Blackstone Second Quarter 2015 Media Call

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Peter Rose

Good morning everyone, and welcome to our 2015 Second Quarter 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 we do every quarter, Tony will give a brief overview of earnings, and then we will be happy to take your questions. Before handing over to Tony, let me remind you that there will also be a call for our investors today at 11 o'clock Eastern Standard Time, and the dial-in numbers are in a press release in our website, and you're all welcome to listen in. Tony?

Tony James

Thanks, Peter, and thank you all for tuning in this morning. I'm pleased to say that overall Blackstone continues to perform exceptionally well and do so across all of our businesses. Every one of our businesses is showing excellent investment performance, investor enthusiasm for new funds, creative new growth initiatives, and terrific leadership. Despite these incredibly favorable results, this quarter, however, illustrates one of the key conundrums of our business. We can be doing really well in every fundamental way, better than ever actually, yet short-term variations in the stock market quarter to quarter can mask this.

This quarter, we reported revenues of $1.2 billion, a drop from last year's blockbuster second quarter of around 46%. Year-to-date revenues were $3.7 billion, flat with last year's strong first half. The decline for this quarter was significantly driven by movements in the trading prices of stocks we hold in real estate portfolio companies that have already gone public. As you all know, that sector of the market was weak this quarter.

These marks were unrealized and simply reflect our mark to markets as of the end of the quarter. With long-term locked up funds, we are never under pressure to sell any asset and are not dependent on public markets when we do. We can ignore public markets when they were down and take advantage of them when they are up. We make investments where we believe we can create significant value operationally regardless of the movements of the overall market.

Because of these factors, returns across every business group, as I will describe in more detail later, continue to be excellent during the quarter both absolutely and relative to their benchmarks.

Economic net income followed a pattern similar to revenues, dropping from last year's second quarter but coming in flat on a year-to-date basis. Distributable earnings, on the other hand, which are the actual investment results our businesses are realizing, increased 35% over last year's second quarter and jumped 83% over last year to date. On a per unit basis, distributable earnings were $0.88 for the quarter and $3.39 for the last 12 months. This represents a yield of about 8% on our current stock price, and that's a great yield for any stock these days.

Fundraising continued to be very strong in the quarter, with virtually all of our drawdown funds hitting their hard caps. This drove a 19% increase in AUM over the last year to $333 billion, despite distributing over $60 billion to our LPs—$60 billion, an amazing number. New funds raised during this quarter were $31 billion, an all-time record. A big chunk of this was our flagship private equity fund which had a blowout first closing, raising $16.7 billion from institutions from which we had binding commitments, well above our hard cap for this fund of $17.5 billion. We had to scale these commitments back to accommodate follow-on retail and other global demands.

Overall, in the last 12 months, we took in $94 billion, $94 billion in gross new inflows, an amazing statistic. We believe this is more than all of our public competitors combined have ever done in any calendar year.

Our investment returns, as we mentioned before, continue to be terrific. Private equity portfolio appreciated 3.5% during the quarter and 16.5% over the last 12 months. Our opportunistic real estate portfolio, despite the backup in public real estate stocks, appreciated 1.2% for the quarter and over 20% for the last year. Our credit for drawdown funds showed gross returns of 6% in the quarter and over the last 12 months were up 9% in rescue financing and 24%, yes 24%, in mezzanine debt, an amazing return for a credit fund.

Notwithstanding difficult public markets, our hedge fund solutions business delivered a gross return of 1.1% for the quarter and 6.4% over the last year while maintaining a volatility of only about a third of the stock market, a great return considering the reduced risks of that product.

At the portfolio company level, the operating performance of the assets we control also continues to be really strong. In private equity, portfolio company revenues are growing in the mid-single digits, about 5%, and EBITDA is growing low double digits, about 12%. Both are well above the S&P 500 growth rates which are essentially flat.

And in real estate operating results are tremendous. General growth of the economy coupled with limited new construction continued to drive occupancies, rents, and operating cash flows all higher across the board.

