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 first quarter 2014 earnings conference call. This call is being recorded today, April 17, 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 first 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 the year ended December 2013.

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.

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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 first quarter results. I am obviously happy to answer any questions.

Net revenues were $9.3 billion, net earnings $2 billion, earnings per diluted share were $4.02 and our annualized return on common equity was 10.9%. The first quarter reinforced two consistent themes that we have seen over the past few years. First, the continued uncertainty around the strength of the global economic recovery; and second, the dominant role that central banks play in driving broad economic activity and capital market sentiment.

With respect to the first, market participants struggle to reconcile mixed economic data across different regional economies that weigh the prospect of a strengthening U.S economy against an improved, but still relatively weak European economy and a slowing economy in Asia. As it relates to the second theme, discussions among market participants are also centered on the potential for additional central bank activity.

In United States, the focus remain on the pace and potential magnitude of further tapering to the Federal Reserves bond buying program. In Europe, the market attempted to weigh the potential for either negative interest rates or the introduction of an asset purchasing program. In Asia, market participants questioned whether the upcoming hike in Japan's consumption tax would weaken positive momentum and require the Bank of Japan to boost its quantitative easing.

Given the uncertainty surrounding the outlook for central bank activity, it is understandable that overall client sentimental risk appetite was subdued. With this backdrop, we are all reminded of the importance of a strong and diversified business. With respect to the client franchise at Goldman Sachs, we continue to see strong relative positioning and performance across all of our businesses.

Within investment banking, we maintained our market leading position in completed M&A. We advised on 31 value transactions, valued at $1 billion or more, the highest number in the industry. We helped underwrite $55 billion in global equity offerings during the quarter, making us the market leader. We also helped to bring a $194 billion of high yield and investment grade debt offerings to market, which is a quarterly record for debt underwriting volume.

Within investment management, total assets under supervision reached a record $1.08 trillion, up 12% over the past year. Despite market headwinds, our performance within FICC demonstrates the benefits of offering our clients a diversified product suite, meeting their needs across rates, credit, currencies, mortgages and commodities. Whether it's from a business, products or regional perspective, the value of diversity was reinforced in the first quarter of 2014.

Now, I'll discuss each of our businesses. In investment banking, we produced first quarter net revenues of $1.8 billion, up 4% from the fourth quarter. This was our highest quarterly performance since 2007. While investment banking backlog declined from yearend levels, it is up significantly compared to this time last year.

First quarter advisory revenues were $682 million, up 17% sequentially. We advise on a number of significant transactions that closed during the first quarter, including Vodafone's $130 billion disposal of its U.S. group, whose principal asset is its 45% interest in Verizon Wireless. Cole Real Estate Investments' $10.9 billion sale through American Realty Capital Properties and Bristol-Myers Squibb sale of its global diabetes business to AstraZeneca for up to $4.3 billion, plus future royalties.

We also advised on a number of important transactions that were announced during the first quarter. These include Safeway's $9.2 billion sale to an investor group, led by Cerberus Capital Management, Hutchison Whampoa's $5.7 billion sale of a 25% stake in A.S. Watson to Temasek and Foster Wheeler's $2.9 billion sale to Amec.

Moving to underwriting. Net revenues were $1.1 billion in the first quarter, down 3% compared to record fourth quarter results. Equity underwriting revenues of $437 million was 30% lower, as industry-wide activity declined in the first quarter, particularly for IPOs. Year-to-date, Goldman Sachs ranked first in global equity and equity-related common stock offerings in IPOs. Debt underwriting revenues increased 29% sequentially to $660 million due to higher issuance activity in both investment grade and leverage finance markets.

During the first quarter we were committed to meeting our clients' diverse financing needs. Whether it was McKesson's $5.5 billion bridge loan and $4.1 billion investment grade notes offering or Hong Kong Electric Investments' $3.1 billion IPO or X2 Resources' $2.5 billion private placement.

Turning to institutional client services, which comprises both our FICC and equity businesses, net revenues were $4.4 billion in the first quarter, up 31% compared to the weaker fourth quarter. FICC client execution net revenues were $2.9 billion in the first quarter. Excluding DVA, net revenues were up 50% sequentially.

Rates and mortgages were both up significantly relative to the weak forth quarter, although client activity and volatility remain relatively muted. Credit improved slightly and was supported by stable credit markets. Commodities revenues improved significantly relative to a weak fourth quarter, as market volatility and client activity increases. Currency was modestly lower sequentially.

Equities includes equities client execution, commissions and fees and security services. Net revenues for the first quarter were $1.6 billion. Excluding DVA, results were down 7% sequentially. Equities client execution net revenues, up $416 million, were down significantly due to less favorable market condition in certain areas, including emerging markets in Asia, particularly Japan.

Commissions and fees were $828 million, up 11% relative to the fourth quarter on solid cash volumes. Security services generated net revenues of $352 million, up 4% sequentially. Turning to risk, average daily VaR in the first quarter was $82 million, roughly consistent with fourth quarter levels.

