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 Fourth Quarter 2013 Earnings Conference Call. This call is being recorded today, January 16, 2014. Thank you. Mr. Holmes, you may begin your conference.

Dane Holmes

Good morning. This is Dane Holmes, Head of Investor Relations at Goldman Sachs. Welcome to our fourth quarter earnings conference call.

Today's call may include forward-looking statements. These statements represent the firm's belief regarding future events that by their nature are uncertain and outside of the firm's control. The firm's actual results and financial condition may differ, possibly materially, from what is indicated in those forward-looking statements. For discussion of some of the risks and factors that could affect the firm's future results, please see the description of risk factors in our current annual report on Form 10-K for our fiscal year ended December 2012.

I would also direct you to read the forward-looking disclaimers in our quarterly earnings release, particularly as it relates to our investment banking transaction backlog, capital ratios, risk weighted assets and Global Core Excess. And you should also read the information on the calculation of non-GAAP financial measures that is posted on the Investor Relations portion of our website at www.gs.com. This audio cast is copyrighted material of The Goldman Sachs Group, Inc. and may not be duplicated, reproduced, or rebroadcast without our consent.

Our Chief Financial Officer, Harvey Schwartz, will now review the firm's results. Harvey?

Harvey Schwartz

Thanks, Dane and thanks to everyone for dialing in. I'll walk you through our full year and fourth quarter results then I am obviously happy to answer any questions.

Let's start with the annual results. We had firm wide net revenues of $34.2 billion, net earnings of $8 billion, earnings per diluted share of $15.46 and a return on common equity of 11%. This is a solid result and a modest improvement over last year's performance despite what at times was a difficult operating environment. With regard to the fourth quarter, net revenues were $8.8 billion, net earnings were $2.3 billion and earnings per diluted share were $4.60.

In looking at the broader operating environment, many of the global themes had dominated 2012, for example, improving economic debt in the United States, central bank activity and political uncertainty continued into 2013. Starting with U.S. economic data, we saw relatively consistent improvement over the course of the year reported GDP consensus estimates in each of the last two quarters. U.S. unemployment rate declined by over 100 basis points to 6.7%, it’s lowest level since October of 2008 and housing prices as reflected by the Case-Shiller Housing Price Index increased by 14% through October. 2013 represented a slow, steady improvement in the U.S. economy, which had roughly a quarter of global GDP naturally served at a stabilizing and positive improvements on global market sentiment.

2013 was also marked by significant Central Bank activity. In Japan the Central Bank announced unprecedented monetary risk [ph] and was to achieve stated inflation targets. Japanese credit spreads tightened and the yen weekend throughout the year. In addition the Nikkei enjoyed it's largest annual game since 1972.

In the U.S. initial commentary from the Federal Reserve about tapering at bond buying program ultimately translated into a December announcement of a $10 billion monthly reduction in the reprogram leading the marketplace to contemplate the world without quantitative easing.

Finally political risk and uncertainty were constant during the year, starting with the Italian elections in the first quarter, continued unrest in the Middle East and the 16 day U.S. government shutdown. This created an environment that requires qualities to constantly reassess their outlook for the global economy. For example what are the implications of Central Bank activity on the global economy? Individual regional economies and specific industry sectors? What are the pushes and poles associated with monetary policy versus fiscal policy? Rising rates and tapering a head win for the U.S. economic recovery or return to a more traditional supply and demand driven economy.

Not surprisingly our client’s activity fluctuated over the course of the year as they were constantly digesting new information. When you boil it all down the 2013 environment it's just one where the world took two steps forward followed by one step back. A dynamic which you could see reflected in both price movements in the markets and client activity. To sum it up while we wouldn’t characterize the last two years as a normal cyclical environment given all the items I previously listed it shouldn’t be lost on us that the long term trend is slowly and steadily improving.

Now I will discuss each of our businesses, in invest banking we produced fourth quarter net revenues of $1.7 billion up 47% from the third quarter.

Three factors drove the increase, a robust IPO calendar, higher completed M&A volumes and debt financing activity that remained strong. For the full year investment banking net revenues was $6 billion up 22% from 2012 on the back of solid underwriting activity.

Breaking down the components in investment banking advisory revenues were 585 million in the fourth quarter. The 38% increase relative to the third quarter reflects the increase in industry wide completed M&A. Goldman Sachs continue to be ranked first in worldwide announced and completed M&A for 2013. We advise on a number of significant transactions that closed during the fourth quarter including Vivendi, $8.2 billion sale of it's controlling stake in Activision. Ingersoll-Rand’s $5.3 billion Allegion and a $2.9 billion sale off Saks to Hudson’s Bay.

We also advise on a number of important transaction that were announced during the fourth quarter including Sysco’s $8.2 billion acquisition of U.S. Foods, ViroPharma’s $4.2 billion sale to Shire and Deutsche Telekom’s 2 million euro sale of Scout 24 to Hellman & Friedman.

Moving to underwriting net revenues were record $1.1 billion in the fourth quarter up 52% sequentially at equity issuance improved significantly. Equity underwriting revenues of 622 million were more than double our third quarter results largely due to an increase in IPOs and convertibles. Goldman Sachs continues to be ranked first in worldwide equity, equity related and common stock offerings for 2013. Debt underwriting revenues increased 9% to 511 million.

During the fourth quarter we actively supported our clients financing needs participating in Darling International, $2.7 billion debt and equity offering. Twitter’s $2.1 billion IPO and Moncler’s $1.1 billion IPO. Our investment banking backlog further improved from third quarter levels which you will recall were already at our highest level in five years.

Turning to institutional client services which comprises both our FICC and equity businesses. Net revenues were 3.4 billion in the fourth quarter up 19% compared to the more challenging environment in the third quarter. For the full year 15.7 billion of net revenues were down 13% relative to 2012. FIC client execution net revenues were 1.7 billion in the fourth quarter or 1.9 billion excluding DVA losses of a 163 million. Excluding DVA, revenues were up 46% sequentially. In particular, currency revenues increased significantly compared to a challenging third quarter. Credit was up on stronger client activity that was supported by tighter credit spreads and solid issuance trends. Commodities revenues were largely flat sequentially and remains a threat by lower volatility in client activity levels. Rates and mortgages declined as client activity levels remained low.

For the full year, fixed client execution net revenues were $8.7 billion or $8.9 billion excluding $220 million in DVA losses. Excluding DVA, revenues were down 14% relative to 2012 at macro uncertainty particularly around central bank policies and lower volatility levels impacted client risk appetite and activity. The decline was more pronounced for rates and mortgages.

In equities, which includes, equities client execution, commissions and fees and security services, net revenues for the fourth quarter were $1.7 billion, up 4% sequentially and included $43 million in DVA losses. Equities client execution revenues increased 9% sequentially to $598 million. Commissions and fees were $747 million, up 3% relative to the third quarter supported by rising equity markets and strong issuance trends. Security services generated net revenues of $337 million largely consistent with the third quarter.

For the full year, equities produced net revenues of $7.1 billion, down 14% relative to 2012. This decline was due to the sale of our Americas reinsurance business in 2013 and the sale of our hedge fund administration business in 2012. In our equity business during 2013, stronger performance in cash products was offset by weaker derivative revenues. Turning to risk, average daily VAR in the fourth quarter was $81 million, down from $84 million in the third quarter.