While near zero interest rates around the world have inflated most asset values, we continue to find interesting opportunities by being creative and disciplined and using our unmatched scale to do transactions that others can't do. New investments made by our drawdown funds were about $5 billion for the quarter and $10 billion year-to-date, continuing the rapid pace of the last several years where we've averaged about $20 billion per year.

About half of this quarter's deployments are outside of the US, showing the importance of having a strong global footprint. And notwithstanding the pricy environment during the last several years, gross returns on the new investments we're making, as measured by those aged over a year from our drawdown funds, have been absolutely terrific. They've averaged 27% in private equity, 31% in real estate, and 28% in credit. Whoa, those are big returns considering what people think of this being a high priced environment and one where we're still putting out a lot of money. In fact, these are spectacular returns in any environment. In total, we ended the quarter with $82 billion in dry powder. That's up a staggering 80% from a year ago.

I want to talk a little bit this quarter about our new initiatives, because it's important to understand that it is innovation that drives Blackstone's growth, not pushing established funds to ever greater size. One of our critical strengths is the ability to create new products that offer superior returns to investors and grow quickly to large scale and that are built on great homegrown talent. In private equity we had an idea three years ago to create a nimble, flexible capital pool to take advantage of temporary dislocations in markets that fell outside of the traditional alternative asset classes. This business, called tactical opportunities, has grown from zero three years ago to $11 billion in AUM today.

In real estate, we took what was an essentially an empty public shell in 2013 and have built that into a leading mortgage REIT with $2.6 billion of market cap since then. We also created a new business in real estate in the core plus area, targeting lower returns in our opportunistic funds. This has grown to $7 billion in AUM in just over two years.

In hedge fund solutions, we started a fun to buy minority positions in successful managers last year, which successfully hit its fundraising target of $3.3 billion. We also created a suite of daily liquidity hedge fund products that have grown to $4.6 billion of AUM in just two years. And in credit, two new products created this year in response to market opportunities, European direct lending and energy select investments, will come out of the box with over $7 billion of new capital. These are big, big growth in assets from nowhere a couple of years ago.

And finally, I just want to note the tremendous success of our recently acquired secondaries business, Strategic Partners. When we acquired Strategic Partners, they had one core private equity secondaries fund of about $2.5 billion. That has now blossomed into a $4.5 billion private equity fund, a real estate secondaries fund targeted at $1.25 billion, a secondary fund for infrastructure, primary funds of funds, and other new products. Put another way, they have essentially tripled their investible capital in just two years.

I want to end my remarks today with some of the themes that I hit on last quarter. Blackstone is not a boutique firm with one or two interesting niche businesses. It is a broad-based global institution that is unique in our industry in having leadership positions in 12 to 15 different product areas spanning the full spectrum of alternative asset management. The breadth and leadership positions of our individual businesses gives Blackstone a balance, a diversity, and a brand strength which is unparalleled in our industry.

The firm has an incredibly talented and deep, yet youthful management team. Our balance sheet strength exceeds that of many of the largest banks and securities firms in the world. We have no net debt. We accessed the credit markets for 30-year bonds this year, and we sold a euro bond with just over a 2% yield. Wow, I never thought I'd hear that as our financing.

But our passion is not size. It is investment performance, and by that measure, across all segments and through all cycles, we deliver returns on a scale and with a consistency that is unmatched. We do this not by financial engineering, but by intervening into the operations of our portfolio investments to create healthier, faster growing, more profitable assets. The ability to do this on a repeated basis gives us much more control over investment outcomes than simply betting on market movements, and this is what makes the success of our funds replicable from cycle to cycle.

And now a farewell salute to our advisory businesses. This is likely the last quarterly call where our three terrific advisory businesses will part of Blackstone. Sometime in the next few months, they will merge with Paul Taubman's surging M&A boutique and be spun off to shareholders of Blackstone as an independent company called PJT Partners. The new company has tremendous momentum, and out from under the inevitable conflicts that have come with our huge investment portfolios, their growth can only accelerate further. I think PJT Partners will be a big success with several world leading franchises, and we wish our longstanding partners and friends at PJT all the success in the world.

And with that, I'd be happy to take your questions.

