STEPHEN A. SCHWARZMAN
Chairman, CEO and co-founder of Blackstone

WHAT IT TAKES

Lessons in the Pursuit of Excellence

'This story literally has what it takes: the anecdotes, the insights and, most of all, the values to guide the next generation of entrepreneurs.'
Mark Carney, governor of the Bank of England

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What It Takes

LESSONS IN THE PURSUIT OF EXCELLENCE

Stephen A. Schwarzman

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MADE, NOT BORN

In spring 1987, I flew to Boston to meet with the endowment team at the Massachusetts Institute of Technology. I was trying to raise money for Blackstone's first investment fund and had set a target of $1 billion. This would make us the biggest first fund of our kind and the third biggest in the world. It was an ambitious goal. Most people said it was impossible. But I've always believed that it's just as hard to achieve big goals as it is small ones. The only difference is that bigger goals have much more significant consequences. Since you can tackle only one personally defining effort at a time, it's important to pursue a goal that is truly worthy of the focus it will require to ensure its success.

Countless rejections later, though, I was starting to panic.

Pete Peterson and I had started Blackstone in 1985 with high hopes and a carefully conceived strategy. But business hadn't been coming in at anything like the rate we had planned. We had gone from the pinnacle of Wall Street at Lehman Brothers, a famous investment bank where Pete was chief executive and I had run the world's busiest mergers and acquisitions department, to objects of potential ridicule. If we couldn't raise this money, it would call our entire business model into question. Our former rivals were hoping we would fail, and I was worried they might be right.

I confirmed our appointment at MIT the day before and arrived on Massachusetts Avenue with Pete, ready to talk about our plans and get a commitment. We found a door with a frosted window, marked MIT Endowment, and knocked. No answer. We knocked again, then a third and fourth time. I checked my schedule to make sure we were in the right place. Pete, who at sixty-one was twenty-one years older than me and had been commerce secretary under President Nixon before joining Lehman, stood behind me looking unamused.

Finally, a passing janitor saw us and stopped. We told him we were there to see the people at the endowment fund.

"Oh. It's Friday. They left a while ago," he said.

"But we have a 3:00 p.m. appointment," I said.

"I saw them leave. They'll be back on Monday morning."

As Pete and I left with our heads down and shoulders slumped, it began to rain. We were unprepared for the weather, without a raincoat or umbrella, so we stood at the exit to MIT's administration building, hoping to wait it out. Twenty minutes later, it was pouring harder.

I had to do something. I left Pete and ran into the street to try to hail a taxi. In no time, the rain soaked through my jacket and shirt straight to my skin. My clothes were hanging off me like rags, the water streaming into my eyes and down my face. Every time I thought I finally had a taxi, someone else grabbed it before me. Desperate and drenched, I spotted a cab sitting at a red light and ran over to it. I banged on the back window and held up a limp twenty-dollar bill, hoping the bribe would be enough for the passenger to let us get in with him. He stared at me through the glass. I must have looked bizarre, hammering on the window in my sopping wet suit. He refused. Two more people did the same. I raised my offer to thirty dollars and finally someone accepted.

It was the closest to a deal I had gotten in weeks.

I waved Pete over and he began slowly walking toward me, wetter and grumpier with every step. His full head of hair was pasted to his head as if he were standing in the shower. Pete was used to having cars waiting for him, drivers holding umbrellas as he got in and out. But a year and a half before, he and I had decided to start a business together. And from the look on his face as he walked through the puddles, I could tell he regretted it.

It hadn't been that long ago that Pete and I could call anyone in Corporate America or in governments around the world and find a receptive audience. Neither of us imagined starting a business would be easy. Nor did we envision being slumped in our seats at Logan Airport on a Friday night, soaked to our skins, without a dollar to show for our efforts.

Every entrepreneur knows the feeling: that moment of despair when the only thing you are aware of is the giant gap between where you find yourself and the life and business you imagine. Once you succeed, people see only the success. If you fail, they see only the failure. Rarely do they see the turning points that could have taken you in a completely different direction. But it's at these inflection points that the most important lessons in business and life are learned.

In 2010, Drew Faust, then president of Harvard, came to see me in New York. We spoke about a lot of things, but spent most of our time talking about running large organizations. When she retired from Harvard in 2018, she found the lengthy notes she had taken at our meeting and sent them to me. Among the many things she jotted down, one stood out: "The best executives are made, not born. They absorb information, study their own experiences, learn from their mistakes, and evolve."

I certainly did.

Not long after I saw Drew, I had a conversation with Hank Paulson, the former US treasury secretary and chief executive of Goldman Sachs, who suggested I go over my old calendars, record my thoughts on building and managing an organization, and have them transcribed in case I might someday want to publish them. He thought my experiences and lessons would be of interest to a much wider audience. I took him up on his suggestion.

I regularly speak to audiences of students, executives, investors, politicians, and people at nonprofit organizations. The most frequent questions I get are about how we built, and now manage, Blackstone. People are fascinated by the process of imagining, starting, and growing an organization and creating a culture that attracts highly talented people. They also want to know what kind of person takes on such a challenge—what traits, values, and habits this person must have.

I never wanted to write a memoir chronicling every moment of my life. I never considered myself worthy enough. Instead I decided to pick events and episodes where I learned something important about the world and my work in it. This book is a collection of some of the inflection points that led to who I am today and the lessons they taught me, which I hope will be useful to you.

I grew up in the middle-class suburbs of Philadelphia, absorbing the values of 1950s America: integrity, straightforwardness, and hard work. My parents had never given me any money beyond my allowance, so my brothers and I had to earn our own. I worked in my family's linens store, sold candy bars and lightbulbs door-to-door, delivered telephone books, and started a lawn-mowing service with two part-time employees—my younger twin brothers. They got half the revenue for doing the work, and I kept the other half for securing clients. The business lasted three full years before we had an employee strike.

Today my calendar is filled with opportunities that I could never have imagined: meetings with heads of state, the most senior business executives, media personalities, financiers, legislators, journalists, university presidents, and leaders of illustrious cultural institutions.

How did I get here?

I had incredible teachers. My parents taught me the values of honesty, common decency, and achievement, and the importance of generosity toward others. My high school track coach, Jack Armstrong, helped me develop a high tolerance for pain and to understand the power of preparation, essential lessons for any entrepreneur. Running track with Bobby Bryant, my high school best friend, I learned about loyalty and what it means to be part of a team.

In college, I studied hard, pursued adventure, and initiated projects to improve our community. I learned to listen to people, pay attention to what they want and need even when they don't say it, and be fearless when it comes to tackling difficult problems. I never imagined myself in business, though; I never took an economics course—and still haven't. When I started on Wall Street at the securities firm Donaldson Lufkin Jenrette, I didn't even know what a security was, and my math skills were modest at best. My brothers never missed a chance to express their amazement. "You, Steve? In finance?"

But what I lacked in basic economics, I made up for with my ability to see patterns and develop new solutions and paradigms, and with the sheer will to turn my ideas into reality. Finance proved to be the means for me to learn about the world, form relationships, tackle significant challenges, and channel my ambition. It also allowed me to refine my ability to simplify complex problems by focusing on only the two or three issues that will determine the outcome.

Building Blackstone has been the most consequential personal challenge of my lifetime. The firm has come a long way since Pete and I stood in the rain outside MIT. Today it is the world's largest manager of alternative assets. Conventional assets are cash, stocks, and bonds. The broad category of "alternatives" includes pretty much everything else. We build, buy, fix, and sell companies and real estate. The companies we invest in employ more than 500,000 people, making Blackstone and its portfolio companies one of the largest US–based employers and one of the largest employers anywhere in the world. We find the best hedge fund managers and give them money to invest. We also lend money to companies and invest in fixed-income securities.

Our clients are large institutional investors, pension funds, government-run investment funds, university endowments, insurance companies, and individual investors. Our duty is to create long-term value for our investors, the companies and assets we invest in, and the communities in which we work.

Blackstone is a remarkable success because of our culture. We believe in meritocracy and excellence, openness and integrity. And we work hard to hire only people who share those beliefs. We are fixated on managing risk and never losing money. We are strong believers in innovation and growth—constantly asking questions in order to anticipate events so that we can evolve and change before we are forced to. There are no patents in finance. A good business with high profits today can be a poor business with low profits tomorrow. Because of competition and disruption, if all you rely on is a single line of business, your organization may not survive. We have assembled an extraordinary team at Blackstone, driven by a common mission to be the best in the world at whatever we choose to do. With a benchmark like that, it's always easy to measure where we stand.

As Blackstone's breadth and reach have grown, so have the opportunities available to me outside business. I would never have thought that the lessons I learned as an entrepreneur and deal maker, coupled with the relationships I built across industry, government, education, and the nonprofit world, would someday enable me to serve as chairman of the John F. Kennedy Center for the Performing Arts in Washington, DC, or establish a prestigious graduate fellowship program in China: the Schwarzman Scholars. I am lucky to have been able to approach my philanthropy with the same principles I apply in business: identifying and addressing complex challenges by developing creative, thoughtful solutions. Whether it's building a first-of-its-kind student and cultural center on Yale's campus, or establishing a college to make MIT the first artificial intelligence–enabled university in the world, or designing an initiative at Oxford to redefine the study of the humanities for the twenty-first century, the projects I work on these days focus on applying resources to change paradigms in a way that will have an impact on lives, not just the bottom line. It has been my privilege to give more than $1 billion to support transformational projects whose impact will far exceed their financial value and long outlive me.

I also spend significant time answering calls or meeting with senior government officials around the world who are facing major challenges and need solutions. I am still astonished every time I hear from a world leader who wants my advice or point of view on a domestic or international issue of importance. In every instance, I do my best to help if I can.

I hope the lessons in this book are of use to you, whether you are a student, an entrepreneur, a manager, a member of a team trying to make your organization better, or simply someone searching for ways to maximize your potential.

For me, the greatest rewards in life have come from creating something new, unexpected, and impactful. I am constantly in pursuit of excellence. When people ask me how I succeed, my basic answer is always the same: I see a unique opportunity, and I go for it with everything I have.

And I never give up.

REMOVE THE OBSTACLES

GO BIG

Schwarzman's Curtains and Linens sat beneath the elevated train in the middle-class Frankford section of Philadelphia, selling draperies, bedding, towels, and other household goods. The store was busy, the products good, the prices fair, and the customers loyal. My father, who had inherited the business from my grandfather, was knowledgeable and friendly. He was happy running the business just as it was. For all his intelligence and hard work, he had no ambition to move beyond his comfort zone.

I started working at the store when I was ten years old for ten cents an hour. I soon asked my grandfather for a raise to twenty-five cents an hour. He refused. "What makes you think you're worth twenty-five cents an hour?" I wasn't actually. When a customer came in with window measurements and wanted to know how much fabric she needed for drapes, I wouldn't have the foggiest idea how to figure it out or what to tell her, or even the desire to learn. During the Christmas season I was put in charge of selling linen handkerchiefs to elderly ladies on Friday nights and Saturdays. I'd spend hours opening box after box of nearly identical handkerchiefs, none costing more than a dollar, and then pack them all away again once the customer had made her choice or rejected everything after five or ten minutes. It felt like a waste of time. In my four years as an employee, I evolved from a grumpy child to an argumentative teenager. I was particularly upset about the toll this job was taking on my social life. Instead of attending football games and high school dances, I was stuck at the store, cut off from the world I wanted to be a part of.

But while I could never master gift wrapping, I could see the potential for Schwarzman's to grow. The Greatest Generation had returned from World War II. We were in an era of extraordinary peace and affluence. Homes were being built, suburbs were expanding, and the birthrate was spiking. That meant more bedrooms, more bathrooms, and more demand for linens. What were we doing with one store in Philadelphia? When America thought linens, it should be thinking Schwarzman's Curtains and Linens. I could imagine our stores from coast to coast like today's Bed Bath & Beyond. That was a vision I could fold hankies for. My father disagreed.

"Okay," I said. "We could just expand all over Pennsylvania."

"No," he said. "I don't think I want to do that."

"How about Philadelphia? That couldn't be too difficult."

"I'm not really interested."

"How can you not be interested?" I said. "We have all these people who come into the store. We could be like Sears."—which was prosperous and ubiquitous at that point—"Why don't you want to do this?"

"People will steal from the cash register."

"Dad, they're not going to steal from the cash register. Sears has stores all over the country. I'm sure they've figured it out. Why don't you want to expand? We could be huge."

"Steve," he said, "I'm a very happy man. We have a nice house. We have two cars. I have enough money to send you and your brothers to college. What more do I need?"

"It isn't about what you need. It's about wants."

"I don't want it. I don't need it. That will not make me happy."

I shook my head. "I don't understand. This is a sure thing."

Today, I understand. You can learn to be a manager. You can even learn to be a leader. But you can't learn to be an entrepreneur.

My mother, Arline, was restless and ambitious, a great complement to my father. She saw our family coming up in the world. She once decided to learn to sail—I suppose she imagined us like the Kennedys, hair blowing in the salt breeze off Hyannis Port—so she bought a twenty-foot sailboat, learned to sail it, and entered us in races—Mom at the helm, Dad doing as he was told. She won lots of trophies. My twin brothers and I always admired her competitiveness and will to win. In a different era, she would have been CEO of a major corporation.

We lived in a semidetached stone and brick house in Oxford Circle, an almost entirely Jewish neighborhood of Philadelphia, and I grew up playing on playgrounds littered with broken glass bottles, surrounded by kids smoking. The father of one of my best friends, who lived across the street, was killed by the mafia. My mother didn't like seeing me with the guys in black leather jackets who hung out at the bowling lanes along Castor Avenue. She wanted better schools for us. So not long after I started junior high, she decided to move us out to the more affluent suburbs.

In Huntingdon Valley, Jews were a rarity, about 1 percent of the population. Most people were white, Episcopalian or Catholic, happy with their place in the world. I found everything there incredibly easy. No one was trying to hurt or threaten me. I did well academically and led the state championship track team.

In the 1960s, the United States felt like the economic and social center of the world. Everything, from civil rights to sex to attitudes toward war was changing, as the United States escalated its involvement in Vietnam. I was part of the first generation to grow up seeing the president on television all the time. Our leaders were not mythical figures; they were accessible to people like us.

Even Abington High School became part of this change during my sophomore year. Every morning at school, in accordance with Pennsylvania state law, we listened to verses from the Bible and said the Lord's Prayer. I didn't mind, but Ellery Schempp's family did. They were Unitarians and felt that the school's Christian emphasis violated their rights under the First and Fourteenth Amendments to the Constitution. The *Schempp* case reached the US Supreme Court, which ruled 8–1 that the Pennsylvania prayer statute was unconstitutional. The case put Abington High School at the center of a national debate, with many Christians arguing that this case was the beginning of the end for their religion in public schools.

At the end of my junior year, I was elected president of the student council. In that position, I first experienced what it means to be an innovator.

My father may have vetoed my idea to turn Schwarzman's Linens into the first Bed Bath & Beyond, but now I was in charge of something of my own. The summer between my junior and senior years, we took a family car trip to California. I sat in the back seat with my mother driving, the warm air blowing in my face, imagining what I could create with my new position. I didn't want to be just another name on a long list of student leaders. I wanted to do something that no else had done, or even thought to do. I wanted to develop a vision that was so exciting that the whole school would rally to help make it happen. As we drove from coast to coast and back, I scribbled notes on postcards to my fellow officers of the student council, random ideas, which I would mail every time we stopped. They were all at home, lounging around, getting this blizzard of cards, while I was in search of a great idea.

