure avoiding channel conflicts, and yet we are a bank with a sizeable balance sheet and a well-recognized brand, which is needed for successful disruption. Our strategy is to acquire customers under our own proprietary brand and to leverage Goldman Sachs relationships to embed our products into the eco-system of our partners.

In three short years, we have raised \$55 billion in deposits on our market's platform; generated \$5 billion in loans; and have built a new credit card platform and launched Apple Card in partnership with Apple and MasterCard, which we believe is the most successful credit card launch ever.

In addition, we're making a number of important infrastructure enhancements across our incumbent businesses to better serve our clients and to operate more efficiently. These include investments in our institutional client platform Marquee where we have seen strong growth to over 50,000 monthly active users and over 1 million API data requests every day.

We are also investing to develop the next generation of electronic trading platforms in both FICC and equities. Taken together, these investments draw on our returns in the short-term, but are critical to expanding our capabilities and our competitive position, and we believe we'll be highly accretive in the medium-to-longer term.

Next, let's discuss the recent Apple Card launch, which was an outstanding effort by the teams involved. Since August, we've been pleased to see a high level of consumer demand for the product. From an operational and risk perspective, we've handled the inflow smoothly without compromising our credit underwriting standards.

Beyond the launch, we are proud of the successful platform build, which was completed in short order. This is a testament for the quality of engineering at Goldman Sachs and the collaborative engagement of our business and control functions in developing, building, and launching a true platform business. This success positions us to attract top-notch engineering talent as our most recent technology hires demonstrate and to execute our plan to build digital platforms across firm.

Before passing over to Stephen, I would like to take a moment to talk about some of the recent leadership changes across the organization. As a management team, John, Stephen and I are very focused on creating opportunities for the next generation of leaders at Goldman Sachs. As we set forth an ambitious long-term strategic plan for the firm, it is natural point in time for some of this transition to occur.

We are fortunate to have an exceptionally people with talent as many of our new business leaders are also 15 or 20-year veterans of the firm, and as we execute this transition, we invigorate and empower leaders across the businesses in the federation. Going forward, I am confident that we have an outstanding team in place to serve our clients and achieve the long-term strategic goals we are setting.

Lastly, I would like to briefly address our upcoming strategic update. We've been actively working to finalize the date and the format for our strategic review and will provide additional details to the market in the coming weeks. Our target timing remains late January. I look forward to that session as an opportunity for us to engage with you on a number of topics, including our strategy, investments in new initiatives, forward plans across each of our businesses and a variety of other key issues.

With that, I'll turn it over to Stephen to walk through the results in each of our businesses.

## **Stephen Scherr**

Thank you, David. As David noted at the start, our franchise performance was solid this quarter against a mixed backup in the market as we continue to execute on our strategic priorities. Let's move through the numbers in detail.

Starting on Page 4, Investment Banking produced net revenues of 1.7 billion, down 9% versus the second quarter and down 15% versus a strong year-ago quarter. Financial Advisory revenues of \$716 million were down 22% versus last year. Our performance is consistent with a roughly 20% decline across the industry and the number of M&A transactions completed during the quarter as measured by deals over \$500 million in value, which as a category is an important driver for revenues.

That said, we advised on 8 of the 10 largest M&A transactions this quarter and continue to demonstrate a strong leadership position. Year-to-date, we participated in more than \$1.1 trillion of announced transactions and closed on just over \$1 trillion of deal volume contributing to our Number 1 M&A league table rankings.

Looking forward, as David noted, the ingredients for continued M&A activity remains solid. Client dialogues are healthy, financing markets are open and we continue to see active interest across sectors, including natural resources and healthcare.

Moving to underwriting, equity underwriting net revenues of \$385 million declined meaningfully versus a strong second quarter, which included a number of significant IPOs and were down 11% versus last year. Year-to-date, we ranked Number 1 globally in equity underwriting supported by nearly \$50 billion of deal volume across more than 280 transactions. While the recent market reception for certain companies has been less favorable, over the long term, we believe investors will continue to invest in growing, innovative, and disruptive businesses that create value for customers and shareholders.

Turning to debt underwriting, net revenues were \$586 million, down 7% from a year ago reflecting a decline in industry-wide leverage financed transactions and in-line with a decline in M&A related financings. Nonetheless, our franchise remains well-positioned evidenced by our Number 2 high-yield league table ranking year-to-date.

Against the backdrop of the quarter's performance, it is important to point out that our Investment Banking backlog increased versus the second quarter as we saw improvements in both advisory and financing. Given our healthy levels of strategic

dialogues, our expanding client footprint, and the nature of our corporate relationships, we continue to be optimistic that our clients will remain active in executing transactions supported by well-functioning and liquid capital markets.

Moving to Institutional Client Services on Page 5, net revenues were solid at \$3.3 billion in the third quarter, up 6% versus last year, driven by growth across our diversified FICC and equities businesses, and as David noted at the start, reflective of progress made across our businesses in terms of our clients and business mix and the development of electronic platforms.

FICC client execution net revenues were \$1.4 billion in the third quarter, up 8% year-over-year, driven by higher client activity in a mixed operating environment. Four of our five FICC businesses posted higher net revenues versus the prior year reflecting the continued strength of our client centric model and improved diversification of our business mix.

Our rates franchise generated solid client activity in both the U.S. and Europe and saw increased hedging flows from corporate, pension, and insurance clients amid the significant rally in government bonds.

In commodities, our business was diversified and produced higher net revenues on higher activity in natural gas and power, as well as in oil, where we supported clients during the September price volatility.

We also delivered solid performance in credit and mortgages where net revenues increased amidst improved activity from our broadening client base. These results reflect our continued focus on improving the velocity of risk inventory supporting more efficient capital management in the business.

Lastly in currencies, net revenues declined driven by a more difficult geopolitical backdrop in emerging markets as volatility in Latin America and in particular Argentina offset strong performance in Europe.



As we've discussed previously, we were investing to expand our capabilities to automate workflows, serve our clients electronically and deliver structured solutions in efficient formats. In our credit business, we are making considerable progress utilizing our systematic platforms to efficiently price, risk manage and execute trades. For example, this quarter, we executed a number of sizable trades in U.S. investment-grade credit providing key financial and insurance clients access to our broad risk intermediation capabilities.

Additionally, we recently enhanced our electronic execution capabilities for commodities by leveraging the infrastructure of our Marquee platform. These efforts ultimately improve client experience, execution and pricing, while at the same time, provide us access to serve a broader client base on a more cost-efficient basis.

