BLACKSTONE Second Quarter 2018 Earnings Investor Call
July 19, 2018 at 11:00 a.m. ET

Weston Tucker: Great, thank you, and good morning, and welcome to Blackstone's second quarter conference call. Joining today's call are Steve Schwarzman, chairman and CEO, Jon Gray, president and chief operating officer, Tony James, executive vice chairman, Michael Chae, 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 the shareholders page of our website. We expect to file our 10Q report early next month.

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. For a discussion of some of the risks that could affect results, please see the risk factors section of our 10K. We'll also refer to non-GAAP measures, and you'll find reconciliations in the press release. 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 $1.6 billion for the quarter, up sharply from the prior year comparable period. Economic net income, or ENI per share, was $0.90, up 55 percent from the prior year due to growth in performance revenues and investment income. Distributable earnings per common share were $0.56 for the quarter, and we declared a distribution of $0.58 to be paid to holders of record as of July 30th, which includes a $0.10 special distribution announced previously.

One final note for me. We'll be hosting our fifth Investor Day on September 21st in New York. We'll be sending out invitations in the next few weeks, but if you don't receive one and would like to attend, please let me know. The event will also be webcast. With that, I'll turn the call over to Steve.

Steve Schwarzman: Thanks, Weston, and good morning, and thank you for joining our call. Blackstone reported an excellent set of results for the second quarter and for the first half of the year. Total revenues, as Weston mentioned, were up over 30 percent in the quarter to $2 billion, while ENI rose 56 percent to $1.1 billion. The firm continued to deliver very attractive investment returns across a growing number of funds, and significantly outperformed global markets.

As a result, our limited partner investors are entrusting us with more of their capital to manage, driving grow inflows of $20 billion in the quarter, and $120 billion for the last 12 months, an all-time record for both Blackstone and any other alternative investment fund.

This fundraising momentum powered growth in our total assets under management of 18 percent year on year to $439 billion. Adjusting for the previous announced sale of our direct lending sub-advisor relationship for $580 million, the underlying rate of AUM growth would have been an exceptional 25 percent, a time period over which we also returned $42 billion to our LPs through realizations, and pro forma AUM was up about $10 billion from the first quarter.

Blackstone is expanding our leadership position in a high growth sector of money management, both by growing our well-established franchises, as well as developing new areas, including permanent capital vehicles. What we do with the capital we've raised is most critical, and in an environment of higher prices in many areas, we're still able to find good investments.

We've deployed nearly $50 billion over the past 12 months, a very active pace, and we will begin raising our flagship private equity and real estate funds in the next several months. We expect our fundraising “super cycle” to bring the firm's total AUM above the $500 billion milestone likely in the first half of next year.

Our ability to continue raising large scale capital begins and ends with investment performance. Across our global platform for the second quarter and first half of 2018, Blackstone's funds delivered dramatic outperformance with less risk. For the first half, if you'd invested in an index comprised of global stocks or high yield, you would have either made very little or lost money. The S&P was about the best performing, up 2.6 percent over this period, but it had high levels of volatility, while the global, Europe, and Asian stock index all declined, down anywhere from minus 1 to minus 5. And the high yield credit index returned zero – nothing.

Blackstone funds, however, produced an extremely different result. Our corporate private equity funds had a remarkable performance, appreciating nearly 10 percent in the quarter, and over 16 percent in the first 6 months of the year. That's over six times the S&P total return during this six month period. Just to repeat it in case you missed it, that's six times the S&P total return during the first six months of this year.

In real estate, our opportunistic funds appreciated approximately 3 percent in the quarter and 6 percent in the first half, despite headwinds from the stronger dollar, which Michael Chae will discuss in more detail. That's more than double the S&P.

In credit, our various strategies were up 4 to 5 percent gross in the quarter, and 3 to 8 percent for the first half, which is 1 to 3 times the S&P. And these are credit funds, not equity funds.

And in our hedge fund area, BAAM's composite gross return also beat global markets, despite its low volatility focus.

Since inception, our opportunistic private equity and real estate funds have returned 15 percent and 16 percent respectively per year, net of all fees, which equates to 650 to 900

basis points respectively over the relative indexes. This type of differentiated performance positions us well in an environment where capital flows are increasingly migrating to opposite ends of a barbell. On one side are the index funds, which primarily just mirror the indexes, and typically charge only several basis points of fees. On the other side are the alternative managers, including Blackstone, the reference institution in our industry.

Our funds have produced materially higher net returns for our LPs than market indices, and protected capital during market downturns. We've also generated higher earnings on AUM for our shareholders, given the combination of higher returns and better fee structures, all of this while consistently growing, with our AUM up fivefold in the last 11 years since our IPO.

