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 Second Quarter 2019 Earnings Conference Call. This call is being recorded today, July 16, 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 second quarter earnings conference call. On this call, we will reference our earnings presentation, which can be found on the Investor Relations page of our Web site at www.gs.com. No information on forward-looking statements and non-GAAP measures appear in 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 on the call, 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, the current operating environment, give an update on several recent strategy decisions and discuss our stress test results. Stephen will then cover second quarter results across each of our businesses. They will be happy to take your questions after that.

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

David Solomon

Thanks Heather. And thanks everyone for joining us this morning. I am very happy to be here with you. Let me begin on Page 1. We reported second quarter 2019 revenues of $9.5 billion, down slightly versus last year, but nonetheless reflecting solid franchise performance amid a mixed operating environment.

Net earnings were $2.4 billion, resulting in earnings per share of $5.81. All in, we posted return on equity of 11.1% and a return on tangible equity of 11.7%. Our business performed well and remained solidly positioned for future growth. In Investment Banking, we ranked number one in global announced and completed M&A and number one in global equity underwriting year-to-date.

Our equity market making business delivered its second highest quarter in four years, and our franchise continues to generate broad based market share gains across regions. We produced the quarterly I&L revenues in eight years, aided by significant gains from our private equity investment - investing activities reflecting our ability to source opportunities for the firm and our clients, and record net interest income in debt I&L which annualizes the $3.5 billion.

Lastly, our assets under supervision increased by over $60 billion to another record of $1.7 trillion.

Turning to Page 2, our second quarter results were generated on an operating backdrop that presented both opportunities and challenges. This quarter perhaps more than others reflected changing market sentiment in each of the three component months. Against this shifting sentiment, we continued to witness relatively solid underlying economic fundamentals. This year, we expect real GDP growth of approximately 2.5% in the US and 3.4% globally. European growth remains a bit more subdued at about 1.5%. As recently reported, China is running in the low 6% range, slower than it has been in many years, but still supportive of global growth.

All in while slowing, the global macro backdrop remains broadly constructive. The strong fundamentals that prevailed across markets were nonetheless overshadowed for most of the second quarter by geopolitical uncertainty. Client activity in April turned quiet amid low volatility particularly in fixed income markets. Conditions in May deteriorated as geopolitical events caused significant shift in risk appetite. Fears of expanding trade wars drove concerns that new tariffs in China and Mexico would erode the prospects for continued growth.

In response, equity volatility then increased; global markets turned risk off, the US yield curve inverted, and client activity slowed across a variety of products as our corporate and investment clients stayed on the sidelines. The trade issues also catalyzed concern among global central banks prompting dovishness with the Bank of Japan and the ECB emphasizing potential further stimulus and the US market is now anticipating multiple Fed rate cuts this year. The articulated dovish sentiment spurred a relief rally and increased client optimism and activity albeit late in the quarter. This set up June to be a stronger backdrop to close out the quarter.

The market sentiment in June has continued through today. We've seen a pause in the US-China trade war, accommodative views from central banks, and continued march upward in global equity markets. Credit financing markets remain open and strategic transactions are getting announced. As we look ahead, we remain cautious on the geopolitical front, but optimistic given the resiliency of global markets. Importantly, our clients' long-term needs for advice, financing, and access to markets endure across cycles.

Switching gears, I'd like to provide some insights on two important strategic decisions we made in the second quarter and our alternatives in wealth management businesses. First, on alternatives, which is our core strengths for Goldman Sachs for the past 30 years, we recently completed an internal reorganization of our investing activities across the firm. More specifically, we have realigned our special situations group, real estate, merchant banking, and several other investing platforms under common merchant banking business.

We have a world-class investing franchise with a strong track record, unique sourcing and execution capabilities, and long-standing relationships with the largest institutional investors. Going forward, these teams will operate across four asset classes; private equity, growth equity, private credit, and real estate. By bringing together our investment professionals, we will accelerate our ability to raise significant third party capital. We expect this change will enable us to generate more durable recurring fee based revenues over time. This will be a transition. We are mindful of protecting the revenue potential of these businesses as we grow third party assets.

Second, we announced plans to acquire United Capital, registered investment advisor with approximately $25 billion in assets under supervision, 220 advisers and 90 offices around the country. United Capital represents a key step forward toward our long-term strategic goal of providing comprehensive wealth management services to individuals across the wealth spectrum. Upon closing the transaction today, United Capital will become a powerful complement to our Ayco business, our leading financial executive counseling and investment advisory business, which serves many of the largest corporations in the United States.

We are excited about the incremental scale that United Capital brings, allowing us to serve a broader set of wealth management clients. On a combined basis, Ayco and United Capital will serve clients with over $80 billion of assets under supervision, representing a strong base from which to grow our mass affluent wealth franchise. It remains ambitious -- it remains our ambition to continue to serve ultra-high net-worth individuals through our longstanding PWM business. Individuals with $1 million to $5 million of investable assets through Ayco and the broader mass affluent segment through a hybrid of digital and human engagement as an extension of markets over time.

Before turning the call over to Stephen, I would like to spend a moment on the recent Federal Reserve stress test result released in late June, which showed bank’s ability to withstand over $400 billion stress losses. Overall, the industry fared well in this year's examination. From where I sit, the results of the stress test clearly demonstrate the overall safety and soundness of the US financial system. We also appreciate the ongoing efforts to increase the transparency of the test and very much agree with the Fed's overall assessment that the US banking system is sufficiently well capitalized to support the economy even after a severe shock.