Moving on to our investing and lending activities. Collectively, these businesses produced net revenues of $1.5 billion in the first quarter. Equity securities generated net revenues of $702 million, primarily reflecting company-specific events, including divestitures and pending IPOs.

Net revenues from debt securities and loans were $597 million and benefited from net gains on certain investments and net interest income. Other revenues of $230 million include revenues from the firm's consolidated investments.

In investment management we reported first quarter net revenues of $1.6 billion. Management and other fees were roughly flat sequentially at $1.2 billion. Incentive fees were largely driven by performance fee related to the sale of an investment.

During the first quarter, assets under supervision increased $41 billion to a record $1.08 trillion. This growth was driven by record long-term net inflows of $40 billion, largely in fixed income assets. During the quarter, long-term net flows were strong across each of our client distribution channels, institutional, high net worth and third party. During the quarter, we also had market appreciation of $14 billion, largely in fixed income and equity assets.

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 benefit, was accrued at a compensation to net revenues ratio of 43%, which is consistent with the accrual in the first quarter of 2013.

First quarter non-compensation expenses were $2.3 billion, 24% lower than the fourth quarter and down modestly from the first quarter of 2013. The fourth quarter included higher litigation and regulatory expenses, higher charitable contributions and higher impairment charges on consolidated investment entities.

Total staff at the end of the first quarter was approximately 32,600, down 1% from yearend 2013. Our effective tax rate was 32.7% for the first quarter.

In terms of capital, there are a number of items to cover. First, during the quarter we repurchased 10.3 million shares of common stock for a total cost of $1.7 billion. These repurchases reflected the completion of our 2013 capital plan. As previously announced, the Federal Reserve did not object to our revised 2014 proposed capital actions.

With respect to our regulatory capital ratio, the Federal Reserve has approved the firm to come off the parallel run. And therefore, starting in the second quarter, our capital ratios are determined under the transitional provisions of Basel III. As a result, the transitional ratios are not only the most relevant, but also a better assessment of our risk-based capitalization.

Our Basel III common equity Tier I ratio on a transitional basis was 11.3%, using the advanced approach. Under the standardized approach, our transitional ratio was 10.9%. Risk-weighted assets under the advanced approach are approximately $600 billion, $355 billion in credit risk, $155 billion in market risk and $90 billion in operational risk.

Let me make a few brief points on the supplementary leverage ratio. Given that the proposed rule hasn't been finalized and won't take effect until 2018, to date, we have not taken any significant actions. When we have a final rule, there are multiple options that we can pursue.

On the capital side of the equation, our regulatory capital levels benefit from a natural tailwind over time as we comply with the Volcker Rule. As you know, we have investments and funds, where we invest alongside our clients. Under the Volcker Rule, we are required to significantly reduce our level of fund investments, which currently creates an approximately $9 billion capital reduction.

With respect to the asset side of the equation, there are also steps we can take if needed. For example, as of yearend, we had over $260 billion of asset associated with secured client financing activities. These are generally lower-risk collateralized assets. We can ultimately decide if needed to reduce the lower returning portion within these balances.

Regarding the new proposal, our best estimate today is 4.2%, including the capital impact of reducing our fund investments to comply with the Volcker Rule, we estimate it would be 4.7%.

To sum it up, we feel confident about our ability to comply in advance of 2018, given the variety of actions that we can take. And we look forward to working with regulators to pursue the goal of enhanced safety and soundness, while continuing to serve our clients and support economic growth.

Before I take questions, let me leave you with some closing thoughts. Our performance in the first quarter is reflective of the ongoing challenges facing the broader marketplace, as the global economy continues its slow recovery. This is being counterbalanced by the continued strength and diversity of our global client franchise.

A sluggish, yet steady improvement in the global economy should drive greater confidence and the durability of the recovery. In response, we would anticipate that market sentiment would improve, which should ultimately drive from our client activity and greater risk appetite.

And the management team, we're focused on two primary goals. First, to focus the bulk of our resources on serving our clients and in the process grow our single-most valuable asset, our global franchise.

Our second goal is to take a disciplined approach to adjusting and reengineering our businesses, so that we are well-position to protect returns in the current environment, and more importantly maximize returns, when a more favorable environment emerges. Simply stated, the goal is to consistently provide superior results for you, our shareholders, across the cycle.

Thank you again for dialing in. And now, I'm happy to answer your questions.

Question-and-Answer Session

Operator

(Operator Instructions) And your first question is from the line of Glenn Schorr with ISI Group.

Glenn Schorr - ISI Group

So taking a look at I&L and maybe we should only focus on the equity side because I think most of the debt in lending will stick. At last look there was about $20 billion in there, $16 billion of it private equity. And given that you reiterated the $9 billion of disallowed -- this is a question, sorry. I'm assuming that you had some realizations in the quarter, but market list still has you at the same level of equity. I'm going somewhere with this, because I'm curious to see how you go about winding that down and getting in Volcker compliance over the next couple years and what the backup plan is, if you don't sell it off? In other words, can you spin some off? Sorry for the long question.

