Goldman Sachs Presentation to the
Bank of America - Merrill Lynch Financial Services Conference
Comments by Lloyd Blankfein, Chairman & CEO

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A year ago, when I presented at this conference, the mood was one of uncertainty and fear. Our industry was rocked to the core, buffeted by extraordinary volatility, and, in the credit markets, extreme illiquidity. Twelve months later, conditions across financial markets have improved significantly, and to an extent very few predicted or thought possible.

This has been helped by aggressive and effective government efforts – from various liquidity and funding facilities to the Treasury's Capital Purchase Program under TARP. It is impossible to know what would have happened to the financial system without concerted government action around the world. But, unquestionably, these efforts averted even more extreme circumstances and we are grateful for the critical role the government played.

At the same time, we have never run ourselves with any expectation of outside assistance. Throughout 2007, we were committed to reducing our risk exposures even though we sold at prices many in the market thought were irrational. Although we had access to the discount window, we increased our liquidity pool by 2.5 times to $170 billion, or almost 20% of our balance sheet. We raised nearly $11 billion in capital -- $5 billion of preferred from Berkshire Hathaway and $5.75 billion in an offering of common equity. We did this not knowing the TARP Capital Purchase Program was coming.

Our self-help actions were consistent with our historical behavior of maintaining one of the most conservative risk profiles in our industry. And through strong risk management guided by a disciplined fair value accounting process, we remain every bit as focused on protecting our shareholders' equity, our client franchise and our reputation.

Over the past year, clients have come to Goldman Sachs because we integrate strategic advice, risk management, financing, trading and investing skills. Our job – our duty to shareholders – is to protect and grow this client franchise that is the lifeblood of Goldman Sachs. And the best way we know how to do that is to safeguard our culture of performance and risk management, which has allowed us to be nimble and reactive, yet defined by prudent, long-term thinking. This culture has also allowed us to actively commit capital and inject liquidity throughout markets at a time when those lubricants for economic growth were scarce.

Today, I would like to describe the strength and value of our client franchise as well as the roles we play and risk we assume in service to that franchise. I will also cover our capital and liquidity positions, and will conclude with a brief discussion on our culture and people and long-term record of returns that they have generated.

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While the extraordinary events and macroeconomic uncertainty of the past year have validated key attributes of our strategy, culture and processes, they have also prompted significant change within our firm. We embraced new realities around regulation and leverage because of our commitment to the long-term stability of our franchise and the overall markets.

The Federal Reserve is now our primary regulator. As a Financial Holding Company, we are subject to the Fed's capital and leverage tests. Over the last 18 months, our balance sheet has fallen by a quarter, while our capital has increased by over a half. The amount of Level Three, or illiquid assets, is down by almost 50 percent and now represents less than 6 percent of our total assets.

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Our client franchise is the core of our business model and strategy, and its quality and depth is shaped by the skill, talent and collaboration of our people. Our strategy is to integrate advice, financing and co-investing with best-in-class risk management to a broad range of largely institutional clients.

A keen and comprehensive appreciation of risk is at the center of everything we do. Whether we execute a sizable portfolio reallocation trade for a pension fund, or a long dated natural gas hedge for a producer, our ability to measure and mitigate risk is paramount to driving shareholder returns.

Our success in executing this model is dependent on our ability to identify opportunities early and allocate people and capital to them quickly and effectively. We have a strong track record of doing so over many years. Recently, to cite two examples, we raised Senior Loan and Mezzanine Funds to provide private capital to clients when public markets were less accessible. And we expanded our non-agency mortgage trading operations as liquidity left that market.

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When we talk about the diversity of our business model, people often think about it in terms of product mix and geography. Another important construct is the breadth of our client base. In Investment Banking alone, we've advised over 1,000 clients in 67 countries over the past 5 years, solidifying our #1 market share position.

Our clients are corporations, financial institutions, governments, investors, pensions and individuals and they are based all over the world. As you can see from this chart, most of our clients interact with us through at least three of our businesses.

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I previously mentioned the value of combining capital with ideas. In 2006, we saw opportunities to participate in large 'take private' transactions, in which clients valued our ability to merge our advice with the provision of capital. That skill set and capacity is no less important today.

