Operator

Good morning. My name is Dennis and I will be your conference facilitator today. I would like to welcome everyone to the Goldman Sachs Third Quarter 2017 Earnings conference call. This call is being recorded today, October 17, 2017. 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 third 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 a 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 2016.

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, global core liquid assets, and supplementary leverage ratio, and you should also read the information on the calculation of non-GAAP financial measures that's posted on the Investor Relations portion of our website at www.gs.com.

Our Chief Financial Officer, Marty Chavez, will now review the firm's results. Marty?

Marty Chavez

Thanks, Dane, and thanks to everyone for dialing in. I'll walk you through the third quarter and the year-to-date results; then, I'll be happy to answer any questions.

In the third quarter, we produced net revenues of $8.3 billion, net earnings of $2.1 billion, earnings per diluted share of $5.02 and an annualized return on common equity of 10.9%.

Taking a step back to review our year-to-date results. We had firm-wide net revenues of $24.2 billion, net earnings of $6.2 billion, earnings per diluted share of $14.11 and a return on common equity of 10.3%. Year-to-date, our firm-wide revenues are up 8% or $1.8 billion versus the same period last year, reflecting a broad contribution across most of our businesses. Revenue strength in investment banking and investment management helped to offset weaker FICC performance. Our investing and lending activities posted strong performance, driven by the quality of our portfolio, increasing asset prices and the ongoing expansion of our lending and financing footprint.

We are committed to expanding our global client franchise and correspondingly our revenue production, despite the challenging operating environment. As Harvey discussed at a recent conference, we had detailed plans across each of our businesses to drive stronger client relationships and shareholder value creation in the current operating environment. With more than $5 billion of revenue opportunities identified, we are executing across those multiple plans.

As it relates specifically to this quarter's performance, revenues increased 6% sequentially and 2% year-over-year. A year-over-year increase is particularly noteworthy, given the strength of our performance in the third quarter of 2016.

Importantly, our emphasis on cost efficiency and commitments to operating leverage for our shareholders continued into the third quarter. These efforts have positioned the firm to accrue a compensation-to-net revenue ratio of 40% for the year-to-date, down 100 basis points versus this point last year. As a result of revenue growth and expense discipline, our pre-tax earnings are up 16% to $8 billion and our ROE is 160 basis points higher at 10.3% for the first nine months of the year.

With that as a broad overview, let's now discuss individual business performance in greater detail.

Investment banking produced third quarter net revenues of $1.8 billion, up 4% compared to the second quarter including strong results in advisory. Our investment banking backlog decreased since the end of the second quarter as replenishment of M&A transactions was lower.

Breaking down the components of investment banking in the third quarter, advisory revenues were $911 million, up 22% compared to the second quarter as deal closings accelerated. Year-to-date, Goldman Sachs ranks first in worldwide announced and completed M&A.

We advised on a number of important transactions that were announced during the third quarter including Worldpay's merger with Vantiv for a combined enterprise value of $28.8 billion, CVC's 5.8 billion euro sale of its majority stake in Ista to Cheung Kong Property Holdings and Home Shopping Network's $2.6 billion sale to Liberty Interactive. We also advised on a number of significant transactions that closed during the third quarter including, DuPont's combination with Dow Chemical and a $130 billion merger of equals; Baker Hughes' $32 billion merger with GE Oil & Gas, and Hewlett Packard Enterprise's $8.8 billion spinoff and merger of non-core software assets with Micro Focus International.

Moving to underwriting, net revenues were $886 million in the third quarter, down 10% on a sequential basis. Equity underwriting revenues were $212 million, down 18% quarter-over-quarter as IPO volumes declined.

Debt underwriting revenues of $674 million included strong acquisition finance activity. Results were down 7% relative to a very robust second quarter. Year-to-date Goldman Sachs ranked 1st in worldwide common-stock offerings, and also had a leading position in leveraged finance.

During the third quarter, we actively supported our clients' financing needs participating in Amazon's $16 billion debt offering to support its purchase of Whole Foods; Japan Post's $10.8 billion follow-on offering; and Discovery Communications' $6.3 billion bond offering to support its purchase of Scripps Networks.

Turning to institutional client services, which comprises both our FICC and equities businesses, net revenues were $3.1 billion in the third quarter, up 2% compared to the second quarter, reflecting a recovery in FICC performance. FICC client execution net revenues were $1.5 billion in the third quarter, up 25% sequentially. While volatility and client conviction remained low, improvements across all of our businesses aided performance.

Following a more challenging second quarter, rates improved significantly amid better U.S. economic data and expectations for central bank actions. Commodities posted a modest improvement sequentially. Despite the increase, third quarter results still represented a bottom decile performance. Credit improved given better performance in our financing solutions business. Mortgages and currencies were up modestly quarter-over-quarter.

Now moving to equities, net revenues for the third quarter were $1.7 billion, down 12% sequentially. Equities client execution net revenues of $584 million were down 15% compared to the second quarter. There was a limited opportunity set in derivatives, and low volatility weighed on results. Commissions and fees were $681 million, down 11% versus the second quarter, as U.S. volumes decreased industry-wide. Security services generated net revenues of $403 million, down 9% sequentially, reflecting typical second quarter seasonality. Balances were slightly higher quarter-over-quarter and funding spreads remained relatively tight, given the close to 90% of our stock borrowed for clients were in very liquid collateral.

