

How Blackstone Will Divvy Up Its IPO Riches

Schwarzman to Hold \$7.5 Billion in Stock; Peterson's Big Payday

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The founders of private-equity firm Blackstone Group will reap billions from its initial public offering of stock, with Steve Schwarzman getting stock valued at roughly \$7.5 billion and Peter Peterson taking home nearly \$2 billion in cash for his stake.

Those are far-bigger initial paydays than even the founders of Google Inc. reaped in their high-profile IPO three years ago.

Blackstone, like other private-equity firms, makes its money by amassing investments from pension funds, endowments and wealthy individuals -- then buying up companies, turning them around and reselling them. It plans to sell 133.3 million common units of the limited partnership for between \$29 and \$31 each in the biggest U.S. public offering in five years. That 10% is valued at about \$4 billion and can be increased by an additional \$600 million. In addition, the sale of a stake of almost 10% to the Chinese government will bring the overall total to about \$8 billion.

While the overall numbers have been known for some time, details of who got what at Blackstone, the subject of constant revision up until the last moment, were revealed yesterday in a regulatory filing. The IPO is expected in the last week in June.

The 60-year-old Mr. Schwarzman, the co-founder of Blackstone and its current chairman and chief executive officer, will own 23% of the company -- a stake likely valued at more than \$7.5 billion -- and walk away with about \$677 million in cash proceeds from the IPO. Meanwhile, Mr. Schwarzman's 81-year-old co-founder, Mr. Peterson, will sell \$1.88 billion of his stake in the firm, leaving him with 4% of Blackstone, valued at roughly \$1.3 billion. Mr. Schwarzman's designated successor and Blackstone's current president, Tony James, age 56, will get \$189 million, and his 4.8% stake will be valued at \$1.6 billion.

Blackstone directors and executive officers in total will have almost 70% of the firm after the listing. In addition, the filing noted that Mr. Schwarzman received \$398 million in cash distributions last year, while Mr. Peterson collected \$213 million as his share of the gain on investments.

Blackstone will use roughly half the IPO proceeds to buy back stakes from Mr. Schwarzman and other owners.

Even as the firm's executives pocketed hundreds of millions of dollars, the offering documents warned that Blackstone could be facing a tough stretch. The firm warned that Blackstone and its investors could be taxed at significantly higher rates if Congress changes the way carried interest in partnerships is taxed. In addition, the document noted that Blackstone expects significant

losses for a number of years following the listing as amortization and compensation expenses will increase "substantially."

Mr. Schwarzman's stake in Blackstone at the offering price is more than double the value of the \$3.3 billion stakes held by Google Inc. co-founders Sergey Brin and Larry Page when the company went public in August 2004 at \$85. Their stakes have roughly quadrupled in value as Google shares have soared to more than \$500 in less than three years.

In the ranking of executives holding stakes in their companies, Mr. Schwarzman's will rank behind Microsoft Corp.'s Steve Ballmer's \$12.6 billion and close to Rupert Murdoch's \$7.7 billion stake in News Corp., according to Equilar Inc.

Blackstone's Billions

What key financiers at Blackstone Group stand to reap from the IPO, if the full amount of shares are sold; what they made last year (performance-based cash distributions); and how much their remaining stakes in the firm would be worth:

Executive/title	What they could make in the IPO	Their earnings last year, in millions	Remaining worth of stake in firm	Stake in firm*
Stephen Schwarzman Chairman and CEO	\$677.2 million	\$398.3	\$7.5 billion	23.0%
Peter Peterson Senior chairman	1.88 billion	212.9	\$1.3 billion	4.0
Hamilton James President	188.5 million	97.3	\$1.56 billion	4.8
J. Tomilson Hill Vice chairman	22.1 million	45.6	\$534 million	1.6
Michael Puglisi Chief Financial Officer	13.4 million	17.4	\$231 million	0.7

*assuming IPO prices at \$30, midpoint of range
Sources: Blackstone filing, WSJ reporting

The division of the spoils at Blackstone, which was overseen by Mr. James with Mr. Schwarzman as the final arbiter, confirms that in fact most private-equity firms hardly function as a partnership of equals. Instead, a small circle of founders control a disproportionate share of the firm, while most partners are left sparring for their cut of the rest.

For example, at TPG (the former Texas Pacific Group), founders David Bonderman and Jim Coulter own most of the firm, and when they bought out the third founding partner, Bill Price, last year, most of his equity went back to the remaining two.

Blackstone executives tried to avoid an internal battle between the haves, the have-lesses and the have-nots. That was complicated by Mr. Schwartzman's penchant for taking big cuts of the firm's profits. No founder of any of the major private-equity firm had ever kept as much of the equity in the firm as Mr. Schwarzman, according to numerous people familiar with the matter, and that alienated some former Blackstone executives, these people said.

This time, both Mr. Schwarzman and Mr. James were determined that the process satisfy everyone, including talented young people the firm wanted to retain. Mr. James suggested

distributing the firm's equity as democratically as possible, according to people who were briefed on the matter.

He told associates that this would avoid resentments, these people say. Blackstone executives consulted with executives at Goldman Sachs Group Inc. for tips on how to avoid internal dissension over money. One result: Blackstone, like Goldman, eventually set aside billions of dollars to reward nonpartners in a bid to keep future stars at the firm content.

Blackstone executives declined to comment on the filing. The Securities and Exchange Commission imposes a quiet period before an IPO.

The division of the spoils became easier when the value of the company became clear. Early in the IPO process, Blackstone's investment bankers put a valuation on the firm, but Messrs. Schwarzman and James believed the number was too high, according to people familiar with the matter. But the January listing of alternative-investment firm Fortress Investment Group LLC confirmed just how valuable their business was likely to be.

Still, the negotiation over shares was intense, these people add. Blackstone has adopted a complicated formula that commits most principals to hold the bulk of their shares for as long as eight years to ensure that they don't leave after their firm goes public. And while senior managing directors all receive a \$350,000 salary, the bulk of what they take home remains tied to investment performance to keep their interests aligned with those of the public shareholders.

It is Mr. Schwarzman and Mr. James to whom potential investors will look for future performance. Since Mr. James joined Blackstone, turnover among Blackstone staffers has slowed greatly. Mr. Peterson has been less active in the firm in the past several years and will formally sever his relationship with Blackstone next year.

For his part, Mr. Peterson himself has told outsiders, "I have reduced my shares on my own. I never wanted a situation where the younger people at Blackstone would feel they missed it." Mr. Peterson plans to devote much of his time and his wealth to charitable causes.

Some analysts note that Blackstone executives received much less cash than the top hedge-fund managers last year. And compared with other private-equity firms, Blackstone tries to cultivate a more modest image. The offer memo refers to the fact that Messrs. Schwarzman, Peterson and James reimburse the company for personal use of airplanes. But other partners are expected to fly regular commercial flights, compared with their counterparts at firms like TPG and Kohlberg Kravis Roberts & Co., a fact that gives rise to considerable complaints internally.

Despite such gestures, Mr. Schwarzman and Blackstone have become candidates for a potential backlash and regulatory action.

"Going public entails another whole level of scrutiny," Daniel D'Aniello, co-founder of Carlyle Group, another large private-equity firm, said at a recent conference. "The government always follows the money."

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