Moving on to our investing and lending activities, collectively these businesses produced net revenues of $2.1 billion in the fourth quarter. Equity securities generated net revenues of $1.4 billion, primarily reflecting company specific events, including initial public offerings and gains in public equity investments. Net revenues from debt securities and loans were $423 million and benefited from net gains and net interest income. Other revenues of $234 million include the firm’s consolidated investments. For the full year, investing and lending generated net revenues of $7 billion driven by $3.9 billion in gains from equity securities, $1.9 billion of net revenues from debt securities and loans and $1.1 billion of other investments.

In investment management, we reported fourth quarter net revenues of $1.6 billion, up 31% from the third quarter primarily as a result of $333 million in incentive fees generated largely from the firm’s alternative asset products. Management and other fees were up 5% sequentially of $1.1 billion. For the full year, investment management net revenues were $5.5 billion, up 5% from 2012 on stronger management and other fees, which benefited from growth in assets under supervision.

During the fourth quarter, assets under supervision increased $51 billion to a record $1.04 trillion. This growth was driven by long-term net inflows of $13 billion largely in fixed income assets. We also had market appreciation of

$20 billion largely in equity assets. On a full year basis, $41 billion of long-term net inflows and $40 billion of market appreciation drove these record levels of assets under supervision. When it comes to investment management, we all know that performance is critical. We are intensely focused on delivering returns for our investment management clients and have seen improvement in our multi-year performance. The $41 billion of long-term net inflows in 2013 were the highest annually since the onset of the crisis. We will continue to focus on delivering performance for our clients and have confidence that the rest will follow in due course.

Now, let me turn to expenses. Compensation and benefits expense, which includes salaries, bonuses, amortization of prior year equity awards and other items such as benefits, decreased 3% to $12.6 billion for 2013 and translated into a compensation to net revenues ratio of 36.9%. Fourth quarter non-compensation expenses were $3 billion, 40% higher than the third quarter and up slightly compared with the fourth quarter of 2012. Other expenses were significantly higher reflecting net provisions for litigation and regulatory proceedings of 561 million more than 400 million higher than the third quarter. Depreciation and amortization included a 196 million impairment charges primarily related to consolidated investments. Finally the fourth quarter also included a $155 million donation to Goldman Sachs Gives our donor-advised charitable fund.

For the full year non-compensation expenses were down 2%. Total staff at year end was approximately 32,900 up 2% from year end 2012. Our effective tax rate was 31.5% for 2013. Before moving on to capital it's worth taking a step back to review our improvement operating efficiency over the past few years. In the first half of 2011 we announced a comprehensive expense initiative. If you look at our cost structure this year versus 2010 before we launched our expense initiative. Total expenses are lower by $3.8 billion. As a result our pretax margin in 2013 increased a 140 basis points to it's highest level in the last four years, this despite having $5 billion less in revenues.

Delivering more operating efficiency is never easy and requires a real focus on striking the right balance. By balance I mean making sure that our actions positions us to deliver for all of our constituents. Our clients, our regulators, our employees, the broader financial system and of course for our shareholders. We believe it's early and ongoing focus on our expense structure has not only benefited recent performance but more importantly also serves as a basis for better results in the future particularly as the opportunity set expands.

Now regarding capital, we repurchased 8.5 million shares of common stock for total cost of $1.4 billion during the fourth quarter. For the full year we repurchased 39.3 million shares for a total cost of $6.2 billion. With respect to our regulatory capital ratios our Basel III Tier I common ratio on a fully loaded basis was 9.8% using the advance approach. Under the standardized approach our ratio was 9.2% of course it's important to note that our transitional ratios are both more than a 100 basis points higher. Risk weighted assets are on the advance approach are approximately $595 billion, $350 billion in credit risk, $160 billion in market risk and about $85 billion in operational risk. Our estimate for the proposed supplementary leverage ratio under U.S. rules remains approximately 5% for the firm and approximately 6% for the bank. These were our best estimates subject to change depending on regulatory clarifications.

Of course last month we also gained regulatory clarity on the Volcker Rule. Most importantly the final Volcker Rule explicitly permitted market making, lending and investing on balance sheets. Regulators permitted these activities given the essential that they plan supporting healthy capital markets and economic growth. Although we only received a finalized Volcker Rule last month. We have obviously been preparing to comply with certain portions of the rule for nearly three years. In 2010 we began closing down our proprietary trading operations, specifically Goldman Sachs principal strategies and our Global Macro Proprietary Trading desk.

In addition we announced in 2012 our intention to redeem certain hedge fund investments. Since 2012 we have redeemed approximately $2.2 billion of hedge fund investments and we will continue to redeem our interests. Now that we have a final rule the first thing that we did was established a Volcker implementation team comprised of senior leaders with expertise across a wide variety of controlling business functions. They are focused on making sure that we’re in the position to effectively and efficiently meet the numerous requirements outlined under this new and intense compliance regime.

In summary as I mentioned earlier while we’re still not at what I would describe that normalized cyclical environment, the underlying macro trend is being improving. To maximize our opportunity set and drive shareholder value we need to continue to focus first and foremost on our clients. Their activity and our connectivity to their needs is our highest priority. We need to continue to recruit and retain a high caliber and dedicated global workforce. We need to leverage our technology expertise to adapt to new regulations and evolving market structures and we need to remain focused on improving our efficiency both from a cost and a capital perspective. Our goal is not only to enhance returns in the current environment, but more importantly over the long-term to position this firm for significant operating leverage as the opportunities that improves. We believe that we have the competitive position, the diversity of businesses, the caliber of people and the institutional will to capture and maximize these opportunities as they present themselves for the benefit of you, our shareholders.

Thank you again for dialing in. And now I am happy to answer any questions.

Question-and-Answer Session

Operator

(Operator Instructions) Your first question is from the line of Glenn Schorr with ISI. Please go ahead.

Glenn Schorr - ISI

Thanks very much.

Harvey Schwartz

Good morning, Glenn.

Glenn Schorr - ISI

Good morning. Just a quickie follow-up. I heard all your comments on Volker just making sure the hedging component, you mentioned about market-making lending investment, anything different on the verb it's related to hedging in your ability to just manage risk across the desks?

Harvey Schwartz

No. We don't see anything in the rule that prevents us from continuing to hedge. I think the early concern before the final rule came out with its reference to portfolio hedging, but we hedge within the business as there is no hedging at the firm wide level, so hedges are hedges.

Glenn Schorr - ISI

Good, good. Also the Fed recently just put out a quick whitepaper that had a testimony on commodities, I think a lot of that was expected, but I am curious to get your update as to what's on plans for the business, but there was a piece in that that threw me for a loop a little bit on the merchant banking and I wasn't sure if it relates to your entire merchant banking business or merchant banking within commodities businesses. So, if you could get quick thoughts on that, I know it just came out, that would be helpful?

