

Goldman Sachs Presentation to

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Introduction

Good morning everyone – great to be here.

Given the significant amount of new regulations being placed upon the industry, there have naturally been questions about capital requirements and the prospect for returns. It has also led some to focus on return targets. And while I understand the appeal of a simple, firmwide target, having one isn't – nor has it ever been – the driver of our returns. Our operating principles and philosophy have been essential to generating superior returns. Underpinning our principles and philosophy is a belief that we should manage our resources dynamically, and therefore circumstances and return profiles should naturally fluctuate across the cycle. Most importantly, it is not a target per se that drives our firmwide returns, but rather our capital allocation process.

As we have discussed in the past, we believe capital – and the regulatory requirements surrounding it – represent a secular change for the industry. It goes without saying, prudent capital allocation remains critical to a financial institution's success. Today, however, managing capital is more complicated due to the multiple capital constraints. You need to manage capital with consideration for both risk-sensitive calculations like the Advanced approach in Basel III, as well as non-risk-sensitive calculations like the supplementary leverage ratio (SLR).

Given the increased complexity, we thought it would be helpful to dig into our philosophy and process around capital management, and how that process works.

Ok, let's get started.

Slide 3: Our Approach to Capital

Having a rock solid financial foundation is the starting point for everything we think about when it comes to capital. Strong risk-based capitalization not only allows a financial institution to be front footed in capturing opportunities, but also provides protection in more difficult operating environments.

Although the circumstances are definitely more complex in the new regulatory world, our approach to capital management – at its core – is unchanged. We continue to believe that our goal isn't to size our business to our capital base, but rather, to size our capital base to the opportunities available. As a result, we grow our capital base

as client activity increases. Conversely, we wouldn't hesitate to shrink if our clients became less active or expressed a reduced need for capital.

A second element of our capital management is the need to be disciplined about returning "excess" capital to shareholders. If risk adjusted returns don't meet appropriate risk return hurdles then we will either: A) return capital to shareholders; or B) hold that capital in reserve for better opportunities down the road. In our view, this approach results in better through-the-cycle returns, largely because it drives you to focus on both better risk management decisions and at the same time, operational efficiency. For risk management, stretching to deploy excess capital can often lead to bad outcomes. And for operating efficiency, the approach naturally forces a sharper focus on the infrastructure costs embedded in your various businesses.

Third, we continue to view buybacks as the preferred method for capital return. While we have increased our dividend over time, share repurchases still represent the lion's share of our capital return. Since 2009, we have returned approximately \$30 billion to shareholders, with share repurchases representing roughly 85%.

We prefer buybacks for several reasons. Unlike dividends, shareholders don't view them as permanent so we can adjust them depending on the environment. And obviously, share repurchases also help reduce share count, and are tax efficient for our shareholders.

Slide 4: Client Needs that Require Capital

We offer a diverse set of services to our clients. We want to be able to provide them with a comprehensive solution. We also want to build lasting relationships that remain valuable to them as their focus and their needs evolve. As a result, our mix of revenues reflects their priorities.

This simple, illustrative graphic ranks our businesses by capital intensity depending on whether it is a risk-based metric like Basel III or a non-risk-based metric like the supplementary leverage ratio. As you can see, capital requirements can change significantly depending on which metric you apply.

For example, equity investing – highlighted in light blue – faces higher capital requirements under a risk-based approach versus a non-risk-based approach. Conversely, Securities Services – highlighted in dark blue – faces higher capital requirements under a non-risk-based approach like SLR. And businesses like Investment Banking and Investment Management are of lower capital intensity under both of these approaches.

Slide 5: Assessing the Capital We Allocate to Clients

We enter all of our risk decisions with a desire to meet our clients' needs, but simultaneously make sure that the potential risk outcomes are constrained within acceptable levels and that the returns are appropriate. Let me outline for you, the approval process for our capital commitment.

As you know, our clients look for capital commitments principally within our Institutional Client Services and Investing & Lending businesses. However, capital requirements vary within each of these businesses. A good way to think about these activities is to define one set of transactions as higher velocity or flow in nature and another set as longer-term "one-off" commitments that use our balance sheet.

For example, high velocity activities include providing liquidity in products like cash equities or U.S. Treasuries. Longer dated activities like hedging transactions for a corporate or investing in a privately held enterprise are more "one-off" in nature. Not surprisingly, there are different processes depending on whether the risk is more "flow-like" or "one-off" in nature.

If we focus on the first category – the more flow-like – these transactions are governed by market and credit limits that are allocated to our businesses. These include more than 170 VaR-related limits, as well as thousands of credit and stress test limits. Other metrics are also monitored, including but not limited to our rigorous tracking of our aged inventory, portfolio concentrations and correlations. Every day the balance sheet is marked to market, simulations are run using updated risk factors and the resulting exposures are compared against our limits. Our risk limits are purposefully set at levels which are low enough that they are regularly approached, which promote healthy, ongoing communication about actual and prospective risk exposures. All limits are set by our risk groups in conjunction with the Firmwide Risk Committee and these limits are regularly reviewed and adjusted as we deem appropriate.