Turning specifically to our performance on the 2019 CCAR examination. As you are now therefore aware, we disclosed the Federal Reserve did not object to our plan of up to $8.8 billion of capital return including a 0.47% increase on our quarterly common stock dividend. This change reflects the board and management view that dividend growth is a critical component to delivering strong shareholder returns, and reflects our progress over recent years increasing more durable fee-based revenues to support the higher dividend.

Lastly, I would like to briefly touch on our strategic communication plan over the coming quarters. Importantly, we continue to work toward providing a strategic update this coming January and we'll share a specific date once confirmed. This update will include the financial targets for the firm to which we will hold ourselves accountable and a broader review of our business strategy.

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

Stephen Scherr

Thanks David. Let's run through the numbers. Let me begin on Page 3 of the presentation. As David mentioned, the environment in the second quarter turned out to be mixed. Against this backdrop, we continue to serve our clients and focus on executing on our strategic priorities.

Let's run through the numbers in detail. Moving on to Page 4, Investment Banking produce net revenues of $1.9 billion, 3% versus the first quarter and down 9% versus a robust year ago quarter. Financial Advisory revenues of $776 million were down 3% versus last year. During the quarter, we participated in announced transactions of approximately $465 billion and closed on $235 billion of deal volume, contributing to our number one M&A league table rankings year-to-date.

Client dialogues remain healthy and we are seeing momentum across sectors including TMT, healthcare and notably financials, which had been rather dormant for a number of years. Moving to underwriting, equity underwriting net revenues of $482 million improves significantly versus the first quarter which experienced the government shutdown and held roughly flat versus a strong quarter last year. Year-to-date, we ranked number one globally in equity underwriting supported by $16 billion of deal volume across over 100 transactions this quarter.

We held leadership roles and bringing many notable companies to the public markets during the quarter including Uber, Avantor, Pinterest and Slack.

Turning to Debt Underwriting, net revenues were $605 million, down 20% from a year ago. The second quarter last year included a number of significant contributions from investment grade and leveraged finance activity, which did not repeat to the same extent this quarter. Our deal flows in this quarter were consistent with trends across the industry, which reflected materially lower volumes in the loan market and lower activity in acquisition related financings, particularly with financial sponsors. Nonetheless, our franchise remains well-positioned with our high-yield league table rank rising to the number two spot year-to-date further reflecting our competitive strengths.

Our investment banking backlog decreased slightly versus the end of the first quarter as we monetized a portion of our pipeline through the completion of several large equity underwritings. Nonetheless, our backlog increased sequentially in both advisory and debt underwriting. And while markets can change quickly, we are optimistic that our clients will remain active in executing strategic transactions in the coming quarters given healthy levels of client dialogue and continued need to access financing markets.

Moving to Institutional Client Services on Page 5, net revenues were solid at $3.5 billion in the second quarter down 3% versus last year, as our diversified business experienced low client activity in FICC, offset by strength in equities. FICC client execution net revenues were $1.5 billion in the second quarter, down 13% year-over-year reflecting both the mix operating environment and generally lower client activity despite notable strength in Europe.

Overall, the opportunity set presented in the second quarter proved more challenging versus a year ago. Specifically, we saw lower volumes in our macro businesses amid low volatility and shifting client sentiment sentiment. Relative to last year, client activity and rates and currencies including emerging markets was more subdued as trade and tariff concerns more than economic data drove sentiment and constrained client engagement. Uncertainty during the quarter around the timing and magnitude of anticipated rate cuts by the Fed was also a contributing factor. As tariff threats lessened and the direction of rates became more apparent, we saw improved client activity, particularly late in the quarter. In currencies, both implied and realized volatility in major FX pairs stood at historic lows throughout the quarter, resulting in very low activity levels among our clients.

Commodities performance by contrast was a positive. Results increased year-over-year on solid contributions from our industrial products, oil, and gas and power businesses. In our micro businesses, we saw lower activity and credit but better results in mortgages. In credit, issuance activity and our inventory levels were down relative to a year ago, as investors remain more cautious following the spread widening experienced at the end of 2018 and grew more discerning in credit exposure selection. We saw lower structured finance client activity versus a year ago, while closing credit came alongside a more muted origination backdrop particularly in investment grade debt and leveraged loans as I had mentioned earlier.

Separately, mortgage revenues increase amidst better performance. The environment notwithstanding and as I have said previously, we are investing heavily to automate our workflows, serve our clients electronically, monitor our cost base and deliver structured solutions in capital efficient formats.

Turning to equities on Page 6. Net revenues for the second quarter were $2 billion, up 14% sequentially and up 6% versus a year ago. We believe our success reflects our continuing consolidation of global market share and a dedication to serving clients across a full suite of cash, derivatives and prime services in both hi touch and low touch channels. Equities client execution net revenues of $772 million increased 13% relative to the first quarter and were up 12% versus a year ago. Results were aided by stronger performance in both cash and derivatives versus the second quarter of 2018.

Net revenues from commissions and fees were $777 million, up 9% sequentially aided by strength in EMEA. We also continue to grow market share in low touch execution. Security services net revenues of $458 million rose 24% sequentially and 5% year-over-year. Sequential improvement was driven by seasonal trends and a rebound in average client balances as sentiment improved.

Moving to Investing and Lending on Page 7. Collectively our activities in I&L produced net revenues of $2.5 billion in the second quarter. Equity securities generated robust net revenues of $1.5 billion, driven by company specific events like IPOs and the performance of corporates in the portfolio contributing revaluations. Second quarter results were up 20% versus a year ago, primarily reflecting higher net gains from public equities. As you can see on the slide, approximately 25% of our net revenues were from real estate and 75% were from our corporate investments. Within the corporate portfolio, nearly half of the performance came from investments that went public during the quarter.