Turning to equities on Page 6. Net revenues for the third quarter were \$1.9 billion, down 6% sequentially from a robust second quarter, but up 5% versus a year ago. Equities client execution net revenues of \$681 million were flat versus a year ago as stronger cash results offset lower derivative revenues. Net revenues from commissions and fees were \$728 million, up 8% versus a year ago aided by higher client activity. Security services net revenues of \$468 million were up 7% year-over-year. Over the course of 2019, we continue to benefit from new prime balances and a rebound in average balances.

Moving to investing in lending on Page 7, collectively, our activities in I&L produced net revenues of \$1.7 billion in the third quarter. Given market movements, particularly in certain public investments, it was a very clear divergence in the performance of equities relative to debt securities and loans.

Our equity investments generated net revenues of \$662 million, down significantly versus last year, driven in part by a reduction in market value on our public investment portfolio. As we discussed on our last call, we hold a number of publicly traded equity investments with customary lockups following IPOs.

Our public portfolio currently includes large investments in Uber, Avantor, and Tradeweb. These three positions, in particular, saw significant price pressure during the quarter and were the primary drivers of the \$267 million of mark-to-market loss in our public

investment portfolio. Taken together, these investments continue to represent approximately 40% of our \$2.3 billion public investment portfolio.

The performance of our private investment portfolio was also lower versus last year, but showed positive results and continued to perform well, given the diversity of our investments. Private equity net revenues of \$929 million were driven by strong underlying corporate performance and events such as sales or additional capital raises. Against that strength and performance, our private investment portfolio was also burdened by certain negative revaluations, including an approximately \$80 million mark associated with our position in the [We] company.

Turning to Page 8, net revenues from debt securities and loans were \$1 billion and included \$891 million of net interest income and modest mark-to-market gains. Our total loan portfolio was approximately \$100 billion, up approximately \$2.5 billion sequentially with the increase driven by loan growth across the portfolio, and we note as we have in the past, that 84% of our total loan portfolio remains secured.

Our provision for loan losses was \$291 million, up \$77 million versus last quarter, driven by idiosyncratic impairments. Importantly, provisions related to our Marcus portfolio were relatively flat quarter-over-quarter. Our firm-wide net charge-off ratio decreased by 10 basis points to approximately 50 basis points and remains relatively low. While credit costs continue to normalize from this cycle's low levels, our overall credit exposure remains appropriately sized.

On Page 9, turning to investment management, we produced \$1.7 billion of revenues in the third quarter, driven by our diversified global asset management business and leading private wealth franchise. Net revenues included record management and other fees of \$1.5 billion, which were up 5% versus last year, reflecting continued growth in assets under supervision. We also saw significantly lower incentive fees and modestly lower transaction revenues from our PWM client trading activity versus a year ago.

Assets under supervision finished the quarter at a record \$1.8 trillion, up by \$102 billion versus the second quarter, driven by \$86 billion of net inflows and \$16 billion of market appreciation. The \$86 billion of net inflows included \$58 billion from the acquisitions of

S&P's Investment Advisory Services business and United Capital; \$12 billion from organic long-term net inflows, primarily from alternative investments and fixed income; and \$16 billion of organic liquidity inflows.

Now, let me turn to expenses on Page 10, our total operating expenses of \$5.6 billion were roughly flat versus the third quarter of last year. This reflected lower compensation expense concurrent with lower revenues and higher non-compensation costs. On compensation, as I have said in the past, our philosophy remains to pay for performance. The reduction in the year-to-date ratio to 35% is a reflection as always of our best estimate of the appropriate accrual for the firm, which for the full-year 2018 was just below 34%.

Also, as we have noted previously, as we grow more platform-driven businesses, we expect compensation to decline as a portion of total operating expenses making our total efficiency ratio a more relevant metric for the firm. Platform businesses should carry higher marginal margins at scale and be less reliant on compensation.

As David discussed earlier, we continue to invest in a number of important initiatives across the firm both to build new businesses and digital platforms, as well as to enhance the firm's infrastructure. To provide you some measure of that investment, a meaningful driver of the year-to-date growth in non-compensation expenses relates to firm-wide technology spending and expenses related to four key projects, Marcus, Apple Card, Transaction Banking, and United Capital.

We continue to expect the depth of that investment cycle will be in 2019 though investment spending will continue into the future years. Year-to-date, the total pre-tax impact of our organic projects, Marcus, Apple Card and Transaction Banking is approximately \$450 million, resulting in a drag of roughly 60 basis points on our ROE. As these businesses scale over the coming years, we expect this drag to reverse becoming accretive to the firm's ROE.

For the year-to-date, our efficiency ratio was 66.2%, up 200 basis points versus a year ago, driven by lower revenues and ongoing investments, partially offset by lower compensation expense. Next on taxes, our reporting tax rate was 22% for the quarter and

21% for the year-to-date. We expect our full-year 2019 tax rate to be approximately 22%.

Turning to capital on Page 11. Our Common equity tier 1 ratio was 13.6% using the standardized approach and 13.4% under the advanced approach. The ratios decreased by 20 basis points and 10 basis points respectively versus the second quarter, driven primarily by increased credit risk-weighted assets and roughly 10 basis point impact from our acquisition of United Capital. Our SLR was 6.2%, down 20 basis points sequentially.

In the quarter, we returned a total of \$1.1 billion to shareholders, including stock repurchases of \$673 million and \$466 million in common stock dividends. Our basic share count ended the quarter at another record low of 369 million shares. Our book value per share was \$219, up 11% versus a year ago.

We note that our \$673 million of share repurchase amount this quarter was less than our \$1.75 billion quarterly CCAR authorization. During the quarter, we elected to suspend our open market repurchases as we had begun discussions with certain U.S. governmental authorities with respect to the resolution of the 1MDB matter. We have since resumed our repurchases under an existing 10b5-1 program, and given our incremental disclosures, we are now resuming additional open market repurchase activities as resolution discussions continue.

To be clear, our decision to step away from the market was not motivated by capital concerns as we remain confident in our strong capital position. As this was the first quarter of our fourth quarter CCAR cycle, we will carry forward the unutilized authorization and will continue to balance our priorities of prudent capital management and return of capital in excess of growth investment via share repurchases.

Turning to Page 12 for our balance sheet, our balance sheet was just over \$1 trillion, up \$62 billion versus last quarter, driven by client demand in Repo and equities. On the liability side, deposits increased to \$183 billion, including consumer deposits of \$55 billion, which more than doubled since last year to become our largest deposit channel.

Before taking questions, a few brief closing thoughts. While our third quarter performance was solid given the market backdrop, we continue to invest in driving the firm forward and aspire to delivering high returns in the future. As David discussed, we are executing on a number of fronts and are making real progress across several of our strategic priorities.

