
GOLDMAN'S FORTUNE HUNTERS

The securities firm that Wall Street envies ranks just 12th in private banking. CEO Lloyd Blankfein wants to change that. Among the tactics: luring young multimillionaires to Bermuda for beachside classes in hedge fund basics.

By ANTHONY EFFINGER

The conference started with a cookout at the Mandarin Oriental hotel on Elbow Beach in Bermuda and ended with a talk by 23-year-old Lauren Bush, an antihunger activist, former model and niece to President George W. Bush. In between, executives at Goldman Sachs Group Inc. taught scions of wealthy families how to invest in hedge funds.

Last October's "Next Generation" gathering was a small prod in Goldman Sachs's push into the lucrative profession of private banking. It's an area of finance that New York-based Goldman—the world's largest securities firm by revenue and profit—doesn't dominate. Instead, Swiss and U.S. banks reign. Ranked in assets held by clients with at least \$1 million to invest, Goldman comes in at No. 12, with \$177 billion as of 2006, according to Scorpio Partnership Ltd., a London-based wealth management consultant.

Goldman Sachs is shooting for individuals with \$10 million in financial assets or more—not counting the beach house, Lamborghini or art collection. The set of ultrarich isn't tiny: Individuals with a minimum of \$30 million totaled 94,970 worldwide in 2006, up from 85,400 in 2005, according to a report last year by Merrill Lynch & Co. and Cap Gemini SA. Their assets rose

17 percent to \$13.1 trillion in the same period. With U.S. housing in retreat, global stock and bond markets shuddering and competitors taking subprime-related writedowns, catering to the rich can offer a measure of stability and steady profit.

"Rich people as a business model are sensational," says Russ Prince, president of Prince & Associates Inc., a Redding, Connecticut-based consultant on financial services for the wealthy. "They're willing to pay to make it easy on themselves. They don't fight over fees if they see value."

Goldman Sachs Chief Executive Officer Lloyd Blankfein says he's pursuing fortunes in Asia, Latin America and Russia. "In the Arabian Gulf countries alone, there are over 200 billionaires," he said at a New York conference in November.

Blankfein put the best face on his company's status as an also-ran in wealth management. "I'm





'GOLDMAN IS A FORMIDABLE COMPETITOR,' SAYS A FAMILY OFFICE EXECUTIVE. 'THEY SMELL WHEN A DEAL IS GOING TO CLOSE.'

happy to say we're not No. 1," he said. "We're not maxed out. There's a long, long way for us to go, and we're going to go there."

Spearheading the push is Peter Scaturro, a former competitive swimmer who turned 48 in March and looks like actor Ray Liotta from the movie *Goodfellas*. He hobnobs with Citigroup Inc. Chairman Emeritus Sanford "Sandy" Weill and serves with Maurice "Hank" Greenberg, former CEO of American International Group Inc., on the board of the New York-based Foreign Policy Association. Blankfein, 53, hired Scaturro in July after private banking stints at New York-based U.S. Trust Corp. (once owned by Charles Schwab Corp. and now part of Bank of America Corp.) and Citigroup, where Weill was his boss.

FEEs EARNED FOR managing the money of the rich, cutting them in on private equity deals and planning their estates might ease Goldman Sachs's heavy reliance on its own trading. Goldman calls itself an investment bank, but in its 2007 fiscal year, ended on Nov. 30, just 16 percent of its \$46 billion in revenue came from advising on mergers and helping companies raise capital. Another 16 percent came from money management and brokerage, a segment that includes parts of private banking. A full two-thirds, or \$31 billion, came from trading, making Goldman look more like a giant hedge fund than any kind of bank. That reliance on trading can be a liability when markets stumble and recession looms.

