

## Fellow Shareholders:

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We started 2016 with concerns about global economic growth, leading some to comment that the world was headed into a recession. While those concerns moderated in the second quarter and the global economic outlook improved in the second half, other concerns drew to the forefront. Few predicted with conviction the outcome of the United Kingdom's referendum on remaining a part of the European Union, the results of the presidential election in the United States or the markets' reactions to either event.

In last year's letter, we characterized 2015 as a "tale of two halves." That was certainly true again in 2016, but in reverse order. As our clients — and by extension, the firm — navigated the challenging operating environment in the first half, our net revenues declined by 28 percent year over year for the period, with the majority of that decline occurring in the first quarter. As conditions improved in the second half, so did client sentiment. As a result, net revenues increased by nearly 16 percent year over year in the second half, including two consecutive quarters of more than 11 percent annualized return on average common shareholders' equity.

The events of the past year are a stark reminder of how quickly expectations and conditions can change, and of the importance for us to be nimble and to concentrate on the things we can control. Despite the difficult start to the year, we remained focused on our clients and operating efficiently, without surrendering the ability to pursue potential opportunities. For the full year, the firm generated net revenues of \$30.6 billion, net earnings of \$7.4 billion and diluted earnings per common share of \$16.29. Our return on average common shareholders' equity was 9.4 percent.

Despite our focus on cost discipline, we did not stop investing in our franchise — including investments in technology, attracting and retaining top talent, and seeking new business opportunities, including our efforts to expand our lending footprint, most notably through Goldman Sachs Bank USA. We believe that our consistent investment in our franchise positioned us to serve our clients when activity increased in the back half of 2016.

Managing the firm with discipline while preserving optionality for upside can be a difficult balancing act. We do not hold preconceived expectations for certain outcomes, but rather approach our own operations with the same mindset we do when helping our clients. We spend a great deal of time thinking about and preparing for downside scenarios, but we are always cognizant that the economy, markets and sentiment could break to the high side, and we position ourselves for that possibility.

We believe our client franchise benefits from our consistent commitment to being a diversified and dependable provider of services.



**Lloyd C. Blankfein**  
Chairman and  
Chief Executive Officer  
*(center)*

**David M. Solomon**  
President and  
Co-Chief Operating Officer  
*(left)*

**Harvey M. Schwartz**  
President and  
Co-Chief Operating Officer  
*(right)*

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In this year's letter to our shareholders, I will discuss these and other topics, including our financial profile and the state of our businesses.

## Financial Profile

Given the challenging operating environment in the first half of 2016, we undertook steps and actions consistent with the difficult conditions.

For the first quarter of 2016, with net revenues down by 40 percent year over year, we accrued compensation and benefits expenses 40 percent lower year over year. We ended the year with net revenues and compensation and benefits expenses nine and eight percent lower than 2015, respectively.

We also completed an initiative that identified a reduction of approximately \$900 million in annual run rate compensation during the year, in which we realized approximately \$500 million, net of severance and other related costs, during 2016. Including these efforts, we have announced and completed \$2.8 billion in savings initiatives since 2011. This demonstrates how our flexible cost base helps us navigate challenging operating environments.

The impact of our efforts can be seen by comparing our results in 2016 to 2011. 2011 was an instructive year — as it was a tough net revenues year, similar to 2016. In 2011, we had net revenues of approximately \$29 billion with operating expenses of approximately \$23 billion. Our compensation and benefits to net revenues ratio was more than 42 percent and our pre-tax margin was over 21 percent.

In 2016, despite higher net revenues, our operating expenses were down by 10 percent vs. 2011, our compensation and benefits to net revenues ratio was down by 400 basis points and our pre-tax margin was more than 12 percentage points higher. This reflects a lot of the firm's work in cost discipline and provides significant operating leverage for the future.