Overall, our client-centric strategy remains simple and unchanged. First, to serve our clients with excellence thus growing and strengthening our existing business. Second, to diversify our business into adjacent and new areas by expanding our offering of products and services. And third, to operate more efficiently and effectively across the entire firm. As we continue to make progress on our efforts, we are confident that we can deliver leading long-term returns for our shareholders and we look forward to providing a more comprehensive update in January.

With that, thank you again for dialing-in. I will now open the line for questions.

## **Question-and-Answer Session**

### **Operator**

[Operator Instructions] Your first question is from the line of Glenn Schorr with Evercore. Please go ahead.

### **Glenn Schorr**

Thanks very much. Big picture question, during the quarter, you know, we saw the funding markets get all discombobulated, still not standing on their own, we also saw the liquid markets temporally get hurt whether it be recent broken IPOs – recent IPOs being broken or resetting of some private valuations, so of the big picture of question I have for you is, I'm listening to you talk and you don't sound that concerned like the plumbing's broken. I know we've seen these things come and go before, but I just wanted to see if you could talk specifically towards those two big issues and just see if hopefully just overstating a short-term impact on the market?

### **David Solomon**

Sure. Thanks, thanks Glenn and I appreciate the question. You know I'd say at a high level, I don't think the plumbing's broken, although I do think that you've pointed to two places where there are certainly adjustments and changes in evolution. There's no question that the short-term funding markets experienced a combination of factors that led to the need for some intervention. I would say some of this is market structure and kind of supply and demand, the liquidity in the market and some of it is the impact of regulatory change over a period of time combining with those things.

We actually saw some opportunity to work with clients in the context of that and deploy balance sheet, and I think you framed it correctly, there's still work to do to move forward with respect to the short-term funding markets. But I don't think it's fundamentally broken, but I think that will be an evolutionary process of finding the right balance. With respect to private capital formation, you know, again, I think the IPO process is alive and well in the United States. I do think – or actually globally to put it in that context, I do think that we are going to see a rebalancing of this process of private capital formation, the size and the magnitude of that private capital formation and the period of time with respect to which people get the public markets.

I think one of the things that public markets do is, public markets provide discipline and process around companies, and that the public markets are very efficient in doing that, and I think the transparency around some of this private capital formation is going to increase over a period of time not that we are more disciplined against it, but I don't fundamentally think that it's broken, I actually think that it's a healthy adjustment for rebalancing. I'd like Stephen to maybe to make a comment or two around our balance sheet deployment in the context of some of these changes on short-term liquidity, but on the high level, those are the comments I'd make on those two issues.

## **Stephen Scherr**

You know Glenn, just to pivot up David's comments, you know, I would say that we obviously are mindful and watch all of the attending risks that sort of present themselves systemically, near-term, short-term liquidity, what happened in the Repo market is obviously one that we're focused on. I would say that in our case, as an intermediary, we

saw an opportunity to source liquidity and to provide liquidity to clients. And so, for us, this is a lot about the elasticity of balance sheet to serve our clients in terms of what we did in stepping in during dislocation, you know, in the Repo market. It had no negative impact to us from a liquidity point of view. We had sufficient liquidity to do it, but I think from the perspective of our firm, stepping in to serve clients, it was a lot about flexibility and balance sheet and growing balance sheet so as to provide liquidity as an intermediary in the market more broadly.

## **Glenn Schorr**

Awesome! I have one little follow up on your comments about the 8K, which I saw on 1MDB. So, I heard a comment on the stopping and starting of the buyback and I saw the \$47 million reserve taken, which I think a lot of people would say is not that much, so I don't want to put words in your mouth, but just how does that make you feel – should we feel like you're fully reserved for 1MDB? Where are we in the process? What's your RPL? If you could talk to those issues that'd be awesome.

## **Stephen Scherr**

Sure, sure. So, I think you should feel comfortable because we feel comfortable that we've gone through, you know, an appropriate process in assessing both the situation involving 1MDB and other legal matters, and in that context, both with internal and outside counsel. You know we have fixed our RPL and our reserve at the level that the accounting standards require in both of those respects. On the RPL, bearing in mind this number is as good as it is till we get to the 10-Q when it's formally set up, but we have that set now at \$2.9 billion. That's up roughly \$300 million from where it was in the last Q.

There was, as you pointed out, a modest adjustment in reserves, and in the context, obviously, both carry a very different accounting threshold and standard, one being reasonably possible, the other being probable and estimable, and in that context, we feel comfortable with where we are, you know, given the standing of legal circumstances both relating to 1MDB and otherwise.

## **Operator**

Your next question is from the line of Christian Bolu with Autonomous Research. Please go ahead.

**Christian Bolu**

Good morning, David and Stephen. David, as you transition to franchise to your target operating model, is there an ROE flow you'd like to maintain while you're at the transition phase? I guess is the 9% ROE this quarter are sort of a good way to think about the flow? Or you're willing to sacrifice, you know, the near-term profitability for the longer-term vision?

**David Solomon**

Thanks for the question, Christian and I – you know I think, I understand, I'd try to put it in, you know what, through the cycle context and also short-term context. If you look at our – if you look at our, you know, ROE year-to-date, our ROE year-to-date is over 10%. But as Stephen clearly articulated on the call, there has been about a 60-basis point drain on our ROE year-to-date given the investments that we're making across our three principal projects, the card, our markets digital consumer banking platform and also transaction services.

We continue to make investments to drive our firm and the returns of the firm higher in the medium and longer term and we are willing to sacrifice some short-term returns to make these investments, better position and strengthen the franchise and allow us to better deliver for our clients in the long run.

**Christian Bolu**

Great, thank you. And then, Stephen, maybe a couple of questions on the credit provisions, on the impairments, maybe it be more color, I think you mentioned it was not Marcus, so just to be more color on what it was? And then, on CECL, I think you disclosed that the day one here to be somewhere like \$400 million to \$600 million, of which half of that is about the consumer book, but as we look forward, we think about the Apple Card, broader plans to grow consumer, how should we think about the day two impact? Sort of any ongoing CECL impact through 2020 and beyond?



## **Stephen Scherr**

Sure. So, maybe I'd take the second part of your question first. In terms of CECL, just to be precise, the guidance we've given is a \$600 million to \$800 million adjustment. I'd also point out that as the portfolio around Apple Card grows in throughout 2020, obviously we're building that reserve from, you know, a base of zero as it relates to the credit card portfolio itself. And so, those reserves will be built in the context of the CECL requirements, so there's no adjustment to reflect in as obviously the reserves are not yet been taken.

