

BLACKSTONE First Quarter 2017 Earnings Investor Call

April 20, 2017 at 11:00 a.m. ET

Weston Tucker: Good morning, and welcome to Blackstone's first-quarter conference call. I'm joined today by Steve Schwarzman, chairman and CEO; Tony James, president and chief operating officer; Michael Chae, our chief financial officer; and Joan Solotar, head of private wealth solutions and external relations. Earlier this morning we issued a press release and slide presentation which are available on our website. We expect to file our 10-Q in a few weeks. I'd like to remind you that today's call may include forward-looking statements which are uncertain and outside of the firm's control and may differ from actual results materially.

We do not undertake any duty to update these statements, and for a discussion of some of the risks that could affect results, please see the risk factor section of our 10-K. We'll also refer to non-GAAP measures in this call, and you'll find reconciliations in the press release on our website. Also note that nothing on this call constitutes an offer to sell or a solicitation of an offer to purchase an interest in any Blackstone fund. This audiocast is copyrighted material of Blackstone and may not be duplicated without consent.

So a quick recap of our results.

We reported GAAP net income of a billion dollars for the quarter, which is up sharply from the prior year comparable period. Economic net income, or ENI, per unit was \$0.82, which is more than two and a half times the prior quarter – prior year quarter – due to greater appreciation across the funds, as well as strong growth in fee-related earnings. Distributable earnings per unit was \$1.02 for the quarter, or about triple the prior year period. We declared a distribution of \$0.87 per common unit to be paid to holders of record as of May 1st. One final note from me: we'll be hosting our fifth BX Investor Day on June 8th in New York.

If you haven't already received a save-the-date e-mail, please follow up with me after call. The whole event will be webcast live with a replay available on the Blackstone website. And with that, I'll now turn the call over to Steve.

Steve Schwarzman: Good morning, and thank you for joining our call. Blackstone posted excellent results in the first quarter, as Weston mentioned – our second-best quarter ever for distributable earnings at \$1.02 per unit. Just a few pennies shy of our all-time record in early 2015. Realizations reached nearly \$17 billion in the quarter, our best ever. And although we were selling a lot, we're also investing a lot, with almost \$12 billion invested across the draw-down funds, our second-best quarter ever, adding to our foundation of future value. In fact, just in the past week we committed an additional \$2 billion to new deals in private equity, and that's just in one week.

ENI, as Weston mentioned, rose to \$0.82 per unit, with broad-based strong fund returns equating to our highest overall fund depreciation in several years. The corporate private equity funds appreciated nearly 7 percent in the quarter, while the real estate opportunity

funds were up nearly 6 percent on a growing base of invested assets. Over the past year these funds appreciated 15 percent, while our credit funds rose over 25 percent on a gross basis. Our liquid hedge fund solutions composite rose 10 percent on a gross basis, with much less volatility than the market, making it an industry outperformer as well. These types of returns are helping our limited partners dramatically exceed their targets on their allocations to Blackstone.

As a result, they keep rewarding us with more of their capital to manage. Pretty logical. Despite our high level of realizations in the quarter, our fee-earning AUM rose 15 percent year to year, to \$280 billion – another firm record, with strong positive growth in every business, as Tony mentioned earlier. Total AUM rose 7 percent to \$368 billion, also another record, which I guess starts to sound a little boring.

While this is clearly a strong set of results for one quarter, greater than that is the output of Blackstone's business model and our ability to drive substantial outperformance over time, beating any relevant index by a very wide margin.

In private equity, for example, our funds have outperformed the S&P 500 by approximately 700 basis points per year on a net basis after all fees since inception 30 years ago. In real estate, that outperformance is 900 basis points per year, versus the real estate index over 26 years. This long-term outperformance differentiates Blackstone in the market, and from almost all long-only money managers. It also positions us very well in a dramatically evolving industry, where capital flows are increasingly following a barbell distribution. On the one hand, investors are migrating towards low-fee, low-friction index funds, with well over \$1 trillion moving to index and exchange-traded funds in the last five years alone, largely at the expense of actively managed equity funds.

On the other side of the barbell are the alternative managers, which in the top quarter, like Blackstone, have historically delivered net returns well above benchmarks with limited downside. And Blackstone is regularly acknowledged by third parties as being at the top of this group. LPs know that the types of returns we generate over the long term can't be replicated in the public markets. Our investment solutions are highly customized, from the fund structures themselves to the way we create value with our portfolio operation experts and asset management capabilities.

In many cases, we're building companies from scratch. We're developing strategies to rapidly expand existing companies, including through acquisitions. This is much different than investing passively in public stocks. The resulting performance is differentiated and largely uncorrelated to most other assets. Our LPs understand the uniqueness of our asset class, so it is no surprise that demand for alternative products continues to increase. Blackstone is taking share of this growing wallet, having raised in the past three years \$224 billion, which is greater than the total size of any of our domestic alternative peers.

There's also an information advantage that comes with size, providing a critical underpinning to our performance. We are basically in the intellectual capital production business. Assuming that our people are equally as smart as the best-qualified investors in

the world, but have a more informed view, then logically we should be able to produce better results. As Blackstone grows larger, our access to information increases, and our returns benefit, which may seem counterintuitive, but as you can see, it happens to be true.

This ability to generate and evaluate information is a key structural advantage at Blackstone. In sustaining this advantage, it has become mandatory to have views on geopolitical events and decisions by governments, which are impacting the business environment to a greater degree than ever before. Senior business leaders globally are spending much more time today on the impact of elections, regulation, legislation, and other changes occurring in countries around the world which can have profound implications. When you also consider rapid technological advances, it's no longer "business as usual" virtually anywhere, about anything. We believe sustaining long-term success requires us to have an educated view on global issues, with enormous alertness to changing conditions. Blackstone's global portfolio provides a truly unique platform from which to learn.

Our portfolio now consists of nearly 150 companies where we hold control or significant influence, with a combined enterprise value of over \$400 billion. These companies employ approximately 600,000 people around the world, making us one of the five largest US-based employers. In fact, our portfolio companies employ as many people as some entire smaller countries in Europe and Asia. As one example, the Blackstone portfolio workforce equates to nearly one-third of the workforce of the entire country of Ireland, and one-fourth that of New Zealand.