Harvey Schwartz

No, fine. It's an important question. So, as you know, the commodity business has been an important business for Goldman Sachs and quite important for our clients for an extended period of time. I think to simplify it I would break down the business growing into two parts. There is – our activity there relate to investing activities. And then there is our franchise business where we are working with clients in a market-making activity. Then in that function, we are essentially providing the same services as anyone would, working with a Treasurer or a CFO on any risk that they would be hedging. So, in terms of a corporate treasurer, if they need to manage their exposure to dollar yen, they will work with us in our currency business. And if they need to manage their exposure to a cost input in commodities, they will work with us on the same hedging profile. So that's a high level as the business breaks down. And on the investing side, we've been an important provider of capital and working with our clients to a capital intensive industry. I think it relates to the whitepaper, I think it's a good step. It's another step in the regulatory process, where people reviewing the businesses. I think the questions make sense. These are things that we consider all the time in our businesses from the safety incentive [ph] perspective. So I think it's a healthy exercise and we will work the regulators, but certainly no change in strategy from Goldman Sachs as it relates to commodity. It's just too important business for our clients.

Glenn Schorr - ISI

I appreciate that. The merchant banking component within that paper, it seemed to be chucked in at the end, is that questioning whether we limit bank holding companies' ability to do merchant banking in totality or it's within the commodity space?

Harvey Schwartz

Don't know. Don't have any special insight in terms of that.

Glenn Schorr - ISI

I know it's early.

Harvey Schwartz

So we will see as it moves along. I don't want to minimize it, but it's a question.

Glenn Sure - ISI

Okay. Moving on to FEA, you guys have been doing this for a while, some banks are catching up. I am just curious on if more of the competition is accounting for the credit spreads and pricing, does that make the business on more equal footing, does it – is it that do you envision an impact on the actual pricing of the business than the competitive landscape?

Harvey Schwartz

No. Obviously, there has been a lot of attention to FEA over the last couple of days just so obviously you are aware of this, Glenn, but we incorporated FEA into our pricing methodologies back in 2010. And if you take the step back for a second, just from the general risk management perspective in the way that we think about risk parameters and inputs, if we identify our cost or parameter we try incorporate as quickly as possible and so we adopted this in 2010. In terms of it's implications I think there is probably two one is really more for you and folks on your side of the table which is obviously it has some degree of distorting effect when you look at things like revenue market share and it's one reason why we look at revenue market share but we don't emphasize it as much as you do necessarily because these pricing inconsistencies they can lead to anomalies in certain points in time. I think the more important issue really in terms of how we run the business is the one that you have mentioned which is regardless of the particular assay class is, if one firm I say Goldman Sachs in this particularly case ends being the one from that's actually pricing our parameter and all the other competitors aren't. It leads to challenging conversations with the clients because you look like an outlier and so you know to get to the gut of your question the extent to which the playing field is level and everyone is pricing on the same terms and managing the risk the same way, obviously we prefer that.

But in the end we're always going to prioritize the risk management over things like market share.

Operator

Your next question is from the line of Matt O'Connor with Deutsche Bank. Please go ahead.

Matt O'Connor - Deutsche Bank

The question I get asked most often when I talk to clients about you guys is how you can improve the ROE over time? And you know to be fair the 11% for the year is above that appears especially if you adjust for the business mix but as we think about you know obviously revenue is a driver but if revenue stays kind of in this type of environment what can you do to optimize the capital and there is still some expense opportunities even after all the progress you've made today?

Harvey Schwartz

So if you go back again a couple of years ago you know we really were focused on building operating leverage into the enterprise and I think in the end of last year you saw that reflected in the response sort of our performance with a 10.7% ROE and this year you're seeing increasing operating leverage but obviously it's important to see the back to back consistency. Now we're always looking to be more efficient. We can certainly do things you know far from corporate [ph] we can certainly do things in terms of capital efficiency and expenses and we're constantly looking at how to leverage technology particularly as we get more visibility into finalized rules so we can adapt. I would say you know my comments before about finding balance. As we have been doing this the most important thing is we want to make sure we're well positioned for our clients when revenue opportunities do look better and I think you see it kind of across the board in terms of market share and investment banking, reachable [ph] presence, growth and asset management all across of our businesses you're seeing it we will try to find that balance and look we always get these things right but that's what we're trying to do.

Matt O'Connor - Deutsche Bank

And I guess as a follow-up, this is just a general question for you and the industry that when people look at the fixed income environment I think there is a lot of focus in all the structural changes occurring and concerned that there will be revenue pressures but I also get the sense that there hasn't been maybe an entire adjustment to that franchise or to the platform as people wait to see what all the new rules are and kind of when Fed that of buying bonds what happens to that market? So I'm just wondering like is that an area where there might be some capacity adjustments because if you see for the industry as a whole?

Harvey Schwartz

It's a really good question; I'm going to break it down in two part. On the first part in terms of the impact of regulation I think it's early you know we haven't even really seen the launch of things like swap execution facilities and the real impact is in ultimately how market structures adjust. I do think though that the big impact from a regulation perspective is the fact that the entire industry is carrying more capital and I think implicating [ph] in your question but you should correct me if I'm not appearing correctly, it would appear that perhaps there is excess capacity in the industry. Now we have been building a lot of operating leverage into our fixed income franchise over the last couple of years and at the same time we feel very comfortable with our relative position in all of our businesses and so to the extent to which capacity comes out we think we will benefit from that in terms of our competitors exiting businesses but we will have to see. We're just focused on doing what we can with our opportunity set.

Operator

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

Harvey Schwartz

Good morning, Mike.

Michael Carrier - Bank of America Merrill Lynch

Good morning. Thanks a lot. Maybe first question just getting back to the ROE given that you have more clarity on some of these rules, whether its RWA leveraged Volcker, you just spent a few years trying to kind of reposition the business. I guess what inning do you feel like you are in terms of repositioning? And then at some point, you sold some of the U.S. reinsurance business, I think the Europeans there, I guess some point you need to be able to either redeploy more than your earnings in terms of capital or are you seeing enough opportunities globally as the economy and the macro environment improves that you can start reinvesting to generate high returns?

Harvey Schwartz

So it's a great question. So obviously we have taken a number of steps over the past several years to in terms of selling businesses that because of rule changes were quite frankly just better held than other people and when you provide the proper return, then as I said going to the hood, we have been building in as much operating flexibility into, for example, our fixed income franchise as we can during this fortune environment. So I guess I would say with respect to capital first and foremost, we just want to make sure that firm is positioned safely and defensively and at the same time we can be offensive when opportunities present themselves, but it's really going to be determined by client activity, economic growth, confidence that will be the opportunity set and will just adjust. It will always be incremental. So you will see us make incremental steps. You have seen us take some move selling things, but you will see us make incremental steps, but really now, it's about that balance, because we don't want to forgo the upside.

Michael Carrier - Bank of America Merrill Lynch

Okay, that's helpful. And then just on the banking side, you mentioned pipeline remains strong. It feels like we are coming off a very strong 2013 just given particularly on the equity side and even on the debt side, but when you look at the outlook and you look at the conversations, is it possible to have multiple years meaning '14/15 with an improving economy, where the investment banking revenues are continuing to grow off this base and maybe partially it's because we had five years of pretty anemic activity in some areas. I just want to get your outlook is this some view that '13 was a great year and some spot and so the growth rate from here might be tougher?

