Founder Stephen Schwarzman Describes Blackstone's Climb to the Pinnacle of High Finance

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Questions Posed by Economic Club of Washington President Rubenstein to Mr. Schwarzman

When you went to Yale, did you think you would go into business for sure?
How did you decide what you wanted to do at Lehman Brothers?
So you become the global head of M&A[1] for Lehman Brothers, and then in 1985 you decided, with Pete Peterson, to leave. Why did you decide to leave and what kind of firm did you think of starting?
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What do you mean when you say that the valuation given to private equity firms is lower than the valuation given to regular asset management firms?
What kind of legacy would you like in the philanthropic world and the business world?
So you're going to stay at Blackstone, not going to government, not going to go do anything else?

[1] Mergers and acquisitions.

DAVID M. RUBENSTEIN: Welcome everybody, members and guests of The Economic Club of Washington, welcome to our third event of our 29th season. I'm David Rubenstein, president of The Economic Club of Washington. Welcome today to this luncheon event in the Grand Ballroom of the Renaissance Washington DC Hotel, welcome to all.

Today we're very honored to have Steve Schwarzman, the chairman, CEO, and co-founder of The Blackstone Group, as our special guest. The Blackstone Group is now the largest alternative asset management firm in the world. It's a firm that today manages about $333 billion of assets under management. It's a firm that has about $82 billion, as of the end of the second quarter, of dry powder, which means money to invest; has a market capitalization of about $42 billion, and in the past 12 months gave back to its investors about $60 billion in distributions, and to its public unit holders over the past year about $4.2 billion.

Steve started this company with Pete Peterson in 1985. Prior to starting the company, Steve was the head of Global Mergers and Acquisitions at Lehman Brothers, a firm he had joined after graduating from Harvard Business School in 1972. He was one of the youngest partners ever at Lehman Brothers, became a partner at the age of 31. Prior to Harvard Business School, Steve was a graduate of Yale, graduated in the class of '69. And before that he had grown up in Philadelphia, graduated from the Abington High School in the Philadelphia area.

Steve is very involved in philanthropy. Many people in the Washington area know that he served for six years as the chairman of the Kennedy Center for the Performing Arts, and was extremely generous in that time to the Kennedy Center, and is still very generous to the Kennedy Center. But he has also made three other gifts that I think got worldwide attention. Let me just mention them.

One is, mostly recently, he gave $150 million to Yale, his *alma mater*, to create a cultural student center, which is going to reform and improve the way that the Yale students, undergraduates, react together and gather, and also learn more about the arts and performing arts. And I think it will be transformative at Yale. He also gave, earlier, $100 million to the New York Public Library. And in his honor, the New York Public Library main building has been named in his honor.

And in terms of things around the world, Steve has given $100 million as part of a $400 million gift – he's raised the other $300 million – to create the Schwarzman Scholars Program at Tsinghua University, which is a leading university in China where students from around the world will get a scholarship to become a Schwarzman Scholar, similar to the Rhodes Scholar program. And that program is now underway.

So that's pretty good for – [laughter] –

STEPHEN SCHWARZMAN: That's good for an intro. My mother would have been very happy with that. [Laughter.]

MR. RUBENSTEIN: So you're growing up in Philadelphia and you came from a middle-class background, would you say?

MR. SCHWARZMAN: Yeah, my dad and his father owned a retail store that sort of looked a little like Bed Bath & Beyond, except it was dramatically smaller. And we all started somewhere around 7 or 8 years old marking merchandise and, you know, smelling dust. And so that sort of makes you want to do nothing tangible. [Laughter.] And that's how both myself and my two brothers ended up in finance.

MR. RUBENSTEIN: So did you ever give your father ideas of how to improve the business, and did he ever accept any of them?

MR. SCHWARZMAN: Yeah, it was interesting. When I was 14, I said, you know, there are a lot of people in this store; maybe we can expand it nationally. And my father looked at me. He said, I don't know whether that's a good idea. So I said, well, let's at least expand it throughout Pennsylvania. And he said, I don't like that. I said, well, how about the Philadelphia area? [Laughter.] We can put a bunch of units all over Philadelphia. And he said, no, I don't want to do that.

So I said, Dad, you have all these people in this store. You've obviously got a good concept. Why don't you want to do this? And he said, because I'm happy the way I am. He said, I've got enough money to retire, to send all of you to college and graduate school. I've got two cars and a nice house in the suburbs. He said, what more could anybody want? I said, well, how about a unit everywhere in America? [Laughter.] And so I decided that maybe working at Schwarzman's Curtains and Linens was not my future. [Laughter.]

MR. RUBENSTEIN: Right.

MR. SCHWARZMAN: Right? But had we done that, you know, I think we would have been Bed Bath & Beyond because that was, like, 1960-something.

MR. RUBENSTEIN: But then there wouldn't be Blackstone, though.

MR. SCHWARZMAN: Yes, this is also true. [Laughter.] Then I'd be fixing up towels, which was my job at the time. [Laughter.]

MR. RUBENSTEIN: So when you went to Yale, did you think you would go into business for sure or did you...?

MR. SCHWARZMAN: No, I had no idea what I'd do after Yale, and it was a bit of a mystery. I mean, I just went to become educated and apparently that was like a full-time job from wherever I started, and it really changed my life.

And I had a variety of unsuccessful job interviews. They'd send these people to campus. And I had one company and they said, well, what do you want to do basically when you grow up? I said, I want to be a telephone switchboard. [Laughter.] And the person looked at me and they said, what are you talking about? I said, well, I want to get all these feeds that come in from the real world and then I want to twirl them around and something will come out and they'll route the right way. And he said, I don't think you're for us. [Laughter.] So that was sort of a failure.