These results included a gain of approximately $375 million from the IPO of Tradeweb. Our investment in Tradeweb which we've owned since 2008 was accounted for under the equity method given our significant influence at the time of the investment. As a consequence, we did not recognize revaluation P&L on Tradeweb over the time of our investment. In addition to trade web, we would draw your attention to several other notable investments that IPO this quarter, including Avantor, Uber, and HeadHunter, which grew the notional size of our public holdings. Taken together, these four investments represent approximately 55% of our $2.6 billion public investment portfolio.

Turning to Page 8, net revenues from Debt Securities and Loans were $989 million, included $872 million of net interest income and modest mark-to-market gains. Our total loan portfolio was $98 billion, up $2 billion sequentially, driven by corporate loan growth and we note 82% of our total loan portfolio is secured. Our credit provision was $214 million, down 4%versus last quarter. Our firm wide net charged-off ratio remains low at approximately 60 basis points.

On Page 9 turning to Investment Management, we produced $1.6 billion of revenues in the second quarter, driven by our diversified global asset management business and leading Private Wealth franchise. Net revenues included management and other fees of $1.4 billion which were up 5% versus the first quarter and up 4% versus last year, reflecting continued growth in assets under supervision. By contrast, we generated significantly lower incentive fees relative to the outsize $316 million last year. Incentive fees in the second quarter of last year were driven by the timing of realizations and performance across a variety of our alternative investment funds.

We also saw lower transaction revenues from PWM client trading activity. Assets under supervision finished the quarter at a record $1.7 trillion, up $61 billion versus the first quarter, driven by $17 billion of long-term net inflows, $12 billion of liquidity inflows and $32 billion of market appreciation.

Now let me turn to expenses on Page 10. Our total operating expenses of $6.1 billion were flat versus the second quarter of last year, reflecting lower litigation and lower compensation and benefits expense, offset by increased expense for technology and consolidated investments. For the year-to-date, total expenses were $12 billion, down 6% year-over-year. Our year-to-date efficiency ratio was 65.6%, up 100 basis points versus a year ago, driven by lower revenues and ongoing investments, partially offset by lower compensation expense.

On the topic of investment spend, as we've spoken in the past, cumulatively we are making very substantial organic investments to build new businesses and digital platforms. The depth of that investment cycle will be in 2019 and 2020. Investment spending will continue into 2020 when we will also see more meaningful impact of the reserve build supporting our initial growth in the Apple Card following our expected launch later this summer.

Year-to-date, the total pretax cost from Markus, Apple Card and our new transaction banking platform is approximately $275 million resulting in a drag of roughly 60 basis points on our ROE. A cumulative pretax loss for these businesses from the inception of each through the second quarter was approximately $1.3 billion which has been embedded in the performance of the firm. As these businesses scale over the coming years, this drag should not only reverse, but become an accretive contributor to the firm's ROE.

Next on taxes. Our reported tax rate was 23% for the quarter and 20% for the year-to-date including discrete tax benefits in the first quarter. We continue to expect our full year 2019 tax rate to be consistent with our medium-term estimate of approximately 22% to 23%. On the compensation ratio, our philosophy remains steadfast to our principles obtain for performance. Reduction in the year-to-date ratio to 36% is a reflection as always of our best estimate of the compensation accrual for the firm, which for the full year 2018 was just below 34%. Also as we have noted in the past, as we grow more scale and platform driven businesses, it is our expectation that compensation will decline as a proportion of total operating expenses and the efficiency ratio will become a more relevant measure for the firm.

These platform businesses should carry higher and marginal margins at scale and be less reliant on compensation as a cost contributor.

Turning to capital on Page 11. Our common equity tier 1 ratio was 13.8% using the standardized approach and 13.5% under the advanced approach. The ratio is each increased by 10 basis points versus the first quarter driven by higher retained earnings. Our SLR was 6.4 % flat sequentially. In the quarter, we returned a total of $1.6 billion to shareholders including stock repurchases of $1.25 billion and $319 million in common stock dividends. Our basic share count ended the quarter at another record low of 372 million shares. Our book value per share was $214, up 10% versus a year ago.

As David mentioned, we are pleased that the Federal Reserve did not object to our 2019 capital plan of up to $8.8 billion of total capital return, including share repurchases of up to $7 billion, 40% higher than last CCAR cycle. While we continue to assess capital return in the context of the market environment and opportunities for accretive investment in our business consistent with our long-held strategy, we are encouraged by the increased flexibility afforded by our strong capital position. We enjoy the option of returning a significant portion of our earnings to shareholders over the coming year.

Following our successful completion of the Federal Reserve's annual stress test, let's spend a moment reviewing our philosophy on capital. First our long-term view on capital allocation remains unchanged. We first look for opportunities to invest in our business at attractive returns to the extent we have access after these investments, we will endeavor to return it to shareholders. Second with respect to dividends versus buybacks, we aspire to having a higher dividend long term. As it's an important component of total shareholder return and it's further reflective of the firm's confidence in our ability to generate more recurring and predictable sources of revenue.

That said we continue to value the flexibility of share repurchases as they allow us to be more dynamic with capital allocations based on the environment and business opportunities. Third regarding the stress capital buffer, based on our calculations and the proposed rule which may differ materially in its final form, we estimate an SCB of approximately 5.5% based on the 2019 stress test results. This would imply a total CET1 requirement excluding management buffers in the neighborhood of 12.5% to 13%, which compares favorably to our second quarter 2019 standardized ratio of 13.8%. While we view the CCAR authorization as a ceiling and not a floor on the amount of capital we will return, we are pleased to note that the $8.8 billion capacity should position the firm well to manage capital at appropriate levels.