Harvey Schwartz

It's a good question. So if you sort of just think about our investment banking franchise and you break it down between let's just say underwriting on one side and advisory services, the merger business on the other. The underwriting activities clearly there is a market component to that in terms of tightening credit spreads people looking to put capital to work and then obviously you saw it in the fourth quarter a big uptick in equity underwriting, the market was there. The advisory business for a CEO making a decision on a merger, it's a career defining decision and against the backdrop. Again, go back and look at 2013, against the backdrop in one quarter you are contemplating what is tapering mean and then two quarters later, you are contemplating a government shutdown at that difficult backdrop to make a career defining decision. And so it's going to lack that client and you are going to see pickup in M&A activity in sectors where you see global confidence and so not surprising to us at all and we have been very protective about franchise obviously a leading franchise.

Now, as it relates to some of the other markets like for example take the debt market, one thing I have learned in the past year, because I think one of the most frequently asked questions I got at the end of the last year was what is the debt underwriting looking like in the environment in 2013? I couldn't have told you that there will be as much activity as there was. We just respond to when we look to deliver for our clients in it. Now, you could paint a picture of a declining debt environment, but also you could see debt transactions of significant swing to mergers. We have seen some of that Europe recovery and a long-term shift to the capital markets, growth markets shifting more towards capital markets due to very long-term trends that are in place. Simple, we will say.

Michael Carrier - Bank of America Merrill Lynch

Okay. And then just last question on FICC, you just I guess given some of the near term trends that we could see. I just want to get an update on how you see some of this transition of the OTC markets under these swap execution facility platforms, maybe we will get it mid-February you know who knows if it will get a delay but it seems like clearing was fine last year. I just want to get your sense on talking to client, talking to customers, is it progressing? So we don't have many hitches, little bit more challenging.

Harvey Schwartz

Sure I actually think the regulators approach and all the industry participants, clients, exchanges and clears I thought that the process of clearing I don't know if you give it higher marks. It was done in stages, it was very orderly. I think the issue with swap execution facilities obviously there is a big technology build and change in behavior across all of our clients and so the only thing I would say about and we will have to see what happens in February is I think that measured approach the clearing was quite thoughtful and I know there is lots of discussion about the approach you know the burden is on all of us to make sure that you know as an industry we adopt these protocols. A lot of burden obviously on swap execution facilities because they are the center of all this connectivity but clients need to be ready. It's hard for me to gage their preparedness but I think if it was staged and I don't mean extended but I think if it was staged and it mirrored the approach to clearing I think at the margin it just I don't know maybe it's just more prudent.

Operator

Your next question is from the line of Roger Freeman with Barclays. Please go ahead.

Roger Freeman – Barclays

Can you just remind us what you think the obviously the market condition is depend on, what that with the realization profile looks like in terms of (indiscernible) I mean is this kind of, so a couple of three years of you know mature investments that we will see coming out?

Harvey Schwartz

So obviously and we talked about this over the course of the year, it's an environment that has been favorable for harvesting and so you're seeing that as we go through. We are also seeing interesting opportunities around the globe for investing but you're seeing the performance as it comes through.

Roger Freeman – Barclays

How should we think about the comp ration? You know it's probably it's not maybe is it explicit there but how do you think about compensation on those and how it's beneficial throughout the sort of managing compensation on the firm?

Harvey Schwartz

So absolutely no change to how we're thinking about compensation. First you know we manage the compensation across the firm it's a collection of businesses and pay is based on firm performance then we go into the divisions and obviously down to the individual and so obviously it's our largest expense. We spend significant time on it; I think you're seeing the benefit of you know some of the tough cost cutting that we embedded into the business over the last couple of years.

Roger Freeman – Barclays

And I guess one more and I know it was Volcker out of the way and now do you think you've got enough clarity around all the rules, the capital requirements et cetera to step up investing on balance sheet again as the opportunity sets in there?

Harvey Schwartz

The short answer is yes but I would breakdown regulatory clarity from the opportunity set. The opportunity set is going to be driven by what we see working with our clients and being very disciplined about returns as we have in the past. In terms of the rules that, you know the rules that gives a road map or the various alternatives under which you can undertake the activities you can you invest with your clients in 3% funds, you can work with other Volcker compliant structures and obviously we can invest off our balance sheet. So but that speaks to how the when and working with clients that will be opportunity driven.

Roger Freeman – Barclays

And secondly, you mentioned that you thought were still not quite in a normal cyclical cycle so I guess how far off do you think we're not time wise but just how much of an impact are these other things having and at this time what would you say the top 2 or 3 sort of issues are that are keeping you from saying this is within the balance of the cyclical norms.

Harvey Schwartz

Yeah so what I was really trying to underscore there is some of the things I mentioned earlier, which is focusing on a shift from quantitative easing to tapering or the entire financial symptoms are adjusting to multi-year processes in regulatory reforms or a government shutdown. Again, things are not normal characteristics of a cycle. And so referencing the script is sort of supply and demand driven see really what are the fundamentals of the economy, what are the fundamentals of performance of companies, and that's really what I was talking about it, it maybe not the best score, but it's more of a return to sort of the normal day to day challenges. And as you have seen in the past, when there was economic growth in activity in a degree of certainty, our clients are willing to make significant decisions, commit more capital and we get to work with them and the activity levels pickup.

Roger Freeman - Barclays

Okay.

Harvey Schwartz

Gently, but the trend is slowly improving, steadily.

Roger Freeman - Barclays

Really obviously just had a couple of weeks there at the start of the year, but how would you characterize client engagement so far?

Harvey Schwartz

Client engagement, we are very, very focused on our clients in terms of the first couple of weeks, way too early to extrapolate anything.

Roger Freeman - Barclays

Yes, okay. Thanks.

Harvey Schwartz

Thank you.

Operator

Your next question comes from the line of Guy Moszkowski with Autonomous Research. Please go ahead.

Harvey Schwartz

Good morning Guy.

Guy Moszkowski - Autonomous Research

Thank you. Good morning Harvey. So on the I&L obviously you had significant gains whether they were to the extent that they were realized or not in a sense that maybe it doesn't even matter, because given the IPO environment and the apparently very much improving M&A environment, a significant amount of this probably will be over the course of the next year or so it seems to me. And so then the question is what's your philosophy with respect to capital return of discrete amounts like that? And do you think it's possible to make a case to the Fed that for significant freeing up of capital of despite it's not necessarily the right approach to kind of compare to earnings?

Harvey Schwartz

So it's a good question. I think the core of your question where you are saying is basically if risk is down. So the consumption of capital is lower and the demand for capital isn't there, the question is can we return or not return it, okay. Now, the way we will look at that question is first and foremost running with periods of excess capital is not a problem if we feel like we are going to be able to deploy that capital. We are never going to force that deployment. So first and foremost is going to be risk judgment about how we utilize it. If we say opportunities, where capital cannot be deployed and I will say for the long-term, for example, in our insurance businesses where the rules have changed, then we will look to return it. And we'll work with the Fed over time in the construct to return that capital, I am certainly not speaking for the Fed here, but I don't think any industry benefits from holding excess capital in the system for an extended period of time.