Then they had the Pan American people come up. And that was a very high-prestige company at that time with those powder blue outfits and everything. [Laughter.] And so I was just meeting with a guy and I said, you know, you should really go into freight. He said, freight? We carry people. I said, well, you know, there's like a war on – Vietnam – and they obviously need stuff, and planes are sort of like just planes, and why don't you fill them up with something else and maybe you can make a lot more money? He said, well, we're Pan Am. We don't do things like that. And I said to myself, now, here's a company that's going to go bust if this is their representative, right – [laughter] – some narrow-minded –

MR. RUBENSTEIN: Have you seen any of these people since you interviewed with them? [Laughter.] Have they ever written you for a job?

MR. SCHWARZMAN: No, but their companies mostly don't exist now, David.

MR. RUBENSTEIN: So you graduated from Harvard Business School in 1972 –

MR. SCHWARZMAN: Yep.

MR. RUBENSTEIN: – and then you went to Lehman Brothers. In those days, Lehman Brothers was privately owned by the partnership, I guess it was.

MR. SCHWARZMAN: Yeah. Sure.

MR. RUBENSTEIN: So did you decide you wanted to be an M&A adviser? And how did you decide what you wanted to do at Lehman Brothers?

MR. SCHWARZMAN: Well, M&A didn't exist in 1972. It had existed in the '60s when everybody was basically buying everything. That was, you know, a conglomerate era where the more you bought, the higher your P/E multiple was, the more it enabled you to buy something that was cheaper and be earning.

So that was like a game that formed the great conglomerates of that era, whether it was ITT or Litten, whatever, and that all collapsed. And then the stocks all went down so they couldn't do that anymore and the M&A business stopped. And so I was very, very lucky that, at that point, investment banking was, like, miniature and we didn't have specialists. So basically it was like an old apprentice business where you did everything if you were in corporate finance.

So you were doing underwritings, you were doing private placements, you were doing rating agency presentations, you were doing road shows, you were analyzing which financings people should do. And so you had to do everything. And my generation, which I guess is sort of moving off the scene except for a few of us hanging on – you know, I'm one of those – [laughter] – you know, we all know that stuff and it helps you stay out of trouble.

But in the merger business – I got in it by accident. I had visited a company for some reason that I can't even remember called Tropicana. So if you like orange juice, this is your place. And so I was in Chicago working on something with a company called UOP, which was in the refining business and additives, and I got a phone call. It was on a Friday night – the end of the day; it wasn't Friday night; it was around 2:00, 3:00 in the afternoon Chicago time – from the president of Tropicana saying he wanted to hire me to advise them on the sale of their company, which was happening over the weekend.

So I guess there were only a few problems. One, I didn't have a ticket to, you know, like, wherever, Bradenton, Florida. But secondly, I had never done a merger. So we shouldn't let this stand in the way – [laughter] – of what became the second-biggest merger in the world in 1977. So I didn't arrive at this place until, like, 4:00 in the morning. And then I didn't realize that you should have gone to a different city. There were no taxi cabs. I was, like, waiting an hour for a taxi.

And, you know, I finally got to a place, didn't sleep, changed my clothes, went to the company and they gave me three different structures of an offer for – I think at that point it was, like, $488 million, which tells you how the world changes. And he said, the board meeting will be in a half-an-hour – [laughter] – and you're going to tell us what to do. And if you have ever really been frightened, I – [laughter] – I encourage you to, like, have this experience to be more frightened.

MR. RUBENSTEIN: Right.

MR. SCHWARZMAN: You know, I wasn't a partner. I was just like, I don't know, 28, 29 years old and there was nobody else there except me. And I had never been to a board meeting of anything, OK? [Laughter.]

So I go into this board meeting. What I did is I frantically tried to call somebody who knew what they were doing at the firm. [Laughter.] I mean, you know, this is like liability. And I realized – what was it— it was the phone is always on the wife's side of the bed, because I was, like, waking people up at 7:00 in the morning after they gave me this thing, and it was always the wife – you know, hand it to the husband. And I'd explain what's going on to a partner of the firm, saying, what the hell do I do with this thing?

So they gave me a little coaching. And I went into the room and there was a bunch of somber people and two tape recorders and a stenographer. I mean, this is, like, really horrible. [Laughter.] And so, you know, then I started talking to them about which alternative would make sense, what the advantages were, whatever. And the guy says something like, thanks for the lesson; what do you think we should do? And so I told him which way to go and then we had a negotiated merger agreement. I'd never seen a merger agreement. So, you know, I'm, like, locked up.

And I got home at – it was the same snowstorm that was delaying me going to Florida. I got home at, like, 3:00 in the morning. I was, like, completely traumatized. We signed this thing, right? And, you know, it was like some huge thing. There was nobody else involved really except me from our firm. And I remember – I don't drink but I put a fire on in the fireplace and – you know, this is like out of a bad "Saturday Night Live" skit, right? I had a brandy snifter of Courvoisier and I had this – and I was sitting there looking at the fire and I put the Bee Gees on, Saturday – you know? [Laughter.] It says Saturday Night – you know, "Saturday Night Fever" album, number-one seller. And I just sat there saying, what the hell did I just do? What the hell just happened to me?

And, you know, that was sort of – I guess the sort of – we all have these, like, mini launches of our respective careers, some good piece of law that we did.

MR. RUBENSTEIN: Did the deal work out?

MR. SCHWARZMAN: It sort of worked out. Yeah, it worked out.

MR. RUBENSTEIN: So you became, like, the John Travolta for your firm. [Laughter, applause.] You must have been a rock star when you got the deal done, right?