Our cost savings efforts in 2016 were part of a broader focus on efficiencies. For example, over the past five years we have grown our head count in our Salt Lake City office by nearly 80 percent, making it our fourth-largest location globally.

In terms of our capital and liquidity, our balance sheet has never been more conservatively positioned as a result of adjustments we have made to adapt to new regulations since the financial crisis. By almost all measures, Goldman Sachs, and the broader financial system, is safer. For example, our Global Core Liquid Assets have increased by almost four times, our common shareholders' equity has nearly doubled and our gross leverage has been cut by more than one-half since the end of 2007.

Moreover, we have reduced our balance sheet size by seven percent over the past five years, while increasing our common shareholders' equity by 13 percent and our book value per common share by 40 percent. Over the same period, we have returned nearly \$32 billion of capital to shareholders through buybacks and dividends, reducing our basic share count by more than 100 million shares, or approximately 20 percent, to the lowest ever.

Importantly, while these efforts helped us to strengthen our balance sheet, they did not detract us from remaining focused on sustaining and improving the quality of our client franchise.

## Investment Banking

Our investment banking franchise reflects deep relationships with more than 8,000 clients across a variety of industries in approximately 100 countries.

We ended the year ranked first in global announced and completed mergers and acquisitions, advising on many of the year's most significant transactions. As has long been the case, our advisory franchise creates other opportunities across the firm, such as in debt underwriting, which is able to serve our clients with

best-in-class debt financing capabilities. Our financial advisory net revenues declined compared to a strong 2015, partially offset by record debt underwriting net revenues of \$2.5 billion. In fact, we ended the year ranked in the top five in global debt and in the top three in global high-yield — areas where we traditionally have not had the same footprint as some of our larger competitors. We also continued to maintain a leading equity underwriting franchise, though net revenues declined significantly in 2016 as a result of the operating environment.

Nevertheless, we ended the year strong, as our investment banking transaction backlog grew in the fourth quarter.

### Institutional Client Services

With a leading, diversified global platform in Institutional Client Services (ICS), comprising our Fixed Income, Currency and Commodities Client Execution (FICC) and Equities franchises, we are one of the few firms that have remained committed to serving our clients' needs broadly across financial products, services and regions.

We did not extrapolate from the exceptional conditions of the past several years to draw hard and fast conclusions about the FICC franchise. These conditions included interest rates near or below zero, a flat yield curve and muted economic growth. That is why we put a premium on maintaining our commitment to businesses that we knew were important to our clients.

We have a diverse client franchise, and one area of particular strength has long been our standing with the hedge fund community. Our product diversity, global footprint, world-class prime brokerage capabilities, and engagement strategy based on content are of particular value to hedge fund clients.

Over the past few years, we also have made it a key priority to deepen relationships with more traditional asset managers. As an example of our progress, we have seen market share improvements in our U.S. cash credit businesses, where asset managers have historically been active.

Both hedge funds and active managers could face a much different and more attractive market environment in 2017. To the extent decreasing market correlations translate into a better backdrop for generating outsized performance, that should also support increasing levels of client activity.

Despite the headwinds that marked the start of 2016, ICS net revenues were down modestly compared to 2015. FICC net revenues increased slightly year over year, which is notable given market conditions in the first quarter. Equities client execution net revenues declined significantly year over year, driven by lower client activity levels.

### Investment Management

Our broad portfolio of solutions and consistent performance have enabled us to be one of the fastest-growing active investment managers in the world. Our product offerings range from asset and liability management for our private wealth clients, to tailored advisory solutions for our institutional clients, to fund products across all asset classes.

Net revenues declined year over year in 2016, due largely to lower incentive fees. However, even in a more challenging environment, we have continued to build our franchise. Over the past three years, we have grown our assets under supervision by \$337 billion to a record of nearly \$1.4 trillion. That growth would be akin to creating a top 30 U.S. asset manager in just three years, and includes \$150 billion of organic active long-term net inflows. During this period, many active investment managers have seen net client outflows.