Harvey Schwartz

I understand. That's obviously an important question, Glenn, thanks. So I think the right way to think about the Volcker compliance is, if you look at the K, we roughly had at the end of 2013, $14 billion of investments in funds. Now, we're obviously coinvested with our clients in all those funds, and those funds are not just private equity, they are private equity, real estate, debt funds, et cetera. And the important thing is really to focus on the $14 billion now.

Obviously, there is a process where we can apply for extensions for two years, which basically takes us out three years in terms of compliance. But just to size it for you, I think it worth breaking down the $14 billion. And so if you start with $14 billion, you can immediately take off $2 billion, what I'll refer to as permitted investments, that brings you down to $12 billion.

And then, you can take off another billion that relates to investments in fund that we're already in a process of redeeming, hedge funds and credit funds, where we have the flexibility to manage our own time path there. And so that takes you down another billion bringing you to $11 billion.

Now within the $11 billion, obviously, for several quarters we've being in a harvesting mode and within the $11 billion, $2.5 billion is already public, but there maybe restrictions on sale down, et cetera. So when you add up all that math, the $14 billion at the end of last year, brings you down sub-9. And so the sub-9 is the number, we really have to manage. And again, we're investing alongside our clients in these funds.

Glenn Schorr - ISI Group

Moving on just a clean-up question related to CCAR. Your plan wasn't objected too, you got tons of capital and you keep producing more, so all those are good things. I'm curious to see, why you think you were so far off from the Fed in both PP&R and R&R and RWA. And I'm not agreeing with the Fed's projections, it's just, you had the biggest distance to the Fed and I'm curious on how you decompose that knowing that you don't have all the answers just yet.

Harvey Schwartz

So that's an important question. So we obviously submitted a plan that we thought was significantly stressful and you can see that in our year-over-year numbers. We don't -- as you know, the Federal Reserve by design has created a process that is not transparent. They've communicated that very clearly. So it's difficult for us at this stage to reconcile our results with the Federal Reserve's results.

We'll obviously work with the Federal Reserve and the material they publish and we'll participate in their forums actively and we'll try and get better insights. I think an important takeaway here is, we certainly as a market participant, we're not encouraged necessarily to replicate their test.

And so in the end they're regulator, we're the regulatee. And so if they see that their results are more severe than ours, it guides the process. And I think this window for modifying your capital actions, is a good part of the process, which we obviously participated in.

Glenn Schorr - ISI Group

And last one is you've been able to put up ROEs in 10%, 11% range in an environment that I think you all would describe maybe a 5 out of 10, overall. So with your cost take out and your share count shrinkage, I'm assuming do you feel like you could do better than that over the cycle. I'm not necessarily forcing you for a goal over the cycle, but just curious to get your thoughts on what you can do in a little bit better times?

Harvey Schwartz

So over the last several years, as we talked about, we've been focused on a number of strategic initiatives, things like, obviously, growing our asset management business, and very focused as you know, on cost reduction and that really is strategically about building operating leverage into the business.

As we've done that through this part of the cycle, we've done it with an eye on finding the right balance, and by balance I mean is, we're obviously running these businesses for years and decades. And so as we're getting more efficient in creating operating leverage, we need to make sure that we protect that franchise. And I think this quarter's results really showed that diversity and the strength that our franchise, whether you're look at investment banking, asset management et cetera.

So I think we found that balance, the right balance so far. Now, if we were to get significant tailwinds and a pickup in activity, we're very confident that we would participate in that significantly. So there is a lot of operating leverage in the enterprise. And with respect to our ROE, again, on an absolute basis, it's not what we want to be able to produce for our shareholders. But on a relative basis, it looks pretty good.

Operator

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

Matt O'Connor - Deutsche Bank

Just going back to the Volcker on the equity exposure. So you went through, how do we should think about the $14 billion running-off over time and addressing that, but I guess how quickly and how big you rebuild the direct investment book that I think is still Volcker-compliant?

Harvey Schwartz

So it's not as much about speed of rebuilding. And as you know, we've never approached capital deployment about speed. It will all be driven by opportunity set. So that's the way we think about all of our businesses. As capital will comes out of those funds, it can be redeployed and obviously can be redeployed anywhere or it can be return to the shareholders, if we don't think the opportunity set offers the best. So over time, this would be completely driven by the opportunity set.

Matt O'Connor - Deutsche Bank

So if you had to take a guess, looking out, I don't know three, five years, does the overall equity book get back to about where it is here or I would think a little smaller, but maybe not a lot smaller?

Harvey Schwartz

It'd be impossible for me to say. Again, there will be maybe opportunities that are more driven by the real estate cycle versus others. And I don't know, my crystal ball barely works for a week. It definitely doesn't work that well for three or five years. But I wish I had one that did.