Turning to risk, average daily VaR in the third quarter was $47 million, down from $51 million in the second quarter, driven by lower commodity price risk.

Moving on to our investing and lending activities, collectively these businesses produced net revenues of $1.9 billion in the third quarter. Equity securities generated net revenues of $1.4 billion, reflecting sales, corporate performance, and gains in public equity investments. Of the $1.4 billion, roughly 60% was driven by public mark-to-market and events such as sales. Given the favorable market backdrop, we've been actively harvesting our portfolio. Net revenues from debt securities and loans were $492 million and included approximately $450 million of net interest income. With respect to the I&L balance sheet, we ended the third quarter with $116 billion in total assets. Given our continued efforts to expand our lending footprint, loans receivable were the biggest growth driver, up $8 billion quarter-over-quarter to $61 billion.

In investment management, we reported third quarter net revenue of $1.5 billion, flat with the second quarter. Assets under supervision increased $50 billion sequentially to a record $1.46 trillion. The increase primarily reflected $13 billion of long-term net inflows, $14 billion of liquidity product net inflows and $23 billion of net market appreciation.

Now, let me turn to expenses. As mentioned earlier, compensation and benefits expense for the year to date which include salary, bonuses, amortization of prior year equity awards and other items such as benefits was accrued at a compensation to net revenues ratio of 40%. This is 100 basis points lower than the accrual in the first nine months of 2016. Third quarter non-compensation expenses were $2.2 billion, up 2% from the second quarter.

Now, I'd like to take you through a few key statistics for the third quarter. Total staff was approximately 35,800, up 5% from the second quarter and reflected seasonal hiring. Our effective tax rate for the year to date was 22.6%. If you exclude the tax benefits related to the settlement of equity awards, our effective tax rate for the year to date would have been roughly 29%.

Our global core liquid assets ended the third quarter at $220 billion and our balance sheet and level 3 assets were $930 billion and $21 billion, respectively. Our common equity tier 1 ratio was 12% under the Basel III advanced approach on a transitional basis and 11.7% on a fully phased-in basis. It was 13.3% using the standardized approach on a transitional basis and 13% on a fully phased-in basis. Our supplementary leverage ratio finished at 6.1%. Increased lending and derivative exposures drove declines in the advanced and standardized ratios whereas the SLR was lower sequentially given increases in the balance sheet. And finally, we repurchased 9.6 million shares of common stock for $2.2 billion in the quarter.

On the subject of CCAR, we extensively engaged with our shareholders to solicit views on potential disclosure. Not surprisingly, we got different perspectives on the topic. It is clear at this point that we are the only CCAR bank that hasn't disclosed. Accordingly, we are disclosing our 2017 CCAR buyback authorization of $8.7 billion.

Of course, the Fed's non-objection to our capital plan is similar to authorizations we received from our Board and our shareholders; it is limit, not a requirement. We will determine our share repurchases in connection with the opportunities and risks that are present in the market. This includes but is not limited to the $5 billion of revenue opportunities we recently presented on.

To close, let me spend a moment on the $5 billion of growth initiatives. They incorporate opportunities from across our global franchise including investment banking, FICC, equities, investment management and lending. The breadth of these opportunities demonstrates the growth potential of each of our businesses. Client feedback continues to be quite positive; and importantly, there is tremendous energy internally around these initiatives. We believe successful completion of these opportunities would drive an incremental $2.5 billion in annual pretax earnings at a 30% marginal ROE. We look forward to updating you on these initiatives as they evolve. And you should have confidence that the full capacity and capability of this firm is concentrated on delivering on these and other initiatives.

Before we move on to Q&A, I want to thank Dane Holmes. As you probably know, Dane will become the firm's new Global Head of Human Capital Management in January. He has been a trusted advisor to me and we are all excited about his new role and his continued ability to drive positive outcomes for the firm and our people.

We also want to welcome back Heather Miner as the new Head of Investor Relations. Many of you will know Heather from her eight years in IR previously. We both look forward to maintaining an active dialogue with our shareholders and the analyst community.

With that, I want to thank you again for dialing in, and I am happy to answer all of your questions.

Question-and-Answer Session

Operator

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

Glenn Schorr

Good morning. So, the balance sheet keeps growing in I&L and it keeps producing, so God bless. A question on the debt side. How much do you think of that balance sheet is relationship lending versus straight investment versus more of an asset management like revenue? And of that $450 million in NII, do you still feel like 400 is about the quarterly run rate, given current balance sheet?

Marty Chavez

Well, Glenn, so let's go through the lending part of the I&L portfolio. There is, as we said, $61.5 billion of loans receivables held for investment, and that figure increased $7.5 billion on the quarter. And so, looking into the components of that increase, I would say $1 billion of that is related to increased lending in our private wealth management business, and then $5 billion of it as a broad category, we will call it corporate and relationship, and that includes project financing, financing for asset managers, relationship lending, mortgage warehousing. When we think about the net interest income and are investing in lending line; that has grown significantly over time, and we see it as a stable and growing revenue source.

Glenn Schorr

And your comments on capital ratios and SLR, do they constrain your ability to continue to do this? You mentioned your buyback is pretty darn big. Should we be thinking those as trade-offs, or can you do both?