Our real estate business is one of the largest private owners of real estate in the world – some might say the largest. We're the largest owner of hotels and offices globally, and the largest owner of logistics in Europe. Our credit business is one of the largest managers of leveraged loans in the world, and BAAM is the largest investor in hedge funds in the world, with almost 140 external managers. We oversee this expansive portfolio with nearly 1,000 investment professionals across 16 countries, plus all of our company management teams and operating partners. We leverage their combined insights and convert them into real decision-making power, ultimately driving better investment decisions, always with the first priority of protecting capital. With this remarkable knowledge base, our track record and our capability to invest basically anywhere in the world, it is reasonable that our market share should continue to increase within the fast-growing alternative sector, with concomitant growth in earnings and cash distributions for our shareholders.

We've demonstrated this type of growth consistently over time. It's not about one or two quarters' results, regardless of how strong they are, like they are in this quarter. For example, as Tony mentioned, over the past three years we will have distributed an average of \$2.50 of value per unit per year to our shareholders. That implies an average dividend yield of 8.3 percent based on today's stock price. Think about all the things that have happened in the world over the last three years, including the significant Chinese market volatility and the projected recession of China, which of course never happened;

the worst start for US equities on record in 2016; the Brexit surprising vote; and the unexpected US presidential election outcome.

Against that background, our shareholders, me being the largest one, still received a consistently high and growing payout of \$2.50 per year on average. Where else in global markets can you find this level of payout, with every reasonable expectation it's going to grow over time? I think it's pretty unique, particularly for a large-cap A+-rated company like Blackstone. The average company in the S&P has a dividend yield of 2 percent, and trades at around 20 times last year's earnings. Blackstone stock trades at 12 times, not 20 times, last year's earnings, with an 8 percent yield, not a 2 percent yield, over the last three years, as I mentioned.

That's despite having leading positions in all of our various businesses. Faster revenue and earnings growth, and a much higher payout – go figure. I don't think they teach that in *Graham and Dodd*. As most of you know, I've been racking my brain to make sense of this disconnect. If our shares were valued the same as the average S&P company based on dividend yield, the share price would be over \$100.00 a share, instead of \$30.00, where it now is.

If they were valued using the average PE multiple, the price would be over \$50.00. That's just math. In any case, this disconnect remains a mystery to me. I leave it to you to figure it out. Thank you for joining our call, and thank you for supporting us over the years. It's great to have you as shareholders and as intermediaries to shareholders. Now I'd like to turn it over to our chief financial officer, Michael Chae.

Michael Chae: Thanks, Steve, and good morning, everyone. Our first-quarter results represent a terrific start to 2017, with record or near-record quarters for most of our metrics, as Steve mentioned. Total revenue doubled year over year to \$1.9 billion, while economic net income rose over two and a half fold to \$986 million, both reaching their highest level in two years. Fee-related earnings rose 18 percent to \$291 million, helped by the first full quarter of management fees for our \$19 billion BCP VII fund. Distributable earnings more than tripled to \$1.2 billion dollars, or \$1.02 per unit.

On last quarter's call, we pointed to at least \$0.60 per unit in DE from sales that were either already closed or were signed and would close over the subsequent months. We delivered on this, and more. Indeed, all of these previously-discussed pending transactions closed in the first quarter on or ahead of schedule, including the Hilton stake sale, the transaction involving Change Healthcare, and the sales of Optiv, Pactera, and our Japan residential portfolio. Subsequently in the quarter we were able to opportunistically sell down additional public stock positions, which together drove the distributable earnings from realizations up to \$0.82 per unit. Combined with growing FRE, the result was our second-best quarter for distributable earnings and the dividend.

From a capital metrics perspective, first-quarter results demonstrated continued robust momentum in each of the major drivers: realizations, deployment, investment

performance, and AUM growth. Further to that, the consistency of the momentum across each of our business lines highlights the firm's unique diversity and leadership position.

First, with respect to realizations, we generated \$16.6 billion in the first quarter, a firm record. The majority of that amount came from our BREP and BCP funds at an average multiple of original invested capital of 2.6 times. The realizations in the quarter from these funds derive from over 30 discrete sales transactions around the world, highlighting the scope of our platform, with sales diversified across region, asset class, and vintage.

Total realizations for the past 12 months rose to nearly \$50 billion, our second highest for any 12-month period. And while we're clearly pleased with this execution, our pipeline of future sales remains quite strong.

Second, investment activity. We deploy nearly \$12 billion in the quarter, closing several large, previously-discussed transactions in private equity, including TeamHealth in our BCP VII fund; Gavilan Resources in our energy private equity area; and SESAC, the music rights company, in our longer-dated new core private equity strategy. GSO also deployed \$2.3 billion in the quarter, their second highest ever, with a focus on European direct lending and energy. In real estate, we're continuing to find things to invest in and scale, with recent emphasis on core-plus and European opportunistic deals.

And our tactical opportunities and strategic partners businesses together invested over \$1 billion in the quarter. It's worth mentioning that those two strategies have grown to a combined \$38 billion in AUM, and have expanded well beyond the original mandates to multiple strategies and fund structures.

Taken together, this activity reflects not just the firms, but our individual businesses' ability to leverage multiple pools of capital with varying mandates, to address the whole market from a sourcing standpoint, and then to identify and go where the value is against a generally challenging and expensive backdrop. This was highlighted well again in our private equity business with our announcements this week, as Steve mentioned, of acquisitions of EagleClaw Midstream off of our energy platform, and Ascend Learning, our second deal in four months by our new core strategy, with these two deals together involving over \$2 billion of committed equity.

So it's about the power of our multiple platforms in each business, and these platforms are fueled by the industry's largest dry powder capital pool of \$94 billion, giving us great flexibility to invest wherever in the world we see opportunity or dislocation.