This is why I have such optimism for the future of Blackstone and the alternative asset class as a whole. Our portfolio companies are in great shape, and are performing very well. The economic backdrop is quite healthy, despite the recent turbulence in markets, due in part to growing fears around the impact of rising protectionism on global trade.

This current situation is complex and highly dynamic, involving most of the major economies in the world simultaneously, which is actually unprecedented since World War II. While our portfolio overall has relatively limited direct exposure to global trade, an open, well-functioning system is important to the longer-term health of the economy and markets. With the volume of issues, the magnitude of potential impact on different countries, including the United States, I think it's logical to assume many of the current issues will get resolved.

However, rebalancing of relationship on issues as far reaching as trade and foreign policy will take some time. In the meanwhile, with $88 billion of dry powder capital, we can wait patiently for any opportunities that might arise from volatility, and move quickly to take advantage of them.

As one example, when real estate stocks traded off sharply earlier this year due to interest rate concerns in terms of interest rates going up, there was little differentiation between the highest and the lowest quality assets and those with the best growth potential. They all went down. Our focus on value led us to complete or commit to six public company going private transactions across three continents.

Across the firm, we're tremendously well-positioned to responding to changing market dynamics, with more strategies, with different mandates than any other alternatives firm. We're able to do more deals across asset classes and up and down the capital structure. And looking forward, we have more large scale new initiatives today than ever before, propelled by the firm's entrepreneurial culture, global reach, and brand.

In infrastructure, we've assembled a world class team comprised of Blackstone people from different areas around the firm, as well as a few key outside hires. We've received broad interest from individual institutional investors around the world, and have closed

on $5 billion or so, and we expect to grow this business substantially over time. We are now fully in deployment mode, and are evaluating a pipeline of interesting opportunities.

Other new initiatives are also progressing well. In insurance, we've added several highly talented professionals, as we continue to build out the best team in the industry. In private wealth, we now offer several products designed primarily or exclusively for this channel, such as our non-traded REIT, our ‘40 Act hedge fund, and our new credit interval fund.

Our non-traded REIT recently broke the $3 billion mark, capturing two-thirds of the entire industry's sales so far this year, as the strength of the Blackstone real estate platform resonates with this previously underserved market.

And in credit, we're rebuilding our direct lending AUM base, both the institutional and retail channels, and expect significant growth over the coming quarters.

In closing, Blackstone continues to deliver for our limited partners and our shareholders. We're relentless in terms of pursuing new markets and asset classes, enabling us to provide more solutions to more types of investors. We remain focused, alert, and hard-working. We're deploying record levels of capital, creating the basis for significant future realizations. Blackstone remains one of the highest yielding stocks of any large company in the world, with $2.22 paid out over the last 12 months, equating to a yield of over 6 percent, and with earnings growth well above that of most other public companies. And we continue to examine other ways to maximize shareholder value over the long term.

Blackstone has created the premier platform in the alternative asset industry, and we have no intention of slowing down. We look forward to discussing our firm and its prospects with you, as Weston mentioned, at our Investor Day in September. Thank you for joining our call. I'll now turn things over to our Chief Financial Officer, Michael Chae.

Michael Chae: Thanks, Steve, and good morning, everyone. Our strong results in the second quarter were highlighted by: very significant growth in revenue and economic net income, as Steve mentioned; stable and attractive fee related earnings and cash distributions; and continued robust deployment and fundraising momentum. I'll address each of these in my remarks this morning, starting with ENI.

Economic net income increased 56 percent to $1.1 billion, or $0.90 per share, the firm's best quarter since the first quarter of 2015. This result was driven, of course, by excellent investment performance, and private equity led the way. Private equity performance revenue and economic income both more than tripled year over year to $636 million and $581 million, respectively, the highest levels in over 3 years.

The corporate PE funds appreciated 9.5 percent in the quarter, and 26 percent for the prior 12 months. The strong performance was broad-based across the private and public portfolios, across sectors, with the energy and technology areas exhibiting particular strength. And notably, in the quarter we signed agreements to sell several companies at an average premium of greater than 30 percent to prior carrying values, resulting in a

meaningful valuation uplift.