On the first part of your question, I'd point out that we took \$291 million loan loss provision, which itself was up \$77 million quarter-over-quarter. That related to a couple of things. One was four idiosyncratic corporate impairments, each of which was less than \$30 million, none of which would give rise to any sort of perceptible trend or impact as it relates to the broader portfolio itself. And net charge-off, I think as I noted in the prepared remarks, that ratio was down 10 basis points quarter-over-quarter to 50 basis points.

I'd say as it relates to, you know, the markets unsecured portfolio, the provisions there were relatively flat quarter-on-quarter. That portfolio is now performing much more in line with our initial modeled expectations. You've heard me talk before about some of the earlier vintages performing at a worst loss rate. Those now have come back in. This is performing more in-line with the model. And so, what's reflected in the provision is not a reflection of any degradation in that portfolio. I should point out though that, you know, provisions will grow as it relates to growth in the portfolio itself. That includes credit cards, that includes unsecured loans, but there's no reflection embedded in that to the quality and the performance of the portfolio itself.

## **Operator**

Your next question is from line of Michael Carrier with Bank of America. Please go ahead.

## **Michael Carrier**

Good morning and thanks for taking the questions. Maybe the first one, just given the lighter equity I&L revenues in the quarter, you mentioned some of the public, you know, pressures. Can you give us maybe some color on the portfolio in terms of the sector breakdown, maybe the current value versus costs? Just trying to get, you know, some context to some of the pressures that we're seeing on private valuations and if we could see that, you know, kind of, you know, bleeding into the future or, you know, most of that, you know, was right size this quarter?

## **Stephen Scherr**

Yes. So, let me start with the public portfolio, the public portfolio, I think as I mentioned, has a carry value of \$2.3 billion. The names that I had mentioned, Uber, Tradeweb and Avantor comprise about 40% of that portfolio, and those were the largest contributors to the downdraft if you will in the public portfolio itself where we mark those is obviously the observable market less some form of the liquidity discount, particularly in situations where there's a lockup or these are other circumstances that warrant it.

In the private portfolio, you know, the size of that I should say is just shy of \$20 billion, \$19.7 billion and there, we mark as I've said in the past, mostly on an event driven basis, meaning, we look at circumstances where there's another round, there's been a sale. We look at the underlying performance of those names and, you know, we make – we set our marks, you know, in that regard. I'd called out, you know, the [We] company in particular because it obviously got quite a bit of notoriety in the press.

As I mentioned, the revaluation there was in the neighborhood of \$80 million in terms of our loss. Our carry value there, I should point out, is approximately \$70 million, which I would tell you is meaningfully higher than where our embedded cost is in that particular name. So, if there was further downdraft, there's still embedded profit in the name itself, but I called that out just given the nature of the press and the notoriety around the name itself.

## **Michael Carrier**

Okay. That's helpful color. And then, just as a follow up, you guys are, you know, fairly significant in the alternative asset managed business. You've created some changes, you know, in that platform. Just wanted to get, you know, your perspective on like how you're thinking about that business going forward in terms of third-party funds? What that could mean for a fee growth? But then also any shift, you know, in balance sheet usage, you know, over time?

## **David Solomon**

Sure. Sure, Michael and, you know, I think we talked about this a little bit on the last call, but we see the opportunity for us as a significant manager of alternative assets both for ourselves and for our clients at the time – at the current time, an opportunity for us to meaningfully grow the client fees that we have. Our teams are working hard at developing a medium and long-term plan. With respect to that growth, we'll certainly communicate more about that when we have our strategic update and review. But I think it's fair to say that the growth of those assets and the development of that business will happen more over time in the medium or longer-term.

As I think we stated publicly before, and we talked last time that we were on the call, we will continue to invest balance sheet capital and people should not see or expect in the short-term a change in with respect to the way we deploy balance sheet, but over time the medium and long-term as we evolve this business and grow other revenue streams, we'll certainly reconsider that and we evaluate what we think is appropriate.

## **Operator**

Your next question is from the line of Steven Chubak with Wolfe Research. Please go ahead.

## **Steven Chubak**

Hi, good morning. So, I wanted to just start with a follow up to one of Christian's earlier questions, it's one that we've been fielding from a number investors as well, which is this concern that you have a long timeline before some of the newer growth initiatives achieve scale, suggesting it could, a lot of time can pass before we actually see the benefits to the

P&L. And so, I was hoping you could speak to higher balancing the need to execute on the longer-term initiatives while still delivering improved near-term profitability? And where could that near-term profitability improve and ultimately come from if you could cite a number of the potential sources that would be really helpful?

## **David Solomon**

Sure, and I'll talk about this, and look, this is a balance and I think it starts from the fact that we have – you know we have an institutional business. We've historically had an institutional business that's very capital market sensitive. We're taking the opportunity to grow more fee-based durable recurring revenues, but that will take some time and we're thinking about building those businesses in the medium and long term for Goldman Sachs over a long period of time.

We've been around for a long time and we look back historically the way we built our asset management business, the way we built our other international business, the way we built our investing businesses. These are businesses we've built over a long period of time organically and that is our thought process with respect to a number of these. When you say a long time, you know, a long time is a subjective word. You know we think about getting real contributions from some of these investments that we're making over the next three to five years, but I understand in the context of short-term catalysts that that might feel like a long time.

In the meantime, though, we are very, very focused on our, what I'll call, short and medium-term performance and we're particularly focused on efficiency in the organization and where there are cost and efficiency opportunities. And we think over the next 12 to 24 months, we can make meaningful progress on that and when we get a strategic update, we will probably quantify that more specifically.

In addition, we are making investments in platforms and some of our clients where we think we will see tangible benefits in the next 12 to 24 months. That can be with respect to footprint expansion, that can be with respect to technology platforms inside our securities business with a lot of better connectivity, you know, to our clients. And so, I think there's a mix of things that both enhance or move us along in the next 12 to 24 months. And then,

we've been talking on this call and otherwise about some of what I'll call the bigger tentpole investments where we will see the benefits over a three to five-year period and we have objectives to build bigger businesses over the next decade.

## **Stephen Scherr**

Steven, the one other thing I'll add to David's comments is around funding optimization and liquidity management, which I think will yield much shorter-term benefit to the firm overall and that work, you know, has already begun. And so, there I'm talking about funding substitution to lower cost retail deposits relative to wholesale. It is being more diligent about overall liquidity management in the firm and sizing liquidity appropriately. I think all of those in addition to what David was speaking about in terms of efficiency and overall operating expenses will be two near-term elements that I think people can look to, you know, in the context of a longer-term profile to some of the bigger investments.