Third, investment performance. The firm delivered attractive returns across the board. As Steve mentioned, our corporate private equity funds rose 6.9 percent in the quarter, and 15 percent over the last 12 months, with broad-based appreciation across sectors and regions. The real estate opportunity funds were up 5.7 percent in the quarter, and 15 percent over the last 12 months, while core plus was up 3.1 percent and 9 percent respectively. Both our corporate private equity and opportunistic real estate funds outperformed the S&P 500 this quarter, even in a very strong quarter for the stock

market. In credit, GSO delivered strong performance in the quarter following a standout year in 2016, with the performing credit funds up 3.5 percent gross in the quarter, and 26 percent for the prior 12 months, while the distress funds were up 2.8 percent in the quarter and 25 percent over the prior 12 months.

And the BAAM composite generated a gross return of 2.7 percent in the quarter, and nearly 10 percent for the prior 12 months. The vast majority of BAAM's incentive fee-eligible AUM is now back above the high-water mark, and that drove a more than doubling of BAAM's performance fee revenue versus the fourth quarter to its highest quarterly level in more than three years.

And fourth, this fund performance continues to drive robust fundraising, as Steve alluded to. Gross inflows were \$14 billion in the quarter, with consistent distribution across businesses. Total gross inflows were \$67 billion over the prior 12 months, which, combined with \$27 billion fund appreciation, drove total AUM up 7 percent to a record \$368 billion.

Every business segment had positive growth in AUM year over year, even despite \$18 billion of realizations in private equity and \$21 billion in real estate. GSO remains our fastest-growing segment currently, up 18 percent year over year. And BAAM's AUM rose 7 percent, with no abatement in its long-term annual pace of gross inflows of around \$11 billion. Although we didn't have our global private equity or real estate flagship funds in the market in the past year, our fundraising numbers are benefiting from continued expansion of our platforms into product and regional adjacencies, as well as having more funds that continuously raise capital versus episodically.

Fee-earning AUM rose 15 percent year over year to a record \$280 billion, our fourth consecutive quarter of double-digit growth in this metric.

Finally, the outlook for distributable earnings remains strong. While obviously it would be incorrect to extrapolate our first-quarter results forward, we do have a significant pipeline in real estate and private equity of both private and public realization opportunities. Most of BAAMs eligible AUM is back above the high-water mark, as I mentioned, and so we could see material contribution from that business later this year. And our core-plus real estate business will be in a position to start generating cash incentive fees later this year, and overall will be a meaningful contributor to DE this year and going forward.

Underlying all of this, we have a solid and growing baseline of fee-related earnings supporting the distribution. Relative to our \$280 billion of currently fee-earning AUM, we have \$43 billion of management fee-eligible AUM already raised but not currently earning fees that will turn on as funds are launched or as capital as invested, depending on the fund. Overall, we continue to expect FRE to grow organically in the low double-digit percentage range in 2017.

I'd like to finish my remarks with the following observation. While predicting ENI or DE for any one quarter is difficult, our business is not a mystery. The model is simple. We raise and invest scale capital over time. We create value in those investments, and then we exit when the timing is right, generating significant cash distributions for shareholders. While there's variation from quarter to quarter, the historical data shows consistency in growth over longer periods than one quarter. As one illustration, it's informative to compare results for the last 12 months to the preceding 12-month period ending in March of 2016. For that prior year 12-month period, we generated a very strong \$3 billion of distributable earnings. You'll recall, however, markets had come through a very volatile period, which put pressure on our ENI for parts of the prior period. So ENI for the 12 months ending in March, 2016 was well below the reported DE. Some expressed concern at that time that our ENI implied too little value creation, and therefore they were worried about future DE.

Fast-forward one year. Today we reported another \$3 billion of DE for the past 12 months, almost exactly in line with the prior year comparable period. We've simultaneously tripled ENI, which was also \$3 billion for the past 12 months. And we've invested another \$27 billion from the draw-down funds alone, bringing total performance fee-eligible AUM on the ground to nearly \$180 billion. So even with our high level of realizations, we're continuing to build our store of future value. Despite nearly \$50 billion of realizations and \$3 billion in DE, total AUM, invested AUM, and fee-earning AUM are all still up significantly year over year.

We think this all bodes well for future earnings' power and performance. I share Steve's great optimism, and think the empirical evidence solidly supports it. With that, we thank you all for joining the call, and we'd like to open it up now for questions.

Weston Tucker: And if I could ask everyone please, we have a fairly full queue, just to limit your first round to one question, one followup, and then if you have additional questions get back in the queue. That'd be helpful.

Operator: And again, ladies and gentlemen, to put yourself in the question queue, please press *1. Our first question will be from the line of Patrick Davitt, Autonomous.

Patrick Davitt: Hey, good morning. Thank you, guys. A few of you have been quite vocal about the idea of, obviously, getting more retail access to alternatives, and particularly in retirement plans and 401(k) plans. So two questions around that. First, now that we're a few more months into the new administration, are you encouraged by what you're seeing kind of below the radar, occurring on that front? I guess relative to where we were last year, do you feel like the opportunity to get more alternatives with these kind of clients is growing?

And, two, what needs to happen now, and what do you think the timeline is to get there?

Tony James: Well, I guess I'll tackle this one. It's Tony.

Patrick Davitt: Thank you.

Tony James: I think first of all you start with a need. We have a looming, huge retirement issue in America. I think everyone knows that. I've talked about that numerous times. And one of the reasons we have it is that the savings that people do put away don't earn enough. People are squeezed on the cost side – student loans, health care costs, child care costs, and other things.

They can't save 10 or 20 percent of their income. They have to be able to build a good retirement nest egg by saving a few percent of their income, and in order to connect those dots, that money has to earn at higher compounding rates than the typical 401(k) earns of 2 to 4 percent after fees. The only answer to that, particularly with markets where they are, is to move out of purely liquid markets into alternatives. So I think eventually both parties are going to realize that they're gonna decimate their elderly population financially if they don't allow this to happen.

And it's not a fix that takes overnight, so we have to get ahead of it. So I think that need is becoming more and more clear, and the answer is becoming more and more clear to both parties. I think the changes in the Department of Labor and whatnot open up opportunities for us, we think, but we've got a long way to go before it's actioned.

Patrick Davitt: Thank you.

Operator: The next question will be from the line of Craig Siegenthaler, Credit Suisse.