Despite such growth, we continue to see significant potential as investors consolidate assets with leading providers. There are bigger players within each of the product categories in which we compete, offering room to garner more market share. We will pursue that growth by providing clients with comprehensive advice, thought leadership and innovative products that will help them to better meet their investing needs.

## Investing & Lending

Investing & Lending is a collection of activities that is synergistic with other elements of our overall franchise, helping us to expand our client relationships. We continue to provide long-term capital by way of direct lending and equity investments, and remain focused on opportunities that provide strong risk-adjusted returns on capital over the long term.

### **Growing Our Lending Footprint**

In particular, we continue to see lending as a growth opportunity for the firm. Approximately one-third of our 2016 net revenues in Investing & Lending was generated by debt securities and loans, which included more than \$1 billion in net interest income.

Over the past four years, we increased our funded loans 2.8 times to roughly \$64 billion. Corporate loans, diversified across sectors and industries, make up 46 percent of the portfolio, followed by private wealth management loans at 32 percent and real estate loans at 17 percent. We continue to see increased demand from our investment banking and private wealth management clients, and we are intent on prudently increasing our lending portfolio.

This past fall, we launched *Marcus: By Goldman Sachs* — an online lending platform designed to provide consumer clients with an alternative to higher-interest-rate credit card debt. The growth in digital finance, combined with our historical strength in technology and risk management, led us to see an opportunity to add value to this attractive new market for Goldman Sachs.

By most measures, the opportunity is broad and deep. The unsecured consumer loan market in the U.S. is roughly \$850 billion. We are focused on creditworthy consumers with \$5,000 to \$30,000 of credit card debt, the majority of whom are not aware of better debt management options. We have received encouraging feedback from our new clients as we have slowly built out the business, and continue to see potential for attractive risk-adjusted growth opportunities.

## Focus on Technology

Technology is central to every part of our business. Simply put, it is a core competitive advantage that drives long-term value in several ways — namely, through enhancing our clients' experience, driving efficiency and creating new opportunities, like *Marcus*.

Our investment in our Marquee platform, a collection of applications for our institutional clients, represents one such cutting-edge opportunity. Marquee allows clients to access some of the same analysis and risk management tools our market makers use.

More broadly, we are investing in infrastructure to improve our electronic execution capabilities, including for systematic investing clients who require speed and differentiated execution, and for straight-through processing.

We have also made successful investments in electronic execution platforms. Our global infrastructure, as a result of this and other investments, is now capable of executing equity and select FICC transactions in a much more efficient manner. Importantly, all of our clients — not just our clients with quantitative strategies — enjoy the benefits of better execution.

We have likewise integrated technology into our recruiting processes, in particular to facilitate first-round video interviews with the goal of widening and diversifying the pool of talent we evaluate. For 2017's intern class, so far we have conducted interviews with candidates from more than 900 schools, reaching 100 more schools than last year.

## Our People

Of course, our most important long-term competitive advantage is our people. Our commitment to attracting and retaining the most talented people in our industry — and beyond — is of vital importance to the firm and the perennial foundation of our success.

We must be diverse and representative of the countries and cultures in which we operate. Our people represent more than 160 different nationalities and speak over 100 different languages.

I am pleased to report that Goldman Sachs remains a highly attractive place to work. In 2016, our summer internship and full-time campus applicants rose by 11 percent. We had approximately 130,000 applicants for just 5,000 internship and full-time campus roles — approximately a four percent hiring rate. In addition, of those who received offers, approximately eight out of 10 accepted. And, in 2016, we were proud to be named as one of *Fortune* magazine’s “100 Best Companies to Work For.” Goldman Sachs is one of only five companies to be recognized every year that the Great Place to Work Institute has issued its list since 1984.