Since obtaining attractive public debt financing for large leveraged buy-outs has become difficult, clients have benefited from our ability to provide private financing through our Senior Loan and Mezzanine funds. A good example of this is a current transaction where we are acting as advisor to The Blackstone Group on its $2.7 billion acquisition of Busch Entertainment from Anheuser-Busch InBev. Our funds participated in the debt financing, which is critical to the transaction. This is what we do for clients – marshal advice and capital to help accomplish their objectives, while contributing to the process of investment and growth.

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And, we are doing more of this in more parts of the world. We remain focused on expanding our client franchise in new high growth markets, and continue to implement a familiar strategy – begin with small principal investments, build underwriting capabilities, expand advisory client coverage, develop sales and trading expertise and grow our wealth management business. We prioritize and evaluate potential opportunities based on the need for our expertise and execution services in each market.

As tumultuous and significant as the financial crisis has been, we continue to believe that this will be the century of the BRICs and other emerging markets. For us, the BRICs are even more compelling post the crisis, and they remain a core part of our long-term growth strategy. Over the past year, we have advised on a number of important emerging market transactions including Satyam's majority sale to Tech Mahindra and China Mobile's strategic cooperation with Far EasTone.

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Built over 140 years, our advisory business serves as our primary point of contact with our clients, and thus acts as the driver of our opportunity set.

Although advisory revenues are near a cyclical low, we have started to feel improvements in CEO confidence and their level of strategic dialogue. As activity levels improve, it's difficult to anticipate what types of transactions will be in favor, or which industries will be active. The key from our perspective is having a broad and deep franchise that allows Goldman Sachs to be relevant, effective and steeped in market knowledge in service to our clients.

The breadth of our franchise is demonstrated by the fact that we retain industry-leading positions in cross-border, acquirer, target and strategic defense advisory league tables. In addition to providing the classic investment banking services, we've had great success in growing our risk management solutions business within Investment Banking. This part of the business encapsulates our strategy of integrating advice, capital and risk management. For example, we worked with RSA Insurance Group to insure liabilities related to its defined benefit pension program. The transaction allowed RSA to take advantage of market conditions to enhance returns while mitigating inflation, interest rate and other risk factors on roughly one-third of its total liabilities.

Our deep client relationships in investment banking provide us with these opportunities, but the revenues often show up in FICC or Equities from a financial reporting perspective. Since 2005, revenues from this activity have grown 22% compounded annually.

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Our banking relationships are also the source of most of our financing mandates. As an intermediary, our job is to match the capital of our investment clients — who aim to grow the savings of millions of people — with the needs of our corporate and government clients — who rely on financing to generate growth, create jobs and deliver products and services.

Since the beginning of 2007, we have underwritten over $675 billion in corporate debt and over $400 billion in equity related products across 1,800 offerings for 750 clients around the world. These clients rely on our advice and execution to provide necessary capital to their enterprises.

We also have a long history of helping states and municipalities access the capital markets. Since Goldman Sachs entered the public finance business in 1951, we have been one of the largest industry participants. Over the past 10 years, we have helped states and municipalities raise over $250 billion of capital. We are currently the #1 underwriter for the Build for America Bond program, which allows states and municipalities to meet their borrowing needs and invest in infrastructure projects. In 2009, we've also raised over $24 billion for non-profit institutions including education services, healthcare and government entities.

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FICC and Equities, our market intermediation businesses, have been a meaningful driver of our strong firmwide performance year to date. Through our role as a market maker, we commit and deploy our capital to ensure that buyers and sellers can complete their transactions -- contributing to the liquidity, efficiency and stability of financial markets. Our Securities Division continues to benefit from a diverse set of businesses. This slide illustrates the performance of individual businesses on a quarterly basis since 2007. The orange bars reflect a Top 3 performance for the individual unit. As you can see, no one business has dominated the mix.

An interesting trend we've seen this year is a 'Macro to Micro' handoff. In the first quarter, Macro businesses like Rates and Commodities were very strong. Beginning in the second quarter, Equities and Credit Products rebounded. By the third quarter, our Micro businesses including Mortgages, Credit trading and Cash Equities had become the most active. This evolution is a reflection of increasing client risk appetite.