Turning to Page 12 for balance sheet and liquidity. Our balance sheet was $945 billion, up $20 billion versus last quarter. On the liability side deposits increased to $166 billion including consumer deposits of over $50 billion, which we have more than doubled since last year. During the quarter, we saw further progress migrating businesses into our bank entities to take advantage of their more diversified and lower-cost funding. Our global core liquid assets averaged $225 billion during the quarter, which we continue to note may decline as we have opportunities to support client demand.

Before taking questions, a few brief closing thoughts. While our second quarter performance was solid despite the mixed operating environment, we believe as David said, the overall economic growth backdrop should remain supportive of our business. As we go forward, we are executing diligently on three core objectives. One, serving our clients with excellence and growing our existing business. Two, diversifying our business into adjacent and new businesses and three, operating more efficiently in all that we do. If we do these things well, we are confident we can deliver strong, long-term returns for our shareholders.

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

Question-and-Answer Session

Operator

[Operator Instructions]

And your first question is from the line of Glenn Schorr with Evercore ISI. Please go ahead.

GlennSchorr

Thanks very much. Maybe to start with a real quickie, you mentioned providing a strategic update this coming January. I'm curious what form you're thinking about meaning Investor Day, update slides on the call things like that?

DavidSolomon

So thanks, Glenn and good morning. I appreciate the question. We're committed to giving a strategic update and in particular providing targets in January. As we're working towards this fall when we know the exact format and also the specific date, we'll communicate it.

GlennSchorr

Okay, well as long as the numbers are good I'm cool. In I&L, I'm curious I know you're going through the process of consolidating the businesses and I'm sure there's some challenges there, but my question is on you've always been good at this but I feel like managing conflicts between advisor, balance sheet investment, and third party funds will just even be that much harder as you bring this all together and grow third party. I wonder if you could talk a little bit about that. And how you will allocate investments across on balance sheet versus third party, things like that?

DavidSolomon

Sure, and I appreciate the question. It's obviously something we spend a lot of time thinking about. We have spent a lot of time thinking about it because when you look at these businesses which in the past had been organized over multiple parts of the firm. We're now internally reorganizing them and bringing them together but we've been doing this for 30 years. We are one of the largest alternative asset managers in the world. We manage a very, very significant amount of third party and client capital. And I can say that there are issues from time to time to come out of this business model, but we're focused on striking the right balance and have proven over the long period of time that I think we can do this consistently.

I think one of the things that you get by streamlining the organization and facing our clients as an integrated operation is it actually should make this process, the decision-making process easier and more clear. And so, we recognize it's something that we will have to continue to do well over a long period of time. We are -- I was talking to our clients and listening to our clients and they feel bringing the businesses together and organizing them, et cetera , will help us do that.

Operator

Our next question comes from the line of Chris Bolu with Autonomous. Please go ahead.

ChrisBolu

Good morning David and Stephen. Just on the targets, we look forward to getting your targets in January but how should we think about the timeframe for achieving targets? Are you setting targets you can meet over the next one to two years? Or should we be looking for more long-term aspirational targets that could take more like five years to get to?

Stephen Scherr

Thanks Christian. I would say that the targets that we will focus on will be both returns and equally efficiency and in the course of putting those out our timeframe will be over the medium to longer term. We're in the midst as I said in the prepared remarks of making some meaningful investments in the business. The depth of that is going to be over the course of this year and into 2020 and the returns on that will play out over the medium term. And so the targets will be that. Along the way, we'll continue to point out as we did on this call with greater clarity as to the precision of what it is we're spending and what we're spending for, and the direction of travel and the type of returns we expect to get.

But in that we're investing in particular businesses like the Apple Card, like Marcus, like transaction banking. Those will have return profiles. Equally, we're investing in platforms that will bring greater efficiency to existing businesses. Those two should have return profiles to them perhaps even inside some of the projects we have. But we will give you the medium-term targets, but take you along in terms of what plays out between now and then.

ChrisBolu

Great. Thank you very much. And then on the alternatives business, so we're excited to see what this looks like when you bring it all together. I don't know if you could help us just preview maybe the size when you put all the strands together kind of what the size and maybe the growth profile of that business looks like today. And then as you look to maybe compete more against alternative asset managers, so that we were tricking one here, but how do you balance the sort of the delicate issue of doing what's right for Goldman versus competing against like a key clientele?

DavidSolomon

Sure. So first, with respect to the business broadly, we plan to operate across four broad asset classes that we operate in today currently. And that includes private equity. That includes growth equity, private credit, and also real estate. And so over time, we will provide more transparency to you on the assets that currently exist in all four of these channels, which are significant and to our aspirations over time to increase the amount of third-party capital that we manage in these different asset classes.

With respect to the balance and operating this, as I said to the previous question, we've been doing this for 30 years. These businesses are very significant in size right now. We have said publicly that when you look at the businesses that we operate here collectively, they make us one of the top five alternative asset managers in the world today. And so we will continue to navigate and execute that the same way we have over the last 30 years in a very, very significant business. And the fact that we're internally reorganizing it, so that we can better serve our clients does not change the process that we've executed on for a very, very long period of time.

Stephen Scherr

The one other -- one other point I'll add to respond to your question is that David rightly points out this will be a transition. During that transition we do not anticipate a revenue shortfall by this movement. Meaning, we'll maintain balance sheet with the flexibility of reallocating balance sheet into different of these sleeves. As David pointed out and it's also worth noting that different sleeves whether it's credit, real estate with respect to for example equity carry different capital density and the opportunity to realize higher returns on the balance sheet deployed will be there.

So we're very well aware of maintaining the revenue flow that's here and as David pointed out this will be a transition over time.