Peter Rose
Operator, can you prompt for questions please?

Moderator
Certainly. First we'll go to the line of Devin Banerjee with Bloomberg. Please go ahead.

Devin Banerjee
Hi, Tony. Thanks for your time as always. I've got a couple questions. I'll try to make them quick. You noted in the press release and you noted on the call healthy deployment activity, and you noted Europe and energy in particular. Can you give us some color on what those transactions were, just some visibility into actual individual transactions?

Tony James
I guess the one that got the most note was the GE transaction, where our real estate guys bought about a $30 billion portfolio of assets from General Electric. What was interesting about that transaction is it included debt instruments. It included equity instruments. It included assets all over the world, and it included limited partnership interests. It was funded by five different Blackstone businesses. It's very interesting. I would say that we took a private REIT in real estate, which was a fairly chunky transaction.

In private equity, this is not a market to do the big blockbuster public to privates. Those prices are too high. This is a market where we have to be more creative and do more individualistic things where you can create a lot of value. A lot of what we're doing, as you mentioned, is in energy, and not necessarily oil and gas, but a lot of it is in power and power development, a lot of renewable stuff, for example, so that's the kind of thing we're doing.

Devin Banerjee
Okay. Second question, I don't know if you caught yesterday this interesting exchange between Larry Fink and Carl Icahn about ETFs and trying to put illiquid products into liquid-type vehicles. Icahn took the position that this is bound for a disaster. It's kind of a similar position that Howard Marks has taken. We're just curious what your views are on liquid alternatives and these types of ETF products.

Tony James
Carl was talking about ETFs around high yield bonds, and those are really not alternatives. We consider that a long only traditional marketable security; however, I think as Steve mentioned in his op-ed, we're very concerned about market liquidity and what has happened to that as the banks ratchet back capital under the new capital regimes and new regulatory constraints. It is something to worry about.

I know Carl loves to tweak people, and Larry has been on the back of activist shareholders, and so I'm not surprised that there was a missile coming back the other way, but I think in general, the liquidity in the credit markets will be constrained by the new regulatory scheme, and I think it's a concern.

Devin Banerjee
Okay. Thanks. Final question, in your most recent 10-Q, you disclosed discussions with the SEC to resolve two issues, the accelerated monitoring fee issue and the vendor discount issue, I believe. Can you give us an update on where that stands?

Tony James
There's really nothing to update. It hasn't changed much since the last disclosure.

Devin Banerjee
Okay. To your knowledge, do you know if any potential resolution would include a monetary fine?

Tony James
It's really not resolved yet, so we'll let you know when it is.

Devin Banerjee
Okay thank you, Tony.

Moderator
Our next question is from Greg Roumeliotis with Reuters. Please go ahead.

Greg Roumeliotis
Hi. Good morning, Tony. Can you give a little more color on the real estate business, particularly where we are in the commercial real estate cycle? You may have seen some comments yesterday in Janet Yellen's report from the Federal Reserve, the semi-annual report to Congress, talking about valuation pressures in commercial real estate rising. I'm just wondering given that obviously Blackstone is a big investor in residential property as well, but I was just wondering what we see today as far as the marks are concerned in real estate. What does this mean for Blackstone, where is it at the moment in the cycle?

Tony James
Okay. So, let me start by saying this is a global business, and the different global markets are at different parts of their cycle, so Yellen's comments, and it sounded like yours was primarily

focused on the United States, so I'll address that first, and if you want to get into other parts of the world, we can do that.

As I mentioned in my comments, in our real estate assets in the United States, across all the different sectors—office, retail, apartments, warehouses, etc., we're still seeing rising occupancies, rising rents, and of course, if you get rising occupants' rents, you get higher cash flows, so things are improving in real estate; however, new building is still subpar, and we still have not caught up. We went through a long period of time where there was very little new building, and new building is still lagging behind, in general, lagging behind demand, which is why, of course, occupancies are going up, which is why rents are going up and so on.