Guy Moszkowski - Autonomous Research

That's there. On Volcker, you mentioned that you have a very high level committee that's looking at implementation and the things that you need to do in order to implement it fully. As analysts should we be focused more on potential revenue impacts of that implementation or the cost of that implementation?

Harvey Schwartz

I think, well, clearly the cost structure issue is one need to focus on, because as I mentioned the compliance burden is pretty intent. I think the revenue again, one of the things in the rule obviously and I have to get the exact language, but basically you said that market-making activities effectively essential, because it promotes healthy capital markets. And so I think that the Volcker Rule is covered, we will have to see ultimately in the implementation what happens, but at least in the intent of the final rule that seems clear that they want to support capital markets. And so those revenue opportunities again are going to be predominantly driven by the opportunity set. That's all I think about it.

Now, in terms of our implementation team, this is just kind of typical how we approach it just making sure that we have identified the right people across entire firm to make sure that we do it as efficiently as possible and then there will be a build, but at this stage, it's way too early to sort of quantify any ongoing cost structure for you.

Guy Moszkowski - Autonomous Research

Okay that's helpful to get the philosophy of how you're thinking about those things. The term to revenue ratio as was mentioned earlier did come in lower for the year and you know to the extent that there was a significant revenue shift certainly in the latter part of the year, it seems to have been in favor of I&L**.** Is 37% sort of a benchmark that we should be thinking about now for next year or if for example in 2014 revenue were similar but the composition was more traditional markets and investment banking and less I&L, would we expect that comp ratio to be higher?

Harvey Schwartz

So that's a great question. It's way too early to tell obviously in terms of how we will think about compensation in 2014. It will be driven as I said before by performance and the performance will be driven by obviously the collection of businesses that we run. I think that the mix issue, I understand why you're asking the question but there is no single business or segment that drives compensation expense for Goldman Sachs and so you know for example if you had asked a question slightly differently you said listen let's just say I&L everything else being equal and I&L was down I would expect that means the performance of the fund is down it's obviously compensation expense would be down but at that point in time we will be incorporating all factors, competitive positioning, and this is we're building because while it's pay for performance for the year it's also investing for the long term.

Guy Moszkowski - Autonomous Research

Just a couple of housekeeping questions. I don't know if you have talked about the impact of the (indiscernible) sale on FICC revenues in the quarter I didn't see it in the release if you could help us with that, that would be good.

Harvey Schwartz

Yeah sure no problem. So on a DVA adjusted basis sequentially and obviously we had a challenging third quarter in FICC, and got a lot of attention but sequentially DVA adjusted revenues were up 46% if you adjust for the sale of the European insurance business it's more like 30% it's roughly about $200 million.

Guy Moszkowski - Autonomous Research

And then final housekeeping type of question. You talked about the SLR being pretty much in compliance on an NTR basis. Have you had a chance yet to think about what the impact would be of adoption of the final Basel add-ons?

Harvey Schwartz

No we haven't, we're still digesting the rule. As you would imagine under that paradigm obviously just because of the nature of our business it impacts our ratio more as a result of things like netting and collateral but we're still digging through the rule.

Operator

Your next question comes from the line of (indiscernible) with Credit Suisse. Please go ahead.

Unidentified Analyst

Just a follow-up on leverage with the question earlier on. Just in light of your relatively stronger position in there. Just given the lengthy timeline for implementation. You know as leverage becomes the binding constraint for your competitors. I would be curious in your thoughts on Goldman's appetite to be more aggressive or more aggressively compete for market share in client centric but balance sheet heavy businesses like prime brokerage.

Harvey Schwartz

It's an important question, if you just split into two parts for a second on the first part we're not going to change or approach to risk and by the way the FDA was a good example earlier. We're not going to change our approach to risk management and how deploy our resources to the extent to which our competitors change their strategy. The other half of the question I think is the way you're asking which is for example if whatever the constraint is it does not to be the leverage ratio but if a firm is constrained, if our competitors are constrained in a particular business and we have relative strength in that business we would assume that we could be a more valuable provider to our clients on relative basis and that relative strength would just improve. I think that paradigm applies for everybody.

Unidentified Analyst

Exactly what I was asking. Thank you. On the compensation policy just given the importance of lower earnings volatility to the regulators and investment community. I was just curious for kind of updated thoughts on how the firms approach to managing the quarterly compensation accrual, do you anticipate quarterly comp accrual will be more sensitive to the revenue environment or should we expect the practice of a 4Q true-up to continue? Thank you.

Harvey Schwartz

So the practice of the 4Q true-up is just that we said competition we have full visibility into the performance of the business is. So again, no change in compensation philosophy, we actually think it's quite important to maintain our philosophy around compensation and for all of our employees at Goldman Sachs to understand it, understand our obligation to the firm and the context for the compensation philosophy ultimately obviously as the largest helmet of our cost structure we incorporate everything you would think we would put into that including our obligation to our shareholders.

Unidentified Analyst

Thank you.

Operator

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

Betsy Graseck - Morgan Stanley

Hey, good morning Harvey.

Harvey Schwartz

Good morning.

Betsy Graseck - Morgan Stanley

So I just wanted to follow-up on the full quick question, I know you have got a lot of that already this call. But in thinking about the I&L I know you called out Volcker pertaining to TE into the hedge fund investments you got, but do I take that to mean that the other components of I&L you don't – you are not constrained by Volcker, so the real estate piece is the credit piece of the loan funds?

Harvey Schwartz

You are into a pretty intricate territory. So they have got [ph] rules of 900 pages. Right, and so I wasn't – what I was basically saying is I was bringing it down to some there is going to be 3% funds.

Betsy Graseck - Morgan Stanley

Right.

Harvey Schwartz

And there are going to be other Volcker structures, so for example, historically, the way people may have defined CLOs, you may have included securities and depending on the very intricate definition of the rules, you may not be able to include some securities. And so however the investing activity and working with our clients' needs to be structured, we are going to comply. I think that the Volcker Rule what it does is it outlines a set of rules where market participants can do that. Again, 3% funds, other covered structures and of course you can invest in line with our balance sheet, which is a pretty straightforward activity, but that's really what I was trying to emphasize. You really have to go to the rules they have to determine whether you can do real estate in a particular way or not and look we will comply.

Betsy Graseck - Morgan Stanley

Right. No, I get that. It's just that as you know and you get some good detail about the balances in I&L and how they are broken down in a couple of different ways. So I mean, I think the Street is just going to be looking at that to understand how the capital is getting freed up and then reinvest in that space, because clearly, if there is reinvest, that would be great and that's not you want to see it bought back. So I was just wondering how you are thinking about disclosing the balances in I&L, I mean, I guess I am just wondering to the degree you can put it in and then a Volcker, non-Volcker kind of disclosure that would be I think helpful for the Street?

Harvey Schwartz

So I think we have been pretty good in terms of disclosure around, for example, what the firm's investment in funds are, it is roughly $15 billion in less than a quarter?

Betsy Graseck - Morgan Stanley

Right.

