

Testimony by David A. Viniar to the Senate Permanent Subcommittee on Investigations

Chairman Levin, Ranking Member Coburn and Members of the Committee:

My name is David Viniar. I have been Chief Financial Officer of Goldman Sachs since 1999 and Head of the Operations, Technology, Finance and Services Division since 2002. I am responsible for risk management, financial control and reporting, and financing our business, among other duties.

I appreciate the opportunity to appear before you and contribute to the Subcommittee's work on understanding some of the causes of the financial crisis. I'd like to focus my comments on our risk philosophy and our approach to risk management, which Craig Broderick, the firm's Chief Risk Officer, will also be addressing in some detail.

As a global investment bank and financial intermediary, Goldman Sachs integrates advice, financing, market-making, co-investing and asset management with its risk management capabilities to serve a broad range of largely institutional clients.

In doing so, we often take on principal risk to help clients achieve their objectives by, for example, facilitating accelerated and block offerings, providing structured solutions to financial problems, or extending credit to support advisory and underwriting business. We routinely evaluate, price and distribute risk across the spectrum according to the specific risk appetites of our institutional clients.

Based on the nature of markets, the roles we play, and our willingness often to assume risk so that we can complete a client's transaction, we know that we will sometimes incur losses – but as a core part of our business model, we pro-actively manage our risk to minimize these losses.

When we commit capital to buy or sell financial instruments, extend credit, or invest alongside our clients, we accumulate both long and short positions – in the form of assets and liabilities and contingent exposures – that have implications for our liquidity, credit and market risks.

As a financial institution, we are concerned first and foremost with ensuring strong liquidity. We do so by holding a substantial pre-funded pool of highly liquid assets, and through disciplined asset-liability management.

As a financial market intermediary, we take credit and market risks with a view to distributing them across the capital markets to investors and counterparties able and willing to assume them, while earning fees or spreads for our financing or intermediation service. We try to distribute these risk exposures in a reasonable period.

Over time, however, we naturally accumulate an “inventory” of long and short positions. The composition and net long or short bias of this inventory reflects the accumulation of customer trades and our judgments about supply and demand or market direction. At any given time, we may have long or short exposures to thousands of different instruments. This does not mean that we know – or even think – that prices will fall every time

we sell or are short, or rise when we buy or are long. We are executing transactions and assuming the risks in connection with our role of providing liquidity to the markets.

Taking all these considerations into account, we deploy a range of risk management capabilities to price the risks of each transaction appropriately, keep the firm's overall exposures within carefully prescribed risk limits, and establish off-setting positions (hedges) or sell and buy positions as necessary to control overall exposure to adverse developments.

Most fundamentally, our approach is to understand the risks we are taking, analyze and quantify them, and keep a firm grip on their current market value. We carry virtually our entire inventory of financial instruments at fair market value, with changes reflected in our daily P&L. This enables us to make informed decisions in real time about the risks we're taking and respond nimbly to opportunities or threats. Such daily marking of our positions was a key reason we decided to start reducing our mortgage risk relatively early as market conditions were deteriorating at the end of 2006.

I'd like to give you a sense for how we managed our risk during the period leading up to the crisis.

Through the end of 2006, we were generally long in exposure to residential mortgages and mortgage-related products. While this long position was the direct result of our market-making activities, it was within our risk limits and we were comfortable holding it. That December, however, we began to experience a pattern of daily losses in our mortgage-related

products P&L as we marked down the value of our mortgage-related inventory to reflect lower market prices. P&L can itself be a very valuable risk metric, and I personally read it every day.

I called a meeting to discuss the situation, bringing together key people involved in running the mortgage business, including senior business leaders and traders from the mortgage desk, as well as senior staff and analysts from our independent control and risk groups. We went through our positions and debated views on the mortgage market in considerable detail. While we came to no definitive conclusion about how the overall market would develop in the future, we became collectively concerned about the higher volatility and recent price declines in our sub-prime mortgage-related positions.

As a result, we decided to attempt to reduce our exposure to these positions. We wanted to get “closer to home” – that is, reduce our overall exposure to the residential housing market consistent with our risk protocols. We proceeded to sell certain positions outright and hedge our long positions in an attempt to achieve this result. We always prefer to sell outright in order to avoid incurring basis risk, but selective market illiquidity, together with our continuing obligation to make markets for our clients, meant this was not always a feasible alternative.

As always, the clients who bought our long positions or other similar positions had a view that they were attractive positions to purchase at the price they were offered. As with our own views, their views sometimes proved to be correct and sometimes incorrect.

We continued to reduce our positions in these products over the course of 2007. We were generally successful in achieving the objective of reducing this exposure to the extent that, on occasion, our portfolio “traded short.” When that happened, even if these short positions were profitable, given the ongoing high volatility and uncertainty in the market, we tended to attempt to then reduce these short positions to again get closer to home. This situation reversed itself in 2008, however, when the portfolio tended to “trade long” and, as a result, despite the fact that our franchise enabled the firm to be profitable overall, we lost money on residential mortgage-related products in that year.

While the tremendous volatility in the mortgage market caused periodic large losses on long positions and large gains on offsetting short positions, the net of which could have appeared to be a substantial gain or loss on any day, in aggregate, these positions had a comparatively small effect on our net revenues. In 2007, net revenues from residential mortgage-related products were less than \$500 million, approximately 1% of Goldman Sachs’s overall net revenues; and in 2007 and 2008 combined, our net revenues in this area were actually negative.

For Goldman Sachs, weathering the mortgage market meltdown had nothing to do with prescience or “betting” on – or against – anything. More mundanely, it had everything to do with systematically marking our positions to market, paying attention to what those marks were telling us, and maintaining a disciplined approach to risk management, which we believe served the firm, our clients, and our shareholders well during this extraordinarily challenging period.

Thank you and I am happy to take your questions.