Given the growing significance of technology in how we operate our businesses, we have increasingly been focused on hiring individuals with backgrounds in science, technology, engineering and math (STEM). In 2016, 37 percent of new campus analysts who joined the firm came from these STEM majors. Today, approximately 9,000 people, or roughly one-quarter of the firm, work in various engineering-related roles.

More broadly, our people continue to see the value of a long-term career at Goldman Sachs. The median tenure of our partners and managing directors at the firm is 15 years, and nearly 60 percent of them joined the firm as an analyst or associate (our entry level positions).

To ensure that the talent we hire is the talent we keep over the long term, we invest hundreds of thousands of training hours in our new analysts, and provide thousands of classroom programs and digital resources for senior professionals.

### **Executive Succession and Our Deep Leadership Bench**

In 2016 and the early part of this year, we saw a number of movements in our leadership ranks, as well as a key addition to our Board of Directors. As chairman and chief executive officer, in consultation with our Board of Directors, one of my most important priorities is smooth and effective leadership transitions.

This past December, then-U.S. President-elect Donald Trump appointed Gary Cohn, then our president and chief operating officer, director of the National Economic Council. Gary was responsible for developing and leading many of the firm’s most important initiatives, and demonstrated a deep commitment to our clients, our people and the culture of Goldman Sachs. We thank him for having served as a trusted advisor, dedicated colleague and friend to so many at the firm, and wish him well.

David Solomon, our former co-head of the Investment Banking Division, and Harvey Schwartz, our chief financial officer, assumed new responsibilities as presidents and co-chief operating officers of the firm. In addition, Marty Chavez, chief information officer, was named deputy chief financial officer of Goldman Sachs and will become chief financial officer.

This past year was also marked by some senior retirements from the firm. Michael “Woody” Sherwood, vice chairman of the firm and co-chief executive officer of Goldman Sachs International, and Mark Schwartz, chairman of Goldman Sachs Asia Pacific and vice chairman of the firm, announced their retirements following decades of service. We wish both Woody and Mark all the best in the years ahead and thank them for their extraordinary contributions to Goldman Sachs.

Richard Gnodde, co-head of the Investment Banking Division and chief executive officer of Goldman Sachs International, and Pablo Salame, co-head of the Securities Division, were appointed vice chairmen of the firm. David, Harvey, Marty, Richard and Pablo have a long track record of distinction in their respective areas of expertise, spanning multiple businesses and geographies.

In December, we welcomed a new member to our Board of Directors. Ellen Kullman is an accomplished business leader who has held a variety of senior roles at E. I. du Pont de Nemours and Company, including as chairman and chief executive officer. We are confident that her deep experience in business and as a board member in both the public and nonprofit sectors will add great value to our Board of Directors.

## **Our Tradition of Leadership and Public Service**

Gary was not the first person from Goldman Sachs to join the government, and we hope and expect that he will not be the last. Five of my most recent predecessors went into government service, and that has not been by happenstance. One ethic that has long pervaded Goldman Sachs is a commitment to public service if one is given the opportunity to serve. And that has been true over time and in many of the geographies in which we operate.

We recruit people who are oriented to the larger world, and their jobs require them to be both outwardly and inwardly facing. In the process, they develop the skills to make a contribution in large, complex organizations and the expertise to help drive economic progress and job creation.

We have been criticized for the fact that some of our colleagues, after long careers at the firm, have moved to work in the public sector. The charge is that Goldman Sachs is able to extract certain advantages that others cannot. In fact, the opposite is true. Those in government bend over backward to avoid any perception of favoritism.

We are proud of our tradition of leadership and public service and believe it is a core part of our culture. That is why we will continue to encourage our people to contribute to government service if they are fortunate enough to be asked.

We also have contributed our expertise and knowledge to broader public policy issues, such as fiscal policy. And, when certain issues impact our people, we have not hesitated to speak up on their behalf. In the past, we have commented on marriage equality, and more recently, immigration policy, because they both affect our ability to hire and retain people from the broadest pool of talent. We will continue to express our views on policies that affect our people, our business and the long-term interests of economic growth.