Craig Siegenthaler: Thanks. Good morning. So I know you can't raise five CLOs every quarter, and it was nice to see some large investments scheduled for 2Q, but I wanted to see if the lower fundraising levels were partly driven by the more challenging backdrop on the investing side.

Tony James: No, I don't think so at all. I think, first of all, if you look at our slate of products, it's actually – despite the fact we had a good first quarter – which I consider to be an excellent first quarter, \$14 billion, by the way – it's back-end loaded for this year, just because of the timing of the fund raises, for number one. Number two, remember, these things are lumpy. And when you have your really big funds, your private equity fund, your real estate fund, and those things, out of the market, you're just gonna see lower levels. And when they're in the market and they have a closing, you're gonna see bigger levels.

So I think it's a real mistake to try to plot this on some quarterly basis. We think there are tons of good opportunities out there, and we're finding them, as indicated by what Steve and Mike were talking about – our investment rate.

Michael Chae: And I'd just add, Craig – it's Michael – that it just so happens that in the subsequent next few quarters, there is a great pipeline of a number of draw-down funds, maybe not the flagship BCP fund. But whether it's tac ops, SP real assets, importantly

Cap Solutions III from GSO, the second Asia fund for real estate, and others that are going to unfold in the coming months and quarters.

Craig Siegenthaler: Thanks, Michael. And just my final one here: any update on the infrastructure business, just in terms of plans for fundraising?

Tony James: Well, we talked about that earlier this morning in the press call. We're laying the groundwork for that, talking to some anchor investors, and putting together our team, and some things like that. Again, it'll take a while to roll this out. The beauty of our business, frankly, is people can't plunge into it, and once we're there, we've got a really sustainable position. But it does take a while to build new capabilities.

Operator: The next question will be from the line of Glen Schorr, Evercore.

Glen Schorr: Hi, thanks. We've got this – I forget, year, year and a half ago when there was talk about CalPERS and some other big LPs insourcing or reducing their exposure on the hedge fund side, and I think Blackstone was a net beneficiary of consolidation of providers. There's renewed conversation, except this time in private equity, about the same kind of thing: high fees paid, maybe some insourcing, maybe some consolidation of providers. I think you're gonna be a beneficiary again, but I'm curious to get your thoughts on, is this a trend? Is this a topic of conversation with your largest LPs, and what you see the outcome being?

Tony James: Okay. Well, let me start by saying that what LPs need are returns. And if you look at the CalPERS announcement, you'll see that the single highest-performing asset class at CalPERS is private equity. And let's not lose sight of the fact that we deliver enhanced returns to LPs, number one, and, number two, they never need them more than they do today, for the same reasons that I just talked about for the 401(k)s. And so, in general what we're seeing is more and more LPs putting a higher percentage of their assets into alternatives, private equity included, fee discussion notwithstanding.

So when we look at the picture, we're seeing the opposite of what you're talking about. We're seeing more people giving us more money. And actually, I would say in general there's no pressure on fee structures, and in point of fact, we're actually making some enhancements to the fee structures from our perspective.

Steve Schwarzman: This is Steve – there was also a survey I forgot to bring with me, so I'm a little derelict on this, but it was done by Preqin, I don't know if anybody in the room has that. But it basically was saying there's a huge buy-in and satisfaction with private equity returns on behalf of investors. And so I look at that, and that kind of objective assessment – I think it was like 84 percent of investors were very happy with their returns, and about half of investors – something like that, we'll get you the numbers – are keeping their allocation as a percentage the same, and the other half are increasing. So assuming that they've done an accurate survey, that gives you a sense of what's going on.

Tony James: And Glen, I do want to comment – part of your question related to consolidation. We are seeing LPs increasingly wanting to consolidate their providers, and there's a few factors there. Number one, the administrative costs of this asset class – it's not like a mutual fund with their draw-down notices, their return capital, and so on and so forth that needs to be reinvested. So these pension funds that have hundreds, literally hundreds of providers, it has its administrative costs for them. Number two, they figured out that if they have lots and lots and lots of providers, essentially they get reversion to the mean, and instead of getting superior performance with top quartile, managers, they have average performance.

And number three, they just want to – they want to get other things, noneconomic things, from their managers, which could be training their people, it could be systems, could be insights into markets, educational things, and so on and so forth. And so we're seeing definitely a trend towards the big providers – the big LPs – wanting to consolidate capital with the big managers like us. Most particularly us, actually. I don't know that anyone else has actually seen this, across asset classes. Yes, they wanna be bigger in private equity, but they also wanna be bigger in real estate, tactical opportunities, strategic partners, and so on, GSO. So that consolidation is one of the tailwinds that we're enjoying and have been enjoying.

Glen Schorr: Excellent. I appreciate all that. Thanks.

Steve Schwarzman: Thanks, Glen.

Operator: The next question will be from the line of Bill Katz, Citigroup.

Bill Katz: Okay, thank you. Good morning, everybody. I apologize if I was doing this math a little quickly. Steve, I appreciate your comments about if you were to sort of yield similarly to the S&P, you'd be \$100.00 stock. So if I just assume a three-year return, I get like a 49 percent compound annual growth rate for that investment. And so I'm wondering, as you do your own math, and you think about the business, I know you've said you'd rather reinvest that back into the business than to repurchase, but with the sort of glaring upside that you see in the stock versus where it's trading today, how are you thinking at all that maybe altering your allocation of capital between reinvesting it back into business versus other uses of return back to investors?

Steve Schwarzman: Yeah, that's something we always look at, and we are starting, and planning to start, a number of new businesses. And we have unpredictable needs for capital for growth. And the higher those needs are, in a way, I guess, the happier we are. And so if we get into an area where a limited partner asks us to pioneer something and needs a certain amount of money put up as good faith money, we always wanna have money to do that. And returns, I guess, as we've discussed in the past, can run up as high as 30 percent for doing that. But even more than 30 percent on just that one situation – it grows the scale of the firm. It grows the number of things we can do for a limited partner. And that's got a knock-on effect that's very substantial. And so we tend to be cautious with our use of money, because that's sort of the greatest return for shareholders in the

long term. And just generally cautious financially because we have a high payout for this stock. Plus we do get presented with acquisition opportunities constantly, and the idea of not having enough money on hand to take advantage of these unique opportunities, as a manager, I look at it and say it's always great to have the fire power to do whatever comes your way that's truly compelling.