Marty Chavez

So, based on regulatory constraints, as you know from the CCAR results, we do not have significant access today, and CCAR has been our binding constraint. Well, as you know, the test evolves. And so, we don't know how the test will evolve. But, based on our own assessment of risk, we have significant access, and that gives us the capacity to support the clients. And so, we will continue with the approach that we've always had, which is for these capital decisions to remain dynamic with the top priority being -- having strong capital and liquidity to support the clients and to support our growth. You've gotten used to the return and we have as well, and we have been through a period of retuning capital, implementing the regulations, all good for systemic safety and soundness. But, we have pivoted to growth. And based on the opportunities that we've been outlining to the market, we would certainly prefer deploying our capital resources to support these 30% and ahead of 30% marginal ROEs, we prefer that to buying back our shares.

Glenn Schorr

Appreciate that. One last small one, acquisition of Genesis Capital in the quarter, commercial lender, could you talk about where that fits in?

Marty Chavez

Sure. So, the Genesis is similar in the businesses that we've been doing for a considerable period of time in our investment management business. And so, the loans fit within all of our risk parameters and we saw an opportunity for accretive returns, plugging it into our platform and our control and saw the opportunities as to grow it by plugging it into our platform.

Operator

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

Mike Carrier

Good morning, Marty. Maybe first question, just on investment banking, the results came in strong, you mentioned on the M&A side some deals closing and then, you also just mentioned the pipeline down, just any context around that? Because I think on the equity side, it seems like the IPO pipeline is strong, so just maybe any color on the M&A front? And then, given that tax reform is a bit more in that line, just any change or change in the number of conversations in different industries, if we get that as a potential catalyst heading into 2018 or 2019?

Marty Chavez

So, as I mentioned, Mike, the backlog is down sequentially and down year-to-date, and that's just natural side effect of the strong closings that we had in the third quarter; some of those deals had actually been in the backlog for a couple of quarters. And so, I won't distinguish the formal backlog from the pipeline. The pipeline, as you noted in equity underwriting is strong also in our conversations with clients on the advisory side. There's no sense of slowdown. We're seeing a pickup in client dialogue, particularly I would note in technology, media, telecom, as well as industrials and natural resources. And so, it's strong for all of the reasons that you would expect that CEOs are confident, equity market support valuations and acquisition currencies, the financing markets are open, the overall levels of financing costs are relatively low by historical standards. That's all constructive on tax reform which you also mentioned, that is certainly a part of our engagement with clients. And I will also note however that clients, it seems to us, have moved towards saying, well, tax reform would be a good thing but it's not stopping us from considering strategic acquisitions and sales right now.

Mike Carrier

Okay, that's helpful. And then just as a follow-up, MiFID II is on the horizon heading into 2018. I know, there's still a lot of shifting strategies in the industry, in conversations, but any kind of indication on how you think that impacts on the industry and you guys, either from a research standpoint, trading standpoint or market share?

Marty Chavez

Sure, I'll go through all of them. First, I would start by saying that it's our view that the MiFID II impact will mean that it's critically important to have not only differentiated content but also scale and a global reach, all of which we have in our businesses. And so, just going through the various aspects of it, as you know it's a significant effort and there is a big bank's go-live date in early January. On the execution side and staying close to our clients, understanding the liquidity provision, execution capabilities that they need and designing them, we have the software, we have the people, and so we are working on all of that and that is progressing.

On the research side, again, it's important to have that differentiated content and the breadth of research, and the conversations about the price discovery for the research product are progressing. And in our asset management business, we and several other asset managers have recently disclosed our intent to pay for research. There's ongoing discussions we understand between the SEC and the European regulators that may lead to some form of release. So, we are following those closely. But to put it all together, again, the emphasis is -- MiFID II is going to make it even more important than it's ever been, and it's always been important to have scale and depth and breadth, and I wouldn't trade our franchise with anyone else.

Operator

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

Matt O'Connor

Good morning. You mentioned a little bit of detail within the loan growth this quarter on an earlier question. But, I guess just bigger picture, what kind of goalpost will you be providing to us on the $5 billion of revenue targets, as we think out the next couple of years here?

Marty Chavez

So, on the $5 billion of revenue targets, it's important to emphasize again that they don't depend on any improvement in the underlying market conditions or any change in regulation. Of that $5 billion opportunity that we are pursuing over the next three years, $2 billion of it -- $2 billion of the revenue opportunity annually relates to lending. And we called out in our discussions in September the various parts of that market, which we've talked about are private wealth management business, GS Select, institutional lending of various kinds. And internally, as you would expect, we've had growth initiatives since forever, and you've seen some of the results of those, whether it's in asset management or in our debt underwriting business or growing our asset management business. And so, we have considerable experience and are putting time and energy into the frameworks, the tracking and the measurements of the milestones, and the resources that we are putting against those milestones. And we will of course give you regular updates as these opportunities materialize over the next three years.

Matt O'Connor

And I appreciate the added disclosure, I wasn't sure everybody did on the CCAR here, and I would just throw out there I think improved disclosure on these initiatives over time, as they take hold, especially the lending and maybe some more breakout effect I think over time would be helpful. You gave the commentary around it but I think having some numbers around as well would be helpful.

Marty Chavez

Well, we definitely are taking that on and going back to what we described in September, there is a breakdown, various aspects of the revenue opportunity as well as balance sheet and capital against it. And so, we will absolutely be having a continuous dialogue with you on that as we progress.

