BX Fourth Quarter & Full Year 2014 Media Call – January 29, 2015

OPERATOR: Ladies and gentlemen, thank you for standing by. Welcome to the Blackstone Fourth Quarter End and Full-Year 2014 Media Conference Call. At this time all participants are in a listen-only mode. Later we will conduct a question-and-answer session; instructions will be given at that time. If you should require assistance during the call, please press star then zero. As a reminder, this conference is being recorded.

I would now like to turn the conference over to your host, Senior Managing Director, Mr. Peter Rose. Please go ahead.

MR. PETER ROSE: Good morning, everyone, and welcome to our fourth quarter and full-year 2014 earnings call for the media. With me is Tony James, Blackstone's President; Joan Solotar, Senior Managing Director for External Relations and Strategy; and Laurence Tosi, Blackstone's Chief Financial Officer.

As he does every quarter, Tony will begin with a brief summary of the quarter's and years highlights and then he would be happy to take your questions. Before handing over to Tony I would remind you that at 11 a.m. Eastern Standard Time we will also have a call with investors. You are invited to listen in on that. The dial-in numbers can be found in the press release on our website. With that I will hand it over to Tony.

MR. TONY JAMES: Okay. Thank you, Peter, and thank you all for tuning in this morning. As you can see from our release, we had a strong fourth quarter and capped off just a great year. 2014 was a record in just about everything for us. Revenues for the year increased 14% over 2013 while ENI, economic net income, jumped 24% to $4.3 billion after tax. We think this makes Blackstone, by a considerable margin, the single most profitable asset manager in the world.

Distributable earnings surged a whopping 61% year-over-year to $2.51 per unit. This represents a highly attractive yield on our stock price of almost 7%. Although we distributed a staggering $45 billion of fund distributions to our limited partners, strong investment results and good fundraising still pushed AUM up 9% for the year to $290 billion.

At the same time we had a very active investing year. Despite generally high valuations for assets, last year we deployed some $26 billion into new deals, up 73% from 2013. This is where we sow the seeds for the future gains, which we realized over the next several years. Despite some variation across our individual groups, the overall increase of 14% in our revenues shows how the diversification and balance of our business and the steady growth from our new products provides consistency to our results.

Revenue growth for 2014 was driven primarily by private equity, which almost doubled 2013 revenue. Real estate came off a great quarter and a great year in 2013 and was down about 7%. But the fourth quarter of this year was still our second best quarter ever in real estate. BAAM's revenues were about flat for the year, but GSO's were down 16% due to the sharp selloff in credit markets for the fourth quarter.

The biggest components of revenue this year were performance fees, private equity, and real estate. Total performance fees this year amounted to $4.4 billion, a jump of 23% year-over-year and reflects strong investment performance. For the year both private equity and real estate portfolios appreciated about 21%. BAAM with its low volatility position was up 7% and that compares to the MSCI all country index total return of about zero for the year.

In credit our drawdown fund investments amazingly were up between 15% and 25% for the year, while our hedge fund was about flat on the year before fees. All these returns reflected currency translation headwinds from a significantly weaker Euro that emerged in the fourth quarter.

Our $20 billion BCP5 fund, which has received a lot of attention, the portfolio appreciated 10% in the last quarter and that fund is now up to 1.8 times investors cost before fees and carry. Our private equity portfolio companies continue to grow their revenue's EBITDA above the S&P 500 average. Although their grow remains solid, we are seeing a gradual slowing in the rate of growth partly due to currency swings.

Our real estate properties however are still benefiting from escalating rents and occupancies along with low cap rates. Just to anticipate a question in energy, we had already sold most of our oil exposure before prices began to fall. We now have over $10 billion of dry powder dedicated to debt and equity investments in energy so we feel we were very well-positioned to take advantage of the current dislocation of capital markets. We believe the recent freefall in energy prices will prove to be relatively short-term so we view this as a good buying opportunity.