It is impossible to predict in which market our clients will be active at any given time. That's why it is a priority to stay close to our clients. And through that proximity, we direct our human and financial capital towards the most important opportunities in the markets.

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Throughout this crisis, we made prices when markets were volatile and illiquid, and extended credit when credit was scarce. More generally, we execute on average over 2.5 million transactions daily for our clients across Fixed Income and Equity products.

Over the past 5 years, the number of trading clients in our credit business has increased 50% to over 2,200. This is a function of our global expansion strategy as well as the continued growth of capital markets around the world. For example, since 2004, the number of Chinese companies with a market cap of more than $1 billion has increased nearly five times to 530.

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In recent months, some commentators have made various statements about the nature and level of risk, including proprietary risk, that financial institutions undertake. There has been concern that institutions may be returning to the practices that contributed to the financial crisis. The fact is that for Goldman Sachs, the vast majority of risk we take and revenues we generate is dominated by trades that advance a client need or objective.

I thought it would be helpful to walk you through a real trade that drove risk taking for the firm. Hopefully, this will help de-mystify the process.

An energy consumer asked us to help protect itself against a rise in the cost of fuel over the next five years, concerned that an unanticipated increase in fuel prices would impact its ability to execute on strategic growth initiatives. Typically on a trade like this, a client would post cash as collateral in the event fuel prices declined during the life of the trade. However, given more difficult funding markets, the client wanted to reduce the risk of poorly timed draws on its cash. To accomplish this, we structured a long-term secured hedge facility that allows the client to post a combination of cash and assets upfront.

In terms of managing our own risk, we bought hedges to offset the fuel price risk we assumed on behalf of our client. To mitigate our credit risk, we revalue the collateral on a regular basis. While we expect the collateral to be sufficient, we have the ability to hedge counterparty risk if necessary. We were able to structure the transaction at a fair price for our client, and generate an attractive risk-adjusted return for the firm. This transaction represents the type of risk that we take throughout the day, every day. It's this type of risk, which we assume and manage as a financial institution, that allows our clients to focus on their underlying businesses.

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Co-investing continues to be an important aspect of our strategy, with two-thirds of our corporate transactions sourced from our Investment Banking franchise. While quarterly returns in this business will fluctuate based on equity market performance, our merchant bank has an excellent history of providing strong returns for our fund investors and shareholders over the long term.

Our funds span the capital structure, including senior debt, mezzanine and private equity. Additionally, there is significant diversity within the funds themselves, with no one industry representing more than 25%. We remain well positioned to be opportunistic in the current investing environment. In 2009, we amended our GS Capital Partners VI fund's strategy to allow for investment in distressed assets. And there is approximately $8 billion available for further investment within that fund.

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Our asset management business offers a range of products across Money Markets, Fixed Income, Equity and Alternatives. And our distribution channels to third party retail, institutional and high net worth clients are robust.

Our client base is diverse, with 2,000 institutional clients and 3rd party distributors, and 25,000 Private Wealth Management accounts. We manage more than $150 billion in assets for over 1,600 pension plans and non-profit organizations.

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Asset Management is an important growth opportunity for Goldman Sachs, and we will continue to allocate significant time and resources to this effort. At the time of our IPO in 1999, our goal was to double assets under management over five years. We were successful. By 2008, we doubled assets under management again.

Going forward, we are focused on continuing to build our distribution and portfolio management capabilities. In fact, we are doubling our third party sales force in 2009, and significantly increasing our Institutional and Private Wealth sales coverage. We are expanding coverage in many areas, including government sponsored organizations, corporate pensions, and insurance companies, as well as emerging markets such as Brazil, the Middle East and China. Our objective is to continue to aggressively grow the business, while generating strong investment returns for our clients.

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Given our roots as a privately held partnership, we've always focused on maintaining a conservative financial profile. We view liquidity as the single most important consideration for a financial institution, which is why we've lived by a funding motto "more for longer."