MR. SCHWARZMAN: Well, but I didn't have the paint can, so, you know. [Laughter.]

MR. RUBENSTEIN: So you're doing M&A, you become the global head of M&A for Lehman Brothers, and then in 1985 you decide, with Pete Peterson, to leave. Why did you decide to leave and what kind of firm did you think of starting?

MR. SCHWARZMAN: Well, it became easier. Pete was thrown out so that – [laughter] – he left in '84. And then the firm – and it's a good lesson to everybody – you know, had a control problem and there was some stuff going on that was not according to risk tolerances, and the firm was basically busted. And so I sold the firm over the weekend to my next-door neighbor, who was in charge of a firm called Shearson.

MR. RUBENSTEIN: You sold Lehman to Shearson?

MR. SCHWARZMAN: Yeah. And, you know, that was owned by American Express. So that was an across-the-driveway deal. It was a really traumatic thing for a company that was 150 years old just to – like, you know, we would have opened and there would have been no net worth, right, on a mark-to-market basis. So the question was, could you keep that secret for a day or two and get a deal done? So it was a ridiculous outcome for a great, great –

MR. RUBENSTEIN: So you left the firm then?

MR. SCHWARZMAN: No, I left a year later and we started Blackstone.

MR. RUBENSTEIN: And where did the name Blackstone come from?

MR. SCHWARZMAN: My ex-father-in-law, who was a Talmudic scholar. And we were really struggling with a name. It was really hard. I don't know why. And –

MR. RUBENSTEIN: You didn't want to try Peterson Schwarzman or Schwarzman Peterson or –

MR. SCHWARZMAN: He didn't want to do that because he had started some other business that didn't work out, so he didn't want his name like that. And he said – he said, what we ought to do is get an impersonal kind of name where we don't have to worry, like a law firm, when the next partner joins, where you end up with 15 names on the door and if somebody doesn't get their name on the door they don't join or they're angry, or whatever; you've got two classes of citizens. So he said, let's just have a generic name.

So we sort of struggled on that. And Pete's wife, Joan Cooney, is a very gifted person. And so Joan said, look, this name thing is really – you guys are ridiculous. And she said, we struggled on a name too and – when I started my company, and so I came up with this unbelievably stupid, meaningless name called "Sesame Street." And it means nothing until you're successful. So she said – she said, here's the deal: Pick a name, any name. If you're successful, everybody will know it. If you're not successful, everyone will forget it. So don't agonize over it; just do something.

And so I was talking to my step-father-in-law, actually, and he said, well, look, why don't you take, you know, the German of your last name – "schwarz" in German means black – and your partner is Greek and "petros" means rock or stone. And his original name was Petropolis – not his, his father's. And he said, just put them together. So I said, OK, what the hell. So that's what we did. The only people who figured this out, interesting, are all from Oxford. [Laughter.] Apparently they really study languages and they have – so sometimes, though – I've probably had seven people who figured it out.

MR. RUBENSTEIN: So you got the name. And how much money did you have to capitalize the firm?

MR. SCHWARZMAN: $200,000 from me and $200,000 from Pete.

MR. RUBENSTEIN: So $400,000.

MR. SCHWARZMAN: Yeah.

MR. RUBENSTEIN: And your business was to advise companies or to make principal investments?

MR. SCHWARZMAN: For those of you who are in the business community – which are a bunch out here, I think – if you want to have a successful business, I think what I call it, you need a worthy fantasy. In other words, you're not supposed to be doing what somebody else is doing. They're already doing it. The world doesn't need you. You think they need you. They don't need you, right? You've got to do something different, not just a me-too thing.

So we struggled for, you know, sort of probably four or five months. Every day we'd sit around. This is really hard work. It's like being in Hollywood or something, coming up with a script. And we basically said, OK, we want to do three things. First, we want to go into the M&A business because we know it. It needs no capital. Big cash flow. We use the money to do other things.

Secondly, we wanted to be in the private equity business. It's now called private equity. It used to be called LBOs. Why? Because it's a wonderful business, right? You can aggregate a lot of capital. You have management fees so you don't have to worry that your year is going to end. Unfortunately, like in the M&A business, if you don't get anybody to hire you and you don't have anything happen, there's nothing to eat.

And then third, finance was evolving. Little companies like Lehman Brothers – which, when I joined, had 550 people; when it died in 2008 had 30,000. So the difference in working at a company of 550, where you know everybody basically by sight, and 30,000 is like so, like, different that I like the smaller feeling, and the communication and the partnership feeling. And so we basically said, what we do is our third part of our company is wait for some amazing opportunities and go into those businesses if we can make a lot of money for customers, give them a great experience.

And then to do that we had two other rules. First, you had to attract someone to run that business who was a 10 on a scale of 10. Nine is not good enough and eights – you know, most people think eights are good. You know, eights are just serviceable in our industry. And 10s, they just make things happen. If the world's bad, they find a way to make money. If the world is good, they make a fortune. They're charismatic. They hire people. They've got great taste. They've got high ethics. So you need a 10. And the third piece is to have whatever new business you start generate intellectual capital so that your first business or your second business is stronger with the addition of this new business.

So that was a letter that we sent out to everybody saying: Hi, it's us. Here's our wonderful plan. You should really do business with us. So this was really a fantastic strategy. And after we sent out the letters, nothing happened. [Laughter.]

MR. RUBENSTEIN: So you went into the business of raising a fund. You tried to raise a first fund. How hard was it to raise your first private equity fund?