It finally came to me as we were driving. Philadelphia was the home of *American Bandstand*, a television show for teenagers hosted by Dick Clark. The city also had really wonderful radio stations, like WDAS, one of the leading African American radio stations in the country. I listened to music obsessively, from James Brown to Motown, the great doo-wop groups of the 1950s, then the Beatles and the Rolling Stones. At school, I could barely walk the halls without hearing the student rock groups practicing the songs they heard in the bathrooms and stairwells, wherever the acoustics were good. One of their favorites was "Tears on My Pillow" by Little Anthony and the Imperials. That was the sound and emotion of high school. *Tears on my pillow, pain in my heart.*

How great would it be, I asked myself, if we could get Little Anthony and the Imperials to come to school and perform in our gym? Sure, they lived in Brooklyn and were one of the most popular groups in the country at the time and we had no money. But why not? It would be unique. Everyone would love it. There had to be a way, and I made it my job to figure out how.

Fifty years on, the details are hazy. But there were a lot of phone calls, a lot of whose dad knows whom. And at the end of it, Little Anthony and the Imperials came to Abington High School. I can still hear the music, see the band onstage, and feel everyone having a great time. If you want something badly enough, you can find a way. You can create it out of nothing. And before you know it, there it is.

But wanting something isn't enough. If you're going to pursue difficult goals, you're inevitably going to fall short sometimes. It's one of the costs of ambition.

Jack Armstrong, my track coach at Abington, was medium height, medium build, with gray hair swept back behind his ears. Every day, he wore the same maroon sweatshirt and windbreaker, the same stopwatch on a lanyard around his neck. And every day, he brought the same positive, cheerful demeanor to work. He never shouted or got angry, just raised or lowered his voice within a narrow range, the slightest change in cadence to get his point across. "Look at what those guys have just done. And you're making pretend you're working out!" There wasn't a day I didn't throw up after practice, sick from the effort.

One day, he'd make the sprinters run a mile, far more than we liked. We'd tell him what we thought, but we knew we were in the hands of a genius. We wanted to please him. Even during winter, he didn't let up. He'd make us run lap after lap around the school parking lot, set on a hill and whipped by the wind. We kept our heads down to make sure we didn't slip on the ice. He stood against the wall, bundled up in his coat, hat, and gloves, smiling and clapping us on. Our high school had no special facilities, but while our rival teams were doing nothing during the winter, we were training in harsh conditions. When spring came, we were ready. We never lost a meet.

Whether he was coaching future Olympians or boys joining in from the bench, Coach Armstrong treated all of us the same, communicating a simple and consistent message, "Run as well as you can," to satisfy the demands of the training schedule he designed. He didn't terrorize or cheerlead. He let us figure out what we wanted. In his entire career, his teams lost just four times: 186–4.

In 1963, we were the Pennsylvania state champions in the mile relay and invited to compete in a special event in New York City at the 168th Street Armory. On the bus ride there, I sat, as usual, next to my best friend, Bobby Bryant, a six-foot African American superstar. Bobby was so warm and kind that it would take him forever to get through the school cafeteria because he had to stop and joke with every table. School was a struggle for him academically, but on the track, he was magic. His family never had much money, so I bought him a pair of Adidas spikes with the money I made working. It was a gesture of friendship, but also more than that: Bobby running in a great pair of spikes made all of us look good.

Six teams lined up in the final. I always ran the first leg, and I never passed the baton in second place. When the gun went off, I broke out in front. But coming around the first curve, I felt my right hamstring rip. The pain was sudden and excruciating. I had a choice: I could pull over and stop, the sensible choice for my body. Or I could continue and find a way to keep us as close as I could and give us a chance to win.

I drifted to the middle of the track, forcing the runners behind me to find a way around. I gritted through the remaining distance, choking down the pain and watching my competitors sprint ahead. I passed the baton to our second leg runner twenty yards behind the leader. I limped to the infield, bent over, and vomited. I had done all I could, but there was no way we could make up the distance. I had imagined victory and worked ferociously to ensure it. I had put in those hard and lonely laps through the winter. Now I was certain we would lose.

But as I stood there, my hands on my knees, I heard the crowd stirring, shouts bouncing off the brick walls. My teammate running the second leg was starting to gain. Then our third runner closed the gap further. The spectators in the balcony took off their shoes and started banging them on the metal panels lining the track. After the third leg, the gap was down to twelve yards, still a huge distance to make up. Brooklyn Boys High School had their best runner, the best runner in the city, waiting to grab the baton. Oli Hunter was six feet three inches tall with a shaved head, wide shoulders, a tapered waist, and extremely long legs, perfectly engineered to run. He had never been beaten in any competition. Our final leg runner was Bobby.

I watched Bobby take off on the flat, wooden armory floor, his eyes wild with intensity, focused on Hunter's back. Stride by stride, he reeled him in. I knew Bobby better than anyone else, but even I couldn't tell where he got that combination of spirit and strength from. Right at the tape, he lunged forward to win. He did it! The crowd went wild! How could that possibly have happened? It had been a superhuman effort. Afterward he came over to me in the infield. He put his big arms around me and hugged me. "I did it for you, Steve. I couldn't let you down." Training and competing together, we made each other better.

During my senior year, I realized that Harvard was the best-known Ivy League university in America. I believed that my record merited my admission. As it turned out, Harvard didn't agree. They put me on the wait list. Coach Armstrong suggested I go to Princeton to run track and even arranged for it. Like a petulant teenager, I said no because I thought Princeton wanted me just for my athletic ability. I won a place at Yale, but Harvard was a fixation, part of the vision I had for myself. So I decided to call the head of admissions at Harvard and convince him to admit me. I found his name and the central phone number for the admissions department. I brought a pile of quarters with me to school to use in the pay phone. I didn't want my parents to hear me make the call; it was something I needed to do on my own. I was practically shaking with fear as I dropped the coins into the phone, one by one.

"Hello, I'm Stephen Schwarzman from Abington High School in Abington, Pennsylvania. I've been accepted by Yale, but I'm on your waiting list, and I'd really like to go to Harvard."

"How did you get to me?" asked the dean. "I never talk with students or parents."

"I asked for you, and they put me through."

"I'm sorry to say we're not taking anyone from the waiting list this year. The freshman class is full."

"That's really a mistake," I said. "I'm going to be very successful, and you'll be very happy that you accepted me at Harvard."

"I'm sure you'll be successful, but Yale is a lovely place and you'll enjoy it and have a good experience there."

"I'm sure I will," I said, persisting. "But I'm calling because I want to go to Harvard."

"I understand that, but I won't be able to help you."

I hung up the phone and practically collapsed. I had overestimated my ability to sell myself. I accepted my rejection and resigned myself to my second choice: Yale.

In the final speech I made as student council president, I laid out a philosophy on education that has remained remarkably consistent throughout my life:

> I believe that education is a discipline. The object of this discipline is to learn how to think. Once we have mastered this we can use it to learn a vocation, appreciate art, or read a book. Education simply enables us to appreciate the ever-changing drama fashioned of God's own hand, life itself. Education continues when we leave the classroom. Our

> associations with friends, our participation in clubs all increase our store of knowledge. In fact, we never stop learning until we die. My fellow officers and I just hope that you will become aware of the purpose of education and follow its basic tenets, questioning and thinking, for the rest of your life.

That summer, as my father drove me back from summer camp where I had been a counselor, he told me that I was entering a world he knew nothing about. He knew no one at Yale or anyone who had been to Yale. The only help he could give me in this new world was to love me and let me know I could always come home. Other than that, I was on my own.

Freshman year at Yale, I shared two bedrooms and a study with two roommates. Luckily, I got the single bedroom. One of my roommates was a private school boy from Baltimore who pinned a Nazi flag to our living room wall. He had a glass case where he kept Nazi medals and other paraphernalia from the Third Reich. Every night we went to sleep to the sound of an album called *Hitler's Marching Army*. My other roommate didn't change his underwear for practically the entire first semester. College was a real adjustment for me.

Commons at Yale is a soaring brick building in the middle of campus. It was constructed in 1901 for Yale's two-hundredth anniversary. It seemed like a train station full of hundreds of people eating. Plates, cutlery, and trays clattering on the tables, chairs scraping backward on the floor. The moment I walked in on my first day, I stopped and thought, *Something's terribly wrong*. It didn't sound anything like the cafeteria at Abington. It took me a moment to figure it out. There were no women. At Abington, I had known everyone. At Yale in fall 1965, there were ten thousand students, of whom four thousand were undergraduates. I didn't know a single one. Two crazy roommates, no girls, and nobody I knew. The loneliness was crushing. Everything and everyone intimidated me.

Although I had told Coach Armstrong I didn't want to go to Princeton to run, the irony was that I'd gotten into Yale because of my sprinting. I had one of the fastest 100-yard times in Pennsylvania and ran leadoff for Abington's state champion 440- and 880-yard relay teams, which were fourth in the United States. I had the good grades and SAT scores. But I was admitted to run.

Yale had a famous coach at the time, Bob Giegengack, who had coached the US Olympic team the year before. New runners went to practice, took a card detailing their routine, and then ran alone. There was no Coach Armstrong to bring out your best. There were no teammates to laugh and joke with, and no one for whom you'd ever run until you vomited. I figured the best I could do was win an Ivy League sprint title. To do that, though, I'd have to train for a lackluster coach and a team that didn't seem to care about me. So, uncharacteristically, I quit. I wasn't sure what I wanted yet, but track, which had been such a formative part of my life, no longer seemed the way to get there.

Academically, I discovered, I was underprepared. I chose an unusual major, culture and behavior, an academic creation of the 1960s that combined psychology, sociology, biology, and anthropology. I chose it because it sounded fascinating, a comprehensive study of the human being, which would help me understand people's objectives and motivations. But I still had a way to go on the basics. There were only eight of us in the class and four professors assigned to teach us. Many of my peers came from the best prep schools in the country. Not only did they all seem to know each other, they also knew the work. My first English paper was on Melville's *Bartleby the Scrivener*. I got a 68. I then got a 66 on my second. I was failing. My instructor, Alistair Wood, asked me to his garret office for a meeting. He was a young man dressed like an elderly professor, wearing a tweed sweater and a J.Press sport jacket with patches at the elbows, a tattersall shirt, and a green knit tie.

"Mr. Schwarzman, I want to talk to you about your papers."

"There's really nothing to talk about," I said.

"Why is that?"

"I had nothing to say, and I said it poorly."

"My God, you're not stupid. I couldn't have put it any better myself. So I have to teach you how to write, and after that, I'll teach you how to think. Because you can't learn both at the same time, I'll give you the answers to the next several essays and we'll concentrate on the writing. Then we'll concentrate on thinking."

He saw I had potential and systematically set about equipping me with what I needed. I'll never forget his patience and kindness. Teaching, I came to believe, is about more than sharing knowledge. You have to remove the obstacles in people's way. In my case, the obstacle was the gap between my education up to that point and the education of my peers. That year, I went from failing to the dean's list, at the top of my class.

After my freshman year, I needed an adventure, something different from the typical summer job. A summer at sea, I thought, stopping in exotic ports might prove a useful cure to the all-male campus at Yale. I started by trying to get a job at the docks in New York City, but the longshoremen's union, then controlled by the mob, wouldn't take an unconnected college kid. They recommended I go to the Scandinavian seamen's union in Brooklyn. The money wouldn't be as good, they warned me, but at least there might be work. I got there shortly before the union building closed for the day and found a wall covered in 3- by 5-inch notecards advertising jobs. I was qualified for none of them. But the receptionist said that if I joined the union, I could have a place to sleep and see if there was anything tomorrow. I took him up on his offer, but my night was interrupted by a giant Scandinavian sailor who tried to get into bed with me. I freaked out, fled, and slept on the street. When the sun rose, I went to a Baptist church across the street for the morning service and waited until the union hall reopened.

The notice board had been rearranged, and I spotted a card that said simply "Destination Unknown." I asked the receptionist what that could mean. He told me that it all depended on the cargo. You found out where you were going as you sailed under the Verrazzano-Narrows Bridge. If you turned left, you were going to Canada; right for the Caribbean or Latin America; and straight ahead for Europe. All that was available was a job as an engine room wiper, the lowest rank aboard a Norwegian tanker. I took it. My job was to keep the engine room clean from grease. As we went under the Verrazzano-Narrows Bridge, we turned right, headed for Trinidad and Tobago.

All we had to eat and drink was smoked fish, awful cheese, and Ringnes beer. It was so hot in the engine room that I could drink a beer and watch it seep out of my body on my skin. When I wasn't working, I read the works of Sigmund Freud, which I had brought with me in a wooden crate. Every last one of his books. The Norwegian crew and I didn't have much to say to each other. But they were there for me when it counted. In a bar in Trinidad, I spoke to the wrong girl and soon punches and chairs were flying, like an old Western saloon fight, as my crewmates rallied to my defense.

After we sailed north to Providence, Rhode Island, I took a bus back to Brooklyn in search of another job. I was hired onto a much more pleasant ship, a freighter, the Danish *Kirsten Skou*, smartly painted in white with blue trim. My job there was second cook. I would wake up at 4:00 a.m., bake the bread, and cook breakfast. I loved it. We turned left toward Canada, picked up liquor and lumber, and sailed to Colombia for bananas. Every time we stopped in a port, the ship had to be loaded and unloaded using nets. There were no containers then, and the whole process would take three or four days, giving me time to explore. In Santa Marta, I spent an evening in a bar on the beach that was lit with Christmas lights. For the only—first and last—time in my life, I got so drunk I passed out. Later, someone drove me to the docks and dropped me there. After two days, I awoke back on the boat, covered in bruises. I must have been robbed and beaten. My crewmates had found me and had taken turns watching over me until I woke up. By the time I regained consciousness, we were out at sea and I could barely walk. We kept on to Cartagena, through the Panama Canal to Buenaventura. And then I had to get back to Yale.

It was a jolt to be back in drab New Haven after three months at sea. On the front page of the *Yale Daily News*, I saw an advertisement saying that if you were feeling depressed, you should see the psychiatrist at DUH, the Department of University Health. I decided to give it a go. The psychiatrist looked the part, with a pipe and a bow tie. I told him about my summer, about the ships, the girls, the ports, and how I didn't want to be back at school.

"Of course you don't," he said. "Why would you? You don't need therapy. You're just suffering from withdrawal. Hang in there. In a few months, you'll be fine."

He turned out to be right. Maybe it was the Freud, or the bars, or the girls I had met along the way. Maybe it was having taken on a challenge and survived. While my classmates were spending the summer hitting tennis balls and working in offices, I had been sweating in an engine room and dodging blows in Colombian bars. But now, I was ready to approach Yale on my own terms.

I moved to Davenport College, one of Yale's residential colleges, where a future president, George W. Bush, was a year ahead of me. The dining room was much smaller than Commons, so instead of going back to my room or the library straight after lunch or dinner to study, I would pour myself a cup of coffee and sit down with any students there and join in the conversation.

To make spending money, I took over the Yale stationery concession and walked every stairway in the entire university trying to get students to buy writing paper with personalized letterhead. With the money I made, I bought myself a stereo. I loved listening to music.

I set my sights on the "senior societies," secretive clubs whose members included the most prominent students on campus, the captains of the sports teams, the editors of student publications, the leaders of the Whiffenpoofs, an a cappella group. The clubs had mysterious names, like Skull and Bones, Scroll and Key, Wolf's Head, Book and Snake. Tapped to join, you swore never to mention it or speak about what went on behind the club's closed doors. Skull and Bones was the most exclusive. I had two years before my senior year to get its members' attention.