Operator

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

Q - Mike Mayo

Can you talk about the potential for reduced regulatory cost, if there is deregulation? And I'm not really asking about risk appetite or how you might change with that but really just overhead cost to comply with regulations today, and what it could be in the future?

Marty Chavez

So, Mike, we, like all of us in the industry, are noting the various treasury reports for instance, the recommendations. We've seen some progress against the recommendations of the first treasury report, for instance. To give just the couple of examples, the OCC has asked for a perspective on the Volcker rule. There has been some news from Basal committee on net stable funding ratio and there are few other examples as well. And so, we are seeing that. And certainly some of the U.S. regulators have been very specific in their discussions about simplifying some aspects of the rules and some others, the CFTC. And so, there is a sense that there is this movement in the topic. But, I would say that for us, absolutely these things are great, if and when they happen. They are not embedded in any of our plans. If and when they occur, they'd be a tailwind to our plans. And as you know, we take a broad and holistic approach to all of these things, not only by training our people but by building all of these regulatory processes into the way we do business.

So for instance being able to do these simulations of our balance sheet and income statement and cash flows several months, 18 months into the future is an important part of how we make decisions and not really seeing it is something that we break out, specifically as a cost and as a cost that would be reduced but certainly I'm happy to say that our focus as just did beyond the implementing of the regulations, which is something we will always do as they arise to growth.

Mike Mayo

Well, as a follow-up on expenses, $3 billion or $5 billion growth initiatives, what are the upfront expenses, were there any in the third quarter and do you expect any special charges or how much the ramp-up?

Marty Chavez

So, on the $5 billion of revenue opportunities, we describe for you the blended marginal margin of those opportunities. And there is a bit of a drag upfront, really relating to hiring to people. So, as we mentioned in September, our lateral hires are year-to-date up – they doubled from the same period last year and we broke out the kinds of professionals we're hiring. And you see that coverage and distribution is the major focus of that. As we progress on the initiatives, perhaps there will be some modest upward pressure on the comp ratio but we wouldn't see that being material in the context of the firm. And we also don't see any significant charges for this growth.

Operator

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

Betsy Graseck

Could we talk about a couple of things? One is Marcus, I know in the deck last September, you indicated that you're looking to drive that to $12 billion footings over the next couple of years. Could you just give us a little bit more color on the average kind of person that you're looking for, and what kind of yields you're expecting and how you think through the impact of a recession on that business?

Marty Chavez

So, on Marcus, we recently passed $1.7 billion in originations, and we're on track to reach $2 billion, 10 weeks now, by the end of this year. Our focus is absolutely on prime borrowers. The FICO score realized is definitely above 700. These are small ticket items. And as we've said and this continues to be the case, this is organically growing business, we're doing it slowly and deliberately.

I'll note that while we have and have had for a long time strong risk analytics, particularly credit risk analytics underlying the business, we're not leading with underwriting in this business; we're leading with a better product and service and digital experience for consumers, and that remains the focus. I would also add on the realized losses, they have been less than what was put into the plan. And we are well aware, as all of us are of where we are in the credit cycle. Even though Marcus is a new business for us, the people who are building and leading that business for us are industry veterans and consumer finance, and we're plugging them in with our long track record of being thoughtful, prudent risk managers for both Marcus and credit risk. And we've also supplemented our teams with people who have consumer finance experience across the board from branding and marketing to the 360 degree customer view and of course to all of the control function. And we're extending the risk culture we've always had into this business where we worry about everything and plan for all of the contingencies and don't take it for granted, and especially remind ourselves every day we're not leading with underwriting, we're leading with a better product.

Betsy Graseck

That'll make sense, that will be helpful if you had a little more detail on that. I know that -- I think you're planning on giving a little more detail around the granularity of the FICO mix and yields and loss content like we get another card portfolio. So, I will appreciate that when it comes. Just a second question I had was on the dividend. I know you gave the buyback of $8.7 billion for the full year. Are you going to let us know what the dividend outlook is here.

Marty Chavez

Yes, Betsy, I'm happy to mention that as well. So, the Fed's non-objection to our plan had in the capital plan the option to raise the dividend by $0.05 per share in the second quarter of next year.

Operator

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

Brennan Hawken

Thanks for taking the question. Good morning. I was hoping if you could maybe unpack a bit the $5 billion of incremental equity tied to your growth targets. I know, we've got -- I think you laid out $28 billion of loan balances. But, I am guessing there is probably some balance sheet consumption on your trading initiatives too. So, could you maybe just give us an idea about that attribution?

Marty Chavez

Sure. So, on the initiatives, we did highlight for you our $5 billion of required equity. I am happy to walk you through it. And again, as with all aspects of what we set out for you and for the market, it's really -- it bottoms up looking at the activities where the businesses, where these activities are going to occur. So, roughly $2 billion of the $5 billion annual opportunity in three years is related to lending. And most of that balance sheet is in our Marcus, our institutional lending and private wealth management and GS Select businesses, and that totals $28 billion of balance sheet. And to get to the equity, we looked at the businesses that these activities are embedded in and we projected the RWA density out from those businesses. So, it was just that, and bottoms up again.