MR. SCHWARZMAN: I think if you like pain and suffering, it was really terrific. [Laughter.] Now, imagine this – it couldn't happen today: Two individuals, neither of whom had ever made an investment, announced that they wanted to raise the third-biggest private equity firm in history, and massively larger than any other first-time fund. So only two demented people would actually think they'd get a good reception, right?

So we just started out. We made an announcement that that's what we were doing and then we went out into the world of endless rejection. And I encourage you to do that sometimes, because if you ever had an ego it's like, you know, the sandpaper. You have nothing left by the end. And you make every elementary mistake you can make, which is you start with your closest relationships first, where you barely even know what you're marketing, and you go to them and say, oh, please rescue me. And they say, well, what's the answer to these 15 questions? You don't even know the answers. And so then they reject you.

So you burn up everybody who you might have gotten because you're so stupid – [laugher] – that they go away. And it took until our 18th person – we mailed 488 documents. It took until number 18 until we got –

MR. RUBENSTEIN: You ultimately raised $750 million for your first fund?

MR. SCHWARZMAN: No, it was $850 million.

MR. RUBENSTEIN: $850 million, OK.

MR. SCHWARZMAN: We said we were going to raise a billion. Dare to be great. And then one of those investors came back a year later, gave us another $100 million. So I sort of felt, you know, it's not a perfect grade, but $950 million for people who really don't know what they're doing, but – [laughter] – you know, is sort of –

MR. RUBENSTEIN: So at that point you were in the private equity business.

MR. SCHWARZMAN: Yes.

MR. RUBENSTEIN: But your firm now, let's say, has four parts: private equity –

MR. SCHWARZMAN: Yep.

MR. RUBENSTEIN: – credit –

MR. SCHWARZMAN: Yep.

MR. RUBENSTEIN: – hedge fund of funds and fund of funds, and real assets and real estate.

MR. SCHWARZMAN: Yeah.

MR. RUBENSTEIN: So let's talk about each of them for a moment.

MR. SCHWARZMAN: Sure.

MR. RUBENSTEIN: You are the biggest owner of real estate assets now – Blackstone is – in the world.

MR. SCHWARZMAN: Yes.

MR. RUBENSTEIN: You've built a very big business. How did you go from no real estate expertise to the biggest real estate owner and manager in the world?

MR. SCHWARZMAN: Well, it was interesting. It came out of Washington. There was a guy here, who many, many people will know, named Joe Robert, who was a real character. Joe's passed away, unfortunately. But he came to visit us. He knew one of our partners. This is after the RTC[2] was created and real estate had collapsed in 1990 and '91.

So Joe comes in the office. And he's sort of a tall guy and sort of assertive. And, you know, I said, well, what do you do? And he said, well, I'm a consultant for the RTC and what I'm doing is I'm selling real estate. I said, well, I don't know much about real estate but I've read in the newspaper nobody's buying any real estate. There's no credit. The whole country's stopped. He said, well, that's interesting; I'm actually selling it and I would know if I were selling it because I'm selling it.

And I said, well, what are you selling? He said, I'm selling, you know, sort of $5 million to $10 million properties to doctors and dentists all over the country. And they have the credibility to go to their bank and borrow the money and so I'm moving a lot of stuff. I said, really? So I said, so why are you here? He said, well, I'd like to buy the stuff I'm selling, in fact, and I don't have any money. I said, well, I've got money but I have no knowledge or expertise, so maybe we're a perfect match.

And so he said, well, let's bid on the second RTC auction, which was a bunch of garden apartments in Little Rock, Arkansas. So, OK. So the stuff comes in. And these apartment buildings are less than five years old and they're 80 percent occupied and they have a certain cash flow coming off of them. So I was faced with the problem of what do

[2] The Resolution Trust Corporation (RTC) was a temporary federal agency established under the Financial Institutions Reform, Recovery and Enforcement Act (FIRREA), enacted on Aug. 9, 1989, to resolve the savings and loan (S&L) crisis of the 1980s.

you pay for real estate, which I had no idea of. So I said, OK, well, if I can get a 16 percent unleveraged yield off of this real estate, that sounds pretty good to me. In our trade that's like six times EBITDA[3], less cash flow, less your capital expenditures.

So I said, 16 percent, that sounds good. I like 16 percent. If we put some leverage on it, we'd make it 23 percent. So 23 percent is better than 16 percent. And then when you come out of a recession, those other 20 percent of the vacant units will get filled, and then that's like a 45 percent compound return. And then rents will go up so that will make it 55 percent compounded. So I sort of looked at this, and that's what we bid. And we won, OK? We won this thing – very frightening. [Laughter.]

So then I realized there was a whole country full that you could buy, because there were no other buyers because everybody in the real estate business was hated by their banks because they were losing money from them. So we started buying. And, you know, we have a terrific group of people. We hired a fellow named John Schreiber, who's – you know, I'm a little older than David – actually I'm a bunch older than David, although my hair is not quite that white. [Laughter.] But he may have a little more – may have a little more.

MR. RUBENSTEIN: Not for long.

MR. SCHWARZMAN: But Schreiber's a terrific guy. He was probably the best buyer of real estate in the 1980s. He picked the top. He sold out. And so we spent a year –

MR. RUBENSTEIN: Right.

MR. SCHWARZMAN: – because Joe was stolen by Goldman Sachs, who brought a table today. [Laughter.] You know, so he went to work and we had nobody. And then we found John.

MR. RUBENSTEIN: So your business is booming in real estate. Let's talk about another business. You are the largest operator of what's called a hedge fund of funds in the world.

MR. SCHWARZMAN: Yeah.

MR. RUBENSTEIN: Explain what a hedge fund of funds is and how you got into that, kind of through a back door, you might say. You made your own money.