## **Steven Chubak**

Thank you both for that helpful color. And just one follow-up for me on the election, certainly encouraging to hear that you're seeing your backlog grow. I was hoping if you could speak about the election certainty, how that's impacting CEO confidence, and maybe just bigger picture as it relates to some of the growth initiatives given the heightened scrutiny of the private equity business by some of the more progressive candidates? How does that inform your decision to deploy more resources towards that expansion, particularly on the alternative side?

## **David Solomon**

Sure, and I appreciate that question and, you know, as you would expect as I travel around and talk to people, people are interested in talking about the election. The election cycle started, but I would just highlight that we are very, very early in the process and I think to speculate on where we wind up with candidates and also depending on which candidates we wind up with, what we wind up in the context of an election, what we wind up in the context of a legislative process after the election and how some of what's going to get discussed in election cycle turns into policy, I still think there's a lot of ground cover.

We're building – to the second part of your question in investment platform for the long run, private investment – private investment, alternative investment activities, whether it's private equity or credit or infrastructure or growth capital, I think despite the fact that there can be dialogue around evolutions in that business or potential regulation of certain aspects of that, that will not change the opportunity in those businesses for us over a long period of time. In addition, I'd just also highlight that I think one of the virtues of our organization is that we're agile, nimble, responsive and adaptive.

We've been around for 150 years. There've been a lot of different political regimes. There've been lots of evolutions in markets, and I think this organization has always proven that it can adapt and it can respond. And so, we're watching the environment like everyone else. I think it's early to draw conclusions, but we'll always be thinking from both a client standpoint, a strategic standpoint, and a risk management standpoint as we have more information how to best position the firm for returns for our shareholders.

**Operator**

Your next question is from the line of Betsy Graseck with Morgan Stanley. Please go ahead.

**Betsy Graseck**

Hi, good morning.

**Stephen Scherr**

Good morning.

**David Solomon**

Hi, good morning, Betsy.

**Betsy Graseck**

Two questions, one you cited the deposit is \$55 billion, you know, obviously a very large number that you've been able to generate over the course of last couple of years in Marcus and others. Just wondering how you are thinking about redeploying that and the growth you are expecting from here into your businesses? Is it all into loans? Or, you know, can you do more than just loans with the deposits?

**Stephen Scherr**

Sure. So, thanks Betsy. On deposits, obviously they've doubled. Retail deposits have doubled in the year and our anticipation is to continue to grow it across the U.S. and the UK platform by about that \$10 billion a year. What that does for us is it enables us to fund a variety of different businesses not limited to loans in the context of that, which sits in the bank. And so, you know, as much as we're raising deposits, we're equally mindful of businesses that can be brought into the bank into these so as to avail ourselves for the deposits we're raising.

And so, there are a number of businesses, including our rates business and equally the movement of our FX business, which is much more suited to consume, you know, short-dated retail deposits than longer duration wholesale funding. And so, we are moving more businesses into the bank, both U.S. and UK bank, you know, so as to take advantage of the growth and the more attractive, both term and pricing on those deposits themselves.

**Betsy Graseck**

Okay, that's helpful. And then, as you think about the reconfiguration of how your, you know, presenting Goldman's, you know, earnings to the Street in January where does the value of those deposits get allocated? Does that get allocated to a consumer bank? Does that get allocated to, you know, the top of the shop to the federation? Just trying to understand how you're thinking through the value of that deposit creation and who gets credit for that?

**Stephen Scherr**

Sure. So, I think it would be a little early to get into that granularity. You know our objective as we get toward the end of the year and certainly at the end of January when we present to the market, you know, our objective is to have enhancement to our disclosure, you know, which will give people a much better sense of how we manage the business, and therefore, how we talk about the business and equally providing all of you, you know, what's kind of the right lens through which to look at our business more broadly.

We've been taking commentary and perspective from investors and from you in the context that where there's been some frustration. I hear it loud and clear on the context of frustration with I&L as an example. And so, you know, we're going to guide ourselves in the direction of segments, you know, to meet some of what all of you have been asking for and just on that particular issue, you know, I think only to wait till we finalize some of what we do.

**Operator**

Your next question is from the line of Mike Mayo with Wells Fargo Securities. Please go ahead.

**Mike Mayo**

Hi.

**Stephen Scherr**

Hello.

**David Solomon**

Hi, Mike.

**Mike Mayo**

If you could just give a little bit more color on the technology investments? I mean you're your stock trades below tangible book value for a company that's grown book value twice the pace of the S&P 500 over the last two decades? So, somebody's not convinced about



your investments and the eventual payoff. So, as a side note, you know, how – when does that drag of 60 basis points to ROE become positive over, you know, how many years? But more importantly, what are the external milestones that we can monitor to see if you're on track or not? Or do we just have to wait three to five years and say, okay, you made it or not? And in my – I know in my career I've covered other companies. They say it's on track then five years sometimes 10 years later your go, oops, it didn't work. So, how do we know that you'll be that – the good version instead of the bad version? And then if you want to add in some governance changes that you're doing, David, it seems like from a tire to be the destination workplace for technologists.

## **David Solomon**

Okay. So, there's a lot there in the question, but let me, Mike, get a couple of things at a high level. And first look, I certainly expect us to be on the good end of what you're saying and one of the reasons that we're working toward the strategic uptick in January is one of the things that we expect to layout for you is targets that will be held accountable to that can also give you a better sense and more transparency on what we're doing and how you should hold this accountable over a period of time toward doing it. And I'd just say and I noticed this might be in some way, you know, not moving as fast as you like or not moving as quickly, but the lens I'd like you to consider, you know, looking through as we started on this journey a year ago and in the context of the year, we're meaningfully increasing the transparency.

We're moving in the direction of doing this and it just takes some time, but I understand the question and the demand that you have that we need to lay out some clear objectives and better metrics and more transparency and I think we're on our way to doing that. I can't comment on, you know, why the firm, you know, values us, you know, where it does, but what I do believe that if we continue to compound our book value on both in absolute basis, you pointed out, you know, over 20 years, I'd point out that our book value growth over one-year, three years, five years, 10 years has outpaced the peer set.

If we continue to do that over time and if over time because the investments that we make add more fee-based or durable revenue to our business mix and we're able therefore to move all the turns higher, I do believe over the time the market will reward us. Now, Stephen, do you have anything else that you would add based on some of the questions that Mike laid out?

## **Stephen Scherr**

No. I think, Mike, maybe to address the question of timeline, so, you know, not all of these initiatives, you know, operate in the same set of time sequence. So, as an example, I think that consumer initiative is one, you know, that will be over the medium to long term. You know what we've built to this point in three years, you know, is effectively a bank that has \$55 billion of the deposits and \$5 billion in loans and a new credit card platform that's begun with Apple, but that can go in a variety of different places and partnerships. I think that will take some time to sort of see that investment payout.