Operator

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

MichaelCarrier

Good morning. Thanks for taking the questions. First one just on capital, so you receive the approval for more buybacks plus the dividend capital ratios have improved a lot. You're doing some on the M&A front, still investing in the business. So I guess just looking for some color on if this is sustainable, meaning being able to do everything given the repositioning of the balance sheet. Probably importantly where you are on that front particularly within like the FICC business and the alternative business.

Stephen Scherr

Sure. So I think it's fair to say as a general matter this year CCAR clearly demonstrates the direction of travel that we want to go in terms of overall capital return. And the scope of what we asked and what otherwise was approved reflects on our commitment to put capital back to shareholders. It's important to note those and as I said in the commentary, our posture has not changed. Meaning as stewards of capital we are looking at and for opportunities where we can invest in an accretive way to generate long-term shareholder return.

We're going to continue to do that and you see that in the investments that we're making. Away from that and in excess of it, will continue to return capital back to shareholders. And I think what played out in the context of CCAR is a reflection of what we are comfortable with in terms of what we're going to look to put out given where the market and circumstances are. On the question you raised about FICC, the focus for FICC not borne of this quarter in particular, but since we came on and started to look and re-underwrite the business has been around capital efficiency and equally cost in the context of delivering into our clients. And so that continues to be a focus of ours in terms of the franchise.

When you look at FICC in particular, I would say that the business is focused on clients in the context of expanding out the corporates, transaction banking and the like. It's focused on the development of platforms, the investment in those platforms such as Marquee, on-pricing engine and investment grade credit equally the e-commodities business and equally having the talent to be good calibrators of risk intermediating which is at the core. When we do this and we do this right and it is a core historical competency for the firm. We're going to continue to look at ways of accomplishing that and greater capital and cost efficiency.

MichaelCarrier

Okay, thanks and then just a follow-up question, just on this strategic review. I think there's a lot of focus on just sort of the revenue opportunities and where you guys are focused. Just given some of the investments and in the longer term to focus on the efficiency ratio, just wanted to get an update or run through some of the initiatives that are in place, and the progress you guys are making to lower the cost base and over time and improve the efficiency ratio.

Stephen Scherr

Sure. So I would -- I'll answer that in kind of two components. One is that the new business is being built whether that's the consumer business, credit card business is a part of it or transaction banking. Those businesses are intended to be built as scale businesses, meaning the compensation component attached to that is lower. You have cost and investment made such that the marginal margin in those businesses is operating at full scale continues to grow. And so you achieve greater efficiency on a higher revenue number that comes in. That's the way I would describe the newer initiatives.

The second component is what we're doing in and around the introduction of platforms and technology to our standing incumbent businesses. I just mentioned a few examples of what we're doing in FICC and in the securities business more broadly. These two are lowering the throughput of trades, it's lowering the ability or I should say the price point to engage with clients where they want to meet us, which is it's less human capital, it's more platform driven; it carries higher efficiency to it and that's the direction of travel.

I'd also say equally true about the incumbent businesses part of what we're doing in the Federation to support the businesses, including in places like compliance is the deployment of technology in order to render us more efficient such that we can support the businesses in a much more cost-efficient way than where we've been historically.

Operator

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

StevenChubak

Hey, good morning. So appreciate the color on the stress capital buffer, certainly the 5.5% reinforces the strength of your capital position. Given your current ratio are 70 to 120 basis points above that you're likely to create additional capital over the next four quarters. I'm just wondering how you're thinking about sizing the appropriate management buffer? And maybe just philosophically what are some of the factors that will impact that calculus?

Stephen Scherr

Well, I think part of the calculus is the direction of travel right of where these regulations are. What the final SCB ruling looks like; equally there are inevitably variability that comes in fluctuation in CCAR results and the way in which stress is imposed. So we will maintain a buffer that's sort of mindful of those very abilities in the overall calculus itself. In terms of the general direction of capital sort of philosophically, it is -- it really is what I had laid out earlier and that is I think you should take the results in this CCAR in particular what we petitioned and what was left un-objected to by the Fed.

As the direction we'd like to go. We've got a lot on our plate in terms of investments that are being made, but we're quite confident under the circumstances of being able to put a reasonable amount of capital back. And I'd also point out that the dividend increase for this third quarter now approved by our board is a 47% jump in the dividend, which is also a reflection of the confidence in the increasing durability and profile of the revenues of the firm.

StevenChubak

Thank for that Stephen. And just one more for me on efficiency. You size the $1.3 billion investment in some of the newer initiatives, given you noted that investment spend will likely peaked in 2019 maybe the early part of 2020, I was hoping you could speak to whether we should expect to see some efficiency progress as early as 2020. And what's a reasonable expectation in terms of the marginal margin? I know the newer initiatives are tougher to assess, but maybe on some of the legacy businesses given some of the changes you plan to implement on the platforms there.

Stephen Scherr

Yes. So, look, obviously the efficiency ratio is in one part of function of revenue. So we'll see where the fortunes of the front take us. On the expense base, I think in the near term there is sort of quick to be realized certain cost efficiencies in our trading costs, meaning what's happening on platforms that are introduced that underpin incumbent businesses that are not looking for, if you will, new flows to command, but we're transacting with clients in a different manner and form than what we've done in the past, just one really small example. If you look at our investment grade business and you look at the bond pricing engine, we can then play both sides of a risk trade in a way that would have taken thousands of man-hours right in order to compute.

You would have had inefficiency in terms of its time value. Now we're able to provide a platform where the client can engage and look to conform and develop a portfolio on a much more efficient basis cost sufficient basis than what has happened in the past. So I think there's sooner efficiency or I should say efficiency to be realized sooner in the context of platforms underpinning incumbent businesses. There'll be a longer timeframe as you note in the context of realizing efficiency and some of the newer initiatives that we're building.