Overall the multiples of invested capital we were realizing when we sell investments has continued to be absolutely terrific. Private equity averaged a very, very strong 2.9 times investor's money on realized investments this year. Real estate's average was 2.3 times; really superb performance for investors.

One of the most amazing things about this year to me was that we could distribute $45 billion back to our investors and still grow AUM. Leaving out market appreciation, the gross new money that we raised from investors was $57 billion. This is not only an all-time record for anyone in the alternative asset management business, but it's more than the capital raised by our three largest public competitors combined.

We are seeing robust demand for each new product and fund. Most of the time we are oversubscribed and hit our hard caps. This reflects the power of the Blackstone brand, which has never been stronger. Recently we began fundraising for our next flagship global private equity and real estate funds. We are very pleased with the initial interest we are seeing from both funds already and expect both to exceed the size of their predecessors.

As you know, during the fourth quarter we announced a combination of our three advisory businesses with Paul Taubman's highly successful new M&A firm. Our advisory businesses are performing very well with earnings up 50% this year. The combination of our businesses with Paul's is proceeding smoothly. We'll shortly make the necessary SEC filings in anticipation of a complete spinoff to our unit holders in the second half of the year.

I also want to add a personal observation from working closely with Paul over the last six months. I knew that Paul Taubman was a great banker, but in addition I found him to be a terrific leader and businessman. He has also been an absolute pleasure to work with on a personal level. As a result, I am more optimistic than ever about the prospects for NewCo to become the single leading best independent advisory firm.

Perhaps our greatest asset at Blackstone is our strong internal culture. We strive to maintain our small firm values as we grow larger and stronger. In that vein I am pleased that once again Blackstone was named the number one employer in financial serves on Vault.com and the best in *Alternatives and Pension Investments Magazine*.

With that I'd be happy to take your questions.

OPERATOR: Ladies and gentlemen, if you wish to ask a question, please press star then one on your touchtone phone. You will hear a tone indicating you have been placed in queue. You may remove yourself from queue at any time by pressing the pound key. If you are using a speakerphone, please pick up the handset before pressing the numbers.

Once again, if you have a question, please press star one at this time. One moment please for the first question. Your first question comes from the line of Devin Banerjee from Bloomberg. Please go ahead.

MR. DEVIN BANERJEE: Hi, Tony. Thanks for your time, as always. There's been a lot of talk about energy opportunities, oil and gas producers for example. I was wondering if you could give us a sense of what type of deals you think these opportunities could be, whether buy-out, equity investment, illiquid debt, liquid debt, funding drilling like GSO I believe is doing with Linn Energy.

And maybe a sense of where in the energy universe do you see these opportunities, whether it is actually upstream or midstream as well or downstream, just a little more specific sense of what type of opportunities you see.

MR. JAMES: Okay. Well I think what's happened when the energy markets backed up is it wasn't very differentiated so everything just got hammered at once. And some companies deserve that and some companies don't. So I think there are some significantly mispriced assets out there.

I think the opportunities will come pretty much all of what you said, but just to summarize there's clearly some very interesting values in the credit markets just buying debt at big discounts to face and getting equity-like returns, number one. Number two, you'll have some companies that are over levered that need to raise emergency equity or sell assets and there aren't a lot of buyers, there aren't a lot of investors. I think we'll be able to and we're seeing both kinds of transactions today. Emergency sales of assets or companies looking to either sell themselves or get an equity infusion. So I think we will see and we are seeing all of that.

Then in addition to that, the company's ability to access capital to drill new prospects or to acquire acreage is very limited today. There will also be farm out deals, drilling deals, acreage acquisitions, things like that at much lower prices, particularly if it's oil, but gas too.

Actually over time if oil production tails off, which it will do, although this year production will be higher than last year just because of what's in the pipeline, that actually should be good for gas because you'll produce less associated gas. But gas prices of course have been very weak for the somewhat warmer winter and whatnot.