Shorter-term, I would say you could look at, for example, transaction banking, where, you know, that platform is one where, as we've said several times, we are the first customer. We're a current customer of that. So right now, you know, we've processed more than \$250 billion of payments for Goldman Sachs through that platform and equally we are on schedule to bring very consequential corporate clients to the firm onto that platform and I think given the nature of that spend, its ability to borrow on some of the technology that was built on the consumer side, you know, we'll have a much faster sort of payback, if you will, relative to the longer cycle around consumer. And so, I think these will vary. But David is 100% right. We will present to you metrics by which you should measure us and we'll hold ourselves to it as we execute along this path.

## **Mike Mayo**

And then, just one follow-up then, I mean if you're in Silicon Valley, you're saying what you're doing is just phenomenal. I mean they're just saying this is fantastic. If you're a competitor of Goldman, I'd have to say they are not taking this too seriously based on my

conversation. So, what is it that your universal bank competitors are under appreciating and by consequence, the shareholders are under appreciating in terms of how they expect the payoff from these investments?

## **David Solomon**

I understand the question at a high level, Mike. But what I'd say here is one way to think about it. Over the course of the last three years, we've built a digital consumer platform that's only beginning to evolve that has \$55 billion of deposits; it has \$5 billion of loans; it is 4 million to 5 million customers. We've also built the first credit card platform at a meaningful period of time and have launched a partnership with it and what we believe is one of the most successful credit card launches, if not, the most successful credit card launch ever. If – we've spent on that, you know, over \$1 billion, a little over \$1 billion. If you were asked, would you spend \$1 billion to get that? You would say, sure, you might spend more.

Certainly, someone could have justified our study meaningfully more to kind of acquire that inorganically. We're very focused on proving what we do over time. I think this firm over time has a good track record of building businesses that are successfully integrated into the firm and really succeed all the time. I pointed this out earlier in the call when I highlighted our asset management business that was built over a long period of time or international business that was built over a long period of time, our investing platforms that were built over a long period of time. And so, we're focused on proving ourselves over time; we're focused on our clients and we're less focused on competitor views on these issues.

## **Operator**

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

## **Brennan Hawken**

Good morning, guys. Thanks for taking my questions. My first one, you guys have done some smaller opportunistic deals recently, but with the potential, it sounds like you are closer and in active discussions on 1MDB in putting that behind you, which is great. Once

you're able to have clarity on that does that open you up for -- to consider some larger deals? And one place that investors have recently started to focus on would be a discount broker space. It's been hit recently with the commission cut; it seems to fit with your new strategic direction. And so, when you think about a deal, I know you probably wouldn't want to talk about anything specific in a particular space, but how would you balance assessing tangible book regulatory capital hits versus long-term growth and maybe attractiveness of low-cost deposits and other benefits like that?

## **David Solomon**

Sure, and I appreciate the -- I appreciate the question, Bren, and we've talked a little bit about this, you know, over time. I think one of the things this management team is trying to do is to think broadly both about our organic growth, but also potential opportunities over time for inorganic growth. I've said on this call and previous calls, the bar for us to do something inorganically, especially something significant inorganically is very, very high. At the same point, it's the job of this management team to have a point of view and to be doing work and to be thinking about opportunities that can expand our franchise.

The online or the discount brokerage area is not one that we're particularly focused on. We are focused on the growth of our wealth management business and the wealth management channel through the acquisition of United Capital that we just made, which we think fits very nicely into our Ayco platform and our access to corporation as the unique and differentiated channel through which to access mass affluent wealth. And so, we're much more focused on the build-out of that of ultimately tying digital capabilities to that and I think that's in the wealth management area where in the near term you'll see our primary focus.

## **Brennan Hawken**

Thanks, David. That's very helpful color. And then, my follow-up, provisions, you guys spoke bit about it, idiosyncratic which makes sense. One book is largely commercial, so, you know, provision build tends to be idiosyncratic, how should we think about that over time though that portfolio is beginning to season? Should we generally think that the trend

is generally upward and do we use this as a starting off point or because, you know, you labeled it idiosyncratic, we should adjust for a bit normalize it and then grow it from there? Is there any color on how to think about that?

## **Stephen Scherr**

Well, it's difficult to predict kind of the forward trend because obviously, you know, we'll be mindful of where the markets are and what risk looks like in the context of taking on accretive lending opportunities. You know in the last year the run rate of net interest income that we are taking in on the book has gone from \$2.8 billion on an annualized basis to \$3.6 billion looking at the near \$900 million that was generated in the quarter. We're doing that on the basis of a secured or largely secured book and we're experiencing very little in the way of NIM compression in the context of, you know, where we're lending.

And so, you know, I would say we'll be driven by client demand, we'll be driven by opportunities that are presented more broadly, but we're going to do it only in the context of ensuring the we're mindful of risk, we're embedding appropriate covenants into our lending. We're lending into a diversified book and we're trying to achieve as much as we can know, you know, to kind of the 84% secured book, you know, that we've been on and I think, you know, you should take that as the general direction we'll go in terms of overall, you know, corporate lending.

## **Operator**

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

## **Jim Mitchell**

Hi, good morning. Maybe just a quick follow-up on the Apple Card. David, you've mentioned a couple of times that that's been potentially one of the most successful launches ever. Could you share any kind of – and I know its early days, but any kind of initial success whether its lending balances, card – number of cards out there? What kind of trend are you seeing with usage that kind of stuff?

## **Stephen Scherr**

Yes. So, I'd say a couple of things on the card. We're not a position to share kind of detailed information about it. What I would tell you though is that we have seen a pretty spectacular reception to the card as a product. The approval rates early on have been lower and I'd say that that's a decision obviously Goldman Sachs is making as the bank, but we're doing that in concert with Apple and it is because we're quite vigilant from a risk point of view, but not being negatively selected out-of-the-box, meaning over time, we'll start to see better credits appear, the approval rates will go up, but we've seen an enormous inbound. We've issued a considerable amount of cards.

We've just been through our first bill cycle, which went smoothly. And so, from an operational point of view, it's gone well. Too early to tell in a shorter period of time as we've launched this as to sort of what the revolver transactor mix looks like, it's just too early. But from an operational point of view, from a risk perspective, you know, skewing to the higher side of FICO bands, I think we're very, very pleased as is Apple with this sort of early month or two or three into this, and, you know, we'll have more to say as we get further into the development of the portfolio itself.