MR. SCHWARZMAN: Yeah, well, we – you know, finance doesn't require, you know, like, enormous innovation. So what happened is when we got that extra $100 million from this Japanese investor, they wanted it paid back in seven years. So we had money for seven years. So the problem with having it for seven years with the maturity is you

[3] The accounting technique EBITDA — earnings before interest, taxes, depreciation, and amortization — is an important standard measure of profitability.

actually do have to pay it back, which means you can't lose it, right? So we wanted that money to generate earnings so we could expand the firm.

So the same fellow who found Joe Robert came into my office and he said, I've got an interesting thing we can do with the money, since we didn't know what to do with the money but we wanted to earn a lot. He said, there's a friend of mine you ought to meet named Julian Robertson. And I didn't know who Julian Robertson was, but as it works out he was the best hedge fund manager in the world for about 20 years. So this was a good person to meet.

So he came in. And he's from, I think, North Carolina, and he's got this charm and, you know, he's so smart and this and that. I just gave him all the money. [Laughter.] So, so much for finance where you're told to diversify risk and do all this stuff. I mean, you know, the guy's had the best record in the world. I mean, how bad can he be? So he was great and that generated us money.

Then what happened is – and this is the innovation part of finance – somebody says to you, who's a client, what do you do with your money? You seem to work 14 hours a day. Do you have any time to invest your money? You say, of course not. We just put it in this thing, right, with Julian, and then we diversify it away from Julian. And they said, well, can we give you money too? This is innovation – [laughter] – when you basically say – when people offer you money, it's usually a good thing to take it, and you figure out what you can do with it, right?

So we said, sure, we'll take your money. And we built a whole business and it's now the biggest in the world. It's about $65 billion, where we give money out to other managers. We also do some directly ourselves. And we have different packages. You know, if you want to be in sort of energy stuff, we can do a special energy thing. We can do sort of a more general long/short equity stuff. We can do bond stuff. So we create a family of things to suit the needs of an investor.

MR. RUBENSTEIN: So in the private equity world, what is the deal you did that you're the most proud of and what is the deal that got away that you wish you had done?

MR. SCHWARZMAN: Well, since I'm in Washington we can get a Washington story. It was our first deal, actually, before we even raised our first fund. Actually, no, it was with the first fund. And we bought a set of assets from USX – it was called United States Steel – all their railroads and barge lines and so forth. It was a very stable business. It doesn't matter what the price of steel is, a steel company will always produce to cover its overhead if it could.

And we bought it right in the middle of a strike. Nobody in the world wanted this thing. We almost couldn't get it financed because they just assumed if the earnings went down because there was a strike, the strike would never be settled. People can be very stupid, you know. You know, like U.S. Steel, the number-one company, is never going to settle a strike. I looked at it and said, yeah, of course they're going to settle the strike.

I don't know when, but it doesn't matter particularly. And then when they finish the strike, the production will go up. And this business just made money based on production.

So we had made one other investment before. We sold a company to a guy named Mitt Romney. You may have heard of him. [Laughter.] And after the deal was closed, I asked the chairman whether we could invest in that deal. Was that a problem for him from a conflict point of view, because we had no discussions about it; I just saw that it would be a good thing. So he said, no, I don't have a problem. So we made 16 times our money on the Mitt Romney deal. So I felt I owed Mitt, so I invited him into our U.S. Steel deal, which was 24 times your money. And that's how I ended up on the Mitt Romney finance committee, right? [Laughter.]

MR. RUBENSTEIN: I thought the deal you had mentioned –

MR. SCHWARZMAN: This is like – these are like – this has got good karma, right, 16 times, 24 times. And, you know, he's –

MR. RUBENSTEIN: Well, those are good deals, but there's one I thought you had mentioned that actually became the most profitable buyout of all time called Hilton.

MR. SCHWARZMAN: Well, that's also Washington.

MR. RUBENSTEIN: Describe how you bought it, then you fixed it a bit, and then it ultimately turned out to be a profit of $10 billion to $13 billion, or something.

MR. SCHWARZMAN: Yeah. Well, Hilton was a company that actually was taken apart. You know, we bought it, what, five years ago? Actually, we bought it – we committed on the deal – I think it was, July 7th, 2007, is when we committed, right before credit started constricting. And before that, probably 20 years before that, they separated their international business and it was a completely independent company in London. And they forgot to expand. I don't know how you forget to expand a company, but apparently these people decided, let's never expand – very interesting strategy – which resulted in a very low stock price, not a surprise.

And so I guess it was a year or two before we looked at buying Hilton, they put these two big companies together. So we paid a high price, knowingly, for the business. I think it was $27 billion. And the business was making, at that time, $1.7 billion in profit. But we looked at it not as if it had $1.7 billion. We thought it had $2.7 billion. And the reason we thought it had $2.7 billion is because they were running their U.S. business, which is in four different lines, with, like, huge overhead duplication – they had never consolidated the business. And in terms of expansion, they had never expanded internationally. They had a great name, number-one name in consumer recognition, no new hotels.

So we realized we could generate $500 million from the consolidation and another $500 million just by opening some hotels and being managers. So this was like we were buying $2.7 billion, So when the recession came, our $1.7 billion had already grown to $1.9 billion. And it went down to $1.4 billion and the whole world thought we were going to go bankrupt. I couldn't understand it because I knew we were really earning $2.7 billion. You just couldn't see it yet. And so, you know, we ended up buying some dead-end stuff when it got low, and then of course, you know, it's back to our original numbers. And I guess we've made, like, $12 billion. So that was good.