Complicating Goldman Sachs's pitch to the rich is last year's stumble by some of its hedge funds. Global Alpha—once its largest, with \$10 billion of assets—was hammered by unwise bets in volatile markets and fell about 40 percent last year, according to a report to investors obtained by Bloomberg News. Goldman spokeswoman Andrea Raphael confirms that some private banking clients are invested in Global Alpha, and Blankfein alluded to the fund's plunge when he was asked about private banking at the New York conference. "We feel terrible about it," Blankfein said of the fund's performance.

One lure for clients may be Goldman Sachs's ability to avoid other pitfalls. It's one of the few financial companies that hasn't had to take a reputation-sullying writedown recently. Zurich-based UBS AG, ranked the No. 1 wealth manager by Scorpio, wrote down \$14 billion in subprime mortgage investments in January. UBS said it planned to raise \$12 billion from the government of Singapore and an unidentified Middle Eastern investor.

As Blankfein seeks multimillionaire clients, he'll be battling more than just Swiss banks such as UBS. An old-fashioned idea, the so-called family office, is making a comeback. Traditionally, a family office handled investments, taxes and estate planning for opulent clans. Rockefeller & Co., one of the world's oldest, got its start in 1884 when oil baron John D. Rockefeller hired two men to handle his personal affairs. These days, family offices cater to more than one family to gain economies of scale.

Assets supervised by family offices in North America grew 20 percent to \$305 billion in 2006 from '05, according to the Family Wealth Alliance LLC in Wheaton, Illinois. Almost one firm in five boosted assets more than 50 percent.

The rivalry cuts both ways. Tom Livergood, CEO of the alliance, asked family offices in 2007 to name the firm they bumped into most when making pitches to wealthy families. The most frequent answer was Goldman Sachs. "Goldman is a formidable competitor," Livergood says. "They smell when a deal is going to close."

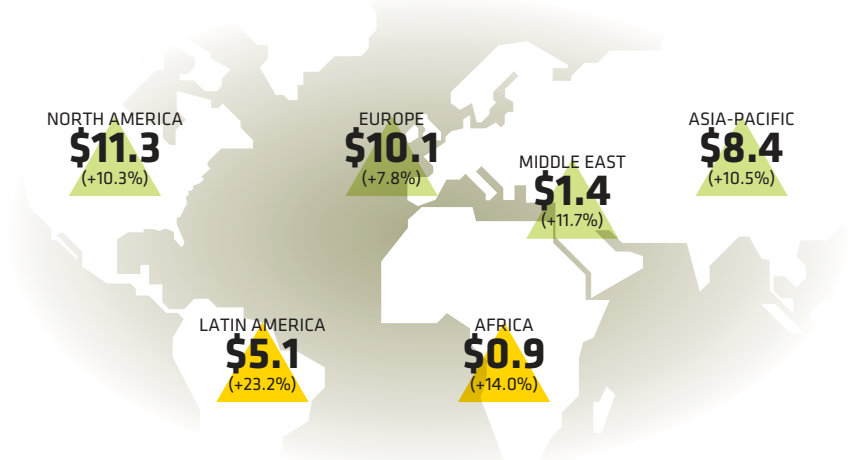
Elizabeth Nesvold, founder of Silver Lane Advisors, a New York-based investment bank that serves the financial services industry, says Goldman Sachs's cachet is real. "People love to say, 'Goldman showed me a deal,'" she says.

Many clients come to Goldman Sachs for a chance to invest in private companies

Where the Wealth Is

Latin American and African millionaires added the most to their fortunes in 2006.

2006 ASSETS, IN TRILLIONS (PERCENTAGE OF CHANGE FROM 2005 TO '06)



Source: Merrill Lynch-Cap Gemini World Wealth Report

the firm has identified as smart buys. In April 2006, Goldman, along with private clients and investors in Goldman funds, paid \$2.6 billion for a 5 percent stake in Beijing-based Industrial & Commercial Bank of China Ltd. ICBC sold shares to the public six months later, giving Goldman a paper profit of almost \$4 billion. During the past three years, Goldman says its private clients have committed more than \$25 billion to such deals.