Most of the opportunities we're seeing right now are in North America I would say, broadly defined. I think some of those projects that are outside of the U.S. that are very big and require massive amounts of capital and infrastructure, are harder to tackle in this market.

But we're pretty much seeing across the board, and the $10 billion that I mentioned is both equity capital and debt capital. Some of it is in private equity and some of it is in GSO. I think we're well-positioned to play anywhere in the capital structure.

MR. BANERJEE: And are you sort of currently looking at these deals like the Linn Energy deal? Do you have some in the works? You don’t have to tell us the name obviously.

MR. JAMES: Yes. Our people are scrambling and trying to come up for air. We're very busy looking at the specific deals.

MR. BANERJEE: Okay. And one more question that's completely unrelated. In the private equity section of the statement today you guys said you have raised money for the new high net worth focused total alternative solutions fund. Can you give us a sense of what that is?

MR. JAMES: Yes. That's a product we created for the retail channel, which participates across the board on a lot of our high return products so that a retail investor can invest in that and get access to private equity, real estate, tactile opportunities, co-investments, and dedicated deals. Sort of all of the things that we do in the high return area. I think it's a fantastic product for retail investors and it was widely over prescribed. Because our capacity to deliver those investments is limited, but I think it could be a big thing for us going forward.

MR. BANERJEE: And what's the liquidity like on that? Is it like a quarterly thing?

MR. JAMES: No. It's illiquid, but it's a three year investment period. It's a shorter investment period and presumably as a result a little shorter holding period. But it's illiquid in the sense it's a drawdown fund. It's not a trade.

MR. BANERJEE: Okay. Thanks a lot, Tony.

OPERATOR: Your next question comes from the line of Will Alden from *The New York Times*. Please go ahead.

MR. WILLIAM ALDEN: Thanks. Actually I'm wondering, Tony, if you could just tell us a little bit more about that retail product. Could you just give an idea of how much money you raised for that?

MR. JAMES: If you don't mind, we haven't really disclosed that, but it's less than $1 billion.

MR. ALDEN: Okay. And is this open to qualified purchasers or accredited investors, or what?

MR. JAMES: Yes. We've marketed it through two ultra-high net worth distribution systems. And we like it because this is where the breadth of Blackstone is a real advantage because there's really no other firm that could offer the full spectrum of alternatives in one convenient place for investors where each component of it is top cortile in its quality.

Only we can offer that. As I say, it blew out where it was offered and we have a lot of other systems. Both the firms that offered it would like more and a lot of other systems would like to have something to put in their system. We've just got to make sure we can continue to deliver the side-by-side and the co-investments and things like that that aren't just fund investments in scale.

It's complex. We have a special investment committee that decides how much they want of the different funds and different sectors. It's a first generation, and I don't mean to say that in terms that it's not a good generation. It's just that we're starting in modest scale, making sure that it all works as planned and that we can deliver the amount of high quality investments that it needs.

MR. ALDEN: Is this the kind of thing where every dollar that investors put into it, like $0.25 goes to real estate, $0.25 goes to Tack Ops? That kind of thing?

MR. JAMES: Well, yes. More dynamic than that. I think we sit there and our investors can decide if it's a good time to go into energy right now so they overweight energy. So it uses the capabilities we have, but there is a strategy and a reaction to environment overlay to it.

MR. ALDEN: Is there a minimum required investment for each investor?

MR. JAMES: There probably is. L.T., do you have that?

MR. LAURENCE TOSI: It's qualified purchases and it's over $250,000. It's in the systems and we did disclose them in the release, Tony. It's about half a billion dollars raised to date in the first fundraise.

MR. ALDEN: Sorry, you said about half a billion raised to date?

MR. TOSI: Yes.

MR. ALDEN: Okay. Thanks, guys.

OPERATOR: Your next question comes from the line of Greg Roumeliotis from Reuters. Please go ahead.