## **Our Commitment to Our Communities**

Goldman Sachs has long embraced our responsibility to help address social and economic challenges around the world. Our approach goes far beyond the significant financial support we provide to a broad array of philanthropic endeavors; we also make meaningful contributions that harness our business expertise, relationships and knowledge to address critical needs in the communities in which we work and live — and sometimes far beyond.

### ***10,000 Women***

Since 2008, the Goldman Sachs *10,000 Women* initiative has helped foster economic growth by providing women entrepreneurs in 56 countries with business education and access to capital. The initiative is now expanding to reach more than 10,000 women through a first-of-its-kind global finance facility launched in partnership with the International Finance Corporation to increase access to capital for women entrepreneurs to grow their businesses. By the end of 2016, the facility had committed more than \$600 million to banks in 17 emerging markets, which will enable more than 30,000 women entrepreneurs to access capital.

### ***10,000 Small Businesses***

*10,000 Small Businesses* has served more than 7,300 small businesses at 31 sites across the United States and the United Kingdom by the end of 2016. This initiative has worked with more than 100 local and national lenders and other organizations to provide access to management training, capital and business support services. Independent evaluations of the program have shown that participants consistently increase revenues and create net new jobs at a pace that outperforms the broader economy.

### ***Goldman Sachs Gives***

Through this donor-advised fund, partners at the firm recommend grants to nonprofit organizations around the

world. Since its launch in 2010, the fund has made more than 28,000 grants totaling nearly \$1.2 billion through the end of 2016 to 5,600 organizations that further *Goldman Sachs Gives*' mission of fostering innovative ideas, and solving economic and social issues. Grants from *Goldman Sachs Gives* have recently supported the Middle East refugee crisis, STEM education for underserved youths globally, medical research across a variety of fields, and need-based financial aid at colleges and universities globally, to name a few key initiatives.

### Looking Ahead

We often say that no one has a crystal ball. Markets change course at a moment's notice, and in response to factors no one can predict with any certainty. Cycles come and cycles go. But, if we manage our business with discipline and preserve our flexibility for upside, we can put ourselves in the best position to meet the needs of our clients and to grow our franchise.

We have long maintained that it is important to remain active and invested in our core businesses, despite cyclical pressures, both as we respond in the short term and orient ourselves for the horizon. In the past decade or so, some in our industry pulled back from sales and trading businesses that, to some, seemed to be permanently and negatively affected by market conditions, regulatory change and other factors.

We remained committed to the value we provide clients in those businesses across cycles. It is difficult to know how effective we have been at achieving the balance between cutting costs and investing in businesses until the cycle fully turns. Regardless of which way the future breaks, we do, however, see many reasons for optimism.

Putting aside one's individual politics, the outcome of the U.S. election raises the possibility of more stimulative tax and regulatory policies, as well as plans for more infrastructure spending. This represents a substantial change in direction for the U.S., and offers many investors and companies a reason for optimism.

Economic growth was showing signs of improvement, even before the election. U.S. interest rates are poised to rise, as policymakers digest improving economic indicators, while other global markets hold steady or even engage in stimulus, creating opportunities for investors in monetary policy divergence.

More durable market trends may yet emerge and spur healthier levels of client activity. Looking ahead to 2017, Goldman Sachs remains committed to working with our clients and leveraging the resources of the firm to help them achieve their objectives, while creating long-term value for shareholders.

I believe that our client franchise is as strong as it has ever been. We have transformed our balance sheet in ways that help us better weather challenging environments, while allowing us to pivot in times of higher client activity. We have prudently managed our operating expenses and capital, building significant operating leverage.

By staying true to our strategic focus, I am confident we can continue to generate industry-leading returns for shareholders and outperform over the long term.



**Lloyd C. Blankfein**

Chairman and Chief Executive Officer