GOLDMAN SACHS HAS been building up its private banking capabilities in recent years. In late 2006, it opened a commercial bank in the U.S., letting it manage cash, sell mortgages and take deposits, which have grown to \$16.4 billion. It got a similar banking license in Ireland last year. Over the past two years, it has hired about 100 private wealth advisers, bringing the total to 600.

Among the new Goldman Sachs hires: Sheryl WuDunn, 48, who shared a 1990 Pulitzer Prize with her husband, Nicholas Kristof, for reporting on Beijing's Tiananmen Square protests for the *New York Times*. Before becoming a journalist, she was a loan officer at Bankers Trust Co. (now part of Frankfurt-based Deutsche Bank AG) and got a Master of Business Administration from Harvard Business School in Boston. And she's worldly and intelligent, says Scaturro. "She's the perfect profile," he says.

The trend in private banking is to divide the roles: one team for asset management and another for attracting new clients and handling customer service. That may not always work with multimillionaires, says former Goldman Sachs private banker Nicolas Sarkis, founder of AlphaOne Partners LLP, an investment advisory firm in London. He worked in Goldman's private wealth unit from 1997 to 2005. "Very wealthy clients want to speak directly to the person who is managing their money, not a salesperson," Sarkis says.

Goldman Sachs may have a natural advantage when it comes to recruiting some clients. In its investment banking role, it assists with initial public offerings. The founders of companies going public often turn to Goldman for personal investment advice. "The source of their private banking business has always been their investment bank," says Scorpio analyst Graham Harvey.

In private wealth, Goldman Sachs is attacking a growth industry. The market is expanding as the rich get richer in the U.S. and Europe and new dynasties are created in Asia and Latin America, two private banking hot spots. The number of people worldwide holding financial assets worth at least \$1 million rose 8.3 percent to 9.5 million in 2006 from '05, according to the Merrill Lynch-Cap Gemini report. Their combined assets jumped 11.4 percent to \$37.2 trillion.

The ranks of the rich grew fastest in Singapore, India, Indonesia, Russia and the United Arab Emirates, the report says. All topped 15 percent growth. China's wealthy rose 7.8 percent to 345,000, while the U.S. was up 9.4 percent to 2.9 million.

To understand how lucrative private banking is, consider New York-based Citigroup. It has both a brokerage, Smith Barney, and a private bank. The brokerage had \$1.55 trillion in client assets at the end of 2007, more than six times the \$236 billion



Peter Scaturro chairs private banking from lower Manhattan.

that Citigroup's private bank had. Even so, Smith Barney's earnings were \$1.35 billion last year, just over two times the \$623 million the private bank earned.

Private banks have been around for centuries. Switzerland became a wealth haven in the 1790s, when the French Revolution prompted the aristocracy to move money out of France.

"What makes us different is that we've been in the private client business for 150 years," says Anthony DeChellis, head of private banking in the Americas for Zurich-based Credit Suisse Group, founded in 1856. He says patience is the key to landing and keeping clients with \$10 million or more. "It's not hiring a star trader and giving him a billion dollars worth of capital that you hope he turns into \$2 billion or \$3 billion of capital in a short period of time," DeChellis says.

While Goldman Sachs sees fertile territory in Asia and Latin America, the Swiss are prospecting on Goldman's home turf. Credit Suisse in 2001 bought Chicago-based Frye-Louis Capital Management Inc. The firm was co-founded in 1991 by Jeffrey Louis III, a descendant of Samuel C. Johnson, who in 1886 founded S.C. Johnson &



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Son Inc., now the maker of Windex cleaner and Ziploc bags. Frye-Louis clients have \$30 million or more each. UBS bought Piper Jaffray Cos.' wealthy-client unit for \$500 million in 2006. Last year, the bank paid about \$280 million for Cleveland-based KeyCorp's McDonald Investments brokerage unit, which serves the rich.