In credit, strong fund performance drove the segment's best returns in each of its performing credit and distressed clusters since 2016. The performing credit funds were up 4.5 percent in the quarter, while the distressed funds rose 3.8 percent in an environment where the high yield index has been flat. Performance revenue tripled to $107 million, and economic income nearly doubled to $112 million. The largest drivers of GSO's funds outperformance in the quarter, Stars Group and EMI Music Publishing, were signature GSO deals involving large scale bespoke private capital solutions for corporates with complex financing needs. These investments are now reaching monetization, and our original $1.1 billion total investment in the two deals combined have generated a realized and unrealized multiple of invested capital of 2.3 times.

Fund appreciation across the firm was attractive in the quarter, despite headwinds from FX, as the US dollar strengthened broadly against most currencies. This impact was most apparent in real estate and Tac Ops, given their significant relative European and international footprints, reducing second quarter appreciation in these areas by around 1 to 2 percentage points. Excluding FX, BREP's appreciation in the second quarter was 3.9 percent, core plus was 3.1 percent, and Tac Ops was 4.5 percent.

As discussed on prior calls, we've been effectively neutralizing the impact of euro and pound-based FX volatility in our firm P&L for our shareholders through our Eurobond and swap positions, with this effect reflected in other revenue.

In aggregate, strong performance across the firm lifted the net accrued performance receivable on the balance sheet to $3.9 billion, up nearly 20 percent over the last 12 months, to its highest level in 3 years. This growth is despite $42 billion in realizations, which generated $1.7 billion of net realized performance fees in this period. This continues to illustrate a powerful and we believe underappreciated characteristic of our business, the ability to grow the firm's store of value while simultaneously paying out substantial distributions to shareholders.

Moving to fee related earnings, FRE increased 1 percent year over year to $315 million, stable despite the discontinuation of the prior direct lending subadvisory fees and spending on growth initiatives. On a normalized basis, underlying FRE growth continued at a double digit percentage pace. We would expect FRE to resume its historical trajectory of growth in the next several quarters.

Moving to DE and the distribution, distributable earnings were $700 million in the second quarter, or $0.56 per common share. Net of the 15 percent holdback, and including the special distribution, the total distribution to common shareholders was $0.58, up 7 percent versus the period year.

In terms of realizations, here real estate led the way. We realized $8 billion in the second quarter, including the final sale of our Hilton stake, which ultimately generated $3.1 times investors' capital, and $14 billion of profit, as well as several other public and

private sales across the firm, including several London office assets purchased between 2012 and 2015, that were sold this quarter for 2.1 times multiple of invested capital, notwithstanding the intervening Brexit event during the period of our ownership.

And we enter the third quarter with strong forward momentum in terms of realizations and distributable earnings. We have under contract an additional $4 billion of realizations, most or all of which we expect to close in the third quarter, including the sales of Ipreo, Intellinet, and the monetization of a private energy asset in private equity, a range of office and other real estate assets in the US, Europe, and Australia, and others.

In aggregate, we expect these sales to generate approximately $350 million or $0.28 per share in distributable earnings.

Moving to the deployment and inflow of capital, both areas in which we are experiencing robust momentum. In terms of deployments, we invested $8.4 billion and committed to another $9.3 billion across the firm in the quarter. This was our seventh consecutive quarter of greater than $8 billion in deployments, prior to which there had been only two such quarters in our history, demonstrating the breadth, diversity, and scaling of our strategies across businesses, and auguring greater value to be harvested in the future from this transformation in the scale of our business.

In terms of the inflow of capital and fundraising, as Steve noted, gross inflows reached $20 billion in the quarter and $38 billion in the first half of the year, reflecting a diverse array of initiatives across the firm. We had closings for strategies across our businesses, including our new infrastructure fund, our third tactical opportunity vintage, GSO's second energy fund, and final closes for our Asia-dedicated funds in real estate and private equity.

In real estate, core plus has grown to $32 million of AUM, nearly doubling year over year. GSO also closed two new CLOs, while BAAM raised $3 billion in the quarter, and nearly $7 billion year to date.

The pipeline moving forward is extensive. In terms of highlights, we expect closes in the near term for both private equity energy and GSO energy. We commenced raising our new secondaries flagship fund. In credit, we expect significant closes this quarter for our new direct lending business, and expect to launch in the second half our second GSO Europe fund.

In real estate, we'll shortly be launching our fourth permanent capital vehicle in core plus.

Finally, of course, as Steve mentioned, we'll soon be in the market with our global private equity and real estate flagship funds.

All told, following on the heels of $108 billion in inflows in 2017, and looking out to the balance of 2018 and 2019, if we execute according to plan, we believe we could amass in the area of $300 billion in new fund capital in the 2017 through 2019 three year period.