I'd often go and sit on a bench in the courtyard of Branford College, the prettiest college at Yale, where I could listen to the carillon of Harkness Tower, and think, *What could I do that would get the whole undergraduate body excited? Something inventive?* One of my more unusual achievements had been to set the university's vertical jump record, forty-two inches, during the physical exam we took when we arrived. But I knew there was more I could do, and my experience at Abington with Little Anthony had taught me a lesson I have replicated throughout my life: if you're going to commit yourself to something, it's as easy to do something big as it is to do something small. Both will consume your time and energy, so make sure your fantasy is worthy of your pursuit, with rewards commensurate to your effort.

The most glaring need I sensed among Yale's undergraduates was the companionship of women. There were thousands of men in neo-Gothic buildings starved of even the sight of women, let alone their company. It was an obvious problem to solve, but nobody was trying. I decided to change things.

When I was sixteen, my parents had taken me to the ballet to see Rudolf Nureyev dance with Margot Fonteyn. Their grace and movement captivated me. Later, still a teenager, I was immobilized for a month with a badly separated shoulder. I listened to record after record of classical music, ten hours a day, starting with Gregorian chants and ending with the great ballet scores of Tchaikovsky. When I arrived at Yale, Mary Jane Bancroft, the wife of my college dean, Horace Taft, the grandson of President Taft, discovered my interest in ballet. She shared books with me and taught me a lot. *So what*, I asked myself, *if I took my interest in ballet, bolted it to my social ambitions, and brought a troupe of ballerinas to perform for Yale's men? That would get me noticed*.

I needed an organization, so I invented the Davenport Ballet Society. Then I started calling the heads of the dance departments at the all-women Seven Sisters colleges, inviting their dancers to perform at the Davenport Ballet Society Dance Festival. Five of them agreed. Finally, I called Walter Terry, an eminent newspaper dance critic, and persuaded him to travel from New York to review the festival. Out of nothing, I brought together dancers, critics, and an audience. My hunch about the Yale men proved right: we packed them in, and I had the beginnings of a profile on campus.

If we could get the best dancers from other colleges, why not shoot for the professionals? The greatest ballet company in the world at the time was the New York City Ballet, where George Balanchine was artistic director. I took the train to New York and hung around the stage door waiting for the security guard to take a break. When he did, I ducked into the offices backstage and asked until I found the manager.

"What the hell are you doing back here?" he demanded.

"I'm from the Yale University Ballet Society, and we want to invite the New York City Ballet to come to New Haven to perform." I had given some thought to what was in this proposal for him. “The students don’t have money, but they love ballet and they’re your future audience and patrons.” I kept talking until the manager caved.

“Look,” he said, “we can’t bring the whole company up. Would it be okay if we just bring a small group?” Absolutely fine, I told him. So a New York City Ballet group came to New Haven to perform. Another big hit. Now that I had a relationship with the New York City Ballet, I upped the stakes again and went back to the manager. “We’re just a bunch of poor college students, hundreds and hundreds of college kids who love ballet. Why don’t you let us come to a performance for free? Because we can’t afford tickets.”

“We can’t do that,” he told me. “We depend on selling tickets. But we do dress rehearsals, so if you want to bring down as many students as you want to a dress rehearsal of *The Nutcracker*, we can arrange that.” So they arranged it on their end, and I took care of it on ours, inviting all the women’s colleges. We filled the house for a dress rehearsal of *The Nutcracker*, men from Yale, women from the women’s colleges. By the time it was over, I had become a student ballet impresario, sort of the Sol Hurok of Yale. I was developing a reputation as someone who made the improbable happen.

Around the same time, I learned that Yale’s efforts to recruit more students from the inner cities were floundering, just as they were at most of the other Ivy League universities at that time. I went to the admissions dean with an idea. Despite its best intentions, Yale did not have enough people on the admissions staff to reach all the parts of America where they might find good candidates. If they couldn’t get out to the cities, towns, and rural areas far beyond New Haven, they could not describe a Yale education or what it offered. Many potential candidates didn’t apply because they never imagined they could fit in, let alone afford it. My idea was to send out small groups of students and invite candidates to visit, at Yale’s expense. Instead of the college going to them, they would come to us. While we had them on campus, we could explain Yale’s generous financial aid program. No one was ever turned down for lack of money.

The dean liked my idea. We decided to start in my hometown, Philadelphia. It would be a pilot project, the first of its kind attempted by a major university. On my first visit to South Philadelphia High School, I met a boy who had been born in Cairo and forced to leave because he was Jewish. He had moved to France, then Italy, and finally to the United States, five years earlier. He had high standardized test scores; spoke Arabic, French, Italian, and English; and read Hebrew. And there he was living in the inner city, a great candidate, and he had never heard of Yale.

I worried that when these students, mostly second-generation immigrants from Europe or African Americans, visited Yale, they might be turned off by a bunch of self-involved Yale preppies, so we designed the day to be as practical as possible. The eighty students who came on the first visit would be broken into groups of two or three, depending on their interests, and assigned to an undergraduate. They would visit labs or use the college broadcast studio. They would then discuss how to pay for their education at the admissions office.

High schools were wary of having their students treated as tokens. We made sure these students knew that this path was not easy. They would have to compete for spots and apply to other schools as well. What mattered was they knew Yale was available to them. The boy from Cairo was eventually accepted and enrolled at Yale, and the program thrived long after I graduated.

In my final year, I decided to take on the biggest issue of all for Yale's men: the 268-year-old parietal rules that forbade women staying overnight in a dorm room. I was dating a woman at a local college, so for me, it was as much a personal as a community issue.

The conventional approach would have been to set up a meeting with a university administrator to try to change the situation. But I knew what would happen. He'd sit there in his blazer and bow tie and tell me women would be a distraction. They would stop the young men from studying. They would change the atmosphere in the college dorms. There was a long list of reasons that a young man like me wouldn't understand. He would smile and nothing would change, as it hadn't for almost 270 years. I needed a different approach, so I started with the students. I made a list of the university's likely objections and turned them into a long questionnaire. Do you think changing parietal rules will stop you from studying? Would having more women around be a distraction? And so on.

I recruited eleven students to stand outside each of the eleven college dining halls during mealtimes and hand out the questionnaire to the entire undergraduate body. We had a response rate of close to 100 percent. Then I went to a friend, Reed Hundt, who was deputy editor of the *Yale Daily News*. (He became head of the Federal Communications Commission under President Clinton.) "Reed, I've got this survey about getting rid of parietal rules," I told him. "It's dynamite."

Three days later, the parietal rules were history, and I made the front page of the school newspaper: "Schwarzman's Initiative: Poll Votes Down Parietals." The university didn't want to fight. It was my first lesson in the power of the media. Skull and Bones later tapped me to be a member, and I was put in charge of Class Day the following June. I would be the public face of Yale College's graduation ceremony.

It had been some journey since my first, lonely meal at Commons.

EVERYTHING IS INTERCONNECTED

Shortly before I graduated, I was asked in a job interview what I wanted to be. I didn't have a conventional answer.

"I want to be a telephone switchboard," I told my interviewer, "taking in information from countless feeds, sorting it, and sending it back out into the world."

He looked at me as if I were a lunatic. But I was sure of it, and even more so after a meeting I had near the end of my senior year. I was looking for ideas about what to do next. I wrote a letter asking for advice from Averell Harriman, a member of Skull and Bones, class of 1913, one of the "Wise Men" of American diplomacy and former governor of New York.

He wrote back, inviting me to his home for a meeting at 3:00 p.m., which he later changed to lunch.

I rushed out and bought my first suit, gray with a white pinstripe, at J.Press. Harriman's house was at 16 East Eighty-First Street, half a block from the Metropolitan Museum in New York. A houseman in a white jacket and black tie opened the door and led me to a sitting room lined with Impressionist paintings. In the room next door, I could hear the voice of Robert Wagner, the former mayor of New York. Finally, it was my turn. Harriman was sitting in an armchair. He was almost eighty, but he rose to greet me and asked me to sit on his right because he couldn't hear well in his left ear. On the mantel was a bust of the brother of slain President John F. Kennedy, Robert Kennedy, a friend of his who had been assassinated the previous year. After we had spoken for a few minutes about the possibility of my going into politics, Harriman said, "Young man, are you independently wealthy?"

"No, sir. I'm not."

"Well," he said, "that will make a great difference in your life. I advise you, if you have any interest in politics whatsoever, to go out and make as much money as you can. That will give you independence if you ever decide you want to go into politics. If my father wasn't E. H. Harriman of the Union Pacific Railroad, you wouldn't be sitting here talking to me today."

He told me the story of his life, a nonstop series of adventures. He attended boarding school at Groton, then college at Yale, where he put his inherited wealth to use drinking and playing polo. After graduating, he built a career in business. With his father's support and connections, he traveled to Russia after the Revolution of 1917 and led a wave of US investment in the new Soviet Union. He got to know Lenin, Trotsky, and Stalin. Back in the United States after the Bolsheviks had seized most of the US funded assets, he came up with the idea for a ski resort in Idaho modeled on St. Moritz in Switzerland. He called it Sun Valley. During World War II, his father's friend, President Franklin Roosevelt, sent him back to Moscow as US ambassador. In 1955, he became governor of New York State and later returned to the State Department under President Kennedy, another family friend. By the time I met him in early 1969, he was America's lead negotiator in the Paris Peace Talks seeking to end the war in Vietnam. While Harriman was talking, the phone kept ringing, the negotiators in Paris asking for his advice.

I was enthralled and lost track of time until Harriman said, "Let's have lunch. Do you mind eating on a tray?" I had never before been in an exquisite house such as his. But I did know about eating on a tray.

After I left, I ran to a public telephone to tell my mom and dad all about it. I had gone to see Harriman for advice on what to do with my life. He had told me I could do anything to which I set my mind. At some point in life, we have to figure out who we are, he said. The sooner we do it the better, so we can pursue the opportunities that are right for us, not some false dream created by others. But if I was going to turn my worthy fantasies into reality, to become a telephone switchboard filled with inputs, I'd need money.

I arrived for my first interview on Wall Street an hour early, because I didn't want to be late. I sat in a Chock Full o'Nuts coffee shop nursing a cup of coffee, the one cup I could afford, checking my watch every couple of minutes. When 9:00 a.m. arrived, I went into the headquarters of Donaldson Lufkin Jenrette at 140 Broadway, up to the thirty-sixth floor. I took a seat in reception and watched as sophisticated young women with black headbands and fancy shoes and young men in ties and shirtsleeves, only slightly older than me, ran around the office alert and purposeful. The energy of the place was electric.

After half an hour, an assistant ushered me in to see Bill Donaldson, the D in DLJ. It was surprising to see a man so young sitting in a rocking chair, but this was fashionable post-JFK. Our meeting had been arranged by Larry Noble, Bill's Yale classmate, who was now working in the Yale admissions office. I had met Larry when I had seen him with his young family at a Yale fifteenth reunion and felt compelled to buy a copy of *Babar the Elephant* for his son. I had no idea who Larry was, but my random act of generosity led to a friendship and now this interview.

"Tell me," said Bill, "why do you want to work at DLJ?"

"Frankly, I don't know much about what DLJ does," I said. "But it seems you've got all these amazing young people working here. So I want to do whatever they're doing."

Bill smiled and said, "That's as good a reason as any."

After we talked a bit, he said, "Why don't you go around and see some of my partners?" I did, but when I got back to Bill's office at the end of the day, I told him they seemed uninterested in me. "Listen," he said laughing, "I'll give you a call in two or three days." He came through with an offer of a job. The starting salary was $10,000 a year.

"That is absolutely terrific," I said. "But there's only one problem."

"What's that?"

"I need $10,500."

"I'm sorry," he said. "What do you mean?"

"I need $10,500 because I heard there's another person graduating from Yale who's making $10,000, and I want to be the highest-paid person in my class."

"I don't care," said Bill. "I shouldn't be paying you anything at all. It's $10,000!"

"Then I won't take the job."

"You won't take the job?"

“No. I need $10,500. It’s not a big deal to you, but it’s a really big deal to me.”

Donaldson started laughing. “You’ve got to be kidding.”

“No,” I said, “I’m not kidding.”

“Let me think about it.” Two days later he called back. “Okay. $10,500.” And with that I entered the securities business.

When I showed up for my first day on the job, I had an office with a majestic view uptown and a secretary. After a while, someone dropped an annual report on my desk for Genesco, a footwear and apparel business. My job was to analyze it. It was the first time I had even seen such a report. As I turned the pages, I saw that Genesco had a balance sheet and an income statement. The balance sheet had footnotes referring to preferred stock and convertible preferred stock, subordinated and convertible subordinated debt, senior debt and bank debt. Reading it today, I could have seen in an instant that it was a company in financial disarray. But at the time, I may as well have been reading Swahili. And there was no Internet or anyone around offering to help me translate. Even today, say the word *Genesco* and I can feel moisture trickle down my back, the fear that at any point someone will walk in, ask me a question, and expose me as a fraud. Here was a world in which huge amounts of money were at stake, yet no one even bothered to train new people. They assumed we were smart enough to figure it out. That seemed like a crazy approach to me.

My next assignment was to investigate a new chain of German-style sausage restaurants being launched by Restaurant Associates, the owner of various high-end restaurants in New York. Zum Zums promised knockwurst for New Yorkers. I arrived at Restaurant Associates’ headquarters, the first company I had ever visited, and began asking questions of the chief executive and other corporate officers. They didn’t seem too friendly, and I didn’t learn much. I took the subway back to my office. My secretary, who usually had little to do owing to my own incompetence, awaited me with a message: “Mr. Jenrette needs to see you immediately.” Dick Jenrette, one of the most charming and intelligent men in finance, would become a close friend and confidant. But that afternoon, he was president of DLJ, and I barely knew him.

"What did you do to these people at Restaurant Associates?" he said. "They're furious at us."

"Why would they be furious?" I said, startled.

"They said you were looking for inside information."

"All I asked for was what I thought I needed to know to predict what was going to happen with their company. How many units do they have, what's their profit per unit, what's the overhead. Stuff like that so I could figure something out."

"Steve, they're not allowed to tell you that kind of information."

"Then how can I know what's going to happen? Why can't I get it?"

"Because the SEC has rules about what you can and can't get, and that qualifies as inside information. If they tell you, they'd have to tell everybody. Don't do it again."

No one had bothered explaining this rule to me.

After my Zum Zums debacle, I began researching National Student Marketing, a company trying to sell anything they could to college students. They were selling a life insurance product, which no twenty-year-old I had ever met would think of buying, and leasing refrigerators to students to keep in their dorm rooms. I had just graduated from college and knew how students treated appliances. It wasn't pretty. This company accounted for its refrigerators as if they lasted six years. Every undergraduate I knew destroyed them in two. When I visited the company's offices, the first executive I met couldn't tell me the name of the person in the next office. He seemed disengaged. I didn't need any inside information to tell me this company was heading straight for bankruptcy. I wrote up my opinion and filed it, not knowing that DLJ was at the same time arranging a private placement of equity for National Student Marketing.

A few years later, as I predicted, the company collapsed. DLJ was sued for selling stock in a company it knew was rotten, and I had to defend my opinion before a roomful of lawyers. DLJ depicted me as an idiot who had no idea what he was doing, which explained why no one listened to me. The plaintiffs portrayed me as a genius savant, who saw what all of DLJ's higher-paid professionals had missed. The plaintiffs won.