On the FICC part of the activity, which is a $100 million of the annual opportunities that we identified and that we are pursuing, that one I would see in a bit of a different perspective; FICC capital is dynamic. We see actually considerable scope for the velocity of our FICC portfolio to increase. And so, it's really portfolio-driven and dynamic, and don't see considerable or specific equity component attributable to that.

Brennan Hawken

Okay, thanks for that. And then, following up on Mike's question about MiFID and your response there, I appreciate all of that. It seems as though if we look through your disclosure about the lateral hires that you've made recently, both EMEA and FICC sales functions tend to feature prominently in some of those lateral hires. Do you all think that the -- does that have to do with positioning yourself in front of MiFID, do you feel as though that FICC sales effort will become more important and therefore you are trying to invest in bulk up there? Can you just -- or am I jumping on the wrong conclusion from that chart? If you could just help understand that that would be great. Thanks Marty.

Marty Chavez

I wouldn't see the hires which we've been talking about and which as you noted are weighted towards sales distribution. I wouldn't see them so much as MiFID-related. I am sure that's in there; of course it's in there but it's not the driver. Really there, it's the coverage gaps that we've been talking about. And we saw the opportunity and noted our ability to bring in the talent. So, of the hires, of the offers we've been making, the acceptance rate's over 80%. And we've looked and we've talked about this in September in some detail, specifically in FICC, looking at all of the clients and noting the ones for whom they say we are a top 3 FICC provider and the ratio of the clients where were a top 3 FICC provider is in the neighborhood of the 30% for banks and asset managers and insurance companies, and this is considerably higher for some other segments. And so just closing those gaps is something that of course requires all the resources of the firm. But it's a people business and so especially the people, and so that's the main driver of the hiring.

Operator

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

Guy Moszkowski

So, just -- not to harp, but I wanted to stand a little bit on Betsy's question about expected loss through the cycle because one of the push backs that I had when I spoken to investors about your growth opportunities is that the implied margins on the loan asset balances don't seem to many people like they really incorporate sort of full through the cycle loss potential. And I was wondering if you could elaborate a little bit on that, maybe look at Marcus and maybe one or two of the other lending categories and talk about what your loan loss expectations look like?

Marty Chavez

Yes. So, on loan loss expectations, again on -- I'll start with the Marcus example, its prime borrowers and that's an important part of the strategy. And there, again, we imply our analytics. The Marcus business is a new one for us, loan level analytics are the old ones for us, particularly as they relate to securitizations of various kinds. And so we have that prudent and comprehensive approach to risk management and prudent reserving. So, the ALLL against that portfolio or something to get a careful scrutiny and attention from all of us and that will continue and that's part of our process. And I also shared with you the realized losses are less than what we expected in our plan and that's so far and that's where we are in our business growth in our cycle. Let's go to a different example, which is on our PWM business. These are high net worth individuals and it's very different business. They are the highest quality borrowers and they are also -- the loans are significantly over-collateralized.

Guy Moszkowski

Fair enough, okay. And maybe just changing the subject and maybe I'll pursue some of these questions on credit with you offline. But on FICC, you noted that commodities were still sort of bottom decile. I guess that means in terms of your historical quarter revenue experience with commodities, but it sounded like it was better linked quarter. I was just hoping that you could give us a little bit of color, on the one hand what got better but on the other hand, why you still believe that you're doing sort of bottom decile quarters here.

Marty Chavez

So, to start with, that's one part of your question. So for commodities business, even though it was an improvement from the second quarter, which I'll remember, was our worst commodities quarter in our history as a public company of 73 quarters. Now it's 74 quarters as a public company, as I mentioned, the third quarter commodity performance was bottom decile of those 74 quarters. And it's on track to have the worst full year performance since the IPO. I would like to step back for just a minute and just quickly go through the sequential drivers, the year-on-year drivers but like to give you the nine-month on nine-month view, a bigger time period as well, because there's some informational content in that view that you don't get if you're just looking at -- if you're just comparing quarters.

And so, sequentially, yes, our FICC business improved and that's obviously something that's good to see. But, it is by no means aspirational. We know we can do better and we know we need to do better. So, it is an improvement. In the sequential comparison in FICC ICS, it's really rates that drove the majority of that improvement. I'll get to the other driver in a second. But it's really the rates business. And there, particularly, in the latter part of the third quarter, there was better U.S. economic data, there were central bank actions, volumes increased, rates broke out of the 10-month trading range, curve flattened, lots of things happened. And so, rates is really the main driver. And the other driver is that the challenges and the inventory challenges we've described in commodities, and by the way, this is challenged on all fronts, not just inventory, but the inventory challenges were a little better in the third quarter than in the second quarter. And there's also a connection to our bar number which declined a bit, $4 million sequentially and the drivers in the bar number going down were all continuing to decline across products but also reduced commodity positions.

So, that's the sequential story. The year-on-year story, as you know, four out the five FICC businesses were lower; mortgages was the only business that was up. And the year-on-year story is really two main factors, lower client activity across the FICC businesses, particularly in the macro businesses and then the inventory challenges in commodities. But, as I said at the outset, I think if we step back and look at the first nine months of this year in FICC and compare it to the first nine months of last year, you see something different that you couldn't otherwise piece together, which is, if you look at the delta in FICC, half of that decline -- and so it's 23% decline, nine months on nine months, half of it is attributable to commodities inventory; and of that amount, half of that occurred in the second quarter. And so, I think that just gives you the whole picture.