So, we're still not building ahead of demand. The way we see it is values are going up because cash flows are going up, but it's got a ways to run before we get worried about valuations. On new investments, we are still buying virtually every asset we buy at less than physical replacement cost, and so if we can buy existing assets at less than physical replacement cost, you're not going to have much new building because, of course, you're paying replacement costs when you build.

Now, in certain markets and certain sectors, they're hotter than others, so in the Bay area, office space is hot, and in somewhere like New York that you'd know from looking at the cranes, apartment building is hot. But in general, the comments that I made are reflective of the fact that we still don't have the kind of new builds that would give us concerns about the market turning down.

Greg Roumeliotis
Okay. And I also appreciate that earnings can be lumpy every quarter. Were basically equity markets to continue kind of flat and there wouldn't be the kind of appreciation in the portfolio that we saw over the last two years, what do you think that would mean for realizations and distributions? Do you think that would mean that more of the portfolio will be monetizedbecause you would have reached some sort of valuation peak, or would some of the funds hold off on monetizing? Can you provide any color?

Tony James
Sure, I'm happy to. I have no knowledge at all about what the future will hold. My own view, if markets stay flat, I think you will continue to see a lot of realizations. And by the way, let's not forget that many of our realizations come from strategic sales, so M&A is booming, and that spawns both an ability to sell companies in into strategics, but it also when there's a lot of M&A activity, it's tended to spawn a lot of new investment activity also because companies rationalize their portfolio businesses. So, I think if the market stays flat, it'll be a great environment.

Greg Roumeliotis
Okay, thank you.

Moderator
Our next question is from the line of Shasha Dai with Dow Jones. Please go ahead.

Shasha Dai
Hi. Good morning, everybody. Tony, I have two quick questions. One is on private equity. Joe spoke at a SuperReturn, and he talked about this coalition of the willing, namely the idea of teaming up with some large investors to buy companies with a longer return horizon. That's been reported, so that's no secret, but what I'm wondering is on the technical level how would the coalition work, especially if it's done on a deal by deal basis? How would you make sure that you can coalesce a consortium that move quickly enough for everybody to do their due diligence and get their commitment approved by their own investment committee and have the money to get the deal done especially in a highly competitive process? I guess technically how does that work?

Tony James
Okay, well, I'm not going to get into the granular details of this, because some of that is proprietary, but I will say that think of it as an investment group where there are a few large gorillas much like a PE consortium of old, but instead of us doing something with our friends at KKR or TPG, we're doing it with our friends at some of the big LPs that will be set up to actually be able to process deals just like a sponsor can. That's no different deal modality than was five or six years ago. It's just with different partners, and now more of the LPs are set up to go direct if they want to go direct. That would be a portion of it.

And then there'd be a portion of it which would be in the form of a commingled fund which we could control, so a bunch of the capital, maybe most of the capital, would be in a form where we have control and discretion and we don't have to include a huge gaggle of people. And collectively that investment group, the fund we control, and a couple of big LPs will make the decision and will make it promptly and efficiently.

Shasha Dai
To clarify, so should that consortium or should that coalition be formed and they will be acting on a deal-by-deal basis, correct?

Tony James
Yes, I guess, but I'm not sure exactly what you mean by that. Every deal we do in private equity, we do deal-by-deal.

Shasha Dai
Got it. Okay.

Tony James
Whether there's a fund or not.

Shasha Dai
Right. Now, next question has to do with the credit and especially energy related credit. I think you alluded to during the last quarter's call that the opportunity in general in energy regardless of whether it's credit or equity had not panned out as much as you guys had anticipated. Now, with this new progress with the new energy credit fund, do you anticipate the outlook to be any different in the next 12 months?

Tony James
As a private market investor, to some degree we compete with public markets. I think the drop in energy scared the bejesus out of people for a while, but then public markets suddenly decided well, it's not so bad, it's over, and a lot of companies that frankly we wouldn't have financed were able to access capital through public debt and equity markets on terms we wouldn't have done, so that I would say reduced the number of opportunities that we expected.