Harvey Schwartz

I think the investing process is going to be one again which is going to be driven by the opportunity set and what our clients want us to do. And so the decision of reinvest or return, we are going to continue to make the decision in the same way. If the opportunity set is not there, we are definitely not going to be a firm that's going to force investing. We are just going to be disciplined and if we don't take the opportunities, then we are going to look to return the capital. Now, you are certainly seeing the impact of those businesses in our capital ratios. We talked about things like the financial institution production in the past. And so there are – there is a lot of aspects to all the rules, not just Volcker, but I am actually 100% sure and I understand your question, so if we need to we connect with them afterwards and we (indiscernible) a bit more.

Betsy Graseck - Morgan Stanley

Yes, sure. Okay, thanks.

Operator

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

Brennan Hawken - UBS

Hi.

Harvey Schwartz

How are you?

Brennan Hawken - UBS

Okay. So you guys have VAR kicked up here this quarter, it's actually kind of at the level we haven't seen in quite some time, could you walk through and help us understand what drove that?

Harvey Schwartz

So really all driven by basically an overall decline in market volatility and then an increase a bit in positional risk, but that really is virtually all concentrated in equities as you would expect very active equity quarter, lots of activity.

Brennan Hawken - UBS

Okay. Was there any kind of positional tailwind for your equities business or should we think about this as all sort of solid flow revenue?

Harvey Schwartz

Usually it was solid flow revenue, when you do block transactions and it was a particularly active block quarter and I got to give credit to our team I think they did a fantastic job in executing blocks because it was a competitive environment. Those block transactions can be large so they will drive LIBOR [ph]**.**

Brennan Hawken - UBS

And on the equities business this quarter certainly was better quarter but when you look back at 2013, and you adjust for the sale of the insurance business the revenues really are not all that strong and then kind of stand out on the street as rather week. Are you thinking about, how you're thinking about loss of share in the equities business and what you want to maybe do to try to counter that till you come up with strategies, what's your view there?

Harvey Schwartz

We are always focused on any area of the business that we can grow and deliver more value to our clients. I would say given our starting position in terms of just our aggregate division in the marketplace, in terms of whether it's prime brokerage, underwriting, the derivative business, our cash business. You know one of the pretty significant position in terms of aggregate market shares. So you know we're trying to get back to these earlier issue of all revenues aren't created equally and so I completely understand you're focused on quarter to quarter changes in revenues. We're focused on delivering over the long term and it's not that we don't look at it but there is risk in these revenues and so you really have to look at the entire set of metrics and how it's our pretext margin looked versus other people's and how are we driving ROE. So we feel very good about our franchise position.

Brennan Hawken - UBS

Okay and that's fair, well we have only blunt tools so we use the tools we got. And then last one for me, litigation expense we saw you know a pretty big uptick certainly when we include many of the money center bank competitors that's being a big theme the last few quarters. It definitely feels like this is something we should probably count on the near term, are you do you guys feel as though you're part of that scrum and how do you feel about your reserve for litigation? Have you had a chance to build it up? Do you feel like you might be a little bit behind the bond upfront, should we count on some build here for the medium term here? Can you give us some color on that? I know it's a hard one.

Harvey Schwartz

This is a very, very important question because all firms in this particular case are not created equally. The way I think for us and the entire marketplace this is our best estimate, so every quarter really no different than mark to market accounting. Every quarter we do our what is basically the best estimate in that particular quarter and we add to the reserves. Now we also obviously disclose a reasonably possible loss which you saw most recently at the end of the third quarter but this is a quarter-to-quarter activity. It is not a budgeted forward looking activity. We incorporate all the information set that we have at this point in time.

Brennan Hawken - UBS

And do you have a view on where your year-end potential losses above you know reserve levels will shake out or how that will change versus your last reported number or is it too early to know on that?

Harvey Schwartz

No again this is not a budgeted, if I knew at the beginning of 2014 that my estimable and probable number was 962, sorry at the end of 2012 I would have taken 962 in the first quarter. So I would encourage you to go in the financial statements if you look at our reasonable possible loss that's a good disclosure item which was $4 million at the end of the third quarter.

Operator

Your next question is from the line of Michael Mayo with CLSA. Please go ahead.

Michael Mayo – CLSA

I'm still not sure on the answer to the Volcker Rule and I understand it's 900 pages, there is lot of work to be done but you know one of your competitor said it should not have a material impact and we can all come up with our own estimates what the impact of Volcker might be on you guys but can you just give us some range like it should impact our revenues you know from X to Y percent or expenses from Y to Z percent or size it to some degree?

Harvey Schwartz

I thought I was clear [ph] in terms of the revenues that at this stage it doesn't look like a revenue impacting items since the Pablo but of course we've already (indiscernible) other businesses early on in the process and made changes. And so I don't think the primary issue at this point in Volcker is about revenue impact although we have to see how regulators ultimately digest all the data they are requesting etcetera. And with respect to the compliance costs that I mentioned, it's just too early to quantify, but there is a pretty extensive compliance regime.

Michael Mayo – CLSA

Okay. And as it relates to VAR, to what degree are you deliberately taking more risk, I think your predecessors used to say we want to live to fight another day as far as risk of mentality, it seems like maybe you are taking a little more risk in equities, but not necessarily elsewhere or what's your risk stance?

Harvey Schwartz

So I think my predecessor also would have said we will never deliberately take more risk. It's just not the way we are going to run the enterprise. It's all activity driven. So that's why I emphasize the equity number picking up during the fourth quarter.

Michael Mayo – CLSA

Okay. And for the year revenues were flat even with much higher stock markets even with gains in investing and lending. So when you look out looking for revenue growth, where do you think that can come from?

Harvey Schwartz

So look I think the most important thing for us this year was how we found that balance in terms of achieving the 11% ROE and at the same time continuing to drive operating leverage. We feel very good about franchise position in an absolute sense, in a relative sense. So I am certainly not predicting the future, but as economic activity picks up, confidence picks up, capital markets around the world, particular regions. I think you could certainly paint an optimistic picture, but I want to be clear I am not doing that.

Michael Mayo – CLSA

Okay. And what is the ROE target for Goldman?

Harvey Schwartz

Yes. Thanks for asking the question that way, Mike. Yes, I understand this is an important issue for all of you and we are getting increasing clarity around the world sets, although the sale a fair bit too dull. When we put out an ROE target, I think first and foremost, we wanted to be credible and we wanted to be achievable. And so when you hear from us that's what it will be. Now, between now and then, no one should get off this call thinking that we are not exquisitely focused on how we are deploying our capital and how we are focused on returns and how we are thinking about returns to our shareholders. So that was the target point today, Mike.

Michael Mayo – CLSA

No, I understand. But I mean when do you think you will have a target? When do you think you have enough clarity around the capital rules to highlight an ROE target?

Harvey Schwartz

I don't know. I can't predict the ultimate visibility into the rules they had and what it means for markets, but when we have – but we know it's important to you.

Michael Mayo – CLSA

Alright, thank you.

Harvey Schwartz

Thanks Mike.

Operator

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

Jim Mitchell - Buckingham Research

Yes. Hey, good morning.

Harvey Schwartz

Hey, Jim.