"Wealth management's our core business," says Marten Hoekstra, UBS's head of private wealth in the U.S. UBS has special services: It helps with art purchases and has vineyard consultants available for aspiring winemakers.

UNLIKE MANY OF his clients, Scaturro didn't grow up rich. He was born and raised in New York and still has traces of a Queens accent. He went to Archbishop Molloy High School, a Catholic private school, where he won national recognition as an All-American in swimming. He was a freestyle sprinter and still has the lean body of a swimmer. His blue, striped shirt bears his monogram—PKS—below the pocket.

Scaturro went to Columbia University in Manhattan, where he earned a bachelor's degree in engineering in 1982. His first job on Wall Street was in the same building he's in now, though 24 floors lower, as a systems analyst for Chase Manhattan Bank, now part of JPMorgan Chase & Co.

Working full time, he went back to Columbia and got a master's in engineering in 1985. He joined Bankers Trust, where he was plucked out of an in-house management program for up-and-comers to do strategic planning for one of the vice chairmen. In 1994, he joined Bankers Trust's private bank as head of strategy and marketing. Weill hired him to run Citigroup's U.S. private bank in 1999. He took over global private banking less than a year later.

Scaturro's career hit an air pocket in October 2004. He and Vice Chairman Deryck Maughan left the company five weeks after Japanese regulators closed Citigroup's private bank in Japan, accusing Citigroup of failing to exercise proper internal controls and doing business with a client whom affiliates had flagged as suspicious. Then CEO Charles Prince bowed in apology at a Tokyo press conference on Oct. 25, 2004. Scaturro and Maughan weren't accused of any wrongdoing.

Six months after his exit from Citigroup, Charles Schwab, founder of San Francisco-based Charles Schwab Corp., hired Scaturro to run U.S. Trust, which the discount brokerage had purchased for \$2.8 billion in 2000. Scaturro made a splash with employees by renting space at New York's Central Park Zoo for a companywide night out. The previous CEO had cut back on everything, including color photocopies, says a

person who worked there at the time.

In return, Scaturro demanded hard work. At meetings with rank-and-file employees, he would brag about working holidays, the person says, and pressured bankers to sell investments. "It became all about selling product," the person says. Scaturro says that wasn't the case.

Schwab agreed to sell U.S. Trust to Bank of America for \$3.3 billion in November 2006. Schwab offered Scaturro almost \$9 million in cash to stay until the deal closed, according to a Nov. 21, 2006, letter from Charles Schwab to Scaturro that was filed with the U.S. Securities and Exchange Commission. Scaturro stayed until it did, on July 2, 2007.

He joined Goldman Sachs that same month as it hired more wealth advisers to attract clients. As an industry, private bankers probably control \$16 trillion, according to Scorpio. That leaves another \$8.4 trillion owned by millionaires that's sitting in retail banks and discount brokerages.

Family offices are trying to rake in some of that. They tout so-called open architecture, industry jargon for offering funds from outside managers. Some also say competitors such as Goldman Sachs want to steer clients into in-house hedge funds to earn more fees. "Their real goal is to gather the assets because that's where the money is," says Patricia Soldano, president of Cymric Family Office Services in Costa Mesa, California. "Our culture is a service culture, not a products culture."

Like most family offices, Cymric charges clients a percentage of assets under management: 25 basis points–100 basis points. (A basis point is 0.01 percentage point.) Charging a family with \$50 million in assets 25 basis points would bring in \$125,000 a year. Family offices often charge extra for special projects, such as overseeing construction of a vacation home or archiving family photographs.