Matt O'Connor - Deutsche Bank

And then just on the comp ratio, looking out the rest of this year. I think last year you changed up a little bit. You kept it steady in the first half and then brought it down a little bit in 3Q, and brought it down again in 4Q. Just any comments on how you're thinking about the timing of phase-in of the comp ratio??

Harvey Schwartz

So as always, in this quarter, it's our best estimate for the year. And we'll evaluate it as we go through the year. And again, really the philosophy in compensation hasn't changed at Goldman Sachs since the day I got here. It's all going to be again the process driven by performance of the firm, and business units and the individuals, and obviously our management of expenses and the returns we want to provide to shareholders. But right now it's our best estimate.

Operator

Your next question is from the line of Christian Bolu with Credit Suisse.

Christian Bolu - Credit Suisse

Harvey, given all the debate around the cash equities market structure and the role of high-frequency trading, just curious to get your updated thoughts on transfer to electronic trading business, particularly the future of the Sigma X platform?.

Harvey Schwartz

So we've been obviously an active market participant in the dialogue. Gary Cohn, as I'm sure you saw, published an op-ed several weeks ago. Our focus on the equity market structure isn't specifically around high-frequency trading necessarily. It's really about the fact that over the last 10-years plus, the market evolution, speed of execution has just gotten ahead of the market infrastructure and the market plumbing.

And so we're very focused on working with all market participants and regulators to ensure that the market infrastructure catches up with the speed. And there is other things in Gary's op-ed that I will refer you to, but that's the primary message. With respect to our own Sigma X platform, I know there has been some things in news. We have no strategic plans for Sigma X at this stage.

Christian Bolu - Credit Suisse

Jut switching over to FICC. Just curious as to what happened to the credit business. Your commentary on a year-over-year decline, kind of contrast with peers while speaking to strength there?

Harvey Schwartz

So obviously from a debt underwriting perspective, I know your question was specifically about credit, but from a debt underwriting perspective very strong quarter for us I think by any measure, breadth of transactions as I highlighted and certainly relative to opportunity in the marketplace. In terms of any one quarter and credit, I have no insight into the competitors. It's been like a reasonably solid quarter for us in credit, so there really are no major takeaways there.

Operator

Your next question comes from the line of Michael Carrier with Bank of America Merrill Lynch.

Michael Carrier - Bank of America Merrill Lynch

First question. I think you gave like some updated numbers around SLR, and I just want to make sure I understand. I know before there was sort of that estimate of greater than 5, but the rules weren't finalized. I guess now you're just in, you got the finalized or mostly finalized rules 4.2, but if you got out of some of those funds you get to 4.7. And I just getting from 4.7 to above the 5, just if you could mention like some of the things, obviously there is earnings power, you mentioned some of the repo part of the business, but I just wanted to understand kind of what's the map in terms of getting there?

Harvey Schwartz

So if I wasn't clear, let me just clarify. So the 5 wasn't that move to 4.2. The 4.2 was a reference to the proposal that just came out, which incorporates the larger denominator. And we've done, as I mentioned in our prepared remarks, we've done nothing to mitigate that.

And as you know, our strategic philosophy on proposed rules is to engage actively in the dialogue with the regulators, but more importantly, we really won't look to mitigate until we feel like we have visibility around the final rule. Because we just don't want to mitigate things, and quite frankly do them in error. So we have done nothing to mitigate it.

The reason I highlight the natural tailwind, as I refer to it, is under the Volcker Rule, the $9 billion have to come out of funds. And that is a dollar-for-dollar capital deduction. So just standing still, we would move to 4.7. But we haven't specifically begun to articulate a strategy internally to get us to 5, but this gap is not material for us at this stage to be extremely focused on it.

Michael Carrier - Bank of America Merrill Lynch

And, then, I guess when you combine the CCAR process and then with some of the other regulations like Volcker, there is obviously some constraint on payouts for everyone. When you think about the other opportunities, so investing in the business, making investments, but on the other hand managing the risk weighted asset side of the equation, are there starting to be more opportunities to invest versus payout? And as the economy improves, does that pick up? Just want to kind of get your sense on the balance there.

Harvey Schwartz

That's a great question. I think the one word that you used that, I think should resonate for the whole marketplace, not just Goldman Sachs, is this notion of constraints. And so every firm will be managing to whatever constraint they perceive. Within that really how do you fundamentally manage your capital? And at this particular stage, we're not feeling constrained. Obviously the 11.3%, Basal III ratio I referenced gives you some sense of potential excess capital.

I think that this, it's an important industry discussion, because obviously for Goldman Sachs, but again the broader industry, the first priority is always about safety and soundness and adequate capital. But I do think that the flip side is there is a risk to excess capital in the system.

And what we're doing is no different than we would have done in the past, if there is periods where we're running with excess capital, we're going to be patient and disciplined and wait for opportunities. And certainly we're in a position today where from a liquidity and capital perspective if there is demand from our clients, we can meet them.