While I was working at DLJ, I moved from sublet to sublet, a succession of cockroach-infested walk-ups. For a while, I lived in one on Second Avenue between Forty-Ninth and Fiftieth Streets above the Midtown Shade Company. This stretch of the road went slightly uphill, so all night long, I heard trucks changing gear. Most nights, I got home and made myself spaghetti with tomato sauce in a single pot on my hot plate. I had no kitchen. The bathroom was down the hall. One evening, I invited a woman out for a date. When I picked her up, she was wearing a mink coat. At dinner, I kept staring at the menu while she ordered, hoping she didn't realize that I could afford an appetizer and dessert only for her, not both of us. I had just enough money afterward to drop her off in a cab. After we said good-bye, I walked home fifty blocks wondering when my life would change.

The other people my age at DLJ were the sons and daughters of famous people in New York. I didn't know any of them. And that wasn't going to change with me living in a hovel, working on the bottom rung of a securities firm. If they weren't all so well bred at DLJ, I was convinced they would have had me emptying the trash. But I at least got a glimpse of what else New York might offer. Laura Eastman, a DLJ colleague a few years older, took pity on me and invited me to her family's apartment for dinner a few times and to play squash in the basement of their building on Seventy-Ninth and Park. Laura's sister, Linda, would soon marry Paul McCartney, and her father, Lee, became his attorney. Theirs was the first Park Avenue apartment I had ever visited, and I'd never before seen anything like it. It had been decorated by Billy Baldwin, the top decorator in the country at the time. At the entrance, there was a small library, its walls covered in beige grass cloth and hung with Willem de Kooning paintings. When I asked Laura about them, she told me that the artist lived and worked in East Hampton close to her dad's beach house. De Kooning had come to him for some legal advice and paid with paintings instead of cash. He had needed a lot of advice, so the Eastmans now had a lot of paintings. This had never happened to the Schwarzmans of Abington. Lee made a great impression on me during those family dinners. He was positive, dramatic, engaged, and insightful. He was living the New York life I aspired to have if I could become successful.

The Vietnam War interrupted my efforts. I had signed up for the Army Reserves instead of waiting for the results of the draft lottery, which would almost certainly have sent me into combat. The Reserves required six months of active-duty training and sixteen hours a month at a local unit for five more years. Six months after I joined DLJ, I was summoned for training. Bill Donaldson was nice enough to invite me for an exit interview. I was candid with him and said I felt bad about my time at DLJ. I had been more or less useless. No one had bothered to train me, and I had drifted around. Unlike at Yale, I hadn't found a way to accomplish much of anything.

"Why in the world did you ever hire me?" I asked. We were sitting in the small employee cafeteria, eating off plastic trays. "You wasted your money. I haven't accomplished a thing."

"I had a hunch."

"Really? What kind of hunch?"

"That one day you'd be the head of my firm."

I sat there, astounded. "What?"

"Yeah," he said. "I have a sixth sense about these things."

I left for the Reserves thinking Wall Street was crazy.

In January 1970, Fort Polk, Louisiana, was a major combat training center for those getting ready to be shipped to Vietnam. It was damp and cold in the barracks and freezing when we had to sleep on the ground during maneuvers. My company trainees were from tiny West Virginia and Kentucky towns, some almost illiterate, most drafted and bound for combat. It was a sharp jolt after Yale and DLJ. Our drill sergeant had been a tunnel rat in Vietnam. His specialty was going down tunnels dug by the Vietcong and North Vietnamese to plant explosives. Armed with just a flashlight and a .45 caliber pistol, he never knew who was waiting for him around a dark corner or what traps might have been set. He was the bravest person I had ever met. He was an instructor now because he had a metal plate in his head and couldn't fight anymore. He had nothing but contempt for the war.

"There's no sense to it," he told us. "None. Zero. You spend your time trying to take a hill. You take it. And five days later, you abandon it and the bad guys go right back up the hill. It's the stupidest fucking thing I've ever been involved with in my life. We don't know who the good guys are or the bad guys are. Nobody can speak their language. They're friends by day, and try to kill us at night. Our officers are mostly idiots." He even told us that if we had to kill one of our officers to save ourselves from a pointless death, we should consider it.

He was a good, brave man whose life had been changed by decisions made at the highest levels of government. His anger and frustration cast a shadow over our experience. Vietnam, I quickly realized, was more than a strategic game for politicians, diplomats, and generals or an ideological piñata for student radicals. It had a personal impact on thousands of Americans. Later in my life, when I found myself in positions to influence decisions of national and global significance, I tried to remember the effects on individual people who would bear the consequences.

I was no longer in the physical shape I'd been at high school, but I hadn't lost the taste for hard effort. I enjoyed toughening up with long runs in combat gear at five in the morning. I liked learning how to use weapons. I didn't enjoy the stupidity. One morning we stood in formation in the pouring rain for an hour and a half waiting to go in for breakfast. Our sergeant had forgotten we were out there and no one had the guts to break formation to tell him. On the days we did get breakfast, we often ran out of food. We were in Louisiana, not Vietnam. There should have been enough to eat, so I took it upon myself to investigate.

When we had arrived at Fort Polk, a colonel had told us that if we saw anything wrong, we should talk to him. I decided to take him up on his offer. I walked into the colonel's office, covered in dust from training. His clerk asked me what I was doing there. I gave him my name and number. "Get the fuck out of here," said the clerk. I refused to move. He summoned a lieutenant. I said I only wanted to talk to the colonel.

"Who the fuck do you think you are?" said the lieutenant. "This is the army. You do what you're told and get your ass back to your company." A captain came in, and we went through the same routine. I thought my own company captain would burst through the door at any moment, grab me by the neck, and dump me in a swamp. But eventually I was sitting in front of the colonel, lean with cropped gray hair.

I explained the food situation. I told him what we got for breakfast, lunch, and dinner, and he looked stunned. He fished out a sheet of paper detailing our company's proficiency scores. We were the worst company in the whole brigade. He told me to go back to my company and not say a word. Two days later, all of our officers were gone. It turned out they were stealing our food and selling it. The colonel called me back in and thanked me for breaking through the structure of the military to make my point. It was the reason he gave that speech to all the incoming trainees, but no one had ever come to see him.

The Reserves reinforced my suspicion of hierarchy and my confidence in going against it if I saw something wrong. The different fates of all of us at Fort Polk also reminded me of the importance of luck. No matter how successful, smart, or brave you are, you can always end up in a tough place. People often think theirs is the only reality, but there are as many realities as there are individuals. The more you see of them, the more likely you are to make sense of them.

Another life lesson I took from my time in the army is that the commitment and sacrifice of our service members must always be honored. This belief is what drove my involvement with the Navy SEAL Foundation many years later in 2016, when I led a Blackstone effort to raise funds in support of the families of SEALs who were killed in the line of duty. I made it a personal mission to visit with every business group to ensure they understood the importance of giving back to the people who were responsible for securing their everyday freedoms. In the end, every single US Blackstone employee contributed and the Navy SEAL Foundation raised a record $9.3 million.

I left Louisiana in July, and by late August, I was sitting in a classroom in Boston. Before I'd left Yale, I had applied to graduate school. My top choice was law school, preferably Harvard, Yale, or Stanford. But the only law school to accept me was the University of Pennsylvania, and I wasn't ready to go back to Philadelphia. Almost as an afterthought, I applied to Harvard Business School. Business schools weren't the smart kids' choice then. They were seen as funnels for middle managers at big corporations, not entrepreneurs or intellectuals. In 1970, getting an MBA meant going to work at military-industrial giants like Dow, the makers of napalm, and Monsanto, which made Agent Orange, both used to kill or maim people in Vietnam. But when HBS offered me a place, I decided to go. Maybe, I thought, this was the way to the fortune Averell Harriman had recommended.

I arrived at Harvard feeling the same way I had when I arrived at Yale: socially isolated and suspecting the brilliant people were elsewhere. The same year I arrived at HBS, Bill and Hillary Clinton started at Yale Law School. The leaders of the future were fighting intellectual duels in moot court, not studying widget companies.

My first class was in a course called Managerial Economics. The core of it was drawing decision trees, chains of logic in which you apply probabilities to different courses of action and try to calculate the best one based on your predicted outcomes. After all I'd seen and done in infantry training, it seemed beyond abstract. Our first case study involved a scavenger company hunting for sunken treasure. The question before us was how much money to spend diving for gold given the expected value of the gold that might lie buried in a galleon at the bottom of the sea. Our professor, Jay Light, was just a little older than we were and in his first year of teaching. At the start of the class, I raised my hand, and Jay pointed to me.

"Mr. Schwarzman, would you like to open the case?"

"Actually," I said, "I have a question."

"Okay, what is it?"

"I read the case," I said. "But it seems to be nonsense. If this is what the class is going to be, it's basically got no practical application to someone like myself."

Jay stared at me. "Tell me, Mr. Schwarzman, why would that be?"

"Because this case about expected value is premised on having an infinite number of dives to find the gold. I don't have an infinite number of dives in my life. When I dive, I have to have a 100 percent probability of finding the gold, because otherwise this whole enterprise can bankrupt me. This case applies to giant corporations that have no practical limit on how many dives they can make. But most people aren't Exxon. They have limited resources. Personally, I have no resources."

“Hmmm,” said Jay. “I never thought of it that way. Let me think some more, and we’ll go on.”[I]

After a few weeks, I concluded that Harvard Business School was teaching only one idea, disguised as different courses. The lesson was that everything in business relates to everything else. For a business to succeed, each part has to work on its own and with all the other parts. It’s a closed, integrated system, organized by managers. If you are making cars, you have to have good research so you’ll know what people want to buy; good design, engineering, and manufacturing so you can produce a good product; effective programs to recruit and train your labor force; good marketing so you can create desire for what you are making; and good salespeople who know how to close deals. If any parts in the system break and you can’t fix them quickly, you risk losing money and going out of business. I got that. What’s next? Three more cases tomorrow that teach the same thing. And after that? Three more cases that teach it some more.

By the time I got to the December holiday, I was ready to drop out. I was bored. Boston was cold. The teaching was mediocre, done mostly by young assistant professors still finding their way in the classroom. Why was I wasting my life here? I was ready to go back to work.

Bill Donaldson, who had hired me at DLJ, had left the firm for a job in Washington as deputy secretary of state. Dick Jenrette had succeeded him as president. The last time I’d seen Dick was when he’d reprimanded me for accidentally asking for inside information at Restaurant Associates. But he had gone to HBS, so I decided to ask his advice.

“Dear Dick,” I wrote. “I hate it here. I’ve gotten their message, and I’m thinking of dropping out. Maybe I could come back to DLJ or go somewhere else. Please tell me what you think.”

To my astonishment, Dick took the time to write a six-page, handwritten reply that changed my life. It said something to the effect of “Dear Steve, I know exactly what you’re thinking. I too was prepared to drop out of Harvard Business School in December of my first year. I found it very unsatisfying intellectually, and I was going to transfer to the economics department to get a PhD. But I stayed. It was the best decision of my life, and it’s exactly what you should do. Don’t leave. Stay.”

I took his advice, and I'm still grateful. Whenever young people write or call me asking for advice, I think back to Dick's thoughtful, considerate letter. Like Jay Light, Dick Jenrette became a longtime member of Blackstone's board of directors. I decided to stay at HBS, and all that I hadn't learned at DLJ I began learning, from the basics of corporate finance to accounting, operations, and management. I completed my first year with honors and was selected by the faculty to be a member of the Century Club, an organization comprising the top three students of each section of seventy-two. I was elected president by other members of the club, and just as I had in high school and at Yale, I set out to make the experience unique and better for everyone. I started a program of inviting successful young men, just a few years older than us, to talk to the club. My first two guests were John Kerry, a Vietnam veteran who opposed the war and would eventually become a senator, secretary of state, and the Democratic nominee for president; and Michael Tilson Thomas, then assistant conductor of the Boston Symphony Orchestra, who would later lead the London and San Francisco Symphony orchestras. During my second year, I also met and married Ellen Philips, who was working as a course assistant at HBS.

I also decided to try to help improve the HBS experience. Fortified by my success changing the parietal rules at Yale and fixing the food mess at Fort Polk, I set up a meeting with the dean of Harvard Business School, Larry Fouraker, to suggest how the school could be better. Fouraker had been a compromise choice for the position, a mechanical, unspectacular administrator who spent most of his time away from the school serving on corporate boards. Despite its still-vaunted reputation, the school was showing signs of major problems. It took five months to get an appointment with Fouraker.

"You've got teachers who can't teach, students who can't learn, and an outmoded curriculum. And the administration is extremely ineffective." I gave him examples of each and proposed solutions.

"Mr. Schwarzman," he replied, "have you always been a misfit?"

I told him I had been president of my junior high school, president of my high school, presided during Class Day ceremonies at Yale graduation, and was now president of the Harvard Business School Century Club. So, no, hardly a misfit. But he might be. At Yale, a university many times the size of

HBS, the president, Kingman Brewster, made a point to see anyone who had asked for an appointment within four days. It was obvious to me, I told him, why HBS was going downhill. "I told you what's going on. I even suggested how you might solve it. And you have no interest whatsoever," I said. "I'm really sorry I stopped in to try to help you."

"I think that'll be enough," said Fouraker.

He took my argument as an affront. I didn't think I was smarter than the dean, but I did have a different perspective from down in the trenches of student life. Despite the school's shortcomings, I had come to care about Harvard Business School. Through her job, Ellen had formed a similarly dim view of the teaching and the caliber of the students, which also informed my suggestions for the dean. My only mistake was to think he might value my honesty. But he didn't even want a conversation.

If ever I ran an organization, I promised myself I would make it as easy as possible for people to see me and I'd always tell the truth, no matter how difficult the situation. As long as you can be honest and rational and are able to explain yourself, there is no reason to feel uncomfortable. No one person, however smart, can solve every problem. But an army of smart people talking candidly with one another will. It was the only lesson I learned from Larry Fouraker.

My time at HBS convinced me that despite my false start at DLJ, finance might be for me. In the cases we studied, I could spot patterns, sense the problems, and suggest potential solutions without getting lost in the numbers. And my extracurricular activities had taught me I enjoyed working with people to take on difficult, even improbable challenges. As graduation approached, I decided that I would like another try at Wall Street, despite my poor start at DLJ and despite my math skills, which were then, and are still now, average at best.

At the time, investment banks did two things. First, sales and trading, which meant buying and selling securities such as bonds, stocks, options, Treasury bills, financial futures, commercial paper, and certificates of deposit. Second, they advised corporations on financial alternatives, capital structures, or mergers and acquisitions. These activities attracted different kinds of people. In the early 1970s, before computers revolutionized the way markets function, trading floors were frenzied and noisy, full of volatile characters.

Advisory work tended to be more cerebral, involving long negotiations and patient relationship building. I'd be trying to get senior executives at major companies to trust what I had to say and act on it. I'd have to innovate, persuade, close, and compete. That seemed like work I might be good at.

I applied to six firms. As I went around their offices, I thought back to my culture and behavior studies at Yale, and an idea struck me for my senior paper in my most important course at HBS: What did these banks' offices suggest about their culture? At Kuhn, Loeb, the firm's history was overwhelming. Just inside the front door was a huge portrait of Jacob Schiff, its founder, and smaller ones of every partner in the firm's history. The partners sat behind closed doors, cut off from the activity in the bullpen where the associates sat. It was dark and inward looking. Unlikely to adapt and survive.