## **Jim Mitchell**

Right, okay. That's helpful. And maybe just switching gears on a follow-up on just sort of the whole efficiency discussion on the legacy business. You talked about whether it's funding efficiency, expense efficiency. Is there anything left to do on sort of capital efficiency standpoint? Do you see material opportunities there as well to boost returns? Or is it mostly expense and whether its interest expense or?

## **Stephen Scherr**

Well, I would say it was in – I think the opportunity sits across all of the categories to be honest. I mean, you know, you're never in a position where you should be satisfied that you're at a static point in capital is always an opportunity to optimize across a range of different businesses and to look to take capital on a consistent basis and deploy it to even higher returns than where its deployed, you know, at any given moment in time. I'd also

say that we're constantly looking, and as David said, we'll share more with you when we present in January at a fairly aggressive, you know, opportunity set to look at expenses and equally and as I talked about, you know, looking at funding opportunities and liquidity, you know, overall.

Some of what we've done, you know, on that score, particularly with as it relates to expenses, is as you know in the context of our front-to-back initiative, which was to take operational and technology resources and put them by in large into the businesses that are consuming what it is that those individuals are up to, keeping back a very central and strong core, both in technology and ops, but part of that is to have the businesses in much better, greater, more proximate control to the expense base in the context of both operations and technology, and we're going to continue to look around the organization, you know, to do that and in the course of it, you know, lower operational risk and raise our overall efficiency.

## **Operator**

Your next question is from the line of Chris Kotowski with Oppenheimer. Please go ahead.

## **Chris Kotowski**

Yes, good morning. I just wanted to get clarification from Steve on two items. One is, when you talked about the pace of investments you said something like that kind of – or the message I took from it is that kind of you're at the run rate of investments now and that it doesn't necessarily increase in 2020, was that the right way to interpret that?

## **Stephen Scherr**

Well, the way I would consider it is that, you know, the rate of growth is going to decrease, right, in subsequent years on the static book of initiatives that we're looking. Obviously, there are other opportunities that present themselves that we deem to be accretive to the overall – you know to shareholder value, we'll pursue them. But against the book of initiatives that we're up to, you know 2019 should be the depth of what you see.

## **Chris Kotowski**

The depth meaning – okay. And then, on the buybacks, you know, you mentioned the [673] versus kind of that 1.75 pace that, you know, would have – one would have assumed from the CCAR, you said you would come or come back into that. I mean does that mean we should expect the pace to go back to 1.75 or are we going to catch up what you weren't able to do this quarter through the rest of the year?

**Stephen Scherr**

Sure. So, let me be clear. We pulled ourselves out of the market, you know, in the context of what I had cited, which was discussions on going with respect to 1MDB. On the back of the disclosures that we've made and just an assessment that we always make about the prudence of being in or out of the market on any number of different variables, including 1MDB, we are now back in the market. We've been back in the market based on an existing 10b5-1 program that we put so as to avoid the vagaries of being in or out, but equally we're now in a position to be back repurchasing in the open market.

I mentioned that, you know, it was in some sense fortunate that this was the first of the four quarters within the CCAR cycle, therefore, we have the opportunity to carry forward what we did not use in the context of this last quarter, and our intention as we sit here given from a position of capital strength is to continue along, you know, the strategy and philosophy that we've had, which is to return capital back to shareholders as into the extent that there's not other deployment that's accretive in the context of growth and shareholder value. We'll continue to do that, obviously now with the benefit of the unused capacity from last quarter now to put against what we can do this quarter.

**Operator**

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

**Devin Ryan**

Great thanks. Good afternoon, David and Stephen. I guess a couple of follow-ups here to some of the newer growth initiatives. In transaction services, you're testing your own platform. It sounds like that's going well, but I just want to dig in a bit since you're moving closer to on-boarding clients, so the question is if you can talk a little bit about just the



early feedback from customers, and, you know, how you're framing the competitive advantages, and really just how you expect that business is going ramp, meaning, you know is the expectation that you're going to win kind of a small piece of customers' wallets initially and then potentially it could scale from there? Or are you expecting, you know, some chunky mandates early on?

## **Stephen Scherr**

Sure. So, as I said, we are now using the platform operationally. And so, it's not in sort of small amount testing. We've been through that period. Now, we're using it, you know, as I said, to tune of more than \$250 billion of payments being made for Goldman Sachs. In terms of the forward end clients, you know, we have been engaged as early as the diligence around the idea with a number of very large corporate clients so as to ascertain a couple of things. One, what if they think was missing from that which they are using currently; and secondly, what could we be building so as to satisfy the needs of what they want.

Many big corporates have a platform that carries three or four banks on that platform much as our longer-term ambition is to be a major player in the place – in the space, and to sit in one or two. You know, our early ambition is to be in the three or four slot, and work our way into the platform, and we will start across the five major currencies. What I think and what we're hearing, many large corporates say about the attractiveness of what we're building is two-fold.

One, that the technology fees is much better, much newer, not nearly as manual in terms of reconciliation as what clients have been accustomed to use for technology that largely has not changed over the last many years. Second, in the context of funding and operational deposits, obviously Goldman Sachs is a good buyer of incremental deposits.

We've shown that in the context of retail deposits, it will be true around sticky operational deposits and what we're not intending to lead with cost, you know doubling if you will want big commercial banks are paying in terms of 1 basis point or 2 basis points to sort of 3, 4 or 5 basis points, I can assure you we will be meaningfully accretive to the firm in terms of funding substitution.

So, I think a function both of the technology interface, the spend or what we will payout for operational deposits, I think our two elements in terms of what's driving the attraction of certain corporate clients into what it is that we're building.

## **Devin Ryan**

Thanks for all the color Stephen appreciate it. And then just a follow up here, you know almost exactly a year ago you announced Ayco's high-profile partnership with Google to provide financial wellness to kind of the entire employee base, I know some of the recent initiatives in the United Capital transaction are going to be synergistic there, is it like David mentioned in the prepared remarks, I'm just curious how you are going to market as you focus more broadly on kind of the full employment employee basis of firms and really whether you are aggressively marketing the platform to some of the larger organizations that I know Goldman has relationships with or if it makes sense to or is there any logic behind trying to connect more into kind of your consumer offering essentially waiting to really push hard so you have a broader platform before you really kind of go through kind of all those relationships that you have on the, at the firm level? Just trying to think about kind of how to gauge what you're doing with kind of the full employee basis of the firms that you're working towards on the wealth management side?