We steadily increased our Global Core Excess pool of liquidity for several years, and it now represents about 20% of our balance sheet. Importantly, it is in cash equivalents, not unencumbered assets. We've consistently maintained a significant amount of term in our funding book. The average life of our long-term debt is more than 7 years, while our short-term secured funding exceeds 100 days. Keeping this pool of liquidity is expensive. It also inflates our balance sheet and our gross leverage metric. But, it's worth it – it is the best insurance policy we can buy for our shareholders.

In the past year, our Basel I Tier 1 Capital Ratio has increased to 14.5%, through earnings generation and a number of capital offerings. In addition, the quality of our capital is very high, with 80% in common equity. Our gross leverage ratio is half of what it was going into the crisis – and that metric doesn't adjust for the cash on our balance sheet.

These ratios are some of the highest in the industry and act as a significant drag on our returns, but we view our actions as essential given the uncertain market environment.

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Of course, human capital in our business is just as important as financial capital. We don't have material 'property, plant & equipment' or 'cost of goods sold'. Attracting and retaining the most talented professionals in the world is core to the success of our business. This focus has translated into a high degree of stability and experience in the upper ranks of our firm. Our Management Committee members have been at Goldman Sachs an average of 19 years. Our Executive Officers average over 23 years.

Throughout this crisis, we have remained focused on our recruiting efforts with every member of our management committee participating on campus and over 120,000 hours committed to recruiting by employees. We invest significant resources in developing our people. Through GS University, we provide 350,000 hours of orientation to our new hires. We leverage our senior leaders as faculty to foster the culture and provide more effective training. Last year, for example, over 5,000 courses were taught by our senior leaders.

Lastly, the people of Goldman Sachs have a strong sense of responsibility to their communities. Our people sit on 1,500 non-profit boards and 500 of our employees have been engaged in our 10,000 Women initiative with another 250 on the waitlist to be mentors. This year, 23,000 of our employees worldwide volunteered for over 800 local non-profits through our Community Team Works program.

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I often hear reference to our higher compensation per employee metric – but what people fail to mention is that our net income generated per head is a multiple of the peer average. The people of Goldman Sachs are one of the most productive workforces in the world. In fact, when you look at the profitability of Goldman Sachs, we have higher pre-tax margins than any industry average in the Fortune 500 over the past 10 years, and we are in the top 10% of all companies.

It is important to keep in mind that these are the profits that go to our shareholders after we pay our people. Our shareholders are pensioners, mutual funds and individual investors and they are all tax payers.

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We believe in pay for performance and when you compare us directly to our peer group, we have the strongest track record of correlating compensation growth to revenue growth. Our EPS growth, ROE and Book Value per share growth significantly outperforms our peers, and our Net Income per employee is almost 150% higher than our peers.

We certainly are not blind to the attention focused on our industry, and in particular, Goldman Sachs. We have been outspoken on the need for significant regulatory reform -- from how institutions account for their assets, to improvements in risk management processes, to better tying compensation to long-term performance.

In this last respect, our compensation to net revenue ratios have traditionally been one of the lowest in our industry. The bulk of compensation for our senior people is in the form of equity which vests over at least three years and has sales restrictions for even longer. And, our senior executives are required to retain 75 percent of the stock they have been awarded until they retire. We have made our detailed compensation principles public and we expect our shareholders to hold us accountable for how we implement them.

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As I've said before, the significance of the government's actions last fall cannot be overstated, and we are grateful. We believe those efforts were critical to protecting the financial system and ensuring the continued viability of the American economy.

Government intervention in the financial system, however, should not obscure the fact that we have been conservative in the management of our capital and liquidity. Before the crisis, we had a strong balance sheet with prudent maturities. And during the crisis, we took the initiative to reduce further our exposure to problem assets and to raise new capital.

During our history, our firm has been guided by three tenets: the needs and objectives of our clients; attracting talented and long-term oriented people; and our reputation and client franchise. We remain every bit as focused on these ambitions. We have a clear strategy to integrate advice and capital with risk management. We have built a diverse set of businesses. We have an expanding global footprint. And, we have established a proven culture of risk management.

We, no doubt, will encounter our fair share of challenges and mis-steps – and we already have. But the legacy of client service and performance for our shareholders, which every person at Goldman Sachs is charged with protecting and advancing, must be continually nurtured and passed on to future generations. And, I have never been more confident of that outcome.