MR. GREG ROUMELIOTIS: Hi. Good morning. A couple of more fundraising questions. What is the formal name of this new high net worth product?

MR. TOSI: Blackstone Total Alternative Solutions.

MR. ROUMELIOTIS: Thank you very much.

MR. TOSI: We refer to it as BTAS.

MR. ROUMELIOTIS: Great. You mentioned, Tony, in private equity and real estate you expect those funds to actually be bigger a little bit than their predecessors. Can you mention a little bit of where they are now under hard cap versus targets based on expected commitments.

MR. JAMES: As I mentioned, we're in the early stages. We haven't even had our first closing yet. And so I think we feel comfortable that it'll be bigger than our predecessors. Beyond that we will see.

MR. ROUMELIOTIS: Okay. As a driver of today's earnings bit - - some analysts are pointing to lower conversation expenses. Can you offer some color on that, particularly given that in many segments performance fees soared? Can you offer some detail as to how this was reconciled with lower home expenses?

MR. TOSI: Greg, it's L.T. We'll go through this in some detail on the analyst call, but the biggest driver of the lower compensation issue with respect to our ENI earnings relates to the fact that the earnings mix is tilting more towards performance fees where we typically have a lower compensation ratio than we do for our typical fee related earnings. There are some one-time events related to some legacy funds where there are lower compensation ratios for pre-IPO investments. But by and large that's the effect and we expect it'll continue for some time.

MR. ROUMELIOTIS: Thank you. And the last question I had is on the issue of portfolio company fees, particularly the way that the SEC is thinking about them at the moment. I had two questions with regards to this. One is, has Blackstone either in its present exam with the SEC or in any other interaction with SEC ever received notice of any deficiencies with regards to the disclosure of portfolio company fees.

And the other question I would have is just more philosophically given that for example in the latest borrowed fund I understand Blackstone has moved to 100% fee offset. What is this philosophy, what is the rationale then behind charging portfolio companies any fees at all?

MR. JAMES: Okay. I think we're in good shape on our fees with portfolio companies and in good shape with the regulators, but I'm not going to obviously get into the back and forth. We have constant dialogue with our regulators. I think we've got a great relationship there. I think they think we're kind of the golden standard, and I hope that stays. We're going to work darn hard to be sure it does.

With respect to why should the portfolio companies pay fees at all, I guess if you go to your doctor and you use them three times as much as someone else would you expect him to charge you a little more than the person that doesn't use him at all? Some companies need a massive amount of resources and that takes from other companies and it's added costs we have to put on to services. And so I think that would be the rationale, but what we do with our portfolio companies is totally transparent to our LPs, totally accepted, very clear, and I think they're all very happy with it and that's the asset test.

In general, but with respect to changing the terms of our funds, we do try to also be LP friendly and we try to listen to our customers just like any other business. If our customers don't like something we try to change it. There are a number of LPs that have philosophical issues with deal fees. So what we try to do is just take some of those out and adjust the management fees accordingly, even up a little bit, so that we get the economics we need in a form more palatable to them.

MR. ROUMELIOTIS: On the issue of disclosure, Tony, do you think that portfolio companies fee agreements? The agreements describing the fees that the GP gets from portfolio companies, should be made available to LPs rather than LPs having to scroll through the SEC website for any portfolio company that happens to IPO or have publicly traded debt just to be able to see a fraction of them?

MR. JAMES: Sounds fine to me.

MR. ROUMELIOTIS: Is Blackstone going to do this? Do you know?

MR. JAMES: We give our LPs whatever they want.

MR. ROUMELIOTIS: Okay. Thank you very much. I appreciate it.

OPERATOR: Your next question comes from the line of Ryan Dezember from *Wall Street Journal*. Please go ahead.