Bankers to the Rich

Private banking is one of the areas of finance Goldman doesn't dominate.

| Bank | Private banking assets, in billions* |
|-------------------------------------|--------------------------------------|
| 1 UBS (Zurich) | \$1,608 |
| 2 Citigroup (New York) | 1,438 |
| 3 Merrill Lynch (New York) | 1,209 |
| 4 Credit Suisse (Zurich) | 642 |
| 5 JPMorgan Chase (New York) | 465 |
| 6 Morgan Stanley (New York) | 450 |
| 7 HSBC (London) | 408 |
| 8 Deutsche Bank (Frankfurt) | 249 |
| 9 Wachovia (Charlotte, N. Carolina) | 206 |
| 10 Pictet (Geneva) | 192 |
| 11 ABN Amro Holding (Amsterdam) | 187 |
| 12 Goldman Sachs (New York) | 177 |

*In most cases, private banking includes clients with \$1 million or more in assets. Assets are for 2006. Source: Scorpio Partnership



Maria Elena Lagomasino
leapt from Wall Street to
GenSpring Family Offices.

Scaturro says Goldman Sachs offers clients plenty of choice. “Goldman has made a serious commitment to open architecture,” he says during an interview in his 41st-floor office at One New York Plaza, on the southern tip of Manhattan. He says one-third of his unit’s private wealth assets are in funds run by independent managers. As for hedge funds, clients have \$29 billion in Goldman funds and \$22 billion in non-Goldman funds, Scaturro says. It shows Goldman’s system is open, he says.

That may be little comfort to clients who had assets in Global Alpha. Many exited the fund as it slumped. In the fourth quarter, investors pulled \$3 billion from Global Alpha and other Goldman Sachs quantitative funds—those using mathematical models to detect buy-and-sell opportunities, Chief Financial Officer David Viniar said during a Dec. 18 conference call with analysts.

Global Alpha’s managers trade everything from soybeans to Israeli shekels. For a time, gains were alluring. The fund posted an annualized return of 19.75 percent, after fees, from Dec. 4, 2001, to Dec. 31, 2005, according to Global Alpha’s 2005 annual report. It didn’t last. By mid-August 2007, the fund was down 26 percent for the year. The decline coincided with a collapse in credit markets. Another so-called quant fund, Global Equity Opportunities, dropped 23 percent in August, and Goldman Sachs had to inject \$2 billion to help shore it up.

With funds that are performing well, Goldman Sachs can win more rich clients. That would add to the firm’s income from management fees and help provide extra profit in lean years. Like most hedge funds, Goldman funds charge a management fee of roughly 2 percent of assets, regardless of performance.

Also, like other hedge funds, Goldman Sachs’s funds keep 20 percent of annual

gains. These fees totaled \$962 million in fiscal 2006. Last year, they plummeted to \$187 million.

The quant fund losses stung. Scaturro calls their performance “disappointing.” Still, he sees no lasting damage. “People understand that the world is complex and volatile and that no one is going to get it right 100 percent of the time,” he says.

Poor performance in another portfolio prompted a client in Europe to consider pulling his money from Goldman Private Wealth Management. The client, who spoke on condition that he not be named, says he became irked with Goldman late last year after suffering losses in a basket of stocks aimed at the wealthy.

The portfolio bought U.S. mortgage lender Countrywide Financial Corp. at the end of June for about \$35, then sold it in mid-August for about \$18, the client says. Goldman Sachs also bought Ambac Financial Group Inc., the bond insurer, in late 2006 at \$87 and sold it in November at \$25, he says.

“They got it wrong all the time,” says the client. “They should have known.”

Goldman Sachs’s Raphael declined to comment, saying the firm doesn’t talk about its clients.

Goldman has been managing money for the wealthy since 1869, when founder Marcus Goldman invested for his family. It added outside clients in 1906 after selling shares to the public for Sears, Roebuck & Co. Afterward, Goldman helped Sears’s founders manage their windfall.

The wealth management unit got a boost in 1967 when a future Goldman partner named Roy Zuckerberg took it over. He kept the Private Client Services group small and picked brokers carefully, according to a former member of the group. Zuckerberg, 71, became a vice chairman in 1997 and left Goldman in 1998. He didn’t return telephone calls seeking comment.