And so it's a bit of a dilemma when you have a stock at a level you don't like, and you're trying to plan for accelerated growth of the business for the future. And at least at the moment, we've sort of come out reserving for those opportunities, because once you start these types of businesses, they grow from little acorns to really giant-sized trees. And that's the best way to create value.

Tony James: The other thing, Bill, is frankly – I understand your 49 percent IRR point – we think the value is there, but we don't have confidence enough in you guys to figure that out. You've disappointed us consistently.

[Laughter]

Bill Katz: Ugh, okay. Michael just quick clarification, you mentioned that you expect FRE to be up low double-digits this year. If I simply annualized the first quarter that guidance seemed to be a little bit light. Is that based on sort of the old way you were disclosing your FRE, or now pro forma for the add-back of stock-based comp?

Michael Chae: No, Bill. It's really a single big driver, which is – this quarter the comparisons were a full quarter of BCP VII versus a quarter when we didn't have a full quarter of that. And so that's really the big driver of the current quarter, but obviously we still expect for the rest of the year and for the full year pretty healthy growth. So I think low-teens is a good thing to point to, and we obviously hope we do better than that as well.

Bill Katz: Okay. Thank you, I guess we'll sharpen our pencils over here. Thank you.

Operator: The next question will be from the line of Michael Cyprys, Morgan Stanley.

Michael Cyprys: Hi, good morning. Thanks for taking the question, and congratulations on the strong quarter.

Just one of the aspects of your business has been innovation: core plus, long-dated PE. What could make sense next in Blackstone's evolution? It seems like infrastructure could be one, but what other product adjacencies or geographic regions make sense next in Blackstone's evolution?

Tony James: Well, we obviously have talked about the infrastructure initiative, so that's one. Let me say, too, that we've been thinking now for a couple of years about the fact that we don't want to be the ultimate old-economy company. And there's a lot of

interesting things going on in the world. Our tech investing has been very successful. Within Tac Ops we've been doing some very successful growth equity investing.

And so we've got what I think is an extremely exciting concept, which I'm not gonna elaborate on, but that's in the whole growth venture area. Let's just leave it at that. We've added some expertise to our board in that area with one of the leading venture capitalists and other things that we've tapped into some of our experience, so that would be an obvious one. I'm really interested in, as countries nationalize and pull back, I'm interested in the whole development finance area, and there might be something there.

And we've talked , historically we've also talked about the fact that one of the areas we're not in is commodities, and I don't see us becoming a commodities trading house, but if we found the right entry point and business model that had sustainable competitive advantages – again, we're all about not just filling out a matrix, but whatever we do, doing better than anyone else, having a moat around it, so that they cannot imitate what we do, and they cannot earn the same returns. But we do have opportunities to do that. We're just patient about them.

Michael Cyprys: And as you think about M&A for your business, what, in your view, could be compelling? Steve, you mentioned that you want to be in a position to be able to do something compelling if it came to you. But what would that – what could that look like? What is compelling, in your mind?

Steve Schwarzman: Well, I love you, but telling you exactly what we're going to be focused on and so forth, so our competitors can catch up with us, is not something that we do with enthusiasm. So I'm gonna pass on that, not to be disagreeable, but just to protect you in the long term, for us being able to do these types of things.

Michael Cyprys: Fair, fair enough. Maybe I'd just ask another one, then, in that case. Just in terms of the payout ratio, just giving the time to give a lot of investment opportunities for your business on the horizon – in what situation could we see the payout ratio adjusted to reflect a greater flexibility?

Michael Chae: We have no plans to do so, Mike.

Michael Cyprys: Okay. Thank you.

Operator: The next question will be from the line of Devin Ryan, JMP Securities.

Devin Ryan: Thanks. Good morning. Maybe one here on the retail industry – it's been one area in the market that is seeing some stress, for obvious reasons. So just curious how you're thinking about your exposure to the sector, maybe directly, and then indirectly through areas like real estate or other second derivatives. And then whether you're seeing any opportunities in that sector just being created as a result of the stress?

Tony James: Okay. Well, yeah, we think retail in general has headwinds, so it's not like we're piling into that. I will say, though, within real estate, we've been a big beneficiary because of the last-mile logistics that e-commerce companies require. And that's been global. It's been United States, Europe, China, Japan, etc. So that's been a key thrust for us there, and the whole Logisor business, which the world is aware of, has benefited from that.

With respect to other retail, there are going to be winners and losers within the retail sector. People still go to grocery stores, and they still need local markets. And so we've, again, been a beneficiary in real estate in the grocery-anchored mall area, or local malls, but would stay away, frankly, from the regional malls. So we're trying to be smart about that. When we look at retailing, though, a lot of the companies we're looking at, say, on the corporate side, are hybrid bricks-and-mortar and e-commerce companies. And very often those things work very well together, and we're seeing some interesting opportunities.

And then, I have a particular bias because I'm lead director of Costco, and I think that company is an amazing company. And I think – I'm not sure I'd wanna be a general retailer anywhere between Amazon on one hand and Costco on the other. But there are ways to win in bricks-and-mortar still.

Michael Chae: And just to add to what Tony said – within our real estate business, US retail is in very small portion of our overall portfolio. It's something like 5 or 6 percent of our overall global portfolio, so the exposure is quite limited. And where we're exposed, as Tony said, the emphasis is on grocery-anchored shopping centers in A locations, and actually no exposure in the US to enclosed malls, which as you know are the more fashion-heavy department store-anchored locations that are facing headwinds.

Devin Ryan: Yep. Okay, terrific color, thank you. Just a quick follow up here – clearly great quarter realizations, I think the outlook all sounds pretty constructive there. But when you think about the opportunities from here, how would you frame the equity markets relative to maybe M&A exits to strategic acquirers? Or is there a better area in terms of what the market construct looks like right not?