Jim Mitchell - Buckingham Research

Hey. First question on equity derivatives, you mentioned that it was significantly lower this year versus last year, I guess that volatility is down, but the market environment was pretty constructive and typically lower utility means little more risk taking. So was there anything unusual this year or I should say last year in terms of derivatives that was so much weaker than '12 how should we think about that going forward?

Harvey Schwartz

No, there was nothing in there. I think you are just seeing the natural tos and fros of client activity and markets, but there is no single item I draw your attention to.

Jim Mitchell - Buckingham Research

Okay. And then maybe on the capital side, you guys highlighted about a 60 basis point difference between the standardized and advanced approach, do you envision that converging over the next few years and what would be the major drivers?

Harvey Schwartz

So, as you know the standardized approach really is in (indiscernible) not as risk centric and so that's not something that we had focused on as much. So things like collapsing derivative notional, which is a good thing to do for managing operational risk. So it's really something that we are starting to focus on now.

Jim Mitchell - Buckingham Research

Because you are going to – the Fed wants you to report the lower of the two, right?

Harvey Schwartz

Yes, well both.

Jim Mitchell - Buckingham Research

Right.

Harvey Schwartz

Now, of course, under the transitional rules as I mentioned, we are north of a 100 basis points higher anyway. So we are going to get fully phased in numbers which we have a couple of years on.

Jim Mitchell - Buckingham Research

Right.

Harvey Schwartz

Jim, from your perspective, I wouldn't consider it as a significant issue.

Jim Mitchell - Buckingham Research

Okay, fair enough. And lastly on compression credits [ph], do you view that as a material benefit for you guys going forward? Do you think its early stages and still a lot of room there as it's sort of more in the margin?

Harvey Schwartz

So it's early, but certainly the rule set, but that's an example of where a rule set comes out and rule set gets behavior and in this case you are starting to see the behavior and I would think you continue to see a pickup momentum.

Operator

Your next question is from the line of Fiona Swaffield from RBC. Please go ahead.

Fiona Swaffield - RBC

Just a clarification on the moving parts on the Basel III look through the 9.8 which seems pretty static. Could you talk us through I think it's given the RWA number but in the last quarter the deductions moved quite significantly and I thought they might continue to do so. Doesn't look like much is happening there and also is there some operational risk inflation? I think it's marginal but I do remember a number being a bit lower than that six months ago. Thank you.

Harvey Schwartz

Sorry can you just say the second half of the question Fiona?

Fiona Swaffield - RBC

I think you said a number of operational risk weighted assets of 85 billion I'm not sure I got it, I think that's slightly higher. I'm just trying to understand why the RWA is not going down a bit more with the natural roll-off?

Harvey Schwartz

Okay so with the type of ratio there is a lots of give and get under the hood and one of the biggest drivers as you know since the final rule came out has really being the financial institutions deduction, well significant and non-significant and so that was really the most significant change in the final rule which drove it but you know for example we picked up a benefit on the sale of the European insurance business of 20 basis points but that was then offset by other risk factors. So they said it's a fair bit happening under the hood.

Fiona Swaffield - RBC

And is it right that on operational risk weighted assets it's trending slightly up, is that an offset of the roll-off of…

Harvey Schwartz

Yeah I know that’s correct slightly higher and as you know operational risk, RWA they are slow moving and they are sticky.

Operator

Your next question is from the line of Matt Burnell with Wells Fargo. Please go ahead.

Matt Burnell - Wells Fargo

Just a couple of housekeeping related items given that we have gone through most of the important questions at this point. In terms of the fixed income inflows that you highlighted in your prepared remarks I guess I’m just curious if you can provide some further color on why those inflows were so much bigger than some of the other areas given you know most people’s view that rates are going to be going higher and that presumably that means investors would be thinking about moving money into less rate sensitive areas.

Harvey Schwartz

Yeah so I think it's a pretty straightforward answer, there is two parts. One is just about differentiated performance in fixed income and also there were funds that we have that are unconstrained fixed income products which you know are giving investors the flexibility I think and give us a more dynamic ability and managing the rate environment but really performance driven.

Matt Burnell - Wells Fargo

And I guess let me follow-up on prior question talking about your opportunities. How do you think about the revenue opportunities over the next couple of years across your geographic regions, I guess broadly speaking U.S., Europe and Asia? Is the greatest opportunity in the U.S. given some of the confidence we're getting relative to the economy or some of the trends you were talking about that we have been hearing about for a long time in terms of fixed income issuance, in Europe finally moving out of the banks and into capital market.

Harvey Schwartz

Yeah so quite frankly hard if not impossible to predict but with respect to our position and our commitment we feel quite good about how we have deployed the resources and how we have made adjustments of the resources during this portion of the cycle. You know for example we have maintained a very strong commitment to Japan. Well certain of our competitors have decreased their emphasis on Japan because you know as I referenced in my comment, the equity market haven't been in deep levels since 1972 and so we feel well positioned to capture the opportunity. Now importantly it's not about any individual region but it's the connectivity across our businesses and ability to connect for example our investment banking clients with resources in institutional client services, our securities division where we can deliver solutions globally. In Asia, people are looking to raise capital and it woo [ph] the U.S. investors that's really where you get the synergistic leverage across the enterprise.

Matt Burnell - Wells Fargo

And I realized question about the backlog has fraught with issues but presumably if you were at a five year high in the backlog three months ago it's grown a little bit since then as of year-end. You've seen very strong improvement in IPOs, IPO issuance. M&A looks like it's building, is the composition of the backlog now moving more towards M&A and less from equities and fixed income?

Harvey Schwartz

No there is not a huge shift in terms of mix although there were some adjustments certainly quarter, but what you are really seeing is and this might have been hard to predict at the end of the third quarter is replenishment, because it's pretty active fourth quarter. And so to the extent which it's a leading indicator it's obviously a positive one. And I do think it reflects as I said earlier sort of global sentiment if you will in confidence and our corporate client base, but look that could change.

Matt Burnell - Wells Fargo

Okay, thanks for taking my question.

Harvey Schwartz

Thanks.

Operator

Your next question is from the line of Steven Chubak with Nomura Securities. Please go ahead.

Steven Chubak - Nomura Securities

Hi, good morning Harvey.

Harvey Schwartz

Hey, Steven.

Steven Chubak - Nomura Securities

So I had a question regarding the investment considerations, particularly as it relates to Volcker on fund related investing versus direct balance sheet investing. So fund-related investing largely limited, direct balance sheet investing appears to be permissible, but I didn't know if it is apparently are the IRR or at least investment considerations meaningfully different between the two?

Harvey Schwartz

No. So IRRs are IRRs, we don't adjust for the vehicle, if you will in terms of how we deploy that capital. So we would never allow, what do we call the term discipline to be corrupted by the particular vehicle in choice. I do think that the capital treatment can vary obviously as we talked about the financial institutions deduction and the money we have in front which obviously have to come out anyway. It's quite significant, but the risk gets captured in any number of metrics. It will be in the capital ratios, it's obviously stressed under CCAR. So it's not a vehicle choice.

Steven Chubak - Nomura Securities

Okay. Well, I actually had a follow-up to that. I didn't know if you could disclose the RWAs attached to the other $45 billion or so of I&L investments that I suppose aren't – that are in fact Volcker compliant?