In the past decade, Goldman Sachs’s private bank has been in flux. Zuckerberg’s group of bankers got much of their pay in commissions, keeping a portion of the fee that Goldman charged clients for buying and selling securities, according to the former broker. Whether they brought in new



David Rosenberg quit Citigroup for a family office on Puget Sound.



‘THEY SAID, “SALES FORCE,” AND I SAID, “WHO ARE THOSE GUYS?” AND IT WAS US,’ SAYS A FORMER GOLDMAN BANKER.

clients, retained them and made them money also helped determine pay, he says. By the 1990s, some of the best brokers were taking home \$10 million a year, the ex-broker says.

JUST BEFORE GOLDMAN SACHS became a publicly traded company in 1999, the firm brought in McKinsey & Co., the New York-based management consulting firm, to help increase profits from the private wealth group, according to the former broker. McKinsey recommended cutting the portion of pay that came from commissions and giving more weight to other factors, such as winning new clients, says the ex-broker.

The change in pay structure prompted many managers to leave, the former broker says. Many took their clients with them, and in Europe, the private banking business started to lose money, according to two people familiar with the situation. “It was in red ink,” says one.

Goldman’s Raphael declined to comment.

Goldman Sachs asked McKinsey to come back in 2005 to examine the European business, and the consultants recommended that the firm require brokers to focus almost exclusively on finding new clients, the two people say. Brokers would then pass the assets along to Goldman fund managers. This way, Goldman could build the business faster and manage clients’ money more efficiently, according to one of the two familiar with the situation. Goldman made the change in Europe. In the U.S., commissions still determined much of the brokers’ pay, according to a person familiar with the matter. Many brokers who wanted to continue managing money left, according to the former broker.

McKinsey spokesman Christopher Colford said, “We never comment on any work we do for clients.”

For all the glamour implied by the term “private banker,” some of the work can be mundane. “My job was a lot of bending over backward and kissing butt,” says a former private banker who worked at City National Corp. in Beverly Hills, California.

The banker says he spent much of his time filling out loan paperwork and pitching clients to invest with City National, generating fees. “Your ultimate goal is to capture the investments,” he says. “That’s where the payday is.”

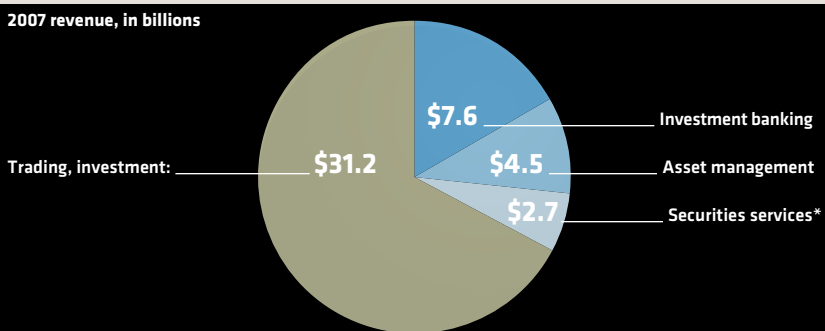
City National spokesman Cary Walker declined to comment.

Christopher Trokey, 35, says Goldman Sachs is no different. He worked in private wealth management at the firm from 2000 to ’02 before being dismissed in a round of job cuts. He says he remembers a class where trainers referred to the aspiring private bankers as the sales force. “They said, ‘sales force,’ and I said, ‘Who are those guys?’ and it was us.”

Now, Trokey works in New York for

Trading Dominates

Revenue for private banking is so small that Goldman doesn’t break it out.



*Including prime brokerage. Figures are for Goldman Sachs’s fiscal year ended on Nov. 30, 2007. Source: Goldman Sachs

GenSpring Family Offices, a unit of Atlanta-based SunTrust Banks Inc. GenSpring says it can get clients into the best third-party hedge funds. Like other family offices, GenSpring doesn't have its own funds. Last May, the company organized a men's weekend in Las Vegas for client families. Jamie Dinan, founder of York Capital Management LLC, a \$13 billion hedge fund firm based in Manhattan, was one of the speakers. His flagship fund returned an annualized 17.2 percent from inception in October 1991 through June 30, 2006. Some of his clients are GenSpring families.