Michael Carrier - Bank of America Merrill Lynch

And then last one. Just on the fixed side of the business, you comment a lot on the quarter-over-quarter. When we look at year-over-year, and you have given that, at least on the OTC side you've gotten your clearing kind of in place and you were starting on the electronic side or the self-side. Just wanted to get your sense, I know it's difficult to piece those changes versus the broad environment given a lot of the volatility and the uncertainty out there. But maybe just from client conversations, how that's progressing and where you see that pan out?

Harvey Schwartz

I think if you look back over the past year, I think clearing certainly manage by the marketplace and the regulators extremely well. I know there were lot of concerns going into it, but I think the multistage launch, really I have to give everybody high marks for that. Swap execution facility is now up and running, still relatively new, so a bit early to tell, but at this stage, really no significant impact in the marketplace. And again, we'll watch it evolve and its impact with market structure, but really nothing to discern at this stage of any materiality.

Operator

Your next question is from the line of Mike Mayo with CLSA.

Mike Mayo - CLSA

Can you talk more about the non-comp expense? I know that's been a focus of your, and it certainly came down a lot, how sticky is that decline?

Harvey Schwartz

So at this stage, Mike, as you know, several years ago, we launched the cost reduction initiatives. And so that was a series of steps, which brought us up to just under $2 billion. At this stage we're still being at the margin, very focused on costs throughout the entire system. And so the sequential decline, as you know was obviously litigation. So that's not the mover, but the focus really is about again keeping cost significantly subdued during this part of the cycle, and again at the same time positioning us for an upturn.

Mike Mayo - CLSA

So are you still looking to have these non-comp expenses decline down year-over-year?

Harvey Schwartz

Yes. As I said, at the margin, we're very focused on expenses in this part of the cycle and in areas where we can get positive results, you should see them.

Mike Mayo - CLSA

A separate question, the 2% buybacks were nice, perhaps you could do even more. And the threshold for the SLR is $700 billion in assets. And I guess you're above $900 billion. But is there any scenario where you would say, let's reduce our assets to below $700 billion, so there is less regulatory burden on the firm?

Harvey Schwartz

No. There's no plans strategically to shift the size of the balance sheet in any way to get underneath some regulatory threshold. However, there is tactical things we can certainly do with the balance sheet, which I mentioned in my prepared remarks, which gives us some flexibility. And I think, for example, for any market participant if balance sheet becomes a constraint, I think there are elements of the balance sheet that either can be repriced as we move through the cycle or can certainly get smaller.

Mike Mayo - CLSA

I've asked this question on several calls, but do you have any published financial targets as of right now?

Harvey Schwartz

Yes, Mike, and I always appreciate your focus on this. There is no targeted ROE. And as I said earlier, at this stage, what we're really doing is strategically finding the balance point with this part of the cycle to make sure that we position the firm for growth, we provide you, the shareholders, with adequate and hopefully superior relative returns. And in the future, we're going to look to take advantage of all the market opportunities as the cycle improves.

Mike Mayo - CLSA

Well, as a key, should I be looking at the proxy? I'm looking at Page 38 of the proxy, and you have the long-term incentive plan and that's based on ROE and growth in book value per share. So should I take that as an indication of what you're most focused on? But then on Page 33, I guess the Compensation Committee reviews results of Goldman versus peers, and it's a laundry list of ROE, EPS, earnings, revenues, comp ratio, non-comp expenses, a couple of other items. So what are you most focused on, if I'm looking at financial metrics?

Harvey Schwartz

So any day of the week, as a firm, we're most focused on serving our clients and growing our activity levels. In terms of aggregate financial metrics, all the things that you'll see in the proxy, whether its book value per share, ROE, those are all components into the compensation methodology, as are those other things that are mentioned in the proxy, whether it's our focus on expenses and aggregate performance, but those are part of our long-term incentive plan. I wouldn't view those as specific metrics as it relates to how we think about our capital.

Mike Mayo - CLSA

Lastly, at what point do you think you have enough clarity to be able to give us financial targets?

Harvey Schwartz

I think, Mike, that we'll continue to communicate our message in a way that we think is appropriate for the context. Right now, obviously, there's still a significant amount of runway in finalization of rules. And as we get more clarity, we will continue to communicate with you how we think about capital. But I'm not sure necessarily having a published target is necessarily the best way to think about how we're managing the franchise, but we'll continue the dialogue, I'm sure.

Operator

Your next question comes from the line of Betsy Graseck with Morgan Stanley.

Betsy Graseck - Morgan Stanley

A couple of ticky-tacky questions. One is on the I&L revenue line. I was just wondering if you can give a little more color around how much was driven from the monetization of the investments. And you're basically looking to understand how that contributed to the higher incentive fees in the investment management?