Guy Moszkowski

Okay. That's really helpful. Thank you. And since I was the guy who gave you such a hard time about the buyback disclosure last quarter, I should certainly thank you for doing it now.

Marty Chavez

We were listening, Guy. Thank you.

Operator

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

Jim Mitchell

Maybe if you could just talk about your deposit gathering efforts, how that's progressing so far?

Marty Chavez

Sure. So, deposit gathering is an important part of our financing strategy. It's continuing to diversify our sources of funding. Our Treasurer, Robin Vince gave quite allusive discussion of this in our Fixed Income Investor Call. We're happy to say more about it. In the deposit gathering, note that of course as you know, we acquired an online savings account platform that had previously been a part of GE, and we're gratified to see the growth in those deposits on really essentially no marketing of it. And so, in those deposits, even though there have been Fed reserve raising fund rates over the last several months, the experience in the online savings account has been that the rates gone from 105 basis points to very recently 130, which is near the top end. And so that tells you something, it's an attracting funding source for us relative to the wholesale market. It also tells you something about realized beta that we've experienced so far.

Jim Mitchell

But then, what were the flows like in the quarter?

Marty Chavez

I'm not going to get into the specifics on the flows. But I think, Heather, that's a good one to get back on.

Jim Mitchell

Okay. And maybe just one question on regulatory change. SLR, I think would be a big positive for you in terms of the leverage constraint but I think there's been some uncertainty about how or if the tier 1 leverage continues or not. How do you -- how do we kind of I guess try to arms around, do you have a thought on if the SLRs changed, would the tier 1 leverage also change, therefore freeing up some capital or balance sheet, or do you think that remains?

Marty Chavez

So, I will get to that but actually I've pulled out the growth in total deposit, this is not just the online savings account; it's about $7 billion quarter on a quarter. But to get back to your question on SLR, so certainly, there has been a lot of discussion about how the SLR ratio might change. And as we said in the second quarter, if the various treasury recommendations on treatment of central bank cash, treasuries, initial margin at CCPs, if those all come into force, and we don't have the details, but that's a roughly 70 basis-point improvement on our SLR of the second quarter; I wouldn't expect it would be much different from the third quarter.

And so, to the extent those changes happen, it would very likely have a thinking differently more expansively about our prime brokerage and matchbook businesses. And then, I think this has been well-highlighted across the industry, if those changes were to come into effect, it would be equivalent of creating another SIFI in terms of SLR capacity for the various businesses that our SLR intensive. So, these are all potentially tailwinds. And as you know, we and many others welcome the initiatives and the detail of the first and second treasury reports that there -- the potential tailwinds, they are not baked into our $5 billion annual revenue plan.

Jim Mitchell

I appreciate that I was just thinking about the constraint in the CCAR from Tier 1 leverage, which would limit any benefits from the SLR. And I'm just trying to get a sense of do you think that would also change to help free up that capacity or not?

Marty Chavez

I would love to know the answer to that question. CCAR is as you know continuously evolving process. I suppose one way of looking at it would be -- the perfect result would for all of the constraints in CCAR, Tier 1, SLR on and on, all of them to be exactly binding by exactly the same amount; that would be a perfect optimization. But of course, it's evolving and we don't know exactly how it's going to play out. As you know, there was a white paper and governor to rule out just before its departure outlined a variety of proposals and we've read them closely, I'm sure you have as well. And we considered the proposal to be thoughtful but many of the important things still remain to be seen and they would have to be in an upcoming notice of proposed rule-making, and that's when we will get the insight on your question.

Operator

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

Steven Chubak

I wanted to start off with two-parter on investment management. So, first just on the quarterly trends. I was hoping you can just shed some light on what drove the decline in management fees linked quarter, just given the strong equity markets that we saw and the pretty health -- continued healthy increasing AUM. And then, just thinking longer term in relation to the $1 billion revenue target to business investment management where we've seen pretty substantial secular headwinds and fee pressures, and I've got a lot of questions from clients as to what's giving you guys the confidence that you can hit that $1 billion incremental revenue target. And I was hoping you can shed some additional light on those opportunities.

Marty Chavez

Sure. So, let me start with the first part of your question. Yes, as you noted, we have grown assets under supervision by $50 billion. About half of that was market appreciation. And then looking into the other half; that was again almost evenly split between gathering long-term assets, mostly fixed income and then, also an increase in assets in our liquidity products. And so, on the effective fee, the effective fee actually has been stable sequentially. And so, really the answer to your question is, it's in the other part of management and other fees; there's some puts and takes that were slight offsets when you do the quarter on quarter comparison.

Going to the second part of your question on the investment management opportunities that we outlined, which was as we said a $1 billion annual revenue opportunity. Look at that in three parts and the three parts are roughly balanced. But the key to all three parts is what has been the key to that business and the successful asset gathering over the long haul that you've seen, which is that it's broad and it's deep across asset classes as well as different products and distribution channels, retail and institutional.

And so, to go back to the breakout of the $1 billion in annual revenue growth, splitting it into the three parts, I'll start with GSAM. So, there, it's growing our alternatives platform, advisory and insurance, EPS and liquidity products. On PWM we're hiring advisors, investing in the platform including digital experiences, adding products and services there. And the third part is Ayco, it's our corporate executives counseling business. And there, we absolutely see opportunities in incoming from our clients on expanding those financial planning services, in two ways. First to more of the people inside the companies that we're already working with; and then in addition to more companies. So really stepping back, it's the franchise which is unique in the case of investment management. It's broad product portfolios, there's room to grow across the board, and it's diversified and hence the opportunity set.