Having said that, it didn't eliminate them by any means. There's still a ton out there of interesting things to do, and our energy credit guys have been very active. They signed up some very interesting big new deals. And in private equity, on the equity side, it's by far the most active sector. I would say almost half of the pipeline that we have that's apt to get done is in energy and energy related stuff, so we have a lot going on there. It's maybe not the tidal wave of activities that it looked like it might be, but there's still a lot going on.

I would say people thought maybe this would be the sharp V, where there would be these collapsed energy prices, and energy prices would pop back up, and it's a little bit like the credit markets in '08. I'm not sure energy is going to work that way. We're already seeing a little W activity down at the bottom, and some of these down legs again got people backing up, and I think there'll be a ton of opportunity.

Shasha Dai
Okay. Last question has to do with GE Capital being bought by CPPIB. What do you think that means for the middle market sponsor financing space from a cost and a competitive standpoint?

Tony James
I think it's good for them that that team and that entity will move over and stay intact. I think some of the other bidders were looking to just buy the portfolio and make a sort of asset trade and dismantle the team. That would have been much worse for the middle market sponsors. Having said that, GE had a huge balance sheet, and it was AAA with access to very low cost funding, and they were able to be quite aggressive. My guess is that under CPP, they won't be able to be quite as aggressive, so it's better than the alternative but probably not as good as what was there once upon a time.

Shasha Dai
Thank you so much, Tony, as always.

Moderator
We'll go to Kelly Holman with Private Equity International. Please go ahead.

Kelly Holman
Tony, thanks for taking time to talk with us today. I had a question, something I wanted to run by you here, a couple questions. You mentioned the enormous amount of interest you had in Blackstone Capital Partners seventh fund, over allocated. We hear there's a number of LPs that are also cutting back their number of relationships with GPs. In that context, we wanted to get your sense on whether Blackstone is also considering cutting back the number of managers that

it works with on the LP side and if you're having more of a focus on working with preferred partners.

Tony James
Kelly, let me just say I think we are seeing too some of the big LPs wanting to concentrate their investments around some core managers, not to the exclusion of everyone else, but more concentration, and they want to do that for ease of operation, ease of administration. They want to do that in the hopes that they can get some preferential terms. Those terms might be economic, but they might be such things as training their young people, access to systems, quarterly calls on global outlooks, or whatever, so lots of things. They're all under cost pressures themselves, so their staff is under pressure.

They've realized that it takes a lot of time to administrate hundreds of GPs, and if you set several funds for each GP, you could have thousands of funds. There are drawdowns, and they've got annual meetings to go to and one thing and another. What they get for that when they have too much diversification is regression to the mean, and so their performance isn't very good either.

So, I think that attitude has changed, and there's definitely concentration. Of course, that's one of the things that has really played to Blackstone's interests because we're sort of the biggest in all the asset classes. I believe we're the best in all the asset classes, but we're also just about the only place someone can go and get a full spectrum of alternative products in a very high quality way, so that's been to our benefit.

Kelly Holman
So, you're not thinking about paring back the number of relationships that you're going to—

Tony James
I realized I haven't gotten to your question. I apologize for that preamble. No, we're not. So simply put, no, we're not planning on cutting back our relationships, really to the contrary. We continue to grow the base. We have more LPs than ever, and we're expanding more and more into retail products, as I mentioned. Retail products year-to-date are—I actually haven't added it all up yet, all the different forms, so a lot of forms, but a lot of money. And so if anything, our LP base is broadening.

Kelly Holman
Great. Okay, super. That's great. I think it's also interesting, earlier you alluded to about half of the capital that you deployed in the second quarter going outside of the US. Do you have a figure that we can put on that in terms of the private equity capital that was deployed in the second quarter outside of the US?

Tony James
I don't know what that would be off the top of my head. It's about half in the first quarter, too. I will say that.

Kelly Holman
About half of the 1.9?

Tony James
Let me see if one of the—

Laurence Tosi
Kelly, it's been consistently around 50% for this quarter, last quarter, and the last 12 months.

Tony James
For PE?

Laurence Tosi
For PE.

Tony James
For PE also? Okay, so it's the same for PE.

