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Wall Street Pay: A Record $144 Billion

Financial Overhaul Has Affected Structure but Not Level; Revenue-to-Compensation Ratio Stays Flat

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Pay on Wall Street is on pace to break a record high for a second consecutive year, according to a study conducted by The Wall Street Journal.

About three dozen of the top publicly held securities and investment-services firms—which include banks, investment banks, hedge funds, money-management firms and securities exchanges—are set to pay $144 billion in compensation and benefits this year, a 4% increase from the $139 billion paid out in 2009, according to the survey. Compensation was expected to rise at 26 of the 35 firms.

The data showed that revenue was expected to rise at 29 of the 35 firms surveyed, but at a slower pace than pay. Wall Street revenue is expected to rise 3%, to $448 billion from $433 billion, despite a slowdown in some high-profile activities like stock and bond trading.

Overall, Wall Street is expected to pay 32.1% of its revenue to employees, the same as last year, but below the 36% in 2007. Profits, which were depressed by losses in the past two years, have bounced back from the 2008 crisis. But the estimated 2010 profit of $61.3 billion for the firms surveyed still falls about 20% short from the record $82 billion in 2006. Over that same period, compensation across the firms in the survey increased 23%.

"Until focus of these institutions changes from revenue generation to long-term shareholder value, we will see these outrageous pay packages and compensation levels," said Charles Elson, director of the Weinberg Center for Corporate Governance.

Firms surveyed said it is too early to comment on 2010 compensation levels. Many firms say that if they don't adequately compensate employees, they risk losing top talent.

The pay numbers show that firms, benefiting from low interest rates and strong international markets, continue to base their pay on economic and market conditions rather than the level of pressure coming from regulators in Washington and overseas.

Still, politicians and market watchdogs have been successful in influencing the structure of pay, if not its levels. They have pushed for more compensation in stock and other deferred instruments. Firms have found other ways to limit the risks employees take for short-term gains, which was mandatory for firms that accepted government funds during the financial crisis.

Many large Wall Street firms have come out from under the Treasury Department's rules about pay. But with the passage of financial-overhaul legislation that aims to change pay policies, many public firms are still awaiting specific rules. Those rules, as required by the Dodd-Frank financial regulatory bill, won't be written for several months.

"The current wave of regulation is helping keep comp relatively flat," said Steven Eckhaus, a partner at law firm Katten Muchin Rosenman LLP.

There are some signs that pay might slow down in coming quarters. Tough new rules about how much capital banks must hold could force Wall Street to cut back on compensation in an effort to preserve returns on equity for shareholders, analysts say. Since Wall Street firms pay out up to half of their revenue in compensation, cutting back can meaningfully increase profits left for shareholders.

"I see a flat outlook over the next couple of years" on pay, said Roman Regelman, a partner in the financial-services practice at consulting firm Booz & Co. More regulations in high-profit businesses like derivatives will continue to hamper traders' pay, he said.

Though higher revenue often means higher compensation, that isn't always the case. At Citigroup Inc., which remains about 12%-owned by the government, analysts projected revenue would increase this year by about 4%. But pay is likely to be down about 8%, according to projections in the Journal survey.

The opposite is true at Goldman Sachs Group Inc. and Bank of America Corp., where analysts project revenue will be down, but compensation will be up, according to the survey.

Goldman's revenue is expected to decline by 13.5% this year to $39.1 billion from $45.2 billion in 2009. Compensation remains projected higher than last year, up 3.7% to $16.8 billion, from $16.2 billion in 2009, according to the Journal survey. Through the first half of 2010, Goldman Sachs set aside 43% of its revenue for compensation. Goldman's ultimate payouts could change drastically. In 2009, for example, it withheld revenue for compensation in the fourth quarter, dropping the overall ratio of revenue to compensation.

This year, employees have jumped to more lucrative opportunities when firms don't pay. Senior staff at Goldman Sachs and Credit Suisse Group in London, for example, defected last year when the firms cut their pay in response to a U.K. tax on bonus payments.

Where revenue falls short, analysts and experts expect that Wall Street will lay off employees in order to keep bonus pools high. U.K.-based Barclays Capital and Credit Suisse have cut some staff, while Morgan Stanley has a hiring freeze in place.

As proprietary-trading businesses were closed to adhere to new regulations, some traders have abandoned Wall Street to join private-equity firms and hedge funds.

Such nonbank firms like Blackstone Group LP, Och-Ziff Management Group LLC and Fortress Investment Group LLC aren't as scrutinized in Washington. All three firms' revenue and compensation are projected to increase.

At Blackstone, revenue is projected to be up 50% to $2.7 billion, from $1.8 billion in 2009. The Journal survey estimates that compensation will climb 12% in the year. At Fortress, which has closed two new funds this year, compensation is projected to climb by 29% to $656 million, from $505 million last year. Revenue is projected to rise 16.6%, to $680.8 million from $584 million in 2009, analysts say.

Acquisitions also have boosted revenue and compensation. Morgan Stanley, for example, acquired a 51% stake in Citigroup's brokerage unit, which affected 2010 revenue and compensation more than it did in 2009. While Morgan Stanley's compensation is expected to be up slightly because of higher revenue, its overall ratio of compensation is expected to drop to 49% of revenue from 62% in 2009.

James Gorman, Morgan Stanley's chief executive, told shareholders earlier this year that 2009's compensation was at a peak when compared with revenue. And he seemed sensitive to shareholder concerns. "We're extremely conscious of the comp-to-revenue ratio," he said at the Feb. 2 conference. "There is nobody on my management team who will ever see again the kind of comp-to-revenue ratio as we had last year."

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