Harvey Schwartz

Yes. I don't have that number, but you are welcomed to follow-up with Dane after the call.

Steven Chubak - Nomura Securities

Okay. And do you happen to have the number of further financial institution deduction for which is roughly $8 billion last quarter, I didn't know if it was roughly around that same level?

Harvey Schwartz

Yes, it's up a bit since the third quarter.

Steven Chubak - Nomura Securities

Okay. And just last one for me on the leverage ratio, I didn't know if there is a specific target that we should be contemplating longer term. So assuming that the 5% ratio are mandated level is the binding constraint, is there some sort of buffer that we should be contemplating on a go-forward basis?

Harvey Schwartz

We haven't given where we are in terms of the proposed rules obviously. And as you know, our philosophy on these things is given the regulators have provided an adequate glide path we will wait to see the final rule, before we will adjust any aspects of our business. And ultimately, you will see us run with a buffer, but we haven't invested any energy in that yet.

Steven Chubak - Nomura Securities

Yes, that's it for me. Thank you for taking my questions.

Harvey Schwartz

Thanks so much.

Operator

And your next question is from the line of Christopher Wheeler with Mediobanca. Please go ahead.

Christopher Wheeler - Mediobanca

Yes, thank you. Good morning. Couple of questions. The first one is on something that's philosophical this morning in the FT after your former partner's testimony yesterday to the social committee, where you mentioned that the European bonus cap was something that wasn't the most appropriate magnet of managing bonuses. Can you talk a little bit about how you are dealing with that issue, because obviously the FT is running with the view that New York is a much more attractive place for people to be (indiscernible) given this bonus cap? I am just wondering about what you think the impact might be in terms of increasing fixed compensation. I know I think you said it's not too many people impacted, but have you had to make or will you have to make too many changes in respect of this?

Harvey Schwartz

No. Look it's more in the context of the firm. Obviously, Europe as a region is critically important to us strategically. So we are very committed to our clients there and our people there. And so no, we will work with the regulators and we will comply accordingly.

Christopher Wheeler - Mediobanca

Okay. And the second question really is really a follow up on I think what Guy and Betsy have been asking, but I am trying just to get really clear my mind about the capital allocation to I&L and how you are thinking about that from the planning perspective? It seems to me that where this perhaps when would be a couple of years ago the thought was that you are going to be reducing capital, because obviously Volcker was going to force you out. It sounds to me like you have no clear view at the moment on reducing capital in that business. It's maybe the fact that you will naturally spin off some capital and you will leave it very much depending on the state of the markets to whether you actually lead it in I&L or whether you actually move it elsewhere in the business where you can get high returns, is that a fair way of describing things?

Harvey Schwartz

So with respect of capital coming out of the business obviously the Volcker Rule is very definitive on what we need to achieve. So early on as soon as we identify that as a likely finalized rule item we announced the reduction in our hedge funds. In terms of some funds will just low off depending on the opportunity set but obviously we're committed to complying with the rule and that's not optional.

Christopher Wheeler - Mediobanca

Yes but what I'm asking is, it sounds like where capitalist is thrown off, you're perfectly happy to absolutely (indiscernible) rather than deploy it elsewhere in the business if you see the opportunity. It's not sort of fixed and concrete but you really want to reduce the amounts of capital in your principal business.

Harvey Schwartz

Okay I'm sorry I understand the heart of your question now. We don't think about capital allocation in other words we're going to deploy an explicit amount of capital to I&L because it's all return opportunity set client driven, so we will be happy to redeploy that capital if it's best use for in another part of our business and if necessary we will look through return on capital.

Operator

Your next question is comes from the line of Douglas Sipkin with Susquehanna. Please go ahead.

Douglas Sipkin – Susquehanna

Just two questions one maybe just on the outlook for headcount growth. I guess year-over-year about a flattish year I think net adds about 200. Any feel for what you guys are going to be looking to grow that or sort of keep it steady state right now based on the environment that you're seeing in front of you right now?

Harvey Schwartz

So no plans for any significant changes, if you dig under the hood a little bit the headline numbers sort of match some of the efficiencies we build. Obviously we talk about that in terms of the build out of for example our Salt Lake City office et cetera and how we're leveraging technology and people and kind of what I will call the pyramid if you will around the organization but there are no significant plans one way or another but it will be dynamic. If you see growth opportunities then you should expect to see us add if we need to and then if the environment is less favorable we will make other adjustments but it will be dynamic.

Douglas Sipkin - Susquehanna

Got you and with respect to the asset management segment obviously you guys have had some positive progress there. I know you guys have done couple of small sort of it feels like opportunistic acquisitions, you know given how the capital model of the firm is changing you know would you guys consider something doing something bigger in asset management on acquisitive side? Is it presented itself given sort of the favorable capital/returns that business provides in the new world?

Harvey Schwartz

I think that, the business itself has been a huge strategic priority for us and you know what you're seeing is not the, it's not the result of a quarter's performance. You're seeing a multiyear commitment to the business which is you know now starting to show some differentiated yield. In terms of opportunity set look if there are opportunities that are accretive with Goldman Sachs or business and our clients you should expect us to consider anything.

Operator

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

Devin Ryan - JMP Securities

So I just have a question on the FICC business. I asked a similar question last quarter but we have now seen outflows out of bound, mutual funds in 29 out of the past 31 week. So I know the number is pretty small in the absolute but just given that your FICC business is more institutional in nature, is that something that maybe you're paying closer attention to now that the trend has picked up some more steam and are you actually seeing any change in client behavior as a result of that?

Harvey Schwartz

So no change in behavior that then I would come in touch with. You know the behavioral changes have been more response to the news dynamic during the course of the year. The issues that I talked about you know what does tapering mean versus QE? What are the government shutdown mean? Those were the kind of things that were little paralyzing at times for clients I think as they contemplated the implications. Obviously over very long periods of time fund flows have an impact potentially in the short one they can when there are dramatic controls [ph] whether it's in the matter with those bond funds or equity flows but I don't think yet we're seeing any major change in behavior.

Devin Ryan - JMP Securities

And then just a question on comp, can you give any color on the mix of cash versus restricted shares and whether there is any meaningful change from last year in terms of how you thought about that and then just more broadly what the competitive environment, feels like today they recruit and retain talent maybe relative to a year ago?

Harvey Schwartz

No. So we don’t disclose details on the competition there, but you should rest assure that for all – for everyone that they are – that is participating, that is receiving equity that maybe there are long-term restrictions on that. And we believe that just basically aligns the broad employee base interest with our shareholders and that’s been historically the case. Now, we thought about it for a long time. With respect to talent, we have seen some tailwinds in the ability and this isn’t recent, but certainly the last year and a half we have seen the ability to acquire talent when needed. And so now having said that, our people are always highly pursued also, but that’s not a new phenomenon.

Devin Ryan - JMP Securities

Great, thank you.

Operator

And this concludes the Q&A session. Please continue with any closing remarks.

Harvey Schwartz

So just want to thank everyone on behalf of the team here for dialing in. We look forward to seeing you during the course of the year and if we don’t see you in the next couple of weeks, we will certainly catch up with you on next quarter’s call. Thanks again everybody.