Kelly Holman
Okay. Great. Just one last question here. You've alluded to your strong focus on diverse asset classes. I know your real estate investment business has really ramped up. In light of that, are you still as committed to pure private equity, and has the asset mix between private equity and your real estate business changed markedly over the last few quarters?

Tony James
These things ebb and flow, and our fundraising is lumpy, so when we suddenly add another $20 billion to private equity, boom, that seesaw shifts. We love the private equity business. It's a great business. The returns continue to be spectacular, and I see no change in that. We love real estate, too. We love all our children.

Kelly Holman
Great. Okay. Thanks very much, Tony.

Moderator
Our next question is from Ryan Dezember with the Wall Street Journal. Please go ahead.

Ryan Dezember
Hi, Tony. Just a quick question. You mentioned how you guys are putting money to work and that half of it or so was outside the US. What specifically are you finding to do in private equity? What is the money going to? You've got a huge new pile of money to put to work, and we're eager to know what you guys are finding out there in this high priced environment.

Tony James
Ryan, I sort of mentioned this in some of my comments. We're putting a lot of money into some interesting— building interesting renewable kinds of assets and things like that where the beauty if you build new companies and you can get private type returns, the beauty of that is it's not a function of trading values. You're buying in at cost, whatever the cost of construction. You're buying in at book value. It's not a question of multiples of earnings and what the publics trade

at. If you go and build—we got a lot of press for an activity we have called Black Rhino in Africa, which is a joint venture with the richest gentleman in Africa building power plants in Africa. We're getting great returns from those kinds—we have a team that does renewables in Mexico and all over. We're the largest owner, or one of them, of wind farms in Germany.

These are new build assets that are yielding great returns and are divorced from market movements and overpricing and bids for public companies and whatnot, so a lot of it is that. And then all markets don't move together. Witness what's happening in China. It can run up big and then run down big, and so there's some values that come out of that. We try to go where people aren't.

Ryan Dezember
Thank you.

Peter Rose
Operator, we'll take the next question.

Moderator
Thank you. We'll go to Jonathan Brass with PERE. Please go ahead.

Jonathan Brass
Hi, Tony. Just touching on the colossal amount of dry powder at Blackstone at the moment in the context of private real estate, generally speaking, would you say it is currently a more straightforward exercise to raise equity for private real estate investments than to deploy it wisely?

Tony James
Let me put it this way, we would never take in more money than we thought we could deploy wisely. The reason that we have these caps and the reason we turn away these investors is because we don't want to take on more than we can invest. We're maniacal about protecting the historic returns. The returns that we earn today are just as good or better than we have ever earned, and we will preserve that as our goal.

Laurence Tosi
I just was going to add, John its L.T., that half of the capital in our dry powder has within two years been raised, so it's quite new and it has a long runway. And also, I'd look closely at—if you look in the release, we talk about that there's $8 billion capital deployed and about to be deployed or committed in real estate, which has really registered a new level of deployment. We're actually putting our capital—

Tony James
And that's the highest ever, by the way.

Laurence Tosi
And it's happening, wouldn't you say, Tony, in more deals and more broad-based globally than we've ever seen, so there are a constant list of deals that's quite different than it was just a few

years ago. We're seeing in Asia, the United States, and Europe, we're just seeing more deals and better flow, and there's good value there.

Tony James
Yes, and we're in new parts of the world. We have a much bigger team. We have more different kinds of businesses. This business has changed dramatically in its organizational footprint in the last three years, so it would be a mistake to think of it as a static team and a static global footprint and a static product mix—by product mix, I mean debt, equity, opportunistic core, and so on and so forth—that we're just trying to put more through.

And indeed, something like core private equity dwarfs in scale all of the opportunistic funds combined, so we're opening up vast new reservoirs of opportunity.

Jonathan Brass
Thanks very much. I supposed I'm just mindful of the notion that we're reaching a few cyclical zeniths in certain markets, and yet there's this unabated wall of the capital that wants into the marketplace. Obviously you guys have done pretty well to harness a fair bit of that, so it's interesting to hear some take on sort of capital versus opportunity, whether there's a match or a mismatch.