And then also, with benign credit markets, it seems that dividend recaps are starting to pick up a little bit. So I'm just curious if maybe you're seeing a better opportunity to do some of those, just to accelerate some capital return off of the private portfolio?

Tony James: Okay well let's start with the recaps first. On the recaps, the credit market's benign, for sure, but it's been benign for quite a while. And I don't see it accelerating, I think it'll continue to be part of the mix. You're not seeing as much as you might expect given the credit markets, though, because equity markets are also very receptive to IPOs and blocks, secondaries. And we have – getting your first part of your question – a good strategic market.

So for the exit side – all three channels of exit are open for business and are welcoming to harvesting value. And yeah, so with strategic buyers, sure, there's plenty of them out there. I think one of the things that's happened with the election of President Trump is there's a little bit more of a forward-leaning attitude on the part of corporate buyers, and I would say that's pretty much across the board. And it's not just US, it's international buyers as well. And we got a question earlier on China, and obviously what China is doing with the currency will affect that, but so far we'll still see China corporates buying successfully, completing strategic acquisitions.

Devin Ryan: Mm-hmm. Got it. Great color. Thank you very much.

Operator: The next question will be from the line of Chris Shutler, William Blair.

Chris Shutler: Hey, guys. Good morning. Regarding the \$7 billion of deployments in private equity in the quarter, I know you mentioned a good bit of that was energy, so maybe EBITDA multiples aren't the right way of looking at it, but maybe just talk a bit about a few of the investments that you made in a quarter, and what gives you the confidence in the ultimate return profile, given where we are in the cycle?

Tony James: Well, okay. So a lot of it was energy. I mean, maybe Michael will give the exact percentage, but as you point out, not only is that not EBITDA-multiple driven, but we frankly feel that energy prices of low-50s today, call it, will be higher out sometime in the next five to seven years. So we do have – we are making a sector bet on that, that we'll face higher prices. The energy deals we're doing today will earn decent returns if prices stay flat. We'll get our money back even if prices drop. But to earn juicy returns – and I'm talking well in the 20s – our price deck has to be generally on point. I'm not talking about the exact timing, but at some point out there. So we think that's a very – that mix has a very nice, risk reward ratio. And what we're buying are not necessarily complete companies when we buy them. We usually end up with a highly, highly competent management team, and then we find the assets to go with that management team and create – by putting those two things together – create a great company. And so a lot of the value is created by marrying those two things. They don't exist – pre-exist. We're not just going and buying energy companies, generally. So that's on the energy side.

On the other side of private equity, we're continuing to do consolidations. I mentioned before – and those things you have, you get a very good management team, you get a position, an industry leading platform, and then you can add things onto it at very attractive EBITDA multiples. So we might pay for some of those consolidation opportunities eight or nine times EBITDA, but after the synergies and the ability to benefit from broader platform, usually we'll be able to get those multiples of the acquired companies down into the 5 to 6 range. And as you'll appreciate, that's a very attractive way to acquire EBITDA in any market.

And then thirdly, a big one this quarter was TeamHealth, and we think that company both was good value because of some idiosyncrasies around that company and an acquisition

they made that didn't get quite off to the start that it wanted, and the market, in my view, overreacted to that around a great company. But beyond that, in a private setting there's some things we can do to create value there. And we think that'll be a – You've got all of the tailwinds you would want in that, with aging demographics and cost pressures on the hospitals, where we're a more cost-efficient solution, and the advance of life sciences creating more things, and all of the demographic trends you could ever want. And we've got a dominant industry leader, and we think that'll be a very good investment over the long term.

And that's one of the great things about that investment, because you've got such good secular trends. You're not dependent on a quick fix, and then hitting an exit. You can hold that company a long, long time and just let that growth drive your value.

Michael Chae: And I might add – you mentioned at this point in the cycle, and interestingly, if you look at our biggest corporate deals that we either closed or announced in the last four months, whether it's TeamHealth as Tony talked about in the health care sector, SESAC, which is a music rights management company, the Ascend Learning deal we just announced in the training area – basically driven by non-cyclical factors. Great long-term organic growth, and we think pretty impervious to the cycle. So that's another way we address those considerations.

Tony James: Yeah, and that's the economic cycle Michael was talking about. But if you're talking about the valuation cycle, again, I want to come back to a point I made earlier to the press. We don't buy big baskets of securities. We're not really affected by the S&P index and where that's trading. We're really looking for really individual situations that're either private assets not affected by the markets, not complete companies, broken situations where we can bring our management in to fix them, and so on and so forth.

So we try to divorce ourselves from overall value in what we buy. And if you disaggregate our returns, over 80 percent of them are drive by things we do to the company, value we create. And obviously, that's not reflected in the value that we pay, because it doesn't exist until we own it. So, obviously, overall valuations mean, when they're high, means we've got to kiss a lot of frogs to find a few.

So the yield of what we work on goes down because a lot of companies don't have that attribute. But if we're good, and we're attentive, and we're disciplined, and we've put enough resources at it, we still find a few diamonds in the rough.

Chris Shutler: Okay, thank you.

Operator: The next question will be from the line of Mike Carrier, Bank of America.

Mike Carrier: All right, thanks a lot. Maybe first question – just on the sustainability, the returns. Tony, I think you mentioned on the other call the EBITDA trends were picking up into the high single digits. And I think, relative to the last few quarters, we've

definitely seen some improvement there. Just – I wanted to get a sense – is it very broad based across kinda the investments, or is it more nuanced or very specific? Just given what we're seeing on the economy and policy changes, delays, it just seems like there's a lot of uncertainty out there. So I just wanted to get some color on that and the sustainability of the returns.

Tony James: Yeah. Well, generally speaking, it's broad based. I mean, those are average numbers, but it's not like the average is dragged up by a couple of rocket ships, and the rest is sort of bumping along. So I would say quite broad based. And yeah, there's uncertain out there, but for a business executive before, it was kind of oppression – I don't wanna overstate this – and now there's kind of life and light and optimism that things could be better. So that's leaving them to lean forward and do a little bit more. And it's being reflected.