HAP PERRY, WHOSE extended family made its fortune in Ballantine beer, started GenSpring in 1990 in Palm Beach, Florida. In 2005, he hired Maria Elena Lagomasino, former head of JPMorgan Chase's private bank, to run it.

To woo the rich, GenSpring opened an office on 54th Street in Manhattan, just behind the Museum of Modern Art, in a townhouse that once belonged to the Rockefellers. GenSpring redecorated, putting in bamboo floors and tables. There are even board games. GenSpring created "Shirtsleeves to Shirtsleeves," which challenges players to keep a fortune from being usurped by the tax authorities and squandered by grandchildren.

"Your daughter Brittany just returned from Vegas announcing her marriage," reads one of the game cards. "You realize that you never mentioned the word 'pre-nup.' They get divorced a year later, and he takes half her trust money. LOSE \$12 million."

To hear Lagomasino tell it, being an adviser to wealthy families is a calling, not unlike the priesthood or social work. "This is like a vocation," she says.

The high-mindedness may be working. GenSpring, which charges a percentage of assets under supervision for all of its services, has 600 families as clients. It says assets have doubled to \$15 billion from \$7.5 billion in less than two years.

David Rosenberg is another private banker who quit Wall Street for a family office. He was chief investment officer at Citigroup's U.S. private bank in New York. In January, he joined Threshold Group, a family office in Gig Harbor, Washington, on the wooded shores of Puget Sound. Threshold makes many private banks look middle class. Many Threshold clients have financial assets of more than \$100 million each

and a total net worth of at least \$200 million. George Russell, who started Threshold, made about \$1 billion after selling the family business, pension adviser Frank Russell Co., to Milwaukee-based Northwestern Mutual Life Insurance Co. in 1998.

Rosenberg, 49, says he moved to a tiny, rain-soaked town across the country and took a pay cut because family offices are the future. Banks care more about getting wealthy clients' assets into their hedge funds, he says. "It's not about long-term relationships."

Scaturro, meantime, is sticking with the big banks. The recent market turmoil plays to Goldman's strengths, he says. "With complexity and volatility comes a flight to quality," he says.

If Scaturro is right, then Goldman Sachs's bid for the rich will be a no-brainer. The Standard & Poor's 500 Index was down 9.3 percent for the year as of Feb. 8. A prolonged slide, though, might be too much complexity, even for Goldman. **B**

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Tracking Goldman's Asset Management

For a breakdown of sources of Goldman Sachs's revenue, you can use the Product/Brand/Geographic Segmentation (PGEO) function. Type GS US <Equity> PGEO <Go> and click on the plus sign to the left of Total Asset Management to further break out the data. Click on the Chart View tab at the bottom of the screen for a graph, as shown at right. For Goldman's 2007 fiscal year, asset management and securities services accounted for 15.7 percent of revenue compared with 18.8 in 2005.

For a list of news stories on Goldman's Global Alpha Fund, the hedge fund that lost about 40 percent in 2007, type STNI GLOBALALPHA <Go>. For stories on wealth management for high-net-worth individuals, type STNI FAMILYOFFICE <Go>.

To view a menu of hedge fund-related functions, analytics and news, type HFND <Go> for the Hedge Fund Home Page. To download a form you can use to become accredited to see data for U.S. hedge funds, type 12 <Go> 1 <Go> 1 <Go>. Under U.S. securities laws intended to protect unsophisticated investors

from taking on risks they don't understand in private pools of capital, hedge funds can be marketed only to so-called accredited investors. Fill out the form and fax it to the number listed, and it will be reviewed by Bloomberg's legal department.

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