I'll close my remarks today with an update on our capital strategy and ongoing commitment to delivering shareholder value. This quarter, we'll be returning approximately $200 million in capital to unitholders through the first of our three $0.10 per unit special dividends, in addition to share repurchases. We initiated activity in our $1 billion share repurchase program during the quarter, and we're purchasing 2.2 million shares at an average price of $32.58. This is a tool we plan to use consistently and programmatically to keep our share count flat on an annual organic basis, and which, combined with our sizeable special distribution, enhances our highly attractive regular cash distribution policy.

With regards to our structure, we continue to consider our options. KKR's recent stock performance subsequent to their decision to convert has been noteworthy, and we will continue to watch and assess that and a variety of other factors over time. We like the position we are in today. We can closely monitor developments in the market and with our peers, and incorporate any learnings into our thinking on how to best maximize long term shareholder value. In other words, we will continue to take a deliberate and hard look at our options.

In the meantime, the firm continues to perform with great strength, and we believe our value proposition remains highly compelling. With that, we thank you for joining the call, and we'd like to open it up now for questions.

Operator: Ladies and gentlemen, if you do with to ask an audio question, please key star one. If you would like to withdraw your question, please key star two. Please limit yourself to one question. If you wish to ask another question, please key star one again to reenter the queue. Questions will be taken in the order received. There will be a brief pause to compile a list of questions.

The first question comes from the line of Ken Worthington. Please proceed.

Ken Worthington: Hi. Good morning, and thanks for taking my question. Maybe just on the insurance initiative, we'd really love to hear anything you can share on product development and the work you're doing with insurance companies and regulators to kind of built out that insurance presence. And if you can't do anything there, just updates on FGL. Thank you.

Jon Gray: So, hey, Ken. It's Jon Gray. I would say a couple of things. First, this is a long term initiative for us. We think the scale here is quite significant, given the underlying needs of insurers. The one thing we found early on is just how much pressure they're under because of where interest rates sit, and because of longevity. And as a result, they need to increase their returns.

So today as a firm, we manage across FGL, which you mentioned, as well as traditional drawdown funds, about $50 billion in this space, and we do expect that to grow considerably over time. That being said, we're in the process, of course, of building our

team. We've made a lot of progress under Chris Blunt. We've made a couple of key hires this quarter. We have some more in the pipeline. So we're moving forward on that. We're meeting with major insurers. We have a number of important discussions going on that could lead to interesting opportunities for us, but nothing really specific we can point to today.

But overall, as I said, a lot of optimism about the need for what we're doing, and also, I'd say we're making progress on building out our private credit origination capabilities. We do that in real estate today and in GSO, but there are other areas underneath those umbrellas we can add to to serve these insurance customers even better.

So I think there is a big opportunity here. It will take a bit of time to get at.

In terms of FGL, we feel good about what we've been able to do in terms of starting to move their assets into higher yielding. I don't want to talk too much about it, as they're a public company, but we feel good about being able to add additional return to their portfolio, which is what we stated at the time they were acquired.

Ken Worthington: Okay. Great. Thank you very much.

Operator: The next question comes from the line of Bill Katz with Citigroup. Please proceed.

Bill Katz: Okay. Thank you very much for taking the question as well. I'll leave the C corp to somebody else. So question just in terms of the super cycle. If I'm doing the math quickly, I think you said about $135 billion over the last 18 months, which is impressive in its own right. That leaves another $165 over the next year and a half or so. A, is that a fair way to think about it? And then maybe more importantly, how do you think about the interplay between the capital raising and sort of the FRE, fee rate, and margins? Thank you.

Michael Chae: Hey, Bill. It's Michael. I think your math on how you – the outlook over the next year and a half or two is generally – I think it's the right thinking, and dovetails with some of the statements I made.

In terms of the economics of the new capital, we basically think it's a stable picture, that we're not experiencing fee pressure, as we've talked about before, in these flagship funds. Our dynamics with our clients are terrific. Nor are we really looking to change things fundamentally around those arrangements with our LPs. So I think you can expect from that standpoint a stable picture.

And in terms of margins, look, I'd say overall, in terms of the contribution and the economics of what these new platforms will do for us, it's obviously very positive, I think from the perspective of all financial metrics.

Jon Gray: Yeah, I would just add obviously, if we're able to successfully raise these funds, which we expect to, it certainly will have a benefit as you look out to fee related earnings in particular, looking out a few years.

Michael Chae: Yeah. I mentioned where we are in the moment from an FRE standpoint, and the resumption of historical growth. I think we do see, Bill, then, in 2019, a return to historical or better FRE growth levels in the area of the strong double digits.