Steven Chubak

Thanks Marty, that was really helpful color. And then, just switching over to just one question on the capital discussion, I think as relates to Jim's earlier question on thinking about various binding constraints, just given your historically strong discipline on managing to what's your most binding capital ratio, I was a little bit surprised to see the deterioration in the SLR linked quarter. I'm just wondering, if you can give us some insight in how you're thinking about the need to focus more on some of the growth opportunities which maybe you had, not emphasized as much given your continued strong capital discipline. And separately, we did see your GSIB surcharge also increase last quarter, or your systemic risk score, and I'm wondering how you're thinking about managing to that as well.

Marty Chavez

Sure. So, I'll start with the SLR, fully-phased. So, as you know, it declined by 20 basis points sequentially, and that is growth in the balance sheet. And you also saw that in the increase in the balance sheet from 907 at the end of the second quarter to 930. And there, it's supporting our clients in deploying the balance sheet when we see the opportunities to do so. It was, as you know, in CCAR 2017, the binding constraints, and that's something that we are deeply aware of. But as we know, much depends on the next evolution of CCAR. And also potentially on recalibration of SLR, there's been different views from different regulators on recalibrating SLR or not recalibrating SLR, we don't know exactly how all of that's going to evolve. Now, can you remind me of the second part of your question?

Steven Chubak

Just around the GSIB score, I think in the past you'd been at 2.5% and it increased to 3% last quarter and how you are thinking about managing that score as you think about some of the growth initiatives?

Marty Chavez

Sure, right. So, also in the third quarter, as the GSIB buffer, we're again in that 3% range and it's something that we look at every day and work with divisional leaders as we see opportunities to have a strong balance sheet and capital and deploy it and invest in our business and long-term growth. We can do both. We can both grow the business and return capital. But at the margins, I would say growth is more valuable. And as for where as you know, the GSIB print at the end of this quarter is an important one, and I can't predict where it's going to end up in this quarter.

Operator

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

Devin Ryan

So, maybe first one here, the securities basis loan arrangement with Fidelity that was announced last quarter was pretty interesting. And I am curious, is that starting to ramp? And it also sounded like there could be more arrangements in the future with additional wealth management firms that don't have those capabilities. So, really just trying to get sense of the broader securities-based loan strategy, the firm with outside firms and then how big that is within kind of the private wealth piece of the balance sheet opportunity?

Marty Chavez

Sure. So, we highlighted for you in the growth initiatives on annual revenue opportunity of $500 million related to PWM and GS Select together. On GS Select, this is something that we're all excited about and focused on, which is to again, and you'll detect this theme in other places, lead with an all digital straight thorough offering. It is extremely early days in that business, and we're very pleased with the Fidelity announcement that you noted. They saw the innovation in the platform and the opportunities just have a great service. As you know its loans of upto $25 million and is significantly over collateralized, and it's interesting opportunity. It's too early to give you progress but it is a part of the initiatives that we outlined, which right now we are aggregating under PWM -- PWM and GS Select together, $500 million revenue opportunity, $11 billion of balance sheet over three years and the implied the yield is evident from that.

Devin Ryan

Okay, that's helpful. And just follow-up here. It sounded like some of the hiring that firm is doing ahead of revenue, could influence the comp ratio a bit but it is sounded like that's going to be modest. Can you maybe just more broadly speak to what you are seeing in the competitive environment in comp dynamics right now? It seems like there are some of the European firms are more aggressively recruiting again in some of the areas that Goldman is also looking to expand. So, maybe that's temporary but I'm just curious kind of how that feeds through as you think about kind of the outlook for the comp ratio?

Marty Chavez

Sure. So, I would say that the most important thing to think about for us and we believe for our shareholders is the operating leverage and comp ratio obviously a part of that. You will notice the first half 2:1 ratio between the revenue growth and the expense growth and you'll also see that ratio in our nine-month results versus nine months of the last year. As revenues grow, I would not expect that ratio to be linear, and we would see even more operating leverage. In the competitive dynamics, as we mentioned and this is continuing, lateral hiring is up significantly, it's doubled from last year. And we are continuously happy to see, but no way take it for granted that we are very successful and attracting the talent.

Operator

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

Gerard Cassidy

Question, lot has been talked about amongst you folks as well as your peers about the lack of volatility in the marketplace, particularly in FICC. With the federal reserve moving into a full unwind next year, have you guys mapped out what the volatility could do because of this changing position by the federal reserve and what it might do for the revenues for your FICC business?

Marty Chavez

Sure. So, we think about volatility a lot and we think at least as much, maybe more about the level of client activity, which is very important for us. And so, looking at the Fed's announcement, so that has been extremely thoughtful and transparent in its communication, and we would expect that to continue. It's just part of how the fed operates. We don't of course know exactly what's going to happen, and we don't make predictions. So, we do create lot's and lot's of contingency plans and so looking at what the Fed has said, as you know they've been very specific, they've given us $10 billion a month and then that's going to increase every three months by $10 billion, and so it gets to $50 billion and letting assets roll off that redemption from their balance sheet and they've given us the mix between treasuries and agencies. They said it's going to -- they expect that mix to be stable with some variations, just depending on the maturities and their balance sheet.