MR. RUBENSTEIN: There aren't that many buyouts that make $12 billion.

MR. SCHWARZMAN: That was good.

MR. RUBENSTEIN: That was a good one.

MR. SCHWARZMAN: But the one that I missed – this is the real Bozo element. David and I make mistakes, and financial accounting works incorrectly. As Warren Buffet would say, they only measure what you do; they don't measure what you could have done that you didn't do. That's the real way to measure success. So, you know, David's missed one or two big ones. And this one was, like, really, retrospectively, so stupid. But I would have, unfortunately, made the same decision. That's what makes it so terrible.

But I was approached by a guy you may have heard of named Mike Bloomberg when he had a little company. And he needed $100 million to expand the business. And Mike had one outside director who was sort of like my mentor at Lehman Brothers and, you know, a guy I talked to every night at home. He was so brilliant, so brilliant. I mean, he saw everything differently. It was always – we all had the same facts. He could get one piece of it and look at it a different way. He was really fantastic.

So Mike said, he should get the money from us, from me – because Steve thought I was gifted, which means Steve isn't perfect. [Laughter.] So Mike comes over and he says, you know, I've got this company and, you know, how would you like to put in, you know, like, $100 million? I think it was for 20 percent of the company. And I said, it sounds like a great idea. You know, I knew Mike a bit socially and he's very talented and driven and creative. And he's "the" Mike Bloomberg, right? I mean, we all know now who Mike Bloomberg is. So I said, yeah, I'm good to go with this. This sounds like a great idea.

He said, look, there's only one catch. He said, I want you to be my partner but I want you to really be my partner. I said, what does that mean? He says, well, you can't, like, sell this, because I'm never going to sell my company. I said, well, I'm managing money and the problem is, you know, the terms of it are that we raise these funds and then we have to sell it and give people their profits and give their money back. Then it was sort of a silly structure. You'd go back to the same people; they give you the same money again. And all you do is you learn how to be a mendicant. [Laughter.]

But he said, well, that doesn't work for me. I'm not in the business of giving you liquidity; I'm in the business of building my company. And I don't want to start thinking about you leaving when I just said hello. He said, that doesn't work for me. I said, well, it really doesn't work for me, but I've got these restrictions. I can't just wait and then see if you change your mind. He said, well, really, that's just like – he said, it just doesn't work. And so Mike left. OK, fast-forward, right? That $100 million would today be probably $8 billion.

MR. RUBENSTEIN: Right.

MR. SCHWARZMAN: So if you want to make mistakes – [laughter] – this is how you make them.

MR. RUBENSTEIN: So, Steve, your company is doing very well and all of a sudden you decide to take it public. Most people have said private equity firms should stay private because there might be a conflict between investors in the funds and shareholders. Why did you decide to take it public, and do you have any regrets?

MR. SCHWARZMAN: Well, we took it public – I had a partner who was 21 years older than me. He was getting old, and if we didn't he would have been redeemed at book value, which was nothing. And as it worked out, he got a few billion dollars. So this is like a moral thing. You know, we started the business together and so there should be a way for him to benefit from that.

Secondly, I had this bad sense about where we were at that time in history, and I had this desire for permanent capital. I just felt something bad was going to happen. Actually, I was on a panel with Bill Conway, I think in this room, and we were both talking about how we had a lower cost of capital than AAA companies. Well, you know something's wrong with that. That can't be. And so the markets were peaking, and I just wanted to be prepared for the "nuclear winter." I just wanted to have loads of money, you know, to take us through anything that was happening. I also thought it would be good for my children and grandchildren, right, so that's a good thing for them.

MR. RUBENSTEIN: You have seven grandchildren now?

MR. SCHWARZMAN: Yeah, I've got to work harder. [Laughter.]

MR. RUBENSTEIN: So you took it public. It went very well.

MR. SCHWARZMAN: Also one other thing, David. I thought it would be a great branding moment for the firm, make people want to do more business with us, whether it's investors or not. And then I thought there would be an X factor, some crazy thing that would happen. I didn't know what it was. I found out there were a number of crazy things, but one of the good crazy things is we got a phone call that two people from China wanted to meet with one of my partners. And, you know, I barely knew my guy in

China. We'd just hired him three months earlier, Anthony Leung, who's a terrific guy and used to be the financial secretary of Hong Kong, which is their treasury secretary.

And so they had a meeting with Anthony and they offered us $3 billion to be in the IPO. Well, this was China. China had never given money to anybody since World War II for equity outside of China. They had state-owned enterprises in China, but they didn't do this stuff outside. So I was watching "Law & Order" and reading my stuff, which is what I do at night when we're not out someplace – my wife and I are out. And I sort of was only half listening. I said, $3 billion? OK. So he said, yes, $3 billion.

So I said, well, who are these people? He said, they're both unemployed. [Laughter.] I said, really? I said, where did they make their money? He said, well, they were government officials. [Laughter.] I said, two government officials who are unemployed are giving us $3 billion. I said, how does that work? I said, where did they used to work? He said, well, one of them was the deputy head of the central bank and the other one was the deputy finance minister. I said, so why did they lose their jobs? He said, well, they're being reassigned. I said, reassigned to what? He said, well, the rumor is they're going to start a sovereign fund in China and these two people are going to be in charge of it. So, you know, I talked about – you know, so I said, let me think about this.

So I went back to work. I talked to my partner, Tony James, who's president of the firm. I said, Tony, what do you think we ought to do with this strange call? He said, take the money. [Laughter.] And I said – I said, well, we don't really need that much money. He said, well, we can split it up. We'll do some more secondary; we'll put more in the firm. And I said, well, I don't know who these people are and it makes me nervous, so why don't we go back and tell them that, you know, they have to vote with us. I don't want to have people who are strangers. And, you know, if they want to sell the stock – they own so much – make them wait, you know, like five years and then they can sell it, a third, a third, a third.