Tony James: And I would just add, too, while you might see – there's mix shift going on here. So stable pricing for each product category, but there are mix shift as we get more permanent capital vehicles and other things that are new to the picture. Even though some of those products have what look like lower fees per dollar of AUM, they're actually over time, as we play through, higher margin to the bottom line, because of the way assets accumulate so much faster than our costs. So you guys should all be mindful of those dynamics.

Bill Katz: Okay. Thank you.

Operator: The next question comes from the line of Rob Lee with KBW. Please proceed.

Rob Lee: Thank you. Good morning. Thanks for taking my question. One of the themes across the whole industry – when I say the whole industry, the traditional and alternatives – has been I think customization. And some of your alternatives peers have talked about they've seen some demand for more customized type of separate accounts that have more flexibility, and a very long dated assets, so they can kind of shift assets for clients pretty quickly, depending on where the best opportunities are.

Clearly, within BAAM, and I'm sure your insurance initiatives, customization is a part of it, but you guys don't talk too much about kind of maybe larger separate account relationships, where you're kind of helping direct at any given point in time where capital should be allocated. So can you maybe talk a little bit, are those some of the initiatives you have underway, or how you think about those types of products or relationships vis-à-vis kind of just raising money for discrete funds over time?

Jon Gray: Yeah, I think the customization for us, given the scale and breadth of our platform, is more focused in retail and insurance, where we're creating new products. BREIT is a great example of that, a private REIT in a space that historically had not been well-served, either in terms of cost or quality. And we created a customized product there. The market, as Steve described, has responded exceedingly well to that.

The same way I think in insurance we'll create vehicles, have begun already, that will target insurers, particularly given their regulatory capital needs. So those two areas, definitely.

In some of our more long-dated vehicles, core plus real estate, and private equity, there's probably a little more flexibility institutionally in terms of customization, but in our

broader areas – and I would say also in GSO, we can do a bit more in the SMA area. But generally, in our sort of mainline flagship areas, because we're so large, it tends to be more in the commingled fund area, and I don't expect that to change dramatically.

Steve Schwarzman: I would say one other thing. This is Steve. We have a business called Tactical Opportunities, which has about $20 billion of AUM. And Tac Ops' mandate is to take that money and put it wherever it looks like it's the best place to be in terms of asset classes and different places in the capital structure.

And so we start sort of in an advantageous position, if you will, with $20 billion there, and some of the separate accounts that I think you're hearing about involve firms that don't have the ability to put money in individual areas. And this is used as a way to seed some of those businesses, and also those accounts typically come with a lot of fee pressure on them, and a variety of other things in terms of crossing carries from different areas.

And we of course have separate accounts of scale, but we're pretty disciplined as to how we approach that area. And our funds almost always are all sold out. And so our system works exceptionally well, and I think some other people really need some AUM, and it helps them develop businesses, albeit at lower fee levels than we typically have.

Operator: The next question comes from the line of Alex Blostein with Goldman Sachs. Please proceed.

Alex Blostein: Thanks. Another question for you guys around the really robust fundraising outlook obviously for the next two years. I guess other than the flagship funds, can you help us unpack a little bit where you guys are assuming in terms of the insurance business and the credit business, that you expect to come in I guess for the next two years to get you guys to the $500 billion plus AUM in the first part of '19?

Michael Chae: Hey, Alex. This is Michael. If you're thinking about Steve's remark and sort of the path to that number in the early part of next year, in real estate, we've obviously talked about the launch of the BREP Global Fund. And we expect to focus on BREP Europe shortly thereafter.

In the core plus area, that has been moving along at a terrific pace, as you know. We've been raising money at about a $8 to $10 billion a year clip with things like BREIT only expanding. I mentioned a fourth BPP platform being launched in the second half of this year. So we certainly expect to sustain that pace.

I mentioned the eighth SP Global Buyout fund. That launch has happened, and we have high expectations for how that will go. And of course, the private equity fund that I mentioned. So – and in the credit area, multiple products: the energy fund, which is ongoing, European direct lending, which we'll launch shortly, as well as the direct lending initiative, which we've talked a lot about, and we're right in the thick of that now. So multiple, multiple strategies, diversity of strategy, and obviously scale.

Operator: Our next question comes from the line of Patrick Davitt with Autonomous. Please proceed.

Patrick Davitt: Hey. Good morning. Thank you. So we're getting – since we last chatted, we've gotten a better picture of what businesses are or could be impacted by the proposed tariffs. To what extent is your portfolio or any specific large holdings exposed to the products that have been announced or could be announced to be impacted? Or do you think it's really just about how it impacts broader economic activity? And within that, could you give an updated revenue and EBITDA growth trajectory for the PE portfolio?