Other individual transactions, including those which involve capital commitments, are reviewed on a more intensive basis, including through various committees formed specifically for that purpose. For example, our Firmwide Investment Policy Committee evaluates longer-term investments, while our Capital Committee provides oversight for lending-related commitments.

Whether a transaction is flow-oriented or one-off in nature, importantly, we fully cost it out. Doing this not only ensures that we understand the true risk return implications of each transaction, but also provides a complete view of how the business is performing. Fully costing out our transactions and businesses requires allocating the cost of liquidity, hedging, financing and CVA/FVA if applicable. These cost allocations also give us better insight into analyzing marginal balance sheet deployment.

Slide 6: Return on Attributed Equity (ROAE)

So what ultimately drives allocation decisions? It's all about balancing risk and return. Any capital allocation decision starts with our own internal assessment of risk, before we look to regulatory capital implications.

As I just mentioned, we then account for all costs, from funding to technology, and ensure that businesses are absorbing the appropriate costs.

After calculating the net earnings, we then have to determine the equity capital associated with any given activity.

This is where it actually gets really interesting. Given regulators have defined capital in multiple ways—we needed to create an equity calculation that incorporates all of the relevant capital requirements. It is a concept we refer to as Attributed Equity. Attributed Equity represents a weighted capital charge and serves as the foundation for a multi-factor model that generates Returns on Attributed Equity or as we refer to it inside the firm – ROAE.

Our attributed equity framework is intended to provide the firm with a realistic view of returns. It is extremely important in a world where one transaction might be constrained by risk-based capital and another might be leverage constrained.

ROAE is an important construct – among many factors we consider– to analyze performance and determine how we should dynamically manage our businesses.

Slide 7: Return Curves

Now let's talk through these concepts in a bit more detail. This slide is a graphical illustration of our approach. You can see a more detailed representation of the return on attributed equity formula at the top of the slide. It incorporates all of the various expenses, as well as the regulatory ratio weightings. Using ROAE as the basis for measurement, we can now construct a "capital curve". This curve establishes a minimum guideline for our return on allocated equity over time.

Maybe one of the easiest ways to describe how we use the ROAE framework is to consider it within the context of an individual transaction.

Let's consider two types. One that is shorter duration and higher velocity would require a lower threshold. For example, a mortgage portfolio, purchased from a client that we plan to have on our balance sheet for several months.

A second type of transaction could occupy the balance sheet for multiple years. This type of transaction would require significantly higher returns with a minimum ROAE expectation in the mid-teens to a level well above that. For example, a private equity

investment that we would expect to maintain for a longer period of time would be at the high end of that range.

Our goal is obviously to meet the minimum return hurdle. This condition alone is certainly not sufficient, as transactions also need to be reviewed on the basis of their individual characteristics. However, there may be transactions that will fall below these minimums. Falling below the line will drive further analysis and discussion. It may be the case that there are justifications for committing capital below the guideline, but significant review is required.

Ultimately, we believe looking at capital allocation in a static fashion or against a single metric just isn't effective. In the current regulatory world you need to think about it across a capital curve that incorporates multiple constraints. As a result, the weights we use to allocate capital and the curve itself are dynamic and will adjust accordingly over time.

Slide 8: Capital Calculator

We also knew that it was critical to give our people the tools they need to make informed decisions. We have invested significantly in creating the infrastructure and technology to manage capital across all of the various considerations.

As I talked about nearly two years ago, we developed a capital allocation tool that we continue to expand and refine. The software captures earnings related information for our businesses and calculates the various capital requirements that we are subject to. It provides the ability to have a top down perspective for senior management and a bottom up assessment for our business heads – right down to the CUSIP level. The tool helps inform our transactional, business and firmwide capital allocation processes.

Since we initially discussed our capital allocation tool, we have deployed it to all of our businesses within Institutional Client Services, as well as our Investing & Lending activities.

Slide 9: Behavioral Changes

We have made a number of strategic capital decisions over the past few years that helped reduce risk and improve our positioning across various metrics.

In response to Basel III capital rules, we sold down our remaining ICBC stake and sold majority stakes in our two insurance businesses in 2013.

Additionally, as CCAR and the SLR made balance sheets more expensive, we undertook a \$56 billion asset reduction in the second quarter of 2014.

Collectively, these decisions, along with other capital initiatives have led to significant improvements across many of our ratios. In the past year, our Tier 1 leverage ratio, which is incorporated into CCAR, is up over 100 bps and the SLR is up 70 bps in the past two quarters alone. Our Basel III Advanced ratio is up approximately 260 bps since the beginning of 2012.

While our most binding constraint could change over time, we believe that the CCAR process is our most binding constraint for the near term.

Slide 10: Client Needs Drive Activity

To wrap up, we have a broad and diverse set of businesses, reflecting the global nature and varied needs of our clients. Our clients' needs have always been dynamic. But today, we also operate under a multi-faceted capital regime.

This certainly presents challenges, but it also creates opportunities. If we are able to effectively and efficiently allocate capital in ways that our clients most highly value – particularly in an era where capital within the industry is more constrained – we are confident that we will be able to continue to generate industry leading returns.

Thank you for your attention and I am happy to take any of your questions.