Operator

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

BetsyGraseck

Hi, good morning. A question on how you're thinking about consumer or credit? And I asked the question for two parts. One is the upcoming Applecart and then the markets portfolio. And on the Applecart, I know you can't go through details, we put some estimates together in a note recently where again based on a lot of assumptions, I end up with an expectation that you're running it about that you would expect to run somewhere around a 1% ROA. Now that's again a lot of assumptions but it's based on the information that's out there on lower rates for the credit quality versus peers, what peers are charging and no fee. And I --the nut of my question is how are you thinking about consumer lending?

Is it a business that you think is inherently more risky than your current business which is running at about a 1% ROA? Or do you -- do I have it wrong? What am I missing? And should this be a business that generates higher than a 1% ROA, that's basically another question.

Stephen Scherr

Sure, thank you. So let me start by saying there's no denying that the consumer business whether card or Marcus is a risk business, meaning no matter that it's delivered digitally or that the credit card will take a different digital sort of profile than traditional credit cards, this is a risk business and that's where our focus is. I would say the risk is not just on credit risk and financial risk, but equally operational risk in the context of what we're building. And so we're quite conscious on all of those elements. What's important for us is that we look at this on a risk-adjusted return basis not simply on a return on asset construct.

And that's what's critical and that's the way we're looking at it. It would be Betsy for me premature to sort of speculate what the pace of growth looks like on this. I would simply say that risk calibration risk decisions in and around the part belong entirely to Goldman Sachs as the bank. And we're set up to make those. I'd also say that if you look at the level and rate of growth in the Markus loan business, while it continues to grow and perform well, we have slowed the increasing growth in that in contemplation of taking on increasing consumer credit through the card business. So we look at it both in its totality, so each is marginally different in a way in which credit is dispersed. But this is a risk business and we'll continue to look at it as we grow it out on a risk-adjusted return basis.

BetsyGraseck

So on really that follow-up has to do with the expected at scale efficiency be that you think you're going to be running these businesses at when they're at scale, given the fact that you did a new build, should I be thinking about the efficiency and of these businesses in line with FinTechs which run at intermediate expense ratio that's 30% of other legacy competitors? Or should I look to bank competitors as a more reasonable expense ratio or somewhere in between?

Stephen Scherr

I would say that while we've been in beta now for a couple of months and have grown the portfolio on that basis, it's nowhere near yet the scale of what our expectations would be as we grow it out. And so it would be premature for me to kind of speculate as to the efficiency. We'll start to reflect more on that once we launch and once we start to build this portfolio out. So it's a little early. What I can tell you is that what we have built jointly with Apple both on the front end and on the back end is intended to be operationally resilient, but equally is intended to be efficient both in terms of the delivery the app, I should say the application all through the delivery and on the backend and so my expectation is that the efficiency will be reflected in that, but again premature to sort of put numbers around it.

Operator

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

MichaelMayo

Hi, to continue on the investment spend, as it relates to expansion of markets outside the US, where do you stand with the additional countries and what else might you consider?

Stephen Scherr

So I think on that Mike, the press has been sort of ahead of our plans in the context of speculating sort of the next country in which Marcus would expand. Obviously, our first place outside the United States was in the UK where the deposit platform has really exceeded our expectations in terms of what it's been capable of generating. There will be opportunities for us to expand in that market. There's been quite a bit of speculation about Germany. It's not surprising that the speculation goes there both in the context of a growing business that we have in continental Europe and the depth of the deposit market in Germany.

But it's too early to forecast as and if and when we would expand there though I understand the speculation on that. So for the moment we've got a lot on our plate in terms of the execution around the platform in the United States and in the UK and we'll continue to pursue that.

MichaelMayo

All right and then one follow-up unrelated question. 1MBD did you take any additional reserves for that? What's the status? There's a new statement by the head of the SEC on July 3rd saying that it might be a little bit easier to resolve these sorts of matters? What's your take on all this?

Stephen Scherr

So just on the reserves, we took incremental legal reserves this quarter of $66 million. We don't give detail on what the elements of that reserve are. I would say that we are adjusting our RPL to $2.5 billion from $2 billion where it was. I should point out that in providing that number to you it's important to recognize that number is our best estimate as of this date. It will be published in the Q events that may play out between now and the Q could alter that RPL. And again there are different accounting regimes and thresholds that apply; one probable, one possible, possible relating to the RPL.

And so that's what I can offer you by way of what's happened financially. In terms of statements otherwise being made, I think it would be inappropriate for me to sort of speculate on what others intend by statements they make. I think as we've said in the past, we're in a cooperative engagement with the authorities. We intend to stay that way and as and when there are further developments, we'll be in a position to talk about that a bit more.

Operator

Your next questions from the line of Kian Abouhossein with JP Morgan. Please go ahead.

KianAbouhossein

Hi. I have two questions. The first one is related to your equity revenues which were clearly very strong. Also gain some PS reporting so far. And I just want to understand where that's coming from? Because clearly the drivers are more muted such as volatility is down on the equity derivative world. Transactions a volume are okayish, but nothing in terms of the numbers that you have shown in terms of year-over-year and quarter-on-quarter rates. Can you just give a bit more color of where the drivers are? And do you see market share movements in this area?

And secondly just coming back to your FICC business. We've now heard from you over the last 12 to 18 months in expansion and more liquid products and traditional client base. And can you bit more detail on the FX and rates expansion both on clients and products? And when should we see actually some of those investments having an impact on your revenue base? Because I don't see you yet outperforming appears in this area, but clearly would be great to get an understanding if you are -- if you feel differently and why and what investments you're doing in order to close the gaps in those two sec?