MR. RYAN DEZEMBER: Good morning, everyone. Tony, you mentioned in your intro your fundraising numbers and how you guys are kind of pulling away from your competitors. And that's happening in a lot of regards with Blackstone. Does that present any challenges from kind of separating from the pack so much in terms of what you guys do on the shareholder side and as a public company? Is there any drawback to that or is it all just kind of superlatives and positives for you guys?

For example, today you guys print a record dividend for the quarter, for the year, all these kind of superlatives, and your stock is down a bit today, which is kind of perplexing. I'm kind of curious. What does it mean for you guys as you kind of distance from the pack in terms of AUM, for your profits, through your sheer size and scale?

MR. JAMES: Ryan, I have a simple philosophy. The stock market has a life and will of its own and it bounces around and it almost never in my view accords to the value to Blackstone that it should. So we're just talking about how much undervalued are we by comparison to any metrics in my opinion. I mean honestly, to have the kind of quality business that we have locked in revenues, leadership positions, margins, growth, and still trade at ten times earnings in a 7% yield, there's no stock in the world that you'd say that was the right value for.

My view is our job is simple. It's not to worry about the stock market. It's not to try to manage the stock market. It's not to complain about the stock market, although Steve may not like that. My job is to deliver consistently great results, investment results, in a few dominant businesses, have fantastic teams on the field, and with that will come scale and size and distance to the pack and hopefully someday the market will recognize and reward that.

MR. DEZEMBER: You guys mentioned kind of a huge war chest of stock in your private equity fund to kind of continue the selling, 14.1 billion. What's the outlook for that this year? Should we expect kind of, or do you expect a similar ability to sell into a relatively high or rising market? And what's your forecast for other sort of realizations, IPOs?

MR. JAMES: Like we said, we're not going to give a forecast of the business, so let me just talk in general. This was a good year in distributions; $2.51. But it's not an extraordinary year. To me this is in a market environment like this, which is reasonably benign, it's a sustainable level. We're not emptying covers. We ended up with more crude undistributed carry when we started the year. The cupboard isn't getting barer. It's getting fuller.

For me, as I say, the market falls out of bed, it's 2008 or '09 again, market falls out of bed, this is terrible. We'd be stupid to sell. We don’t have to sell. The beauty of our fund structure is we never have to be forced sellers, so we can time it. But in a benign environment where values are reasonably fair this is a sustainable level. This isn't like a peak or something.

Also I want to say that our portfolio companies are performing very well. Our private business was up 21% last year in value, our portfolio company. BCP V was up 10% last quarter in a quarter that some people found difficult. These are good performers. Our companies are growing. They're paying down debt. They have great management teams. We're continuing to accrue value in that portfolio. I feel very good about where we are and about the future.

OPERATOR: Your next question comes from the line of Dan Primack from *Fortune Magazine*. Please go ahead.

MR. DAN PRIMACK: Hi, Tony. Good morning. Tony, you said during your comments at the beginning that prior to the oil prices starting to go down that Blackstone had unloaded most of its exposure to oil. Are you able to quantify that at all and then explain why it would be that you guys would be getting out when you did?

MR. JAMES: Yes. I could probably quantify that. Let me have someone try to find the number for me. We had made some great investments. We tried to be counter cyclical. We got into oil early and played the shales and things like that, and created a lot of value. I'd say the average multiple of our money was over four probably in those deals, and it was time to sell. We felt oil prices at 100 were above where they should be long-term. We had a mature investment. The value was created. It was many multiples our investors cost and oil was above normal. Perfect time to sell.

And it's just kind of the risk/reward chance. It wasn't that there wasn't potential left in those investments. The upside versus the downside shifted to where we were comfortable taking some money off the table.

MR. PRIMACK: When you talk about this are you talking specifically about the private equity portfolio or firm-wide including GSO?

MR. JAMES: Well those comments were about the private equity primary. GSO doesn’t worry quite so much because if the companies have credit with you they'll get their principle in interest.

MR. PRIMACK: That's what I was looking for. If you're able to give a number on exposure at some point that would be fantastic.