Jon Gray: So I would say to date it's definitely been probably more market-focused. The China market has traded off the most, but global markets have been choppier, clearly, as a result of this.

On the ground, we've not seen a lot of impact. As you know, tariffs have just begun to be put in place. As it relates to Blackstone specifically, the good news is most of our portfolio companies are focused domestically in their home markets, be in the US, Europe, or Asia, or are service-oriented businesses.

The number of companies we have in the global supply chain, and we do have some who are exporters, is fairly limited. And as I said, to date, we haven't seen much of an impact. What's been a bigger impact, of course, is the strength of the US economy, which has been surprising everyone, including us. And that's really been the dominant theme on the ground.

So over time, of course, if this escalates, is protracted, spills into the broader economy, it could have a broader impact, and we're obviously watching that. But we're hopeful, as Steve said, these things will get resolved. They may not get all resolved at the same time with the various participants, but as it looks today on the ground, and with our portfolio, it's relatively limited impact.

Oh, growth statistics. What I would say is if you look at our overall private equity portfolio in the first half of the year, we're seeing EBITDA running call it about 10 percent up sort of since the start of the year. And probably more importantly, looking forward, when you talk to our CEOs and we survey them, their optimism is as high as its been, and I think that bodes well, of course, because CEOs are thinking about cap-ex and hiring and so forth. We saw that in the hiring numbers in the US, up 17 percent year to date.

So I think the forward outlook, at least on the ground in the US, it feels pretty good, and frankly, globally, there seems to be a fair amount of confidence. Obviously, that can change.

Operator: The next question comes from the line of Craig Siegenthaler with Credit Suisse. Please proceed.

Craig Siegenthaler: Hey, good morning, Steve, Michael. I wanted to better understand what factors you're analyzing as you make your final decision on the C corp conversion.

Jon Gray: Hey, Craig. It's Jon. As Michael pointed out, this is obviously a big decision for us, and one we can only make only one time, and it's got meaningful implications on the tax side to our shareholders, and so we're going to be really thoughtful and deliberate, as we pointed out.

Things we're looking at are obviously our facts and circumstances, tax and otherwise. As we look at other market participants, it's index inclusion, it's mutual fund ownership, and it's stock price performance. And as Michael said, we've got the benefit of watching some others, and this is obviously a significant issue, and we're going to try to be as thoughtful as possible before we make a decision.

Craig Siegenthaler: Thank you, Jon.

Operator: The next question comes from the line of Devin Ryan with JMP Securities. Please proceed.

Brian McKenna: Hi. This is Brian McKenna for Devin. Thanks for taking the question. It seems to be a common theme that deployment outside the US has been accelerating recently, but can you talk about some of the different drivers of this activity? And then when you think about the $88 billion of dry powder today, do you have any sense of how much of that could potentially be deployed outside the US?

Jon Gray: So I'll start with the second question. It's really hard to know where capital is going to be deployed over time, because for us, we sort of base it on where the best opportunities are, where we see compelling value. That's where we'll deploy. So I think going forward, hard to say.

Why are you seeing significant deployment from us globally? In some cases, real estate is a good example, there's probably a more attractive risk/return profile today as we sit, because there's some legacy distress in places like Spain. Interest rates are likely to stay I think lower for longer there. And so we've been leaning forward.

In other sectors, like private credit, I would also say Europe today there's a little less competition, and so we've been active there as well. Asia, where we've just raised new funds in real estate and private equity, is a big part of the world, growing faster than the rest of the world, significantly faster, and we've been taking advantage of that across the region, Australia, China, Japan. I think India in particular, given what's happening in IT services and business processing, has been a very positive theme for us, both in private equity and real estate, where we've been a big buyer of office buildings.

So I think it again speaks to what Steve and Michael were talking about, just the strength of this global platform. If you look back at our business 10, 15 years ago, it was much

more domestically focused, with a little bit in Europe. And today, if one market gets tougher, we can deploy elsewhere just like we can in other sectors.

So I think we're in different stages in valuation cycles in different countries around the world, and those things can change relatively quickly. I would say, however, on the US front, as I mentioned earlier, growth here in the US is pretty good, which is a positive as we look at deployment going forward. The challenge, of course, rising interest rates and inflation.

Michael Chae: And just to give you a number, about 40 percent of our deployments in the first half of the year were outside of the US. Outside North America.

Brian McKenna: Got it. Thank you.

Operator: The next question comes from the line of Glenn Schorr with Evercore ISI. Please proceed.