So we went back to Anthony, who was dealing with these people. And the next night I'm still watching "Law & Order." You could do that the rest of your life, by the way. [Laughter.] I mean, there's just so many reruns. And, you know, they said they don't want to do five years, they want to do three years, but they really don't want to vote with us. It's a little cumbersome. Why don't they just not vote? So then I realized I like these people. [Laughter.] This is good. Washington people vote a lot, you know. I don't like that. In our little world, you know, these people not voting makes –

MR. RUBENSTEIN: So it worked out. They came in.

MR. SCHWARZMAN: Yeah, they came in. And, by the way – because a number of people here touch government – we did this whole negotiation with that guy who was dealing with the premier of the country. We negotiated and signed it in 10 days. For those of you have ever been in government, the idea that anything happens in 10 days is, like, a mystery, right? This is from first contact to signed deal. I mean, this is like – when these people want to do something, get out of the way. They know how to do it.

And it's very – and when they don't want to do something, of course then you experience reality. But it's really –

MR. RUBENSTEIN: So in the end you were very happy you went public –

MR. SCHWARZMAN: Yeah.

MR. RUBENSTEIN: – though at one point your stock went way down and now it's come back a fair bit.

MR. SCHWARZMAN: Yep. It's no fun when these things go down. It's much better when they go up.

MR. RUBENSTEIN: So you have been very vocal in saying that the valuation given to private equity firms is lower than the valuation given to regular asset management firms. And could you explain what you mean by that?

MR. SCHWARZMAN: That's because David and I are bad salespeople – [laughter] – apparently. For some reason, what happens in our type of business is, you buy something – say you buy a company, you buy real estate, something – and you always have a plan to fix it up. So you fix it up and then it grows faster than regular companies. Our companies now, just on that side of our business, they are growing about 50 percent faster than the economy. So this would be viewed as a good thing, right?

And then you put some borrowings against it, so the price earnings multiple usually goes up when you grow faster. And then if you have debt on top of it, you've invested less equity than you would have. So that little third-grade numerical equation creates a higher rate of return. And then you pick the time you sell it. And so you make very high returns on these types of investments with almost no losses – sort of amazing business.

For some reason, the fact that you only sell when it's a good time to sell instead of, like, you know, sort of selling to make the earnings flow even – you know, some people say, well, geez, that magic trick will never happen again. And that's ridiculous. It's only been happening for 30 years, right? Why is it going to stop this week because somebody is writing a magazine article or something? They don't understand. We explain it. It keeps happening.

And because of that and the cash flow not being exactly the same all the time – you know, our investments -- hard to believe, right? They're sort of – we grow it like double the stock market. That's what we deliver. This is why people give you money. Some people try and get money anyhow, but if you grow it double the stock market for 30 years it's, like, a good thing. I don't understand why markets, David – maybe I should ask you the question. David, why do you think? [Laughter.]

MR. RUBENSTEIN: I don't know the answer, but tell me this, Steve – in the time we have left, a couple of questions: One, now that you have reached the pinnacle of the financial world – you are obviously very successful, your company is extremely successful, you have made a great deal of wealth – what is it that you want to do with this great wealth? You've obviously given away a lot of money. Do you have plans to do other things? How does somebody get $100 million out of – you've made $300 million plus gifts. I assume you've got some more coming. Maybe you want to announce some today, but – [laughter] –

MR. SCHWARZMAN: Next week.

MR. RUBENSTEIN: Next week, OK. So how do you decide? Everybody must be calling you saying, oh, you just gave $100 million here; why don't you give me $100 million? And how do you decide what to do with your money? And what kind of legacy would you like in the philanthropic world and the business world?

MR. SCHWARZMAN: Well, those are great questions, and you only get them when you're older, typically.

And David faces the same question and really does an amazing job, you know, in terms of sort of supporting not just the Washington community in all kinds of ways but doing things all over the country, and has made a huge, huge impact, you know, around the United States, and chairing organizations, and not just giving his own money but, you know, getting other people to do things. It's really – you know, I don't know when this man sleeps. I mean I sleep five hours a night but he must be down to three. So it's –

MR. RUBENSTEIN: That's why my hair is so white.

MR. SCHWARZMAN: Yes, I see. [Laughter.]

MR. RUBENSTEIN: So what are you going to do with all this money, and what's your legacy going to be?

MR. SCHWARZMAN: But, you know, I think some of this stuff, it's evolving. In other words, if – I saw a survey on –one of these lists of – there was a Forbes 400 list or something, and I think it was 85 percent or 90 percent of the people are self-made on that list, and 85 percent of them still think they're middle class. In other words, that's why they keep going. They don't realize there's been some, you know, shift, at least to the outside world. And so, you know, that's the majority of Americans who were successful like that.

So it takes a while to realize that you actually have, you know, really large surplus assets because your job is still to build them. If you are in the business world, you're trying to make your company good, and what comes along with that is the concept of, you know, more happens for your shareholders if you're a shareholder, which I am a substantial size, then there's more.

So I think, like a lot of life, it's a function of what interests you. I believe that, without the kind of educational intervention that happened in my life, whether it was my high school, whether it was Yale, or whether it was Harvard Business School, you know, I'd probably have a really great group of, you know, hair salons or something like that. And, you know, I would have been successful on one level but not what I did.