Tony James
That's a very fair observation, but that's why in my comments this wall of money and the overvaluation is not something that's just a creature of this last quarter. I think we'd all agree things have been very highly valued '15, '14, '13, '12. Forget '08, '09, and '10, go back and try, but in the last few years, interest rates have been near zero, and asset values have responded. But in that period of time, that's why I mentioned that we've been delivering returns of high 20s, 30%, across private equity, real estate, credit in that environment over the last three years, putting out record amounts of money. So yes, you can raise a lot of money, but we've been able to deploy a lot on great returns. I hope we can sustain those returns.

Jonathan Brass
Yes, yes. Okay, thank you very much.

Tony James
Right.

Moderator
We'll go to the line of Steven Gelsi with Buyouts Magazine. Please go ahead.

Steven Gelsi
Tony, how are you doing?

Tony James
Good. How are you?

Steven Gelsi
Good. I just wondered if you could give a little more color on the flagship fund. You said you're near the top of that. Just connecting the dots a little bit between some of the other funds you've been raising, it seems like you're limiting your flagship fund, even though there's more demand, and then you're starting up a lot of other new funds, so can you talk to that dynamic a little bit and walk us through a little bit more on the flagship fund and how that did with fundraising?

Tony James
The flagship private equity fund, Steven?

Steven Gelsi
Yes, ok.

Tony James
We went out, we thought this would be the usual kind of one year fundraising, and the investment results have been really strong. As Jonathan was saying, there's kind of a lot of money out there right now looking for decent returns, because if you look at what you're going to get in public bonds or even in public equities from here, one of the big investment banks doesa study each year where they project forward returns, and they estimated that government bonds would yield 2%, corporate bonds depending high yield or not would yield 3% to 4%, and equities would only yield 3.5% for a five-year return.

If that's your opportunity set for most of your money, all those are the liquid markets, then what we do looks pretty darn good. Couple that with the fact that there's been a massive amount of redemptions, not only ours. As I mentioned, we gave back $60 billion in the last 12 months, but other firms are giving back a lot of money, too. So LPs in their alternatives are not only eager to put more money to work because their alternatives and publics are worse, but they're getting a lot of money back while they're trying to put that money to work, so they've got run a little faster to stay on the treadmill. That creates obviously a good fundraising environment, which sure, we benefitted from that, but we benefitted from that because our returns have been so good and because our distributions back to LPs have been so strong.

So, instead of taking a year, it took like four months, and instead of having a series of closings over the year, all of sudden lo and behold we could have done more than the whole fund in the first closing, so we had to cut those people back to leave room for a few investors that couldn't have their board meetings, one thing or another, or just some of the international investors were a little slower because of their government agencies and whatnot. And then we do like to diversify our fund base, so we had made commitments to certain retail systems to have a certain amount of product we could offer into those retail systems, and that was scheduled out a ways, so we had to leave some capacity for those systems.

But let me just say this, that we have enough contractually committed demand from the first closers or from our institutions to take anything that's left and then some, so as far as we are concerned, this was one of the most successful fundraises we've ever had.

Steven Gelsi
Are you going raise the hard cap at all or just keep it, it's around $17 billion, I guess you said?

Tony James
It's $17.5 billion of investible capital, so if you compare that to some of the other firms when they announce their fund size, they include an estimate of the management fees and other things to be included. We don't include that. We're just investible capital. I think if you included the management fees and whatnot, this would be something over $20 billion.

We feel we should be disciplined. We feel we like living with the constraint, delivering high returns. Look, if we could invest it faster, we'll just be back sooner, but it keeps us disciplined, and I frankly I actually think it's good marketing for LPs. LPs love the discipline that comes when you give them money back or stick with a reasonable cap.

Steven Gelsi
Okay. And one other quick point, have you guys ever considered looking at BDC? I don't think Blackstone has a public BDC. Have you looked at doing that? The collapse in the marketplace now is mixed. The performance of them in the public market has been very mixed lately, especially from one of your big competitors.

Tony James
Actually we have something called Franklin Square out of our GSO. So, Franklin Square actually controls the GC, but Blackstone does all of the investing. It's performed extremely well and is actually the biggest BDC.

