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Megabucks deals for an elite few

By Ben White in New York

Compensation for top private equity bankers and hedge fund managers is likely to far outstrip even the huge payouts going to Wall Street chief executives, according to analysts.

The disparity will once again underline that the biggest money in finance is made at private groups rather than publicly traded investment houses.

For instance, the $53.4m bonus paid last month to Lloyd Blankfein, Goldman Sachs chief executive, is likely to be less than a quarter of the $220m or more that hedge fund executive Dan Och is likely to make for 2006, according to Charles Gradante, co-founder of the Hennessee Group, which advises hedge fund investors.

Mr Och's Och-Ziff Capital, which has about $20bn under management, gained about 14 per cent in 2006, according to the Hennessee Group.

The $40m bonus paid to John Mack, Morgan Stanley chief executive, is likely to be a fraction of the several hundred million dollars Ken Griffin, chief executive of hedge fund group Citadel, will make. Citadel, with $14bn under management, rose by about 17 per cent in 2006, according to the Hennessee Group.

Hedge funds typically charge investors 2 per cent of assets and 20 per cent or more of gains. In the best years, top hedge fund managers such as Edward Lampert of ESL, James Simons of Renaissance Technologies and T. Boone Pickens of BP Capital have made $1bn or more.

Even in a generally lacklustre year such as 2006, top hedge fund managers can earn far more than Wall Street chief executives. "The hedge fund business is the most cost-effective use of one's career," Mr Gradante said. "Where else can you make a billion dollars a year?"

The answer may be at a private equity group, though the compensation structure at buy-out shops is different from hedge funds.

Top private equity executives, such as Stephen Schwarzman at the Blackstone Group or Henry Kravis at KKR, can earn annual compensation in the hundreds of millions of dollars through deal fees and special dividends payments from portfolio companies.

That is especially true in a record year like this, where buyouts reached a record $709.8bn.

The big money in private equity comes from the "carry", the accumulating stake executives have in portfolio companies. Those gains, typically 20 per cent of profits, are generally not realised until a group sells or lists a portfolio company. When the big paydays come they can run into the hundreds of millions and more.

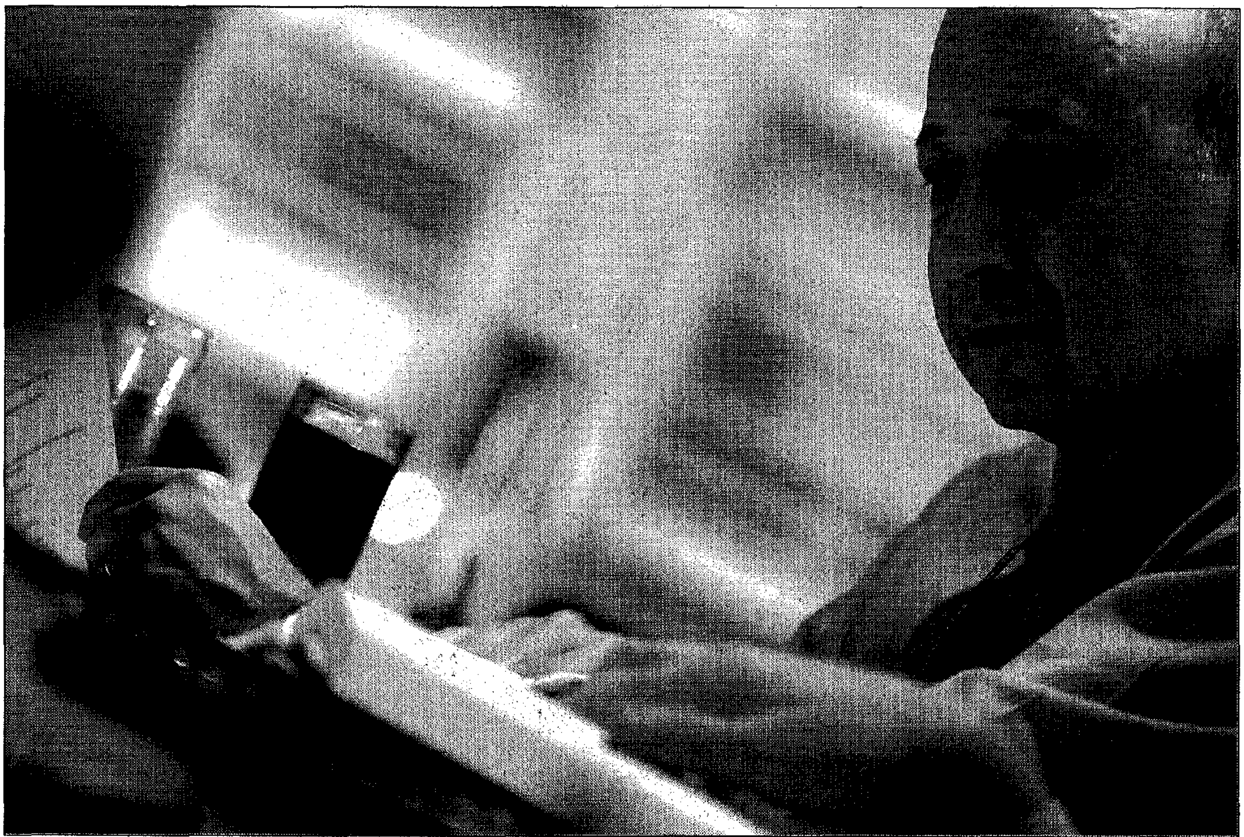
"The economics are almost beyond imagining," said Peter Gonye, co-head of the private equity and investment banking speciality practice in the US at executive search group Spencer Stuart. "Only hedge funds can compare to it."

Mr Schwarzman, whose net worth is estimated at $3.5bn by Forbes magazine, told the Financial Times recently that he expected private equity pay for 2006 to have hit a record.

While the biggest money at private equity firms goes to a relatively small number of partners, even junior bankers can outpace their counterparts at listed Wall Street banks.

A senior associate or vice-president at a big private equity group – typically someone who is one or two years out of business school – can now expect to earn $400,000 to $500,000 in annual salary and bonus, according to Brian Korb, head of the private equity practice at consultancy Glocap Search.

That amount does not include the equity the young bankers are accruing in portfolio companies. Similar employees at Wall Street banks can expect about $350,000 in salary and bonus.



Slim pickings: The $53.4m bonus paid to Lloyd Blankfein, Goldman Sachs chief executive, pales by comparison with hedge fund and private equity rewards Anna Gordon