Morgan Stanley was in the same building as DLJ, but right at the top and flooded with light. Gold carpets and antique roll-top desks in the partners' area were reminders of the past, but otherwise it was modern and open to change. Then there was Lehman Brothers at 1 William Street, a massive, ornate stone building like an Italian palazzo with a Romanesque tower on top. Every floor was divided into a warren of small offices. It felt to me like a feudal castle with lots of intrigue and nothing transparent. Anyone who worked there would have to fight to succeed. Lehman, I thought, would do well until the infighting destroyed it.

The paper was easy to write. It had no numbers in it, no research. My professor thought it was creative and gave me a great grade.

My interviews didn't go nearly as well. First Boston didn't have a single Jewish professional in 1972, and apparently I wasn't going to be the first. Goldman Sachs said they liked me but worried I was a little too much my own person, and I never got an offer.

Morgan Stanley was the most prestigious investment bank in the world at the time. It served the most important companies, the definition of the establishment. It had one Jewish professional, Lewis Bernard, who was a partner. Otherwise, it was straight white Anglo-Saxon Protestant. They invited me back for a second-round interview and assigned me a shepherd, an older employee who took me around to meet the partners. My shepherd talked a lot about the importance of precision in the drafting of prospectuses.

Precision was clearly important to the culture at Morgan Stanley, but it wasn't exactly thrilling.

Finally, I was invited in to see Robert Baldwin, the president of the firm. Bob had been under secretary of the navy. A navy flag and the flag of the United States stood behind the desk in his office. Morgan Stanley would be hiring just seven associates that year, and Bob offered me the chance to be one of them. It was an enormous honor, but it came with a significant condition: I would have to change my personality. Morgan Stanley was a buttoned-down, hierarchical culture. I couldn't be my opinionated, proactive self. Bob said I had the talent to work there; I just had to adapt.

I thanked him for the offer but said I couldn't take it. I would rather work somewhere where my personality was a natural fit. He should rescind my offer and give it to someone more suitable. But Bob refused. If Morgan Stanley makes you an offer, he said, it's yours to do with what you will. His firm would always keep its word. I was impressed. Over the next decade, Bob would transform the culture at Morgan Stanley, modernizing it and shedding many of its old traditions. But he had to do so with guardrails and under certain conditions, respecting the culture he inherited. He saw he would struggle to domesticate me, but had a sense I might help take the firm in the direction he wanted.

Lehman was much more attractive to me. It wasn't an MBA factory. It was full of interesting characters—ex-CIA agents and military, strays from the oil industry, family, friends, randoms. No two floors were designed the same, and there were no layers between the thirty partners and the thirty associates. It seemed an exciting and complex place to be.

On the day of our interviews, the interviewees began sitting around a table in the partners' dining room, with the partners sitting in back. The chairman, Frederick Ehrman, was wearing a very un–Wall Street cowboy belt with a big silver buckle and told us we would be interviewed in pairs: two interviewees rotating through pairs of partners in forty-five-minute sessions through the day. This pairing strategy, I thought, could end in disaster, with two interviewees dueling to outshine each other. If I were my most supercompetitive self through nine interviews, we'd end the day with blood on the carpet, so I figured the best approach was to be generous and friendly with my partner, a woman my own age. It turned out I was right: the firm rejected the people who fought and competed during their interviews. Those who cooperated received offers.

There was an even longer-term benefit to my decision. My fellow interviewee, Betty Eveillard, had a long, successful career in investment banking. We often ran into each other professionally. Decades after we navigated that treacherous day of interviews, we serve together on the board of the Frick Collection, an art museum on the Upper East Side of Manhattan, where she became chairperson. Those early encounters and friendships have a way of reappearing throughout your life.

At DLJ, I had been left to myself to grope through the fog of Wall Street. As soon as I was offered a job at Lehman, I was assigned a partner, Steve DuBrul, a product of both HBS and the CIA, to guide me. Steve was a corporate financier from central casting: tall, slim, handsome, his dark hair parted to one side. He had been a protégé of the previous chairman, Robert Lehman. He took me to dinner and explained how the firm worked.

But just a week after I accepted Lehman's offer, Steve called me at home. "I don't want you to find this the least bit upsetting," he said, "but I'm leaving Lehman. I'm joining Lazard."

"Hold it," I said. "You're the guy wining and dining me. And you're disappearing? Why shouldn't that affect me?"

"It doesn't have anything to do with the quality of Lehman Brothers, and you'll fit in great there. You'll be enormously successful. But I've spent my entire career here. It's time for me to move on. I wanted to tell you personally, so that you understand that this is personal for me. It's not about the firm. You should feel good about being at Lehman."

"If you're going to Lazard," I said, "maybe I should go with you."

"Your loyalty shouldn't be to me. It should be to the firm. But if you want, I can set you up for an interview." I took him up on the offer and flew to New York to meet with Felix Rohatyn, the famous mergers and corporate finance adviser at Lazard Frères. Rohatyn, a slight man in a rumpled suit, was a commanding force in the financial world. He had come to New York as a boy at the start of World War II, escaping Europe with his mother. He had joined Lazard straight out of college and become New York's preeminent investment banker. His greatest act would come in 1975, when he helped save New York City from bankruptcy. We talked in his office for an hour or so. At the end, he said, "Steve, you're an interesting guy. If you want to work at Lazard, I'll make you a job offer right here on the spot. But I advise you not to take it."

"Why?"

"Because at Lazard, there are two types of people: masters like me and slaves like you would be. I don't think you'd be happy being a slave. You should go work at Lehman Brothers, let them train you, and then come here to Lazard as a master."

When I flew back to Boston, Ellen asked me how it had gone. "Rohatyn made me a job offer. Then he told me not to take it. It's crazy down there."

So I went to Lehman to be trained, to sit in the middle of Wall Street with feeds running in from around the world, to be a telephone switchboard.

I. Jay Light continues to put up with my questions. Despite my best efforts to disrupt his career, he went on to be dean of Harvard Business School and has been a longtime member of Blackstone's board of directors. Whatever I thought of his sunken treasure case study, I've been lucky to have his advice ever since.

HOLD THE TABLE: ADVICE ON INTERVIEWS

Being a strong and accurate assessor of talent is perhaps one of the most critical skills required of any entrepreneur. I've been thinking about how to do this well since those early interviews on Wall Street.

Finance is a field that is filled with capable, ambitious individuals looking to leave their mark. But being capable isn't always sufficient. When I interview people for Blackstone, I'm looking to understand whether an individual will fit our culture. At a minimum, this includes the airport test: Would I want to be stuck waiting at the airport with you if our flight were delayed?

After thousands of interviews, I have developed my own style of interviewing. I rely on a combination of verbal and nonverbal cues, looking to see how a candidate reacts to my attempts to engage. I don't have a set formula, but in every case, my goal is to get into candidates' heads to assess how they think, who they are, and whether they are right for Blackstone.

I prepare for an interview like most others do, by reading a candidate's résumé. I look for consistency in terms of a narrative and make special note of any anomalies or stand-out pieces of information. Sometimes candidates are surprised that I have read their résumé so closely, but mostly they are relieved when I can ask them about a familiar topic or interest.

My goal is to start the conversation with something that both the candidate and I will find interesting, but I won't know how I'm going to start until we are in the same room. I choose my course by intuition.

Sometimes I go straight to one of the anomalies on the résumé. Other times I'll take a lead from what their body language tells me before they even say a word. Do they look happy or sad, alert or tired, excited or nervous? The more I can get candidates out of interview mode and into a natural conversation, the easier it becomes for me to evaluate how they think, react, and might adapt to change.

In some cases, I ask candidates if they had fun meeting people at the firm, if our people met their expectations, and how Blackstone is different from the other organizations they have worked or interviewed with.

Other times I will have just finished doing something exciting and will tell them about it to see how they react. Most candidates don't expect to be drawn into my world so quickly, and how they respond can be telling. Do they withdraw, or are they able to find a way to actively participate? Does the unexpected situation make them nervous or uncomfortable? Even if it's a topic or experience they know nothing about, are they able to find common ground and enjoy the conversation?

Alternatively, I'll ask about something fascinating or newsworthy. If they are familiar with the topic, I'll look for how they approach the discussion. Do they have a point of view? Is their assessment logical and analytical? If they don't know what I'm talking about, do they admit it and find a way to move on, or do they try to fake it?

In reality, this is all an exercise in evaluating their ability to deal with uncertainty. Finance, and investing especially, is a dynamic world in which you must adjust to new information, people, and situations quickly. If a candidate doesn't demonstrate the ability to connect, engage, pivot, and change course within the bounds of a conversation, chances are that person won't fare well at Blackstone.

Our people are all different, but they share some common traits: self-confidence, intellectual curiosity, courtesy, an ability to adjust to new situations, emotional stability under pressure, a zero-defect mentality, and an unwavering commitment to behaving with integrity and striving for excellence in all we choose to do. Being nice—thoughtful, considerate, and decent—doesn't hurt either. I will never hire anyone who isn't nice regardless of his or her talent. It's also important to me that Blackstone remains free of internal politics, so if jockeying for position is part of your nature, we don't want you.

Here are my rules for how to have a successful interview:

1. *Be on time.* Punctuality is the first indicator of how much thought and preparation you have put into an interview.

2. *Be authentic.* Interviews are a mutual assessment, a bit like speed dating; everyone is looking for the right fit. Be comfortable and natural, and chances are you will be liked for who you are. If you share who you are and the interview results in a job offer, that's great. If it doesn't work, it's likely that the organization wasn't right for you either. Better to know and move on.

3. *Be prepared.* Learn about the company. Interviewers always enjoy discussing what's happening in their environment. Plus it's a good way for you to hear how enthusiastic an employee feels about the place where he or she works. Describe what draws you to the company and why. An interviewer wants to understand your motives and whether they fit with the organization's culture.

4. *Be candid.* Don't be afraid to talk about what's on your mind. Focus less on impressing the interviewer and more on being open and striving for an honest conversation.

5. *Be confident.* Approach the situation as an equal, not as a supplicant. In most situations, employers are looking for someone who can hold the table. Provided they are not arrogant.

6. *Be curious*. The best interviews are interactive. Ask questions, ask for advice, ask your interviewers what they enjoy most about working for their organization. Find a way to engage interviewers, and always make sure the conversation goes both ways. Interviewers like to talk too, so that they can share what they know.

7. *Avoid discussing divisive political issues unless you are asked.* In which case, be straightforward. Describe what you believe and

why, but don't be argumentative.

8. *Mention people you know at an organization only if you like and respect them.* Your interviewer will be judging your taste in people.

THE BEST WAY TO LEARN IS BY DOING

My first assignment at Lehman came from Herman Kahn, a cantankerous old partner I had seen but not yet met. He wanted me to prepare a "fairness opinion" analysis on a manufacturer of airline seats. Companies ask banks for fairness opinions when they want an objective evaluation of the price to be paid in a transaction. In this case, the manufacturer had been sold three years earlier for a high price just as the market for airplane seats had peaked. Since then, sales of airplanes had declined and the company's value had decreased dramatically. Kahn asked me to figure out if the price paid in 1969 had been fair.

It was not an easy analysis. Today, we do the research and calculations using computers and relevant databases. Back then, it required days in Lehman's basement archives going through back issues of the *Wall Street Journal* and the *New York Times*. I'd come up after ten hours covered with newsprint ink, only to get to work with my slide rule making the calculations. It was kludgy and mind-numbing work, but it was essential to learning my craft.

I wrote a sixty-eight-page history of the company and its shifting value based not only on the trajectory of its stock price but on its prospects, the market trends, and everything else I considered relevant. I included appendixes and footnotes for clarification. Then I took this work of beauty to Herman Kahn on the partners' floor. He wasn't there, so I put it in the middle of his desk where he would see it as soon as he sat down. I went to my office and waited. A few hours later I got a call.

"Is this Steve Schwarzman?" Herman Kahn was hard of hearing and his voice was loud, nasal, aggravated.

“Yes, it is.”

“Schwarzman! This is Herman Kahn! I got your memo! There’s a *typo* on page 56!” And he slammed the phone down.

I looked at page 56. The only error I could find was a misplaced comma. *Jesus*, I thought. *This isn’t Harvard Business School. These people don’t fuck around. I’m living according to their rules. I had better learn to play by them*. I never heard from Herman Kahn again on the project.

A few months later, a group of us, including the deal teams as well as others at the firm, were summoned to the boardroom. Lehman was the lead underwriter in the initial public offering (IPO) of the Student Loan Marketing Association, the precursor to Sallie Mae. We were supposed to raise $100 million, a lot back then. So far we had only $10 million. Lew Glucksman, the head trader and number two person at the firm, wanted to know why. I was the most junior person on the team, the junior associate to a more senior associate, responsible for a couple of numbers. Lew glared around the table and settled his gaze on me.

“Who the fuck are you?” he screamed. “And why aren’t you sitting up straight?”

I could feel my cheeks burn. Everybody around me was looking the other way. I went back to my office afterward, shaking. Later, people came up to me one by one to commiserate and assure me I hadn’t done anything wrong. Two things came out of that meeting. First, to this day, I sit straight in important meetings. Second, I had caught Lew Glucksman’s attention. He must have asked about me and heard good things, because shortly afterward, he called and told me to get to work on fixing this broken IPO. I had never raised money and had no idea how to do it, but I knew better now than to try figuring it out by myself. I reached out for help.

Steve Fenster, my senior associate, had become my closest friend at Lehman. Before entering finance, he had been one of Robert McNamara’s whiz kids, the group of brilliant young men brought in to modernize the Department of Defense during the 1960s. He had a probing, provocative intelligence and the rare talent of looking at the same facts everyone else did but finding things no one else could see. We talked together almost every night, and he explained to me how IPOs and mergers worked—loan structures, debt instruments, mergers and acquisitions, the machinery of a financial firm.

Steve was also one of the firm's eccentrics. Every day he dressed in a dark suit, a repp striped tie, and wingtip shoes. Only on vacation did he wear loafers. One time he had to go straight from vacation to see a client and found he had packed two left wingtips by accident. The idea of wearing loafers to a business meeting was unacceptable, so he wore the two left shoes instead. The client noticed. But Steve was so brilliant that no one cared.

"It's not that hard," he said of my latest assignment, trying to settle me down. "You build a model of why this is a good investment. Everything's a spread." This company simply made loans and charged more for the loans than it cost them to borrow money to make the loans. All I had to do was calculate how many loans it could make and I could determine the company's profit potential. "Then you go to some financial institutions and show them why they would want to buy into this thing." I had to identify the investors and institutions that might be interested and then craft a pitch that persuaded them they needed the Student Loan Marketing Association as part of their portfolio of investments.

Since this was a company that made loans to students, I figured one place to start was with universities. Harvard had the largest university endowment, so as a recent graduate, I called and got an appointment with Harvard's treasurer, George Putnam. Putnam was the head of Putnam Investments, a giant mutual fund company he had founded in the late 1930s. For a first-year banking associate with his little road-show book begging for an investment, meeting Putnam was like meeting one of the gods of New England.

I opened my pitch book and began my windup.

"Mr. Schwarzman," said Putnam, interrupting me. "Can you please close your book?" I closed the book, nervously. "Mr. Schwarzman, have you ever heard of the UJA?" The UJA, the United Jewish Appeal, three letters it never occurred to me would be crossing George Putnam's lips.

"Yes, I've heard of the UJA."

"Have you ever heard of card calling?" Card calling was a common practice at the UJA's fundraising dinners. The chairman would call out the names of all potential donors, announce what they gave last year, and everyone would listen for what they were going to give this year. It was a way to create a level of expectation and apply peer pressure.

"Let's start this meeting over, Mr. Schwarzman. You say, 'Mr. Putnam, you're the treasurer of Harvard University, and I'm starting the largest—what will be the largest—student loan lending business in the United States, and I've got you down for $20 million.' Now, say that." I said it.