Harvey Schwartz

So the equity line was driven by a portion of the portfolio, which as I referred to as divestitures and IPOs. And the deadline is really investment-related gains and interest income. And obviously to some extent, you'll see it in the broader market this is a solid harvesting environment. And so you're seeing us do that.

Betsy Graseck - Morgan Stanley

And did it have any implication for the incentive fees in investment management or not?

Harvey Schwartz

As I said, the incentive fees this quarter, obviously largely influenced by a single asset that was sold. Again, I would put them more in the bucket of it's a harvesting environment. And so if we have performance, you're going to continue to see incentive fees.

Betsy Graseck - Morgan Stanley

And then the $8.5 billion that you're going to be managing down over time, I mean your clients went into these funds with an expectation of typically 10-ish years or so. But you're not beholding to that timeframe if obviously there's opportunities to extract value early?

Harvey Schwartz

So a number of these are older vintage funds. Obviously, we had some visibility on the Volcker Rule, when it was first launched. And so we have obligations to our clients. But again, we'll work with the regulators and continue to harvest the funds in the profile that I gave you. The clients obviously value these returns.

Betsy Graseck - Morgan Stanley

And then just on the Basel III, the transitional numbers we got. I'm just wondering if you can you give us a sense of what your fully phased-in number is, since that's what we've been looking at for a while?

Harvey Schwartz

9.7 on the fully phased-in. But I would remind you again that we have to have the capital coming out of the Volcker funds. And so the transitional measure is maybe the best indicator.

Betsy Graseck - Morgan Stanley

And then that 9.7 is standardized or advanced?

Harvey Schwartz

9.7 was advanced, I thought that that you're asking about, and standardized is 9.3.

Betsy Graseck - Morgan Stanley

And then just lastly on the SLR. You walked through how the Volcker is going to be benefited? Can you give us a sense of how the CCAR would benefit as well?

Harvey Schwartz

I think around Goldman Sachs, now we refer to that as CCAR by the way, but I'm not sure that's in the marketplace yet. So we've looked and if we've studied it at the margin, it could in the neighborhood of 10 or 15 basis points. But we're still digging through the details of that. But it's a tailwind too.

Operator

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

Guy Moszkowski - Autonomous Research

So it just a follow-up on the last question. So you gave us fully-phased. The 4.2 on SLR, that's a transitional, is that correct?

Harvey Schwartz

No. That would be a fully phased-in, if you will.

Guy Moszkowski - Autonomous Research

And the increase to 4.7 would just be completely static if you were out of the $9 billion or sold funds today without any other change?

Harvey Schwartz

Yes. We stand still. We do nothing.

Guy Moszkowski - Autonomous Research

And then you'd to add that 10 to 15 bps for the CCAR potentially just on top of that?

Harvey Schwartz

Look again, early days on the CCAR -- and by the way, I'm glad you've adopted the CCAR acronym already. The early days, I think studying the CCAR, so that's why I didn't mention it earlier. But obviously I'm happy to give you a range on it. But the $9 billion that comes out, that comes out. CCAR is obviously a tailwind too.

Guy Moszkowski - Autonomous Research

I just wanted to make sure that we sort of put them all in one place and then it was clear that they're all in the same basis?

Harvey Schwartz

That's correct. And that would give you 4.8 or 4.85, if you will.

Guy Moszkowski - Autonomous Research

Moving back to FICC, I know you don't usually disaggregate, but it would be helpful maybe this time around, because we've seen such diversity of results among some of the different players. If you could give us some color on a year-over-year basis on the divergence that you saw between macro businesses like rates and FX versus credit and commodities, and the more numbers you can help us with, the better?

Harvey Schwartz

I think the takeaway from the FICC business this quarter is really given them the market backdrop we had, where sentiment was really fluctuating. We had concerns about Asia growth and then political events. I think it really reinforces that if you're going to be in these businesses, you really need the diversification.

And so as we mentioned, the quarter was helped by commodities, because we have a strong commodities business and you saw in certain segments, really unusually strong volatility. So we had opportunities to work with our clients. We just don't look at it on a quarter-to-quarter basis. We look at in a multi-quarter basis. And in this particular quarter, you saw us outperform.

Guy Moszkowski - Autonomous Research

And just a follow-up question on the commodities. Was that mostly within the energy complex, where you saw the greatest strength?

Harvey Schwartz

So that's where the primary volatility was.

Operator

Your next question comes from the line of Chris Kotowski with Oppenheimer.

Chris Kotowski - Oppenheimer

You flagged in the release, the investment banking pipeline, the backlog was down, which is a first time I remember as anyone doing that in a long time. And I'm curious, is that just because of the underwriting calendar or do you sense that M&A is also kind of out of peak and backing off?

Harvey Schwartz

No, it was down. That shouldn't be a surprise. You may remember, Chris, that backlog had hit a post-crises high in the third quarter, then it hit another post-crises high in the fourth quarter. And obviously, the fourth quarter tends to be more of the build quarter and then coming-off of relatively strong quarter, and it wasn't down significantly towards yearend.