MR. JAMES: Okay. We'll follow up with you.

MR. PRIMACK: Thank you.

OPERATOR: Your next question comes from the line of Shasha Dai from *The Wall Street Journal*. Please go ahead.

MS. SHASHA DAI: Hi. Good morning, everyone. I had questions about energy, high net worth fund, and the exit environment, all of which has been asked and answered, so thank you very much.

MR. JAMES: Thanks, Sasha.

MS. GREY: Sure.

OPERATOR: Your next question comes from the line of Evelyn Lee, Private Equity GLC. Please go ahead.

MS. EVELYN LEE: Hi, Tony. Good morning. I had a question regarding your real estate earnings. Can you explain the decline in the earnings both in terms of the fourth quarter and the full year? What were the factors behind that?

MR. JAMES: Remember that these are - -. I think the fourth quarter we had a huge gain in Hilton. We had a few other things. We're in a business where sequential quarters are the kind of things that ebbs and flow. That's just timing of events. It's a few events, so it's lumpy you've got hundreds of events that sort of average each other out. There's a few events, they are large events, and if they happen to fall in one quarter or another quarter you get that kind of variation.

In general virtually every asset in our real estate portfolio is appreciating nicely and I think the portfolio is just in fantastic shape. I think the distributions this year will look even better than last year.

MS. LEE: Okay. Thank you very much.

OPERATOR: And your final question today comes from the line of Chris Witkowsky PE HUB. Please go ahead.

MR. CHRIS WITKOWSKY: Good morning, Tony. Thanks for taking my questions. Just a couple questions for you. First, I just wanted to clarify exactly. Is Blackstone no longer collecting monitoring fees? That was an article in the Journal in the fall, but I just wanted to clarify. Is that accurate?

MR. JAMES: No. We still get monitoring fees. We changed the structure of them and we changed the sharing of them with LPs on our new funds. We can collect monitoring fees under our old funds. If you go way back 100% of monitoring fees were at Blackstone and zero to the LPs. Then it was 50/50. Then it was 60/40. And now in our new fund it's 100% monitoring fees go to the LPs basically. But we still collect the fees from the portfolio company.

I think the question is left whether you collect the fees or not and what happened to them and how much the LPs get. That's been a longstanding trend. Has nothing to do with the SEC. It's just the economics of the business. And really the LPs demands are such that more and more of them go right to the LPs.

MR. WITKOWSKY: Got it. So in fund seven it's going to be a 100% share with the LPs on monitoring fees.

MR. JAMES: Yes.

MR. WITKOWSKY: Okay. And also I just wondered if you could just talk a bit about the Strategic Partners private equity secondaries team and just how things are going there. Are they busy? I know that pricing environment and private equity secondaries is as high as it's ever been. How is the activity for that team?

MR. JAMES: Really high. I know GSO was a great acquisition for the firm. This is a fantastic one too. When we bought those guys their last fund at Credit Suisse had been a $2.5 billion fund. This round between the new main fund and the spinoff funds, the real estate and the infrastructure and some of the new products, it's going to be over seven I think.

A tripling of the kind of size of the business if you run rate size of the business in 18 months. Their investment rate is very high. Their SP, whatever it was, their last main fund, which we closed less than a year ago up from 2.5 to like over 4. They'll be back in the market in less than a year. It's a lot of activity. They've done some great deals and I couldn’t be happier with the way that's going.

MR. WITKOWSKY: Got it. Okay. Thank you very much.

MR. JAMES: Alright. Thanks, Chris.

OPERATOR: And I'd now like to turn the call back to Peter Rose for closing comments.

MR. ROSE: Thank you all for listening. In the course of your reporting, if you have further questions just call media relations office and we will find you the right answer. Thank you, everyone.

OPERATOR: Ladies and gentlemen, that does conclude your conference for today. Thank you for your participation and for using AT&T Executive Teleconference. You may now disconnect.

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