Glenn Schorr: Thank you. I'm curious if I could maybe get your updated thoughts on building a broad capital markets business. You continue to grow in size and across the capital structure. It feels like there's a ton of money to be made. I'm just curious what factors play a role in doing it or potentially not doing it.

Jon Gray: So I would say that there is some opportunity in that space, given the fact that we're at the intersection of so many different businesses, assets, different parts of the capital structure. So on the one hand, I do think we can do more there. On the other hand, I think everybody on this call knows we have been reluctant to be investing in balance sheet. We like our capital light approach and what we do. In our funds, we have a very modest amount of capital generally deployed. And we're focused on using our people and platform in order to raise capital.

And so to the extent we can grow our capital markets business without deployment of a lot of capital, I think that's an opportunity, but if it's going to mean putting up a lot of risk, I think we're going to be reluctant to do that.

Glenn Schorr: I appreciate that.

Operator: The next question comes from the line of Mike Carrier with the Bank of America Merrill Lynch. Please proceed.

Mike Carrier: Thanks a lot. I just wanted to, on the realization and the distribution outlook, so you guys gave some color for the third quarter. I just wanted to get some insight. When I look at the net accrued, the performance of some of the funds, both on the private equity, real estate, there could be some – when you look at maybe the seasoning of the portfolios, is this a kind of good run rate when we're looking out over the next 12 months, assuming that the market remains constructive?

Michael Chae: Mike, look, I think all of the stats are obviously positive around the pipeline and around the growth in the receivable. The receivable is – the carry receivable, it's maturing in terms of kind of the average hold, which is always a good leading indicator of monetizations. And our DE in the second quarter was higher than the first quarter, and we enter the third quarter with the pipeline I mentioned.

So we tend to look – you have your best visibility in near term around this stuff, and we like that outlook. We would hesitate to look far in the future. But again, we're in good position in terms of the basic situation of value on the ground, value seasoning, and the ability to get at that over time.

Tony James: And momentum, operating momentum of the assets.

Mike Carrier: All right. Thanks.

Operator: The next question comes from the line of Jerry O'Hara with Jefferies. Please proceed.

Jerry O'Hara: Great. Thanks. Maybe just one on the infrastructure initiative, the $4.6 billion cited in the – as the first close. Was that something that was already matched dollar for dollar, or perhaps is that kind of from the structural perspective on the comp? And then I think earlier today on the media call you had mentioned some deployments that were already kind of in process, not specific deals, but perhaps can you simply talk a little bit thematically about how you are approaching that?

Jon Gray: Sure. So just to clarify, we did have $4.6 at the end of the quarter. Shortly after the end of the quarter, we got to $5 billion. That includes the matching from our anchor investor. And as we've said, what we built here now over the last six months is a terrific team of people, both of existing Blackstone people and some outside folks.

In terms of the pipeline, nothing we can say directly, just that we're actively working now – you know, it's hard to invest when you don't have capital. Once you have a closed fund, it's game on at that point. And so we're starting to look at things.

Specifically, there are sectors like the midstream space, where reading in the papers, obviously, volumes are growing, particularly coming out of places like the Permian, and there is need for midstream assets infrastructure there. But we're looking across the landscape, telecom, infrastructure, water, renewables, and obviously, some public to private partnerships as well, and more traditional infrastructure.

So this is a business that we think we're really well-positioned in, because of the need for large amounts of capital. We're going to build a scale business. It's in an open-ended structure, which I think sometimes is hard for some of the folks in the media to follow, because it's different than our traditional you raise all the money up front. This gets raised over time.

The best model for this is what we did in core real estate, where we started with $1 billion in these open-ended structures, and are now over $30 billion today. So we feel really good about the start we've got, the matching funds we've got, and the investment outlook, but now it's time for us to execute.

Jerry O'Hara: Great. Thank you.

Operator: The next question comes from the line of Brian Bedell with Deutsche Bank. Please proceed.

Brian Bedell: Great. Thanks very much. If you could just go back to the fundraising and the FRE build. So of that incremental $165 billion or so over the next six quarters, is the incremental $35 billion in infrastructure , the gap for targeting $40 billion, is that in that number? And then also, if you can comment to what degree you have any plans for large insurance deals in that number – are those over and above? And then I don't know if you can talk about the timing, rough timing, of the launch of the flagship private equity and BREP funds, and the potential stepdown of fee rates of BCP7 and BREP8 as you bring those funds on.

Jon Gray: So in terms of infrastructure, just as a reminder, again, we said that that's an objective over time to get to the $40 billion, one we still expect to, but that's not something we're saying will happen in such a short period of time. This is a business we're going to build over time, where we have to deploy the capital, and as we do that, we'll continue to raise money.