Steven Gelsi
I always thought Ares was the biggest BDC, so okay.

Tony James
No.

Steven Gelsi
All right, that's great. We'll make sure we keep that on the radar. Thanks a lot.

Tony James
All right, Steve. Thanks.

Moderator
We'll go with Anna Devine with Private Debt Investor. Please go ahead.

Anna Devine
Hi, Tony. Thanks for your time. I just wanted to ask you about your view on the direct lending for private debt market in Europe. Some say that the investment environment is the most difficult there since the crisis in terms of pricing, so I just wanted to hear what your view was and if you have any thoughts on how it could pan out.

Tony James
Okay. First of all, we're finding it to be a very, very good market right now. We're doing a lot, and we're getting very nice returns for the risk, we think. I think Europe is in some ways the most difficult market in terms of pricing for private equities, but for direct lending, we feel very good. And remember, the structure of the banking system in Europe is different from the US. It's traditionally much more that of loans stay on the bank's balance sheets. In the US, the big banks originate a package and distribute those loans. In Europe, they originate and hold them for the most part.

Incidentally, we are the largest non-bank buyer of loans in another business in Europe, so we're on both sides of that. But what happened with the European banks is, because they can't distribute, their balance sheets get full, and they're under the same capital pressures or maybe worse than the US banks. In fact, their balance sheets are generally much more leveraged than the US banks are, and they haven't raised the amount of equity than US banks have raised.

You can just list the names, Duetsche Bank, Standard Chartered. Compare that to JP Morgan. BofA came out and made $5.5 billion, announced yesterday made $5.5 billion for the quarter. The European banks are smaller, are more capital constrained, are under the same regulatory pressures, and yet they don't have the ability to originate and distribute assets. So, as a result, the European direct lending—there's a little bit of a vacuum in Europe for new direct loans, and we're finding the returns to be excellent.

Anna Devine
Okay. So, you touched a little bit there on comparing it to the US market. Do you think though that the opportunity is better in the US market?

Tony James
No.

Anna Devine
No?

Tony James
I actually like direct lending better in Europe for all the reasons that I mentioned, because in the US, you compete much more with the public markets and with securitizations and things like that, and there's just a much deeper capital market. I think Europe is much better. I would also say that our view of Europe is it's just in terms of the economic cycle, it's bottomed out, and there's a long runway ahead of it, whereas the US is more towards the mid part of the recovery cycle. So, we think Europe is going to be good.

Anna Devine
Okay. Could you just touch on Asia, too, if you have a view on that, on the private debt market there?

Tony James
Okay, Asia is a completely different kind of debt market, where depending on the country, creditor's rights might be extremely limited or not, it depends on the country, but in general, they're much more limited. For us, it's not a direct lending market that we're focused on for a lot of the creditors' rights, transparency, judicial system issues. The private debt markets in Asia that where people have done pretty well tend to be more loans against equity positions, so they're almost like sort of holding company loans, and you've got to know the sponsors pretty well, and you've got to know the equity values pretty well. We're not sizable there.

Anna Devine
Okay. Thank you. I was just wondering as well if you could give any color on your European direct lending fund in terms of size or strategy or how much capital you've deployed from that.

Tony James
Okay. I think the strategy is sort of direct lending to medium-sized businesses, and it's got about$2.9 billion of capital in it today.

Anna Devine
But would it be senior lending mainly, or would you branch into other areas in terms of the capital side with that fund?

Tony James
It's mainly senior lending, but sometimes they'll do a top to bottom capital structure, which will have some subordinated in it but most of the assets going into senior loans.

Anna Devine
Okay. What size of a ticket, what's the biggest size of ticket you could write with that?

Tony James
I don't know, but it's generally sub $250 million.

Anna Devine
All right. Well, thank you very much.

Tony James
Okay.

Moderator
With no further questions, I'll turn it back to you, Mr. Rose.

Peter Rose
Thank you all for listening. Again, a reminder of the call with investors at 11 o'clock. If you have further questions in the course of your reporting, please call the media relations office, and we'll do our best to help you. Thank you for joining us.