So really, you can't get much more specific and communicative than that. And also just note that there's a positive backdrop, so the U.S. economy is performing, there's improving GDP growth depending on who you talk to, the U.S. is at or perhaps even beyond full employment. And at the same time, all of this unwinding quantitative easing is unprecedented territory, never happened before. So, you could see volatility and spikes showing up in this process, simply because it's never happened before. We don't see duly unwind risk priced into the markets. You could imagine of all spikes that that client confidence make market making difficult, you could also imagine a positive scenario with modest fall, more conviction, more activity, all of these things could be catalysts for the FICC business, rising inflation, any changes in central bank policies against the expected trajectory, clarity on U.S. policies of all kinds, tax, obviously regulation, also infrastructure, all of these things you could see as better catalysts.

The important thing to note and pause on is that the Fed has been clear that the economic backdrop is good and that's generally good for business.

Gerard Cassidy

Great. And then, second question, can you give us some color on -- you talked about the total dollar amount of the capital return on the call today. The dividend payout ratio, is there any guidance where you think that may eventually end up in a more normalized adversary of the next 12 to 24 months where you guys are comfortable to have a dividend payout ratio.

Marty Chavez

So, all we know for now is that a $0.05 increase -- the option to increase by $0.05 is embedded in our capital plan, which is what the Fed has approved. And as for the dividend payout ratio, it's been around 15% for a while, and I'm not going to predict what it will be in the future. Just that $0.05 is all we know for now, we continue to emphasize buyback, as you know, but really as we said, a month ago and so important for us, we would always prefer to execute on these 30% plus marginal ROE opportunities compared to buying back our shares.

Operator

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

Marty Mosby

I'm going ask two questions. One was, when you think of the investing and lending especially on the equity side where you said you all given the market conditions or you said kind of harvesting aggressively. Is part of that related too, because if you look at the increase, there're about $1.8 billion increase in what you had in the equity security gains. There's about a $1.3 billion decline in fixed income so you kind of have offsetting effect with those two things, which is letting your overall revenue still grow this year. So, just to know if you all were doing that just because of market conditions, are you trying to balance the mix and so should we expect this when we have some volatility in other sides of the business?

Marty Chavez

Well, you definitely noticed those offsetting effects and we did too obviously. I would say in that area of our business, we're fiduciaries. And so, we see it as in the interest of our clients to harvest these investments and the asset price levels in the market are supportive. So, it's a good time. That portfolio as you know while we report on the results quarterly, we think of it over much, much longer time horizon than quarterly.

Marty Mosby

Then my second question is, if you look at the seasonal progression of that comp ratio, given that you do have this investment lending gains your revenues are still kind of at the same level you had last year. So, should we still see the drop off in comp ratio kind of at the end of the year as you true up your bonuses and get all that squared away?

Marty Chavez

So, yes, revenues sequentially are up, year-on-year are up and year-to-date importantly are up 8%, which is significant. As for the comp ratio, of course we -- it's an important part of our business and we put a lot of time and energy into considering it and setting it appropriately. And the 40% that we took it to, so 40% for the nine months, year-to-date is as we mentioned the 100 basis points lower than last year and at this point it's the best estimate we have.

Marty Mosby

Yes, usually seasonally we drop down around 30% in the fourth quarter, so just to know if that was still reasonable assumption or is there anything different about this year that would cause that to vary from several prior years where we've seen that trend?

Marty Chavez

Of course that trend is there, I would just say go back to the commitment to operating leverage, something we think about everyday of the many things we think about every day. But really, I can't say more about where we are going to end up this year other than it's the best estimate, taking in all the information that we have right now.

Marty Mosby

Perfect. So, year-over-year, operating leverage would be something to make sure we kind of still assume, so that would make sense. Thanks, appreciate it.

Operator

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

Brian Kleinhanzl

Hi, Marty. Yes, a question on capital return with that disclosure that you gave. So, I mean, the share repurchase authorization is up 30% year-on-year. When we look at kind of your DFAST CCAR results, I mean your capital level was up a little bit -- at the starting point was up a little bit year-on-year, the losses that you saw within DFAST were up modestly as well. So, what allowed you, I guess within this year's CCAR to kind of return more capital? Was there some kind of change in how the Fed looked at RWA inflation or something else? I mean, because I think historically you said -- previous CFO had said that there was kind of check mark to your minimum ratio, is that still the case?

Marty Chavez

Yes. So, the main difference is just the different starting points in the capital ratios.

Brian Kleinhanzl

And there was no other real changes from the Fed side and…

Marty Chavez

Not -- nothing too surprising, right? There were some things that the Fed said they would over a two-year period, and that's what happened. There really wasn't any big -- any surprises of note, it's just the different starting points.

Brian Kleinhanzl

Do you know the capital dollar amounts were only up less than $2 billion year-on-year starting points or really increased by more than that, is it just the ratios are higher simply?

Marty Chavez

Yes, it's just the ratios are higher. That's right.

Operator

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

Marty Chavez

Thank you for calling in, and look forward to meeting with many of you over the balance of the quarter. If you have any additional questions, please contact Heather, and for those of you who were not able connect with, enjoy the upcoming holiday season, and thank you.