Goldman Sachs earns $4.79B in Q4, cuts bonus pool

STEVENSON JACOBS - AP Business Writer - Associated Press

Goldman Sachs Group Inc. said Thursday it earned $4.79 billion in the fourth quarter — a windfall that came in part from slashing its compensation ratio in response to political pressure over lavish Wall Street bonuses.

The company rewarded employees with $16.2 billion in salaries and bonuses for 2009. That's up 47 percent from the previous year but much lower than many had expected. In all, compensation accounted for 36 percent of Goldman's $45.17 billion in 2009 revenue, the lowest annual ratio since the company went public in 1999. In 2008, Goldman set aside 48 percent of its revenue to pay employees.

The company is also shifting more pay into deferred stock, allowing it to hold off recording compensation costs for years.

The pay restructuring helped the bank easily top analysts' earnings estimates. Goldman earned $8.20 a share in the last three months of the year, well above the $5.20 a share expected by analysts surveyed by Thomson Reuters.

Trading of fixed income, commodities and currencies buoyed Goldman's profits for the third straight quarter. The bank also reported higher fees from underwriting stock and debt offerings.

But by constraining compensation, Goldman "certainly boosted its bottom line," Brad Hintz, analyst at Sanford C. Bernstein & Co., adding that investment banking and trading revenue was mostly in line with estimates.

Goldman, which has long outperformed other financial companies, has been the strongest bank throughout the financial crisis. It had less exposure to toxic mortgage-backed securities than other companies and also has been more aggressive in its trading.

But even as Goldman impressed investors, it faced a new potential threat to its business as President Obama on Thursday called for tougher legislation that would limit the size of large financial institutions and their ability to engage in high-risk trades.

Restrictions would be placed on what's known as proprietary trading by commercial banks to separate those institutions from investment banks, Obama said, in a move that would resemble some of the sweeping reforms imposed after the Great Depression. Proprietary trading involves transactions a bank makes with its own money to try to boost profits.

Fears over how the rules would affect banks sent financial shares and the overall market sharply lower Thursday. Goldman's stock fell $9.55, or 5.69 percent, to $158.25 in midafternoon trading.

For the full year, Goldman earned $13.4 billion, almost as much as the $15 billion earned by the five other big national banks combined. 2009 was a difficult year for the banking industry, as companies with big lending operations lost money in those businesses.

JPMorgan Chase & Co. earned $11.73 billion for the year on the strength of its investment banking business, and Wells Fargo & Co. turned a $7.99 billion profit. But Citigroup Inc. and Bank of America Corp. lost a combined $3.81 billion. And Morgan Stanley, whose problems have been attributed in part to a lack of aggressiveness in its trading business, lost $907 million.

Despite its big profit, Goldman's compensation costs came in well below the record $20.2 billion the bank paid to employees in 2007. Goldman said it reduced its compensation pool by $500 million in the fourth quarter and put the money in the bank's two-year-old charity, Goldman Sachs Gives, a move apparently aimed at blunting criticism of Goldman's outsized pay packages.

"I believe it really should diffuse some of the tension" over bonuses, said Michael Wong, equity analyst with Morningstar Inc.

Bonuses in the banking industry have come under attack by lawmakers and the public after the companies lost billions of dollars in bad debts on mortgages, contributed heavily to the credit crisis and recession and then had to be bailed out by the government.

Goldman Sachs received $10 billion in bailout funds, and was one of the first to repay the money last year.

David Viniar, Goldman's chief financial officer, said the bank's employees performed "quite well" in 2009 and that the risk of losing top talent to other firms factored into the pay calculations. Still, he said the bank tried to strike a balance on pay.

"What we attempted to do was be fair to our people ... but show restraint," Viniar said during a conference call with reporters.

Goldman employees will still do well. The $16.2 billion in 2009 pay works out to about $500,000 for each of the bank's 31,700 employees. The money, however, won't be distributed equally, and top performers stand to earn millions.

Besides lower compensation costs, aggressive trading drove Goldman's earnings. The bank had $6.41 billion in revenue from its trading and principal investments unit, down from $10.3 billion in the third quarter of 2009. That's in line with earnings reports from Morgan Stanley and JPMorgan Chase, which also saw a slowdown in trading in the fourth quarter.

Investment banking revenue, considered the foundation of the company's business, rose to $1.64 billion, up 58 percent from the fourth quarter of 2008 during the height of the financial crisis and 82 percent higher than the third quarter.

But Goldman's impressive showing was largely overshadowed by Obama's call for new bank rules.

Asked how the overhaul would affect Goldman's business, Viniar declined to give specifics but said that it would be impractical to reinstate the Depression-era law banning commercial banks from engaging in risky trading.

Viniar said that proprietary trading was a "very small part" of Goldman's overall business, accounting for roughly 10 percent of yearly revenue. Limiting such activity wouldn't prevent future financial crises, he said.

"If people are focused on the causes of the crisis, it wasn't trading," Viniar told analysts. "That's the wrong place to look."

Still, some financial observers have speculated that Goldman may seek to reclaim its previous status as an investment bank to evade tougher regulations. Goldman became a commercial bank holding company at the peak of the crisis in 2008, making it eligible for government aid but also bringing tighter regulatory scrutiny from the Federal Reserve and other agencies.

Viniar, however, said the bank has no plans to give up its bank holding company status.

"We're now regulated by the Fed, and I expect we will be on an ongoing basis," he said.

Going forward, another big question for Goldman will be whether compensation remains constrained or eventually returns to pre-crisis levels. The company's CEO, Lloyd Blankfein and his management team are refusing cash bonuses for 2009 and instead are only taking stock that can't be cashed in for several years. Other employees are also taking more money in deferred stock.

Under that structure, Goldman's full compensation costs wouldn't be recorded in the fourth quarter. Instead the expense would be recorded when the stock vests, meaning compensation costs could jump higher again in future quarters.

However, a permanent reduction in Goldman's employee compensation costs, historically among the highest in the industry, would greatly benefit the company's profitability and be "very good for stockholders," said Hintz at Sanford C. Bernstein & Co.

Viniar declined to give details on the bank's future compensation plans.

Employees' 2009 pay was "what we thought was appropriate," he said. "In the future, we'll have to see what the environment is."

AP Business Writers Stephen Bernard in New York and Ieva M. Augstums in Charlotte, N.C. contributed to this report.