DavidSolomon

So I'll start with equities. I make a broad comment on FICC and Steven will give you a little bit more detail. I--we were very pleased with the performance of equity franchise broadly. The performance really was across the franchise. It was throughout derivatives in cash, I would say given the market dynamics broadly, there's some sense of consolidating share and I think we've been benefit of that and as we've been stating on this call and over the handful of the last quarters, we continue to make the investments in our low touch activity or our low touch capabilities, and we're starting to see some benefits from those investments in our low touch capabilities.

With respect to FICC, broadly I do want to highlight as was highlighted I think on page 5 of the presentation, our business is 90% market intermediation, a much higher component of market intermediation than the people that we compete or we benchmark against. So if you have a 60/40 mix and market intermediation is softer, which it clearly was given the environment we had this quarter, your NIM portion or your non market intermediation portion has less volatility, but we continue to make investments as you highlight in some of these products and particularly in broadening out the client base, I'd ask Stephen to provide just a little bit more detail on how we think some of that's point through.

Stephen Scherr

Thanks David. So just a pivot to FICC and to be direct to your question. If you look at FX and rates and part of the progress that we were making is on broadening out the client franchise to more corporates than to the institutional clients to which we typically, if not exclusively have engaged. And we're starting to see some early progress in that. I would say in this quarter in particular within Europe. I'd also say that as part of an effort to expand out and penetrate further the corporate base around FX and rates, we're seeing some benefit come to us by way of the joint venture between banking and FICC, where banking obviously owns an entry point into the corporates and the ability to carry through those products into the corporate franchise, where we have a demonstrably strong set of relationships, I think will bear dividend.

What's more I would say that if you look at a variety of different initiatives and builds including transaction banking or corporate cash management, this once built and will carry the potential to bring forward a more captive FX business that didn't exist inside the firm. I think that too could prove to be a benefit and just on that particular project Goldman Sachs is already a customer, if you will, of our own platform and we aim to bring customers and clients on in across 2020. And so we're seeing early signs of progress on this, but there's no running from the observation you make which is we have yet to sort of perform at the potential we're confident this business can show.

We're very confident in unlocking that potential. Some of these new initiatives will no doubt take a little bit of time before they bear out, but the direction we're moving is a positive one.

Operator

Our next question comes from the line of Brennan Hawken with UBS. Please go ahead.

BrennanHawken

Good morning, guys. Thanks for taking the question. NII as a portion of the I&L debt portfolio, could you maybe help us think about rate sensitivity there? Depending on how you calculate NIM, if it's a 360 or 365 day count

NIMs down either a few or upper single digits bps quarter-over-quarter. What are the benchmark rates, gents, predominantly in that portfolio we should watch? How much of the strong NII growth that you guys have seen over the past few years has been balanced versus rate? And then how should we think about how the softening rate environment might impact NII growth going forward? Thanks.

Stephen Scherr

Sure. Thanks for the question. I think the best way to answer that question is to just point out where we differ, if you will, from some of the bigger commercial banks. In the context of both, we have a different liability mix and equally a different composition to our assets. On the liability side, there's a portion of our funding that's fixed to portion that's floating. And so it's not as dynamically correlated, if you will, to the way in which rates otherwise move.

And I think our NII growth generally speaking will benefit from a liability mix that's starting to skew towards deposits. And so that's the perspective I would offer on the liability side. On the asset side, much of the assets that we have are floating rate based and equally and importantly is a higher velocity term to the assets that underlie this. And that too has a more or leads to a more muted impact to what otherwise might see in some of the bigger commercial banks as a function of the direction in which rates are moving.

BrennanHawken

Okay and then the part on how much we've seen as far as rate or NIM improvement versus balances last year's? Is it possible to break that down or is that some might have to follow up?

Stephen Scherr

I think I would encourage you to follow up sort of with for an answer that's more precise than one I can give you now. I would say that some of this has to do with balances in terms of the size and scope recognizing that the lending that we're doing which is generating this net interest income is quite strategic in the context of the clients that are served by the lending itself. And I'd also point out as I did in the remarks that about 82% of this is secured financing. And so I offer that to you but Heather and the team can provide you with greater insight onto the particulars.

Operator

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

JimMitchell

Hey, good morning. Maybe just a quick follow up on the fixed-income discussion. Just want to make sure I understand how you get your assumed internal ROE targets in that business. Is it you see it entirely coming from efficiency improvements and expanding the footprint into more flow business or is there some component of capital that comes out whether it's derivatives or something else? Do you need to see the level of capital decline as well or can it come from those other ways?

Stephen Scherr

Sure. So the way we've been looking at it as we've been scrutinizing and re underwriting that business is we're focused on both the numerator and the denominator of the ROE calculation, meaning it's important that nobody lose focus that we need to mind how much revenue is coming in, i.e. how do we want to define the tangible market that we face. What's the revenue capture that we can take in? What's the expense as an offset to that revenue to establish the numerator in the calculus? And none of that is to ignore capital efficiency in the context of what the denominator contains.

So this is really as we've talked about it a wholesale re-underwriting of the business, but be assured both of these are in scope in the context of the way in which we're looking at the business. Both revenue net of expense and looking at capital and the revenue being driven largely by an ambition to have a more expansive addressable market to include corporates in addition to that which we otherwise have focused on historically.

JimMitchell

And as you pull that capital out it, did you worry at all there's any kind of revenue risk in that pivot to a lower capital or denominator or do you feel that's not really the case?