"That's a great idea, Mr. Schwarzman," he said. "I'm in for twenty." He had read up on the company before I walked into the room and would not be convinced by me one way or the other on its merits. He just wanted my help in making a quick decision on how much to invest. "Now what you do is take your book, get on the train, go to New Haven, and see Mr. So and So at Yale, and say, 'Mr. So and So, I'm raising money for the Student Loan Marketing Association, which is going to be the biggest lender to students in the United States. I've got Yale down for $15 million.' Try that. See what happens. After that, get back on the train, go to Princeton. Ask them for $10 million."

By the end of my university pitches, I had raised the better part of the $100 million, the money that founded Sallie Mae. Putnam gave me a lesson in raising money that would stay with me throughout my career as I raised fund after fund at Blackstone. Investors are always looking for great investments. The easier you make it for them, the better for everyone.

Steve Fenster and George Putnam were good teachers. But I also learned by making my own mistakes. Late in my first year, I was sitting on a plane with Eric Gleacher, a smart, no-nonsense ex-marine, a few years older than me, who had just been made partner. We were on our way to St. Louis to see a food processing company about spinning off its chain of convenience stores.

I had prepared the financials, laying out the various options. Eric would be presenting. Compared to the huge teams at investment banks today, banks then were much smaller. There wasn't the diligence, checking and rechecking of presentations. When we got settled on the plane, I handed my work to Eric. As he turned the first page, his brow began to furrow. He looked at the next page even more quizzically. After the third page he said, "Steve, I think you've made an error." I had gotten one number wrong early on, and it had affected my calculations on about half the pages. "This is a mess," said Eric.

"But we can give the presentation anyhow. Just take out the bad pages, and I can talk my way through the rest of it. It's okay."

Herman Khan had been outraged because of a typo. Now I had messed up an entire deal book. Eric buried himself behind his newspaper while I tore out the offending pages in all the copies of the presentation. We landed in St. Louis and took a cab to the company, Eric still silent. We sat down at the board meeting, and Eric passed out our booklets. There was some introductory talk. Then he began his presentation.

"As you can see from the analysis . . . I think we have a statistical error." As he spoke, he all but launched himself across the table grabbing our presentation books from the board members. "I can talk you through this without any numbers."

I had been so freaked out by my mistake that instead of tearing out the bad pages, I had torn out the good ones. I could have melted under the table. We left the company, got in the cab, and rode back to the airport. Not a word. Right before they called the plane, Eric turned to me: "If you ever do that to me again, I'm firing you on the spot."

Painful as it was, Lehman was the school I needed. Like any other craft, finance has to be learned. As Malcolm Gladwell pointed out in his book *Outliers: The Story of Success*, the Beatles needed to go to Hamburg from 1960 to 1962 to transform themselves from a garage band into the Beatles, and Bill Gates spent hours as a teenager on the computers at the University of Washington close to his house before he could write the software for the first PCs. Similarly, people who succeed in finance must start with repetitive practice before they can ever hope to achieve mastery. At Lehman, I observed every step of the process and was trained in all details, any one of which, done wrong, can bring everything crashing down.

There are people who come to finance from other professions, from law or the media perhaps, but the best I've ever worked with grew up in it. They learned by doing the fundamental analysis. They established strong foundations for their careers by discovering that the smallest things matter and suffering the indignity of their early mistakes.

During my second year at Lehman, a new chairman and CEO arrived. Pete Peterson had been CEO of Bell and Howell, a maker of media equipment, and most recently President Nixon's commerce secretary. He had great CEO contacts and was widely respected in business and government. He arrived at Lehman to find it in financial trouble, struggling to survive, and rife with the kind of infighting that I had predicted in my Harvard Business School paper would kill it.

Pete had an ally in George Ball, a partner who had served as deputy secretary of state under Presidents Kennedy and Johnson, and eventually as ambassador to the United Nations. They worked their international contacts and persuaded the Banca Commerciale Italiana to provide capital to help Lehman survive. Once Lehman was off life support, Pete sent out a memo to the entire company asking for ideas. After a year at the firm, I figured I knew enough to write a strategic plan involving money management and investment banking. A week after I sent it, Pete called me to see him. At the end of our meeting, he said: "You seem to be a capable young man. You and I should work together."

The word on Pete was that he was smart but had no experience in finance or investment banking. He asked five times as many questions as anyone else, and people found him exhausting to work with. His relentless questions enabled him to get to the heart of the problems at the firm, but the process was trying.

If he didn't really know what he was doing and I still had so much to learn, it would be a case of the one-eyed leading the blind. I suggested we wait until I was better prepared. Pete took my candor well. But about two years later, he called again: he wanted me on his team. We were a good match. I knew what he didn't but was young enough not to get in his way.

One day, he invited me for lunch with Reg Jones, the CEO of General Electric. Pete and Reg were both on the board of General Foods and had become friends. Reg wanted Pete to meet a young executive he was grooming at GE.

"This is Jack Welch," said Jones.

"Hi, Steve. Nice to meet you." He had a kind of high-pitched voice, squeaky and with a strong Boston accent.

"Reg is here because Jack will be the next CEO of General Electric—but that's currently a secret," said Pete. "He'd like us to teach finance to Jack. So that's your job."

"Okay," I said, hesitantly.

"Yeah, yeah, yeah," Welch said. "It's good." This squeaky guy with his "yeah, yeah, yeah" is going to be CEO of General Electric? He's either got to be the smartest guy on earth, or else Reginald Jones was off base in choosing him.

When Jack came to learn finance, it took me about one minute to see that Reginald Jones wasn't off base at all: he had hit a home run. Having Jack Welch go to work on you was like having your brain connected to a dust-buster sucking out everything you know. I've never met anyone like him before or since. He never stopped asking questions—torrential, relentless questions—and he instantly grasped the links between one idea and another, even if they were entirely new to him. He was like Tarzan swinging through the trees at blistering speed, never missing a vine, learning more quickly than I could teach.

Getting to know Jack and watching him in action reinforced my growing belief that the most important asset in business is information. The more you know, the more perspectives you have and the more connections you can make, which allow you to anticipate issues.

Jack became CEO of General Electric in 1981 and began a run as one of the greatest CEOs in American history. Pete's introduction also led to a long friendship. After decades, I'm still amazed by Jack. Meeting him was one of the gifts of being part of a major firm so early in my career. Wall Street and business are small worlds. If you start at a great school or a big firm, crossing paths with the best people of your generation, you'll keep running into them. Many of the friends I made at Yale, Harvard Business School, the Army Reserves, and in those early years on Wall Street have remained my friends. The trust and familiarity of those early relationships have enriched my life in ways I could never have predicted.

ALL DEALS ARE CRISES

An investment banker's job is to deal with change and often high-stress situations. You suggest an acquisition or a sale of a division, identifying a target purchase or a buyer. You propose that a company borrow more debt to fund expansion or repurchase shares when its stock price is low. How you initiate and manage that change is the measure of your success.

By late 1978, I had been with Lehman for six years as an associate. My responsibilities had grown, and I was under consideration for partnership. One Friday, I was in Chicago on business when I got a call from Ken Barnebey, the CEO of Tropicana, the orange juice company. Earlier in the year, I had been to see him at the company's headquarters in Bradenton, Florida, to propose various financial ideas. It was a casual, get-to-know-you meeting. But naturally I had hoped that one day something would come of it.

"We've got a very sensitive situation I'd like to talk to you about," he said. "We've been approached by a company that wants to buy us, and we're considering what to do." Barring any conflicts, he said, he wanted me in Bradenton Saturday at 8:30 a.m. to speak to his board. I called our New York office. My colleague Teddy Roosevelt asked around and confirmed there was no conflict. If any other divisions at Lehman had been working on deals involving Tropicana, I wouldn't have been able to proceed. I called Ken back, and he described the terms of the bid. The price had been agreed in principle, but the buyer was presenting different packages of cash and securities the seller might accept, which would make the deal more or less valuable to them. My job was to assess these different structures on behalf of the board and make a recommendation.

Chicago was in the middle of a snowstorm. All flights to Sarasota-Bradenton airport were delayed. By the time I got on a plane, it was late, and the flight almost empty. As we headed south through several storms, all I had to help me understand the proposed transaction was a copy of the *Stock Guide*, which contained the basic financials of public companies. I looked up Tropicana and found its earnings and a few other ratios. I could see how much money it made, its profits as a percentage of revenue, and the amount of debt and equity on its balance sheet—the simple metrics of a company's financial health. I could also look up other food companies and see how they compared to Tropicana. But there had been little merger activity in the sector since the stock market crash of 1973, so I had no recent, comparable deals to guide me.

We landed at four in the morning, and it took another hour and a half to find a cab and get to my motel. I lay down on the bed for a few minutes, then took a shower. I had been planning to fly right back to New York from Chicago, so had only the clothes I had arrived in. I put them back on and tried to clear my head. At 7:30 a.m., I walked into Tropicana's offices.

"We're in a rush because we've already approved the deal in principle," said Ken. "Beatrice [the acquiring company] has too. We have to announce when the market opens Monday, which means we have to get everything in place right now. Beatrice is offering three different types of structures. One is a combination of common and straight preferred stock. One is common and convertible preferred. One is common and cash. We need you to advise us which of these to take, if any. We've got an hour before the board gets here."

I had had no sleep, had no partner with me, not even another associate, and I had never done a merger. *You are in such trouble*, I told myself. *What are you going to do?*

When I started in finance, I was ill prepared for the stress of the work. Every point in every negotiation was a fight, with a winner and a loser. People in this business weren't interested in carving up the pie so everyone got a slice. They wanted the whole pie for themselves. I observed that when I was the one making the decisions and the voices rose and tempers flared, my heart would beat faster and my breathing would become more shallow. I became less effective, less in control of my own cognitive responses.

The fix, I found, was to focus on my breathing, slow it down and relax my shoulders, until my breaths were long and deep. The effect was astonishing. My thoughts became clearer. I became more objective and rational about the situation at hand, about what I needed to do to win.

That morning in Florida, I slowed down my breathing until I could relate to everyone and figure out the issues at hand as if there were no stress at all.

In my relatively short career, I had learned that deals ultimately come down to a few key points that matter most to each side. If you can clear everything else away and focus on these points, you will be an effective negotiator. You cannot let all the voices, paperwork, and deadlines overwhelm you. What Ken and the board needed from me now was some clear thinking.

The equity portion of each of the structures would be tax free if Tropicana's shareholders accepted more than 50 percent of their payment in Beatrice stock. The simplest structure was for common stock and cash: Beatrice would pay Tropicana's shareholders 51 percent of the $488 million purchase price in its own stock and the rest in cash. The appeal of the other two structures depended on what you thought of the future of a combined Beatrice and Tropicana. If you felt reasonably confident, you might take the straight preferred stock, which came with no voting rights but a guaranteed dividend paid out before any dividends to common stockholders. And if you felt really good about the deal, you'd take the convertible preferred, which came with a lower dividend but the right to swap it at any time for common stock. If the stock went down, you'd still have the dividend. If it went up, your upside was unlimited. There was no way I could figure this all out for myself. Exhausted and bleary, I needed advice—and cover, if this deal went wrong. I called Pete.

"I'm seeing Tropicana's board in an hour. What should I do?" He advised me to call Lew Glucksman, and then Bob Rubin, one of the senior banking partners. I called Lew and woke him up. "Lew, here are the multiples, based on the *Stock Guide*."

"I think the price is fair," he said, and he recommended one of the three structures.

Then I called Bob Rubin. "Bob, I'm sitting here at Tropicana, I talked to Lew, I talked to Pete. Here's the situation. What should I do?"

"The price sounds okay," Rubin said. "In terms of the structure, it's a matter of taste."

As the five members of the board arrived, I felt at least a little more confident. Then I saw the stenographer and two tape recorders in the room. Everything I said would be recorded. The chairman, Anthony Rossi, looked and sounded like Marlon Brando in *The Godfather*, in the scene where he is playing with his grandson among the tomato plants, just before he keels over and dies. “Come, Mr. Schwarzman,” he said, pointing to the chair next to his. “*Sit-a* here, next to me.”

Rossi had emigrated from Sicily as a young man. When he arrived in Florida, he had opened a grocery store, then went into the citrus business and founded Tropicana. He ran it so tightly that he didn’t allow anyone to have windows in their offices in case they might get distracted. He was the only one with a window, so he could watch the trucks bringing the oranges in and make sure no one was stealing. This deal was the consummation of a life’s work. He was a Baptist and planned to give away a lot of the money he was about to make to a religious foundation. He wasn’t a financier, but he was shrewd enough to have built a strong business. I owed it to him to be straightforward and clear.

“Tell us, Mr. Schwarzman,” he said, “what do you advise us to do?”

Another trick I had learned for managing stress was to take a moment to slow myself down. People were always happy to let me have that extra moment. It even seemed to reassure them. They would be even more eager to hear what I had to say once I was ready. So I took a moment and then began.

“The first thing is that you do not have to sell the business.” It was important that Rossi hear that. That he still feel in control. “But as you’ve decided, next you have to figure out whether the price is attractive. I understand you’re already satisfied with that, which would be my opinion as well.”

I told the board they should feel comfortable about Beatrice, given its financial health, and laid out the details of the various purchase structures, the issues of tax and timing, drawing on Lew’s and Bob’s insights. I explained to Rossi how the convertible preferred would give him a steady income, with the possibility of further upside if the stock went up. After an hour and a half of discussion, they chose the mix of convertible preferred stock and cash and asked me to finalize the deal terms with Lazard, Beatrice’s bankers.

When I left the room I called Ellen. She had been expecting me home the previous night.

“Sweetie, I’m so sorry . . .”

“Where are you?”

“Bradenton, Florida. I just did this amazing deal.” I couldn’t quite believe it myself.

“What? We’ve got a dinner party tonight.”

“I can’t make it to the dinner party. I’m under enormous stress right now, and I have to finish what I’m doing. I’ll catch up with you later.”

Lou Perlmutter was one of Lazard’s masters, a senior partner and expert in mergers and acquisitions. He could easily have tried to take advantage of my inexperience.

“Steve, this deal’s meant to happen,” he said. “I’ll give you the standard down-the-center thing. Just say yes, because I don’t want to overnegotiate. It would only make a mess.”

Lou knew that Beatrice wasn’t the only company interested in Tropicana. Others were circling. He didn’t want a long negotiation with Tropicana’s financially unsophisticated board and their young banker. All he needed from me was to convince the board quickly so we could print the deal and go home. Lou knew that if he jammed me, I would find out, or someone at Lehman would find out, and the deal would get held up. So he made it as easy as he could. We worked together the rest of the day.

As I was flying home, the snowstorm that had hit Chicago the previous night was slowing air traffic into New York. I made it home around 4:30 a.m., beyond exhausted, trying to get my head around what had just happened. $488 million! It was the second biggest M&A deal in the world that year. By the time I got home, I hadn’t slept for forty-eight hours but still I couldn’t go to bed. I put some logs in the living room fireplace and started a fire. I hardly ever drink, but I poured myself a glass of Courvoisier and put on the Bee Gees’ *Saturday Night Fever* album. I sat back in the easy chair, imagining John Travolta strutting across the disco floor. $488 million. What had I just done?