But also, beyond that, I don't wanna put too much credit to the election, the economy's continuing to get better, and it just – our companies, many of them, are big enough to be global. Europe is definitely on the rebound. And I'd say China's come through sort of the wobbles that people worried about, very well. Modi's gotten a new mandate, and India's feeling good. And so it's a global business, and – Brazil feels like it kind of – certainly in the business attitude down there, they found bottom, and they're more optimistic with the change of the presidency. So in general, global business is continuing to get better, and that's what you're seeing.

Mike Carrier: Okay. That's helpful, and then maybe – Michael, maybe just on taxes and the potential reform, seems like you got plenty of time to try to ponder what plays out. But given that you've had a little bit more time, there's been a little bit more details and different plans, just wanted to get any update on whether you guys think there's some potential in converting the corporate structure, or obviously too early, and what you said in the prior conversation still stands.

Michael Chae: Yeah, Mike, I think the prior conversation still stands, maybe even more so. In terms of timing and outcomes on taxes, we're watching it as you are. And so we'll take that into account as it plays out.

Mike Carrier: Okay. Thanks a lot.

Operator: The next question will be from the line of Alex Blostein, Goldman Sachs.

Alex Blostein: Hey, guys, good morning. A question for you guys around core-plus real estate. Michael, it sounded like you guys obviously anticipate cash incentive fees to start to contribute later on this year. Any sense, given kind of current returns in that business, what that should be? And I guess, as more funds go through, [*indecipherable*] maturity, how should we think about that progressing into 2018-19?

Michael Chae: Yeah, we're feeling good about it, and the math around it is pretty analyzable, given the structure. And so, in terms of sort of the first occurrence of cash

performance fees for BPP – as you know it works off of sort of three-year anniversaries of when capital first came in – that first tranche will be in the second half of this year. And for the full year, I'm not gonna give specific guidance, but it's a meaningful number, and it will be even more meaningful in 2018. And frankly, when we talk about core plus, we now think about both BPP and BREIT, which will also be a material contributor over time.

One very simple way to think about this is over time, for certainly the BPP complex – once you're up and running on these three-year anniversaries kind of waterfalling on cash incentive fees, very rough math is about 1 percent of AUM in the BPP program translates into a very healthy DE stream. So it's about \$100 million of DE for a \$10 billion AUM slug of core plus, for example. So you can sort of extrapolate those numbers. It'll be very powerful over time, and we'll probably talk more about that Investor Day.

Alex Blostein: Got it. That's very helpful. Thanks, guys.

Operator: The next question will be from the line of Brian Bedell, Deutsche Bank.

Brian Bedell: All right, great. Thanks very much. Most of my questions have been answered, but maybe a couple more just on the hedge fund solutions business at BAAM. The flows did improve on a net basis this first quarter. Maybe just some context on what's been going on in the hedge fund industry in terms of the redemptions on overall pie, the size of the pie of the industry. Do you see yourself, as a result of what's been happening, gaining share, and are you seeing any pressure on fees in the hedge fund space?

Tony James: Well, we're clearly gaining share, as we have been really consistently ever since the meltdown. And that's undiminished. And I would say the enthusiasm for our product is actually growing. And one of the nice things is people – some of the prior questions related to "well, the world feels uncertain." The more uncertain the world is, the better for BAAM. It's a way to get essentially equity returns or close to it, although historically we've actually done better, with much less volatility and risk than the overall markets. So they do well when people get a little more concerned.

So if you feel the values are toppy, it's a good thing for BAAM. And so clearly picking up share, and I think our investors continue to be very positive. Was there a second part of your question? Maybe I missed it.

Brian Bedell: Are you seeing any pressure on fees whatsoever, given what's going on in the industry? On – just on the hedge fund side. You already answered the private equity side.

Tony James: Well, not on our fees per se, but we're using our – the importance of us as probably, as the biggest customer out there for hedge funds, to make sure that our LPs get as low aggregate fees as possible on their investments. That is to say, we're getting concessions from managers, which, candidly, underwrite most of our fees.

Michael Chae: So – Brian, it's Michael. Over 70 percent of our capital in BAAM we have with the underlying manager either a fee deal or a customized strategy. And so, as Tony said, that is a big part of our value add, and so we're creating value for our customers. I'd say also, just in terms of the structure of the business, you can sort of break it apart. In our core BPS platform, the classic fund-to-funds business, over the last few years there's been some dilution on management fees, very gradual, slight. And part of that is because the average account size has grown, which is a good thing for us. And also clients have sought to weight fees a little bit more towards performance-based fees in a lower-return environment historically. Although it's important to say one big chunk of our core BPS business are commingled areas, which is about \$20 billion. Fees there have been very, very sticky.

And then other parts of our business like the new retail platform, the mutual fund, obviously our stakes business – those are good things from the fee standpoint, in terms of the mix. And you'll see more of that over time as those two areas grow.

Brian Bedell: Great, great. That's very helpful. And just a question for Steve. Obviously, with the new administration, coming into the new year, you're definitely very bullish on not only economic growth prospects, which you seem to continue to see, but also on tax reform and regulatory changes. Has your view changed on that at all since the last earnings call, given that we have seen sort of a slower progress from the administration on that?

Steve Schwarzman: Well, there's obviously been sort of a setback in terms of the health care, which was a bit of a driver in terms of monies available that could be put to tax reform. And so that's created a slow-down which – I think you saw Steve Mnuchin made a comment that was publicly reported on that. So it feels like, from wherever you were three months ago, there'll be a delay on some of this. On the other hand, in the regulatory area, things to me appear to be proceeding, sort of with a lot of enthusiasm. There's a lot of very productive work being done in the infrastructure area, in terms of how to de-bottleneck the system, which now has great difficulty building things.

It's hard to believe that both Germany and Canada can permit projects within a two-year window, and our average is somewhere around ten years, sometimes longer. And there's all kinds of things that can be done to facilitate that, and there's a lot of work being done on that. And there's still a great appetite for bringing trapped cash, if you will, from abroad back to the United States for a variety of purposes. So what I'd say is, a lot of stuff is moving, which is why there is optimism in the corporate community. There is some stuff that's sufficiently complex, like health care, that is clearly a difficult type of thing to resolve. And I think things will just be slower. That's a reasonable expectation.