So the richness of my life in the broadest sense, not financially, was really fashioned by whatever I brought to the table, but by all these wonderful external influences. And so I have real interest in helping other people get those opportunities, because if you don't get them, particularly in a globalized world, you don't have really good opportunity, or you have a much more modest opportunity to do well.

So I like supporting educational things. I also like making change. That's a problem for me, because this Schwarzman Scholars thing, I mean, it's – I mean, forget the money. I mean, the amount of time I spend to make this wonderful and make it the best program that you could do in the world and – because when I do something, I'm all in. I'm not a diversified kind of person like that. And so I've taken this on. And, you know, raising another few hundred million, you know, sort of person by person, that's not the easiest thing to do. I'm used to getting almost 100 percent sales response at Blackstone. This is, you know, philanthropic, and some people don't care about China, and some people don't care about, you know, the safety of the world.

So I'm busy doing that, but that takes a lot of time. So one of the challenges for me is to figure out, over time, how many major things can I take on to build and change, as opposed to just giving somebody money who's doing something? I tend to like creating things.

MR. RUBENSTEIN: So at this point in your life, you're like your father. You've reached happiness. You're really happy.

MR. SCHWARZMAN: Yeah, I'm really happy, absolutely. I still have enormous drive. I mean, I love what I do and I love our firm.

MR. RUBENSTEIN: And you're going to stay at Blackstone. You're not going to government. You're not going to go do anything else. This is what you're going to be doing for the next....

MR. SCHWARZMAN: Well, I like and respect what the people in government do, and any way that I can be helpful, you know, to the United States and to helping the country get on the right track, I mean, that's really a core motive that I have. I don't have, you know, sort of some kind of narcissistic need for doing something.

I like being helpful in crises. I helped Hank[4] out a lot during the financial crisis. Boy, that was really fun! If you're a financial person, I mean, the idea of trying to help – you know, like, intervene, to come up with solutions to save the world, wow, what a test! How terrific! And there was a great team in the government working on it. There were a number of kibitzers on the outside coming up with ideas. I mean, that was, like, a moment. I was just in China talking to their people two weeks ago. You know, things haven't gone exactly as anticipated there.

And so when you can intervene and help people like this – I mean, I'm not trying to be anything, David. I'm, like, just trying to be helpful. That's –

MR. RUBENSTEIN: All right, well, you've done a great job. And I want to thank you for coming this afternoon and for your success. [Applause.]

MR. SCHWARZMAN: Thank you.

MR. RUBENSTEIN: Let me give you a gift, on behalf of the members of The Economic Club of Washington, a gift, a replica of the original map of the District of Columbia.

MR. SCHWARZMAN: Well, that's very nice. I was looking for the Magna Carta but, you know, still – [laughter] –

MR. RUBENSTEIN: All right. Thank you. [Applause.]

MR. SCHWARZMAN: You know, one thing I'd say – I was chairman of the Kennedy Center, and we had to pick a successor and David was among those candidates. And the same way David says, I'm going to a Carlyle meeting after this; what am I doing interviewing Steve Schwarzman, when there was a choice to pick somebody, David was the obvious choice. And I did that with enormous enthusiasm, because he's got so much energy, so much drive, good intention, and he doesn't like failing. And I thought the Kennedy Center would be in great hands with David in charge, and look how it's worked out. It's magnificent. So my hat is off to David.

MR. RUBENSTEIN: Thank you.

MR. SCHWARZMAN: He has done a marvelous job. [Applause.]

MR. RUBENSTEIN: Thanks very much. Thank you. [Applause.]

Stephen A. Schwarzman

[4] Henry Paulson, former Secretary of the Treasury during the Administration of President George W. Bush.. Henry Merritt Paulson, Jr., is an American banker who served as the 74th Secretary of the Treasury. He had served as the chairman and CEO of Goldman Sachs.

Stephen A. Schwarzman is Chairman, CEO, and Co-Founder of The Blackstone Group. Mr. Schwarzman has been involved in all phases of the firm's development since its founding in 1985. The firm is a leading global asset manager with $333 billion in Assets Under Management, as of June 30, 2015.

Mr. Schwarzman is an active philanthropist with a history of supporting education and schools. Whether in business or in philanthropy, he has always attempted to tackle big problems and find transformative solutions. In 2015, Mr. Schwarzman donated $100 million to Yale University for the establishment of a state-of-the-art campus center, the Schwarzman Center, by renovating the historic Commons and Memorial Hall. In 2013, he founded an international scholarship program, "Schwarzman Scholars," at Tsinghua University in Beijing to educate future leaders about China. With an endowment fundraising goal of $400 million, the program is modeled on the Rhodes Scholarship and is the single largest philanthropic effort in China's history coming largely from international donors. In 2007, Mr. Schwarzman donated $100 million to the New York Public Library, on whose board he serves.

Mr. Schwarzman is a member of The Council on Foreign Relations, The Business Council, The Business Roundtable, The International Business Council of the World Economic Forum, and the Berggruen Institute on Governance's 21st Century Council. He serves on the boards of The Asia Society, The Board of Directors of The New York City Partnership and The Advisory Board of the School of Economics and Management at Tsinghua University, Beijing. He is a Trustee of The Frick Collection in New York City and Chairman Emeritus of the Board of Directors of The John F. Kennedy Center for the Performing Arts. In 2007, Mr. Schwarzman was included in *TIME's* "100 Most Influential People." Mr. Schwarzman was awarded the Légion d'Honneur of France in 2007 and promoted to Officier in 2010.

Mr. Schwarzman holds a B.A. from Yale University and an M.B.A. from Harvard Business School. He has served as an adjunct professor at the Yale School of Management and on the Harvard Business School Board of Dean's Advisors.