Stephen Scherr

No. I mean, listen, this never is kind of a linear calculus, okay. So the business is for us in FICC are not themselves four-walled, meaning anything we do with respect to a business and FICC has knock-on implications for businesses that sit outside the securities business. Take for example whatever it is we decide to do around credit or commodities, it has knock-on implications. So the thread on the adjacency of all of our businesses gets pulled. So we're mindful of that and need to take stock of what we do around capital. The one other thing I would point out, which I've talked about publicly before is in addition to thinking about both the numerator and the denominator.

Embedded in the numerator is equally an effort to sort of optimize our own funding, meaning how do we bring our cost of funds down, retail deposits has been an example of that, but our treasury team is working hard both in terms of the amount of liquidity we run with? How that liquidity is managed in addition to identifying more efficient, lower-cost funding sources in order to render these businesses more competitive.

Operator

Your next question comes from a line of Devin Ryan with JMP Securities. Please go ahead.

DevinRyan

Great. Good morning, David and Stephen. First question just on the United Capital with the deal closing, just look to maybe get a little more perspective on how you're thinking about the business opportunity. I guess broadly and as it connects with Ayco is there a bigger appetite to expand into the mass affluent segments whether it be adding financial advisors or more M&A? Or does United Capital really give you just a big enough footprint to achieve what you're looking to do in the business especially with Ayco?

DavidSolomon

Sure. I appreciate the question. We're excited actually, today, I believe we're closing the United Capital acquisition on this very day. And obviously it brings with us our 220 RIAs and 90 offices around the United States. And what it's really doing is we think we have a very, very interesting channel to continue to build the mass affluent segments through Ayco. But this particular transaction accelerates our ability to do that between Ayco and United Capital of $80 billion of assets under management that's a good base from which you grow from.

We think we can continue to make progress in what we'll call the $1 million to $5 million of investable assets mass affluent wealth management category through this channel. And that we can have good growth with the extended platform we now have. But if another opportunity came up that we sought to further accelerate it because this is still a very fragmented business, and we have a very, very big infrastructure, so we can continue. The fee in terms of all the wealth, in terms of all the asset management and wealth management products, we have in our asset management business, we'll consider it.

This was not something, this acquisition was not something that was targeted for a year that we were really running after it, it came up for sale, we looked at it, we thought it was a really good fit to accelerate our business. And so we decided to act on it.

DevinRyan

Got it, very helpful, thanks. And then just a follow up just to think about the third party alternative capital fundraising. Any expectations on whether it could be trajectory or cadence of how we should be thinking about that just as we're sort of think about modeling it?

DavidSolomon

Yes. I appreciate the question, Devin. I know that you're all anxious to model it. Over time, we will provide a lot more transparency on how we see that plan went out. As you would expect, we have a lot of businesses across the firm we put them together. And the first thing you do when you put those people together is you task them to develop plans on a go-forward basis. And we are in the process of that and as those plans come forward we will be more communicative and transparent as to what expectation we think you can have with that business over time.

Operator

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

GerardCassidy

Thank you. Good morning. In your comments on the debt underwriting you mentioned deal flows in the quarter were consistent with the trends across the industry, which reflected material lower volumes in the loan market and M&A activity area. And you specifically cited it was with the financial sponsors. Can you share with us what are the financial sponsors seeing today? What do you think will stop them from doing more deal activity in the quarter? And any outlook for the second half of the year from those financial sponsors?

DavidSolomon

Well, look, at a high-end there's now -- at a high level, there is no question that activity has been more muted. I guess when you think about the cycle and you think about the continued run at equity markets and the accommodative monetary policy we have which is certainly inflated for assets, it's steady, it's been tougher more competitive, you have to pay more in order to succeed. I also think the financing environment in particular the SNIP regulatory overlay, it has some impact over this cycle and muting how far the private equity activity they have moved in this cycle has a regulatory environment been difference.

That said the private equity investors still have an enormous arsenal of unspent capital big reserve. And I think this business continues that secular growth and so as the environment evolves, I think there will be periods of time where we will see increased activity versus what we've seen in the first half of the year. I don't think we have a great explanation of this specifically has done it. I mean if you think about what the first and a half of the year has brought in terms of the macro overlay, it's not surprising probably that it's not a little bit more muted.

GerardCassidy

Very good and then as a follow-up on slide 12 you give us your balance sheet of course the allocation. And you mentioned that in the quarter there was a $20 billion quarter-to-quarter increase reflecting client demand to use your balance sheet. Can you share with us the total loans or total assets what percentage of it is clients using your balance sheet? And then second and when you look at the revenues those customers bring to you as a percentage of those assets where those stand and how is that compared to about a year ago?

DavidSolomon

So as always the fluctuation in the balance sheet is a reflection of our ability to respond to opportunities and the interest of our clients. And so balance sheets fluctuation is all a function of client service. It's hard to decompose the balance sheet to say what's client -what not, what is not client. Truth, we know all of it, right, is in some manner or form related to client activity and across all of our businesses in the firm. And so that's really the way I would view to the balance sheet both in terms of growth size and its composition.

Operator

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

BrianKleinhanzl

Yes, thanks. Just one quick question. On the market we saw that the rate pay came down towards the end of the quarter, kind of can you just walk through what your -- how you came up with that decision to lower the rate size just looking at the Fed Funds futures. Should we expect more rate cuts there and kind of what's been depositor behavior --

Stephen Scherr

Sure. So we made a decision and it was the first since we began our retail deposit business. We made an adjustment downward. We did it in the context of rendering ourselves competitive in light of what others had done. It's also worth noting at or around the time we reduced the rate we saw others in the competitive set reduce the rate as well. We saw no material adverse reaction to our movement, no to the pronounced outflows nothing to really call attention to.

I think you should assume that we will be fluid and flexible and agile in rate movement up or down relative to where the competitive set is. And will sort of comport ourselves that way both in our US platform and in the UK.

End of Q&A

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 October.