So people I think have focused on that announcement, and maybe extrapolated too quickly. We're going to get there, but this will be like other business, take a number of years for that to happen. Michael can comment on what's embedded, but I don't think there's anything – some sort of huge sea change in insurance embedded in our numbers. We do have a tendency to find things over time that are large and interesting, like we did with Fidelity Guaranty, or we did with the Logicor transaction in real estate, but nothing I think is embedded in our assumptions there.

In terms of timing, we're going to launch very soon on our latest global real estate fund, and we potentially could have a closing as early as the end of this year. I don't know that for sure. But that's a potential. On the private equity side, again, we'll probably be launching here in the next quarter, let's call it, and we would expect the first closing in that to be sometime in the first half of 2019.

Operator: The next question comes from the line of Mike Cyprys with Morgan Stanley. Please proceed.

Mike Cyprys: Hi. Good morning. Thanks for taking the question. It's been about seven months or so now with tax reform in place. I'm just curious if you could talk about the impact that you're seeing on the economy, what signs you're seeing that it may accelerate the end of the cycle, and just lastly there, what's your view that the tax law may actually

increase cyclicality, given the cap on NOLs and the cap on interest deductability? In other words, could downturns be more severe with greater default rates on the back of tax reform?

Jon Gray: Well, I would say on the ground, talking to our CEOs and other companies we interact with, tax reform has increased in many cases their cash flows and has made them more confident, and so I do think it's having some impact. You can see it in the numbers, S&P cap-ex spending in the first quarter I think was up close to 20 percent. S&P earnings are up 20 percent. And so when companies' earnings are up, they tend to be more inclined to hire, they tend to be more inclined to spend cap-ex, they tend to be more inclined to travel. And you've seen that in the hotel business, where there's been a reacceleration of same store sales in that sector, as an example.

So I would say what we're seeing on the ground is positive, and some of that I think has to be attributed to the tax reform. In terms of the increased cyclicality, I haven't really thought about that. I don't see that as an impact in terms of one of the – the fact that companies are paying less tax. I think the bigger impact obviously is around potentially deficits and what happens with inflation and interest rates. I see that as a more significant impact than some sort of pro-cyclical impact.

Michael Chae: Yeah, Mike, I'd just add that I think that was the theory before tax reform, when we were all doing our models as to whether sort of the cuspiest credits or distressed credits or stressed credits, because of that change in deductabiltiy, would get pushed over. We've not seen that in practice. We all see the default rates. And also add to that the fact that we have a pretty healthy economic context, and you have a lot of – a lot of these borrowers obviously have covenant light credit structures.

So that may get tested as we get into a true distressed cycle, and there may be some subsection of companies that sort of wouldn't have defaulted, if not for that. But it's pretty theoretical. It hasn't materialized yet.

Mike Cyprys: Great. Thank you.

Operator: Our final question comes from the line of Chris Shutler with William Blair. Please proceed.

Chris Shutler: Hey, guys. Good morning. I just wanted to follow up on Glen's question earlier on the balance sheet. So could you be more specific on the – any hesitations you have. Clearly it adds risk, but I would think at a minimum, you might be able to be more aggressive deploying capital in the more stable core plus, core PE types of deals, as a way of enhancing long term shareholder value. So any comments there would be helpful.

Jon Gray: Yeah, I think there are situations where, as you're raising a new fund, you might use, and we have in very – a small number of circumstances, some commitment where we have good line of sight that we're going to raise the money, but getting into the business of committing to very large deals, putting it on the balance sheet, syndicating

that out, that hasn't been, I don't think it will be, our model. We really rely on the confidence of our investors. Because of the great returns we produce across the entire firm over long periods of time, we've generally been able to raise third party capital to execute our business plans. That's what we want to stick with.

There may be circumstances where we need to use our balance sheet, but I would use those or think of them as exceptions.

Tony James: Yeah, and I would just say, rather than accumulating a lot of cash on our balance sheet, we're paying it out to shareholders, even in terms of dividends or in buybacks. And we're maintaining a strong – we believe in maintaining a rock solid balance sheet for a rainy day, so that we can do the kind of things Jon's talking about, but not using it willy nilly, just to load up.

Chris Shutler: Yeah. Just thinking you might be able earn better returns than a lot of your shareholders. Thanks.

Tony James: They should invest in our funds.

Operator: I will now turn the call back over to Weston Tucker for closing remarks.

Weston Tucker: Great. Thanks, everyone for joining us today, and please follow up after the call if you have any questions.