I think more importantly, I've made two observations. One that's specific about the backlog, which I mentioned is up significantly versus the first quarter of last year. But I think the takeaway on M&A is an important one. We've now seen a couple of quarters with higher M&A notional volumes.

And so these things can all change quite quickly, but right now it does feel like it's an environment where we're far enough away from the epicenter of the crisis, where CEO competence is at a point where strategic transactions are occurring and there is an important takeaway about the nature of the transaction, which is some of them are very large.

And when you have a large transaction environment, I referred to the 31 transactions we did in excess of $1 billion a quarter. Large transactions can have, they won't always, but they can have a catalytic effect, either on the industry or they create subsequent transactions themselves. So again, it could all change on a dime. But right now this trajectory for merger activity feels pretty good. And obviously, over time that feeds a lot of other activity.

Chris Kotowski - Oppenheimer

I guess, that's what I was getting at. Everybody is looking for an M&A cycle. And in your view, it's alive and well and that's not the reason for the decline in the backlog?

Harvey Schwartz

No. The level of engagement and conversation is quite good. And then again, look, again I referred to my crystal ball earlier not being great, but right now it feels pretty good.

Chris Kotowski - Oppenheimer

And then switching gears, the easiest line of your income statement to predict a last couple of years has been the investment management business, because the AUM was always $850 billion and there was always a $1 billion base management fees, I think going all the way back to 2008. And all of a sudden, we're seeing a significant amount of inflows and AUM are up nicely two quarters in a row, what's happening there? And what should we expect? And what's different?

Harvey Schwartz

We've articulated this in the past. Obviously, this has been a strategic growth area for us. And it really has been about, it's a bit old fashion, but it's been focused on performance, delivering for our clients and having differentiated performance. And when you look at our historical multiyear numbers, it looked like strong. And so you're really starting to see the inflows.

Chris Kotowski - Oppenheimer

Nothing beyond that?

Harvey Schwartz

Because there has been some small bolt-on acquisitions, which were disclosed, but this is really the core drivers' performance, particularly in fixed income this quarter.

Operator

Your next question comes from the line of Steven Chubak with Nomura.

Steven Chubak - Nomura

So Harvey, you made a very interesting point regarding the SLR tailwind from the sale of Volcker assets. Looking at the metrics and where they stand today, assuming that SLR will remain binding, the elimination of the disallowed assets will provide a meaningful boost to the numerator, which will help both your risk and SLR ratios.

However, the capital relief from any additional shrinkage in I&L, I presume it will impact the denominator exclusively, which if SLR is binding actually incentivizes as you're engaging more risk intensive activities. So should we expect that you'll boost your permissible I&L investments as you optimize the ROE opportunity that you currently see based on the capital constrains as they stand today?

Harvey Schwartz

I think we should be really clear on this. In no way shape or form are we going to let the regulatory guidelines or ratios or constraints encourage us to change our risk taking philosophy or how we deploy our capital. I can't underscore that more strongly. We often make mistakes and we're far from perfect, but as a firm, our risk culture focused on mark-to-market and our philosophy has served us well.

And we're certainly, as I said, not going to be influenced by metrics that would maybe encourage risk taking. Quite frankly, we would always rather deploy this capital into our franchise businesses and we'll do that as opportunities present themselves.

Steven Chubak - Nomura

And just one more from me. The Fed in ANPR published earlier this year, suggested that it would consider imposing some tougher restrictions on merchant banking activities, whether via more punitive capital requirements, restrictions on holding periods, what have you. I recognize this is really in the very early stages, but can you help us think about how your business or the merchant banking operation could adapt if tougher restrictions are imposed? And what level of I&L assets would be classified as merchant banking x those, which are disallowed under Volcker? Really just trying to identify what could potentially be exposed?

Harvey Schwartz

It's very early in that process. And so I have no discrete insights for you. We'll obviously participate and have participated in the Federal Reserve's AMPR and it will be an evolving process. Again, I think the fundamental takeaway for you to consider and the way we approach these things, is if needed, if you had outcome that restricted our abilities, we would weigh that outcome and our ability to drive value for that capital. And if we felt, we couldn't drive value for that capital, then we would look to return it to the shareholders. I think it's that simple.

You've seen it too before in things like our insurance business in Europe and our reinsurance business in United States, and that's the length that will evaluate all of our capital opportunities. But, obviously, we'll discuss this as we get more clarity.

Operator

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

Brennan Hawken - UBS

Coming back to the commodities, solid results for this quarter, certainly encouraging. Maybe can you talk about your commitment to the physical side of the business and whether or not you think that a regulatory surcharge on that business could make it still economically viable for you all?

Harvey Schwartz

It all depends, obviously, on the outcome. We don't have any visibility into the outcome. But again, it will depend on whether or not regulatory constraint is too high bar. I think more importantly today, as you know, we have a long history in the commodity business, providing our clients corporate treasurers and asset managers around the globe with hedging solutions and access to the marketplace and liquidity, not unlike we do in the corporate bond market.