At 7:00 a.m., the phone rang. It was Felix Rohatyn. He had spoken with Lou Perlmutter. My head was still full of Courvoisier, exhaustion, and *Saturday Night Fever* as Felix began. “I just heard about the Tropicana deal,” he said. “First, I want to congratulate you. That’s fantastic. Second, you’re thirty years old and you’ve done something huge. And by yourself, I understand, without a partner or anyone else. So this is a huge breakout moment in your career. A lot of people are going to hate you. Don't worry about that. You are different from them. Do not let that bother you!

"The third thing is that you now have a responsibility to speak out in public. You will need to speak up when you see something wrong that can be corrected. Don't fear doing that, because certain people have an obligation to society to do that. I'm one of those people. You are now one of those people."

Felix had a particular vision of the contribution bankers could make. But all I could think about was who would hate me.

The phone rang again. It was Peter Solomon, Lehman's vice chairman.

"Who the fuck do you think you are? You sold Tropicana? I'm working on a deal to buy them for Philip Morris! We were going to make them a tender offer. Philip Morris is the biggest client we have. And you put yourself in the way? I'm talking to the executive committee on Monday. We're firing you! On Monday, you're history!"

"I know Teddy Roosevelt talked with you," I replied. "You never mentioned anything about Tropicana to him."

"Monday morning, Steve. Monday morning you're out of here!" Slam.

I knew the truth, though, and called Pete. I assured him that Teddy had specifically spoken to Peter about conflicts and he hadn't said a thing about Philip Morris's interest in Tropicana.

"That's ridiculous," Pete said. "Don't worry about it."

On Monday Solomon raged to the executive committee about his broken deal with Philip Morris. Everyone in the office speculated about my future. I was surrounded by jackals. But thank God for Pete. He wasn't having any of it.

MONEY IS A POOR CURE FOR A BAD SITUATION

The Tropicana deal secured my promotion to partner, and I celebrated by redecorating my office. If I was going to be there twelve hours a day, I wanted it to be a cocoon against all the psychological stresses of my work, cozy, like a beautiful sitting room or library in an English house. I had the walls painted partly in reddish-maroon, the rest covered in the kind of grass cloth I'd seen at Lee Eastman's place. I installed a chocolate carpet, chintz chairs, and a partners' desk from the 1890s. It was exquisite. No one else at the firm had ever done this. It wasn't how they thought about work. But I didn't consider myself to be at work. This was my second home, and I wanted it to be beautiful, comfortable, and visually interesting.

When I arrived at DLJ in 1969, I had my face pressed up against the glass of a life I could only imagine. Nearly a decade afterward, I was living it. One day in 1979, I had just finished a deal when another partner stuck his head in my door and asked if Ellen and I would like to come with him to Egypt. Tomorrow. For dinner next to the pyramids. One of our clients was sponsoring the event, and Lehman had bought a table and needed to fill it. The next day, we left on a Pan Am plane with one hundred other guests. While we were in Paris refueling, the door opened and fifty of the most beautiful women I had ever seen in my life—models who were going to appear in a fashion show for us—boarded our plane. In Cairo, we went straight past customs, and a motorcycle escort cleared the way to our hotel next to the Sphinx. That night we attended the fashion show by the designer Pierre Balmain. The following afternoon, we went for tea with Anwar Sadat, Egypt's president, and his wife, Jehan. Sadat had won the 1978 Nobel Peace Prize for negotiating peace with Israel. On the final evening, we had dinner with five hundred people on the sand in front of the pyramids and the Sphinx. I sat at the table next to President Sadat. The night ended with Frank Sinatra singing *New York, New York*. It was one of the most memorable evenings of my life.

On our flight home, almost everyone came down with amoebic dysentery, including me. But it didn't take the shine off an extraordinary trip. It was the kind of astonishing experience I had hoped to have someday. Now I wanted even more.

In 1980, the *New York Times* profiled me on the front page of the Sunday Business Section with a large picture as Lehman's "Merger Maker." The reporter credited me with a "drive to succeed, a strong persistence (he once finished running a cross country course even after he tripped and broke his wrist) and an infectious vitality that make other people like to work with him." The cross-country race had been in ninth grade, and I had to be rushed to the hospital. She went on: "Mr. Schwarzman says he approaches problems by asking himself, 'What would I want if I were in their shoes?' That, he says, is what gives him his rapport with people. Still a student of behavior, he listens hard to what people say, believing that things that are said are said for a reason. This art of listening gives him an unusually high gift of recall."

It was a pretty accurate picture of me at the time. Listening to people seemed obvious. But it evidently marked me out on Wall Street. I didn't just try selling whatever it was I had to sell. I listened. I waited to hear what people wanted, what was on their mind, then set about making it happen. I rarely take notes in meetings. I just pay very close attention to what the other person is saying and the way he or she is saying it. If I can, I try to find some point of connection, an area of common ground, a shared interest or experience that turns a professional encounter into a more personal one. It sounds like common sense, but apparently in practice, it's relatively rare.

One effect of my intense listening is that I can recall events and conversations in detail. It's as if they are imprinted and stored away in my brain. A lot of people fail because they start from a position of self-interest. What's in this for me? They will never get to do the most interesting and rewarding work. Listening closely and watching the way people talk puts me much closer to answering the question I'm always asking myself, which is:

How can I help? If I can help someone and become a friend to their situation, everything else follows.

There is nothing more interesting to people than their own problems. If you can find out what they are and come up with solutions, they will want to talk to you no matter their rank or status. The harder the problem and the scarcer the solution, the more valuable your advice is. It's in those situations, where everyone is walking away with averted eyes, that the field clears and the greatest opportunity awaits.

The early 1980s weren't just good for me. Five years in a row, Lehman notched record earnings. Our return on equity beat all our competitors. I rose to be chairman of the mergers and acquisitions department, advising some of the firm's biggest clients. At Lehman's Water Street offices, there were never enough hours in the day. Our department was second to Goldman Sachs in deal size, but we led them and the rest of Wall Street in deal volume.

By then Pete had been Lehman's CEO and chairman for ten years. He had pulled Lehman back from the abyss. Although he didn't enjoy finance in particular, his strength was his range of contacts in business and politics. He could get anyone on the phone. He was twenty-one years older than me, but we had developed a close working relationship. We complemented each other. He could bring people together and nurture relationships; I could originate and execute deals. He was a thinker, tolerant and reflective. I could be confrontational if necessary. I ran and closed many of the deals that Pete initiated. People around the firm considered us a team. We trusted each other implicitly. But it was Pete's tendency to trust people in the feuding castle of Lehman that eventually got him into trouble.

In the early 1980s, Lehman's traders were racking up huge profits in a bull market. Their leader was Lew Glucksman, who had been helpful to me during the Tropicana deal. But generally he was as volatile as the markets themselves. Self-restraint was not in his emotional vocabulary. He roamed the trading floor in a rumpled suit or in shirtsleeves, his shirttail hanging out, an unlit cigar clenched between his teeth. He once got so angry that he yanked a phone out of the wall and smashed it into a plate glass window. Another time, he got so pumped up, he ripped his shirt open, tearing off the buttons, and stomped around bare-chested.

In 1983, he went to Pete and asked for a promotion. Pete agreed and made him president of the firm. Pete thought that was only right and fair. But he didn't understand men like Lew Glucksman. A few months later, Lew walked into Pete's office and said that was just the first banana. Now he wanted the whole bunch. He wanted to be co-CEO. Pete didn't want to fight, so he acquiesced. Eight weeks later, Lew was back. "I need to be CEO myself. I want you gone." He had organized a putsch with the trading partners. Pete didn't tell me about Lew's ultimatum until he had caved in. I was appalled.

"Why didn't you fight?" I said. "You could have marshaled your own resources and pushed this guy out. You've got a lot of support among the partners. Why didn't you at least talk to me?"

"I knew what your advice would have been," he said. "You would have wanted to kill him. I know you. I'm not like you. I've been here for ten years already. I turned the place around. We were at the brink; now we're making a fortune. Why would I want to destroy it? It's just not worth the fight. Besides I don't know anything about trading. If I forced Glucksman out," he said, "what would happen to the trading division?"

"You don't need to know about trading," I said. "You hire the best guy from Goldman or JPMorgan."

"It would rip the firm apart."

"If somebody challenges you, you've got to be ready to rip the place apart. Then you put it back together."

"No, no," Pete said. "That's what you'd do. Not me. I've been fighting people here for ten years. I'm tired of it." And with that, he walked away. Pete was fifty-seven years old and had undergone surgery for a brain tumor, which turned out to be benign. The firm was going to require him to start cashing in his stock when he turned sixty. If he could get out with a good settlement, that seemed the best option for him and his family.

I knew things weren't going to turn out well for the firm. Only months after Pete left, Lehman was in deep trouble. Lew and some of his allies in the London office had made a huge trade in commercial paper—loans to companies with no collateral. If the borrower defaults, the owner of the paper cannot lay claim to any assets. These loans can be profitable if leveraged, and they are ordinarily short term (thirty, sixty, or ninety days), which means they aren't that risky. Usually you can be sure they will be paid back over such a short period.

Lew and his team had gotten greedy in a rising market and bought notes with five-year maturity dates, which had higher interest rates, making them a lot more vulnerable. The markets turned against them and the value of the securities plummeted. Their losses on the trade amounted to more than the firm's total equity. Lehman was back on the edge of collapse.

Lew had made these trades in secret, but word started to get around, first in London, then in New York. I had heard what was going on from a good friend in the London office, Steve Bershad, who had been sent to England to build the firm's corporate finance business. He had been so disturbed by what he saw in the trading room that he had called in auditors to take a look. "The firm's busted," Steve told me on the phone. "We have no equity."

Lew called a meeting of all the partners. With over seventy of us sitting in the thirty-third-floor large conference room, he said, "I know there are rumors about some position in London. These rumors are completely false. We have no problems. And I will instantly fire anybody who says that we do!"

Instead of sharing the problem and asking for help, Lew had decided to lie. I was expecting one of the senior partners on the firm's board of directors to challenge him. Instead, they listened in silence and left the meeting whispering to each other, visibly scared and confused. Lew's leadership had proved toxic, and immediately people were wondering how they could secure their stakes in the firm before it went bankrupt. Sheldon Gordon was head of Lehman's investment banking division and the firm's vice chairman. He had worked as a trader alongside Lew. People considered him to be one of his closest allies. But I knew he was smart and decent, and I heard he was exploring options with other members of the board. I went to see him.

"You realize this is going to blow up," I said. "There are a lot of people who know Lew is lying. I know the firm's busted, you know it's busted, and if the outside world finds out we have no equity, we're going to collapse. The partners won't take him on because they're afraid he'll fire them. If we don't sell the business and somebody learns about this, don't you think we're dead?"

“Yes,” he agreed. “We’ll be finished.”

“Do you want to sell the firm?” As the head of mergers and acquisitions, I thought I might be able to find a way for a stronger firm to step in and rescue us. Even with all our problems, Lehman was still a great firm, with a global brand and talented people.

“Absolutely,” said Shel. “If this gets out we’re dead and gone. But you’ll need to get the thing done in a couple of days. We don’t have any time here.” As he spoke, I was already thinking about potential acquirers.

The first name on my list was Peter Cohen, chairman and CEO of American Express’s Shearson investment unit. He was my age, one of the youngest CEOs on Wall Street. American Express had the money to buy Lehman, and I knew that Cohen was ambitious to expand Shearson into the investment banking business. He was also my next-door neighbor in the Hamptons. We knew each other socially. It would be easy enough to make a quiet overture. I called him late that Friday. The next morning, I went to see him. We met in his driveway.

“We’ve had a big trading loss,” I explained. “We’re not really looking to sell the firm, but we probably should. If you’re interested, this is a one-time special—if you can act on it in the next few days.” Over that weekend, he spoke to American Express’s CEO, Jim Robinson. On Monday, he called and said he’d like to do a deal. He offered $360 million. Salomon Brothers had been sold two years earlier for $440 million, but Salomon had a much bigger trading business and wasn’t on the verge of bankruptcy. It was the best we could get, given the time constraints.

Shel told the partners. He said they would all receive rich payouts. If they waited, they might get nothing. The other partners excluded Lew from the discussions. All but one of them, one of Lew’s closest allies, approved the sale. Two days later, the deal was announced on the front page of the *New York Times*. There were still details left to negotiate and a risk it wouldn’t go through. But this way, we controlled the news, and we put American Express publicly on the hook in case they had second thoughts. The day of the announcement, investors and journalists clamored for information. Lehman Brothers, founded in 1850, had been an institution on Wall Street for over 125 years. The sale was a shock.

It wasn't until the early evening that I realized I still hadn't spoken to Lew. Shel and the other partners had outflanked him. The firm had been sold, and his failure as CEO was complete. I went down to his office, Pete's old office. It was dark. I thought he must have gone home but knocked on the partially opened door.

"Hello. Is anyone here?" A small voice answered, and I could just about see Lew sitting at the end of the couch over against the wall.

"Why are you sitting in the dark?" I asked.

He said he was ashamed. He had destroyed the firm he loved. "I'm thinking about blowing my brains out."

I asked if I could sit down. He waved me over.

"Lew, you didn't intend this. Sometimes things happen that weren't intended."

"I know," he said. "But I'm responsible, so it's my fault, whatever I intended."

"You were trying to do something good, and it turned out wrong. And it *is* a terrible outcome for the firm. But people are going to have to go on with their lives. It's going to change nothing if you kill yourself. It'll just be another tragedy on top of a tragedy, and you're not that old, you know. There's always a future. You'll reinvent yourself in some way."

We talked for half an hour or so; then I went back to my office. I was thirty-six years old, and I had sold Lehman Brothers. I was now free to leave a firm I had come to find intolerable. I felt light, exhilarated. But then there was Lew Glucksman sitting there deciding whether to shoot himself, worrying how that would affect his daughter. He loved the firm, he said. The tragedy was that he undoubtedly did.

All I wanted was to get out of Lehman as fast as I could. I had told Peter Cohen early in our negotiations that I had lost faith in Lehman's partners when they had failed to fire Lew. He had agreed that I could go. Then during the negotiations, he called and asked me to stop by. He was insisting that all of Lehman's partners sign a noncompete agreement, barring them from working for a competitor for three years if they left the firm. I told him a noncompete was irrelevant to me. He knew I was leaving.

"The problem is the American Express board met yesterday," he said. "Since Peterson left and Glucksman's effectively gone, you're the person who's best known to the board members. What they said at the meeting was that we're buying talent, and if we don't keep the talent, there's no reason to do the deal. You exemplify the talent. So they're requiring a noncompete. That's the deal. If you don't want to do the deal, don't do the deal."

"The deal's been announced," I said.

"I know it's announced. But if you don't sign your noncompete, we'll unannounce it. Your firm will go bankrupt. I don't care one way or another. You decide."

"You've got to be kidding," I said. "You and I have an agreement."

"I'm not kidding." I was the only partner who hadn't signed the noncompete. The whole deal now hinged on me. If I refused, the deal would collapse, and Lehman with it. But three years was a high price when I was so desperate to be free. Ellen said three years was no big deal, and I would figure it out. My partners swarmed me to cooperate.

The day I started at Lehman, one of the partners had told me, "Nobody at Lehman will ever stab you in the back. They'll walk right up to you and stab you in the front." It was competitive, every man for himself. I had seen that in the architecture of the place and written about it at HBS. But I had loved that about it. There was a gallows humor to all the infighting. My friend Bruce Wasserstein, when he was running mergers and acquisitions at First Boston, once said to Eric Gleacher and me, "I don't understand why all of you at Lehman Brothers hate each other. I get along with both of you." "If you were at Lehman Brothers," I told him, "we'd hate you, too."