## **David Solomon**

Yes. So, I'd say, we obviously think we have a uniqueness distribution channel through Ayco and our corporate relationships as you highlight Devin, and we've started the process of going after that, but I would say we saw a lot of upside, I would say you know the footprint of Ayco's connectivity to the Fortune 100 is high. The footprint of connectivity to the Fortune 1000 there is an awful lot of upside. And one of the things that the acquisition of United Capital does is it allows us to accelerate the penetration in those corporations and one of those things we've found is if you deliver a good product and service to the top of those organizations or the most senior people in those organizations, the ability then to next step leave it to the organization follows on quite clearly.

So, we see a good opportunity and a lot of upside to expand the channel. That's why we're very, very focused on it. Over time, I do think as you highlight there can be digital connectivity as we build a more digital two market platform, but that's still something that's often the future, and so we continue to focus on really penetrating a broader set of corporate clients where we have good relationships and access to their employee base.

## **Operator**

The next question is from the line of Gerard Cassidy with RBC Capital. Please go ahead.

## **Gerard Cassidy**

Thank you. Good afternoon Stephen and David.

## **David Solomon**

Hi.

## **Gerard Cassidy**

Question I have is, obviously as you guys pointed out in your numbers, your number one year-to-date in global equity underwriting, can you guys give us some color on what your views are about the direct listing that was apparently a big meeting out in California and you probably saw, written about in the third quarter or possibly even in October, but can you just give us your thoughts on the threat to the equity underwriting business possibly from these direct listings?

## **David Solomon**

Sure. At a high level I would say that the utility of direct listings and the number of direct listings that we will see over time is still something, but I think there is a lot of question. There have been two direct listings. We've participated as a lead advisor on both those direct listings. I think the companies were in some way unusual in the context the way they approached the market, but I still think that whether or not this is the best path or a path that could be open to lots of companies approaching the market is still something that's questionable.

One of the things that the IPO process does generally is, you raise capital and therefore there is a price discovery around creating depth of liquidity because people are actually raising capital. Obviously the two companies have gone through a direct listing process did not need to raise capital. It is interesting to note where those companies are at the current point. We are engaged as others are in dialogue about this. We are very, very open to helping our clients if they are interested in considering a direct listing, and so we are participating actively in those discussions.

I'd say, I think the noise around this really disrupting the IPO market or potentially disrupting the economic opportunity for the leading banks like ourselves and a handful of others in the IPO market is overstated at this point, but I do think that they will continue to be evolution in these processes and there are ways that we can so clients better or find ways to get them to market more efficiently. We're certainly willing to do that. I like where we sit as the leading firm or one of the leading firm's because whether a direct listing or a traditional IPO process, we benefit from both those channels.

### **Gerard Cassidy**

Very good and then moving over to the equity markets business, clearly, we've all seen on the consumer side, Charles Schwab, Fidelity bring their commission rates down to 0, when we know in cash equities institutional rates have fallen and electronification has helped everybody manage that decline in rates. Do you guys ever envision that we could get to 0 commissions in cash equities similar to what we see in the retail side?

### **David Solomon**

Look, I think it is a more complicated equation because I think the leading franchises and the equity business you really have an integrated platform at scale on a global basis that's providing value in a variety of ways. And it's very hard to pull that apart entirely. So, the answer to your question is, scale really benefits us and the other people that are in a leading position. It is not just execution, but it is also financing and those things get lumped together. I think it's unlikely that it goes to 0, but I do think to a degree that is more pressure on commissions, which there has been and they will probably will continue to be.

The organization's that have global scale and ability to use financing and balance sheet as an integrated capability I think should continue to do well. If you actually go back and look at the market share or the wallet share that the top three platforms have over the last 5 years to 10 years, they have actually gained wallet share in that period of time and you could really see the benefit of scale.

**Operator**

Your next question is from the line of Brian Kleinhanzl with KBW. Please go ahead.

**Brian Kleinhanzl**

Yes. I just have one quick question. Now you are giving some of the pluses and minuses around expenses and some of the growth investments that you are doing this year, but if you think about it, is it right way to think about this, if you had a flat revenue environment you still should be able to see expenses decline, therefore generate positive operating leverage? Thanks.

**Stephen Scherr**

Sure. I mean, I think much of the investing we are doing is consuming operating leverage that exist in the business, and the forward initiatives that David and I have talked about in terms of funding rationalization and expense reduction are all initiatives that need and must go on and they will continue to create operating leverage in the business, which will be put toward growth opportunities in the firm or shareholder return in the absence of them.

**Operator**

Your next question is from the line of Marty Mosby with Vining Sparks. Please go ahead.

**Marty Mosby**

Thanks. Couple of questions. When you look at your net interest margin 43 basis points can you kind of parse out, what you get from the markets and what that margin looks like and what the net interest margin looks like in your banking business because as you are

growing, the banking side, you should be able to see the margin kind of widen out, and we hadn't really seen as much of that, so I've been kind of counting on that as part of a business mix is that your higher margin business is growing faster and just was wondering if that's something we should be able to assume over the next year or two?

## **David Solomon**

Well. The one thing I would say is, I would be careful to sort of look at NIM across all of our businesses as kind of the relevant metric for how well we are producing. So, for example, it is less relevant metric or element in for example our trading business. Rates have moved up and down, there is higher turnover et cetera, et cetera. I think the relevance to NIM is more in our debt INL line because that looks and is more like the extension of credit and the margin you harvest on credit extension more broadly and because I think I responded earlier, our NIM has been very steady, literally marginal compression in the overall NIM in the book and I say that in the context of that book growing to an annualized basis of something on the order of \$3.6 billion a year.

Again, with all the attending vigilance to risk and the like. So, I think NIM is more relevant in the context of debt INL, less relevant in terms of observable metrics about the performance of our business most notably within the trading business itself.

## **Marty Mosby**

And could you give us some feel for what level of margin is in that business? Is it more relevant to that particular business?

## **David Solomon**

Well. I don't think I'm in a position to sort of give out the margins for each of the businesses. I would say that as you look across our businesses it wouldn't surprise you that on a segment basis investment banking and investing and lending carry with them very high margins, lower margins in the context of certain of the other businesses most notably in FICC and equities. So, I think that's probably a good survey if you will of sort of general direction of margin as and among the segments themselves.

**Operator**

At this time, there are no further questions. Please continue with any closing remarks.

**Stephen Scherr**

Okay. Since there are no more questions, I would like to take a moment to thank everyone for joining the call. On behalf of our senior management team, we hope to see many of you in the coming months. If any additional questions arise in the meantime, please don't hesitate to reach out to Heather, otherwise enjoy the rest of your day, and we look forward to speaking with you in January. Thank you.

**Operator**

Ladies and gentlemen, this does conclude the Goldman Sachs third quarter 2019 earnings conference call. Thank you for your participation. You may now disconnect.

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