And separately, we feel we provide value in providing debt and equity capital to the investing side of the business. But it will evolve over time and we'll adjust accordingly. But it's a bit of a wait and see.

Brennan Hawken - UBS

Have you seen any impact in that market as some high profile editors have announced plans to exit or sell or what have you?

Harvey Schwartz

This is an important business to us, because it's important to our clients. I don't want to read through too much of this, because it's only one quarter and I think it's hard to extrapolate anything from a quarter. But certainly in commodities this quarter, in certain sectors, the feedback we're getting from clients is that, there may be, and again I have very limited visibility into our competitors businesses, but there just maybe some benefit to those market participants that stay strong in commodities like us, by those that are deemphasizing or exiting, particularly when the market is volatile.

Brennan Hawken - UBS

Can you speak to trends of MD and partner headcount over the last few years maybe across the firm and by division?

Harvey Schwartz

Obviously, as I mentioned earlier, we've been very focused on cost. We continue to drive efficiencies throughout the organization, in terms of non-comp expenses and obviously also in people. But I don't really have any specific color for you, in terms of by division, et cetera. Obviously, we're managing those resources in the context of the business activity that the businesses are seeing.

Brennan Hawken - UBS

I was just trying to get a sense, the shift to a more pyramid structure that you guys have referenced in the past.

Harvey Schwartz

This is a partner year for us. So it's been two years since we made partners. And so obviously, we'll be grinding the entire organization through that process this year.

Brennan Hawken - UBS

And then the last one, just sort of in reference to this $9 billion that you've chatted, where we discussed a bunch here and the dollar-for-dollar capital hit in I&L. Does your experience this year in sort of [indiscernible], which I certainly recognize as positive, trying to shrink the equity base? But does that make you a bit nervous about potential friction in returning that capital and the possibility of trapped capital for a while here as I&L shrinks?

Harvey Schwartz

It doesn't. This year, again, there was a difference in outcome between our results and the Federal Reserves results. We obviously thought we submitted a severe test and the outcome was more severe. Again, I think this process of giving firm the opportunity to adjust, I think it's a good one and it provides us in the marketplace all the flexibility. So again, I have to believe, again, in my opinion only, so discount it as you will. I have to believe, we'll be able to return excess capital over time for the exact reason that excess capital on a sustained basis for any industry, I don't think is a healthy thing. But again, that's just my opinion.

Operator

Your next question comes from the line of Matt Burnell with Wells Fargo Securities.

Matt Burnell - Wells Fargo Securities

Just two quick ones. You obviously spent some time today talking about the ratio at the holding company. Just curious if you could update us on the SLR ratio at the bank level, if that's materially changed from or materially different from what you were talking about maybe a quarter ago?

Harvey Schwartz

So, again, I think what we should just do for the purpose of this conversation is, ignore the last quarter and I'll just focus on the supplementary proposal that's out there, because I think the proposal is probably more relevant for your work. And that number in the bank would be 56.

Matt Burnell - Wells Fargo Securities

And are there any other mitigating actions you can take within the bank relative to what you talked about in the holding company?

Harvey Schwartz

I haven't focused on it. But obviously, there are lots of things that go into the supplementary leverage ratio. So it's not a primary concern.

Matt Burnell - Wells Fargo Securities

And then you mentioned, and I'm sorry, if I missed it, but you mentioned in the equities trading side of things, the particular strength in cash in the first quarter. I guess I'm just curious if you could give us some color in terms of the trends in the equities derivatives and PB businesses?

Harvey Schwartz

You can't really read anything, I don't think into one individual quarter. But I think that this quarter in particular was probably in some respects tougher for our client-base than the headline indices would read just in terms of their ability to drive performance. But again, the equity business, to be a leading player, you really have to be strong in all facets of it, which means the prime brokerage business, you have to have a strong research footprint, you have to be able to drive IPOs and secondaries, and obviously you got to be able to commit capital, that's very important, and obviously you have to have a huge commitment of technology. And so, right now we feel quite good about things.

Matt Burnell - Wells Fargo Securities

But in terms of the client activity levels or risk appetite, it sounded like that was a little bit lower than maybe the headlines would have suggested across your non-cash equities businesses?

Harvey Schwartz

So if you look at our commissions and fees line, you can see it's up year-over-year and sequentially. But I would say, again, for certain segments of the client, client-based asset management, in particular for example and some of the headwinds, I think it was a tougher quarter for them. But I haven't studied all the full results. That's what I would expect to see.

Operator

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

Harvey Schwartz

So since there are on more questions, on behalf of the team, I'd like to take a moment to thank all of you for joining the call. Hopefully, I and other members of senior management will see you in the coming months. If there are any additional questions, please don't hesitate to reach out to Dane or the team. And otherwise, please enjoy the rest of your day. Look forward to talking to you soon. Take care.