Brian Bedell: But you still think things will get done this year in that regards, just maybe a little bit more slowly?

Steve Schwarzman: Well, that's a separate thing. There's so many things I just mentioned. Where they go in an envelope is something that's hard to just give a

judgment. But I think the thrust of where things are going remains on track, whether you get exactly the type of cut on health care – excuse me, on taxes, that people are expecting – that's one of those imponderables. As you look at how the political system adjusts to different elements that would be necessary to create super-low rates, depends what the political resistance is. Your judgment on that is at least as good as mine.

Brian Bedell: Right, right. Okay. Fair enough. Thank you.

Operator: The next question will be from the line of Robert Lee, KBW.

Robert Lee: Great. Good afternoon, and thank you for your patience, taking all the questions today. I'm just curious, you have benefitted in strategic partners from kind of the expansion and growth in the secondaries business. I'm just curious – is that having any knock-on effect in terms of primary demand, in terms of more LPs willing to commit more capital, given that the secondary market is developing in different private investment areas?

Tony James: Well, the simple answer is yes. A lot of the secondaries – the sellers of secondaries – are LPs that are interested in consolidating their GP mix to fewer core providers, selling off a lot of the old funds with GPs they're not gonna re-up with, and then having more money to concentrate on the fewer managers that they really want be with going forward. And we've been a beneficiary of that on both ends, both purchasing the secondaries, and then we've gotten more than our fair share of the new money as they consolidate on the bigger, higher-performing managers. So that's one thing.

Secondly, they also – if you look at the return profile over time of a private equity fund, or a real estate fund, or an infrastructure fund – we have – in NSP, in strategic partners we have dedicated strategies around each of those things, which is part of the driver of the growth, by the way. You'll see that once a fund gets mature, once it gets long in the tooth, the compounding rate of interest goes down, and so it's higher in the early years when a lot of the value is created, and then it goes down to something lower over time.

And so a lot of LPs, what they wanna do is, once it's mature – it's lower risk, but it's lower return – take that money and reinvest it in the higher return, earlier life cycle funds. And so, again, we benefit really on both sides of that. So it's been a helpful trend for the industry, I think, and for us in particular.

Robert Lee: Great. And this maybe is a followup. I mean, obviously you talked at length about, I guess I'll call it the lifting of the regulatory cloud maybe in the US, but as you look around the world, is there any place where you have any concerns of some kind of regulatory change? Whether it's the ECB talking about leverage-loan limits or whatnot, are there any – when you look outside the US, is there any place that gives you pause?

Steve Schwarzman: That's an interesting question. I have had meetings in the last two days with very senior regulators from around the world. And I was quite surprised at those meetings. And they came in to see me for a different reason; it wasn't regulatory

stuff, actually. I guess it was three of them from Blackstone per se, but more to talk about the system.

And they all were saying that they think the US is too tight, that we've over-regulated, that our standards are beyond the Basel requirements, and that that's taken a – had an impact of slowing down growth in the United States, and it's starting to affect their countries as well. Because some of the kind of regulatory and enforcement and Justice Department impact has scared people around the world. And so I was really surprised. And what they were saying is, "we'd like you people to change, so we can run our world in an easier and more normalized kind of way." So it didn't sound to me as a group – and I can't speak to what the ECB is doing, because sometimes the EU ends up doing some things that we find a little unusual.

But overall, I think there's a sense that we've tightened this thing up awfully tight, and it's sort of consistent with what the new administration is talking about. They just wanna know how loose you're gonna make it, but you're sort of in the right direction, and I was really surprised. You would think that when senior regulators come in and talk to you, they're talking about, "you're not adequately– “not Blackstone, but your country – “needs more, or we're gonna do more," or whatever. And I actually met with a fourth today, this morning, before this meeting. And it's all in the same pile.

Tony James: I'd make two other notes on the regulatory front. First of all, we're watching how Brexit unfolds, because we obviously have a big operation based in London. We do business around the continent. What the regulatory impacts of how that unravels is something that may affect some of our business. It probably – the more regulation and the more separate regulations probably adds a little bit of cost. Nothing significant to Blackstone, but overall we're still watching that carefully. We're well set up, actually, with our operation in Luxembourg, I think, to accommodate whatever happens, but nonetheless, it is out there.

The other thing that we're watching, of course, is China, what it does to currency controls, because the Chinese have been active buyers, not just for Blackstone but for a number of assets, and we've been a beneficiary of that, as have others, and so that's another area that we're watching closely.

Robert Lee: Great. I appreciate the color. Thank you.

Operator: Your final question will be from the line of Gerald O'Hara, Jefferies.

Gerald O'Hara: Great. Thanks for squeezing us in. Earlier you mentioned the investment in EagleClaw. I was hoping we might be able to get just a little bit of context around what you find attractive, particularly in the US oil and gas industry, whether that's been impacted at all by the new administration. And then, just related – if you could remind us, after several active quarters in that area, what the total exposure to energy is currently in the portfolio? Thank you.

Tony James: Okay, well, I'll let Michael and the guys talk about the energy exposure, because it falls in both debt and equity. But the simple answer to your question is, no, we're not – our energy investing has not been significantly impacted by the change of an administration. It's really been impacted by where energy prices are, where they've been and where we think they're going, and by the, frankly, capital squeeze that a lot of the traditional participants in the industry are suffering. And when they suffer a capital squeeze they either have to sell assets or raise money on less – for them – less attractive terms. We interpret that as being higher returns.

So it's not really driven by the Trump administration. Michael, do you have an energy exposure number you wanna give out?

Michael Chae: Yeah, I mean, across the firm, Jerry, on our total assets, it's something in the 10 percent area of the total firm. For our private equity and GSO businesses, it's always been a more significant number. It's probably about double that, in the 19 to 20 percent area.

Gerald O'Hara: Great. That's helpful. That's it for me. Thanks, guys.

Operator: And at this time I show no further questions in the queue. I would like to turn it back to Mr. Weston Tucker for any closing remark.

Weston Tucker: Thanks, Eric. And thanks, everybody for joining us today.

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