But with Pete gone and the firm sold, I wanted to go. I knew that I could always make money somehow. I needed some space to think. I booked a room at the Ritz Carlton on Central Park South. I went for long walks in the park. And I thought until I figured out a compromise. I called Peter Cohen and proposed I stay for one year, not three, and then start my own firm instead of joining one of his large competitors. He agreed. In the end, despite what he had said, he wanted the deal as much as I did.

Once the takeover was finalized, Jim Robinson, the CEO of American Express, asked me to come and see him.

"I hope we're going to have a very productive relationship," he said. "But I've heard you're not too happy."

“Why would I be happy?” I said. “I’m working at a place I don’t want to be.” He said he had known nothing of my negotiations with Peter Cohen.

“This is a pretty terrible thing we’ve done to you,” he conceded. “Why don’t you come here and take the office next to mine? It’s right between me and Lou Gerstner.” Gerstner was then head of American Express’s travel and credit card businesses and would later be president of American Express and CEO of RJR Nabisco and then IBM. “You can work on some deals for American Express and teach Gerstner something about finance. He’s an operating guy.”

That seemed better than sitting over at Lehman. So I had two offices and began spending a lot of my time at American Express next to Jim Robinson. I was grateful, but he could quickly sense how eager I was to get out. He proposed I take a job in Washington to complete my noncompete period. He even arranged an interview for me with Jim Baker, then President Reagan’s chief of staff.

The opportunity to spend some time in the capital appealed to me. You could not do the kind of work I had been doing in finance and not be fascinated by Washington’s influence over the economy. Averell Harriman and Felix Rohatyn had convinced me of the appeal of a life at the intersection of business and politics, linking two worlds that so often operated at cross-purposes.

I’d met Jim Baker at the White House in 1982 at a meeting about stimulating the economy. The borrowing cost for even the best rated companies at the time was 16 percent. There were about twenty of us in the room, and I will never forget how scared those guys looked, worried that they would never be able to return the US economy to growth. Baker, though, was impressive, smooth, and effective in the combative world of Washington.

Our meeting went well. We discussed my being the number four person on the White House staff. Then Baker became secretary of the treasury. The only job available there was to run the government’s debt issuance. It had gone unfilled for two years, so I told Jim it clearly wasn’t a job that needed doing. The moment for me wasn’t right.

I still had six months left, but I began negotiating my exit. I suspected it wouldn’t be easy. Peter Cohen hadn’t been transparent with the board about how he had gotten me to stay. I needed a lawyer in my corner, but given the size of Shearson American Express, it was hard to find anyone who would take me as a client. Finally, I found one brave attorney, Steve Volk, the lead M&A attorney at Shearman and Sterling. He would go on to be vice chairman of Citibank. His associate was Philippe Dauman, who later in life would go on to be CEO and chairman of Viacom. They listened to my story and promised to fight for me.

My hunch about Cohen turned out to be right. Despite all his promises, he had no intention of allowing me to leave. He worried I would take clients with me and that if word got out to the other partners that I had gotten a special deal, all of them might demand the same. Shearson insisted I not compete for one group of clients and give them a percentage of my fees if I did business with another. Our negotiations were long and angry, but I wanted to get out and get on with my life. Pete intervened to help us get to a final agreement. Cohen and his team failed to show up to sign the agreement not just once but twice, leaving me sitting in an empty conference room with all the closing documents on the table. When at last we did exchange signatures, the anger and resentment were palpable. It was a terrible ending to a great run, but it was also the chance for a new start.

I had learned so much about myself by then. From high school, through Yale, HBS, and time and again at Lehman, I had proved to myself that I could survive almost any situation. I could create worthy fantasies and make them real. Coach Armstrong had taught me the value of persistence, of running those extra miles and making those deposits of hard work, so they were there when I needed a withdrawal. And I had figured how to invest them to advance my career.

My early mistakes on Wall Street, the typos and calculation errors, and the embarrassment that followed, had taught me the importance of rigor, eliminating risk, and asking for help. Today on Wall Street, you can do many of the calculations with a keystroke that we used to have to do by hand. But learning the way I did, I saw the intricate ways in which deals can be structured, the subtleties that must be negotiated. Mastery like that takes experience, endurance, and tolerance for pain. And it yields the greatest rewards.

The Tropicana deal had shown me that under pressure, I was capable of far more than I ever thought. Pete Peterson had shown me the value of a great mentor and partner. I had forged some treasured relationships with wonderful people—colleagues at the firm and executives like Jack Welch who would keep popping up throughout my career. I had experienced Wall Street at its best, the highs of executing complex deals, that sense of being at the center of the universe, exchanging information with some of the most interesting people in the world.

And my exit from Lehman had shown me Wall Street at its worst, everyone for themselves. Watching the Lehman partners fail to take on Lew Glucksman had shown me how morality and ethics can buckle under fear and greed. I had seen that some people are vindictive and jealous. My experience selling Lehman and being forced to stay against my will not only taught me the worth of a good lawyer but also that money is a poor cure for a bad situation.

PURSUE WORTHY FANTASIES

THE HARDER THE PROBLEM, THE MORE LIMITED THE COMPETITION

Now that we were free of Lehman and could work together again, Pete and I began talking in earnest about starting something of our own. We had our first conversation at Pete's house in East Hampton with our wives.

"I want to work with large companies again," said Pete. Since leaving Lehman, he had started a small firm that did small deals.

"I just want to work with Pete again," I said. I was thirty-eight, and the money I had made at Lehman had provided for my young family. By now, we had two children, Zibby and Teddy, both healthy and going to great schools. We had an apartment in the city and a house near the beach. Professionally, I had reached a point where I wanted to start my own business. I felt I had learned enough and acquired enough personal and professional resources to make a success of it. Ellen, who had seen how miserable I had been during that last year at Lehman, said, "I want Steve to be happy."

Joan, Pete's wife, was the creator of *Sesame Street*, the children's television show. She had an objective even Big Bird could understand: "I want a helicopter."

"Okay," I said. "We know what everybody wants. Now, let's go."

Many great businesses in Silicon Valley, from Hewlett Packard to Apple, have been founded in garages. In New York, we have breakfast. In April 1985, Pete and I began meeting every day in the courtyard restaurant at the Mayfair Hotel on East Sixty-Fifth Street and Park Avenue. We were the first to arrive and the last to leave, talking for hours, reflecting on our careers and thinking of what we could do together.

Our main assets were our skill sets, our experience, and our reputations. Pete was a summa cum laude, Phi Beta Kappa, process-oriented, analytic person. There was nothing he couldn't figure out through method and logic. He knew everyone in New York, Washington, and corporate America and had an easy, casual way with all of them. I considered myself more instinctive, quick to read and figure people out. I could make decisions and execute fast and was now well known as an M&A specialist. Our skills and personalities were different but complementary. We were confident that we would be good partners and people would want our services. Even if most start-ups failed, we were sure ours wouldn't.

Observing my father at Schwarzman's and all the businesses and entrepreneurs I had advised subsequently, I had reached an important conclusion about starting any business: it's as hard to start and run a small business as it is to start a big one. You will suffer the same toll financially and psychologically as you bludgeon it into existence. It's hard to raise the money and to find the right people. So if you're going to dedicate your life to a business, which is the only way it will ever work, you should choose one with the potential to be huge.

Early in my career at Lehman, I asked an older banker why it was that banks had to pay more to borrow money than similar-sized industrial companies did. "Financial institutions go broke in a day," he told me. "It can take years for an industrial company to lose its market position and go bankrupt." I had now seen that happen up close at Lehman—that sudden reversal of fortune, a bad trade, a bad investment that can destroy you in finance. We weren't going to start this journey in a tiny rowboat. We wanted to build a reputation for excellence, not bravery.

From the outset, we strived to build a financial institution strong enough to survive multiple generations of owners and leadership. We did not want to be just another of those groups on Wall Street who set up a firm, make some money, fall out, and move on. We wanted to be spoken of in the same breath as the greatest names in our industry.

What we knew best was M&A work. At the time, M&A was still the purview of the big investment banks. But we believed there would be an appetite for the services of a new kind of boutique advisory firm. We had the reputation and the track record. M&A took sweat equity but didn't require capital, and it would provide income while we figured out what else we might offer. I worried about the cyclicality of M&A and that alone it wouldn't be enough to sustain us. If the economy sputtered, so would our business. Eventually we would want steadier sources of income. But it was a good place to start. To get big, though, and build a stable, lasting institution, we would have to do much more than that.

As we sat in the Mayfair evaluating ideas, one potential line of business kept resurfacing: leveraged buyouts, or LBOs. At Lehman, I had advised Kohlberg Kravis Roberts (KKR) and Forstmann Little, the two largest LBO firms in the world. I knew Henry Kravis and played tennis with Brian Little. Three things had struck me about their business. First, you could gather assets and earn income from recurring fees and investment profits whatever the economic climate. Second, you could really improve the companies you bought. Third, you could make a fortune.

A classic LBO works this way: An investor decides to buy a company by putting up equity, similar to the down payment on a house, and borrowing the rest, the leverage. Once acquired, the company, if public, is delisted, and its shares are taken private, the "private" in the term "private equity." The company pays the interest on its debt from its own cash flow while the investor improves various areas of a business's operations in an attempt to grow the company. The investor collects a management fee and eventually a share of the profits earned whenever the investment in monetized. The operational improvements that are implemented can range from greater efficiencies in manufacturing, energy utilization, and procurement; to new product lines and expansion into new markets; to upgraded technology; and even leadership development of the company's management team. After several years, if these efforts have proved successful and the company has grown considerably, the investor can sell it for a higher price than he or she bought it, or perhaps take the company public again, earning a profit on the original equity investment. There are a lot of variations on this basic theme.

The key to all investing is using every tool at your disposal. I liked the idea of leveraged buyouts because they seemed to offer more tools than any other form of investment. First, you looked for the right asset to buy. You did your diligence by signing nondisclosure agreements with the owners and getting access to more detailed information about what you were buying. You worked with investment bankers to create a capital structure that gave you the financial flexibility to invest and survive if economic circumstances turned against you. You put in experienced operators you trusted to improve whatever you bought. And if all went well, the debt you put in place enhanced the rate of return on the value of your equity when the time came to sell.

This type of investing would be much harder than buying stocks. It would take years of effort, excellent management, hard work, and patience and require teams of skilled experts. However, if you did this successfully over and over, you could generate significant returns and develop a record the way Coach Armstrong did at Abington High School, 186–4, and also earn the trust of your investors. The returns these investments earned for investors—pension funds, academic and charitable institutions, governments and other institutions, as well as retail investors—would also have the benefit of helping to secure and grow the retirement funds of millions of teachers, firefighters, and corporate employees, among others.

Unlike M&A, LBOs didn't require a constant stream of new clients. If we could persuade investors to put money into a fund, locked up for ten years, we then had ten years to earn management fees, improve what we bought, and turn a big profit for our investors and ourselves. If a recession hit, we could survive it and, with luck, find even more opportunities as panicked people sold good assets at low prices.

Back in 1979, I had studied the prospectus for KKR's eye-popping buyout of Houdaille Industries, one of the first big LBOs. This deal was the Rosetta Stone of buyouts. KKR had put in just 5 percent of the cash to buy Houdaille, an industrial manufacturing conglomerate, and borrowed the rest. Leverage on that scale meant the company could grow at 5 percent, but the equity would grow at 20 to 30 percent. I had been keen to do a similar deal using Lehman's resources, but I couldn't muster the internal support.

Two years later, I was the banker for the legendary media and electronics company RCA when it decided it wanted to sell Gibson Greetings, then America's third biggest greeting cards company, an asset that didn't fit with RCA's other businesses. We contacted seventy potential buyers. Only two were interested. One was Saxon Paper, which turned out to be a fraud. The other was Wesray, a small investment fund co-founded by William Simon, a former treasury secretary. Wesray offered $55 million for Gibson, and we set a date to close the deal. Wesray's investors were putting in just $1 million of their own capital but assured us they would have the rest of the money by the closing date. When they didn't, we gave them a one-month extension. Still, no money. There were no other suitors. They pleaded for one more shot. I found out later that they were trying to finance the deal by arranging to sell and then lease back Gibson's manufacturing and warehouse buildings. That would have given them the cash they needed, but they couldn't get it done. That, I thought, was that.

In the meantime, Gibson's earnings started going up. Although we hadn't yet found a qualified buyer, I recommended to Julius Koppelman, the RCA executive handling the sale, that they increase the price they were asking for Gibson. He proposed an additional $5 million. I told them that wasn't close to reflecting Gibson's value given its rising profits, but they wouldn't budge: RCA was desperate to sell and wanted the deal done. They weren't interested in getting the highest price. When RCA asked me for a fairness opinion on a $60 million sale, I refused to give one, a controversial and highly atypical stance at the time. When the deal closed six months later, Koppelman left RCA to become a consultant for Wesray. After Wesray bought Gibson, I made sure to go to Pete and Lew Glucksman to tell them what I thought of it. Wesray would make a lot of money one day, I said, and we'd be accused of incompetence. When you disagree, it's important to get your opinions on record so you aren't blamed later when things go wrong. Sixteen months later, Gibson went public, valued at $290 million, and Lehman was highly criticized by RCA's investors and the press for selling it too cheaply. Wesray had made more money on a single deal than Lehman made in a year.

Gibson was widely publicized for being one of the first successful, highly profitable leveraged buyouts. It was also the perfect case study of the type of deal Pete and I hoped to do at our new firm.

The good news was that after the Gibson IPO, LBOs had Lehman's attention. Pete, then CEO, was all in. Before his next trip to Chicago, he asked me to come up with a list of possible acquisitions. I settled on Stewart-Warner, a maker of dashboard instrument panels and the scoreboards at sports stadiums. Pete, of course, happened to know the chairman, Bennett Archambault. We met him at his men's club, an old-school place with wood paneling and moose heads all over the walls. Pete suggested he take his company private. I walked Archambault through the process: how we could raise money to buy the stock, how we could pay the interest, enhance the value, make the company work better, what it would mean over time.

"I think you can make a lot of money personally," Pete said to him. "And your shareholders can do well. Everyone can profit." Archambault got it. The existing shareholders would be paid a premium for their stake. As the head of a private company, he could improve it over the long term instead of worrying about quarterly earnings to placate the stock market. And he would end up owning a lot more of the company. "There don't seem a lot of reasons not to do it," he said.

Back at Lehman, I rushed into action. I staffed the deal and asked Dick Beattie at the Simpson Thacher law firm to start designing a fund for Lehman to do LBOs. Dick had been counsel in the Carter administration and had since become an expert on the legal intricacies of LBOs. We were confident we could raise the $175 million to take Stewart-Warner private. Pete and I moved the deal through the Lehman vetting process and brought it to the executive committee. The executive committee turned us down.

They saw an inherent conflict. They didn't feel we could give M&A advice to our clients while at the same time trying to buy companies our clients might be interested in. I understood the basics of their position. But I was sure that there must be a compromise that could properly address the potential conflicts. Fine, we couldn't buy every company we wanted. But there must be a way to buy some of them. The opportunity in this business was too big to ignore.

In the years after the executive committee rejected our idea, a wave of LBO money transformed the way America bought and sold companies. More buyers had emerged, eager to buy assets they could never afford previously. Banks were developing new kinds of debt, with higher yields or novel repayment terms, to fund their acquisitions. Corporations saw the opportunity to sell businesses they no longer wanted to buyers who could do more with them. To be taken seriously as M&A specialists, we had to master this dynamic new area of finance. But the even bigger opportunity, Pete and I thought, would be to become investors ourselves.

As M&A bankers, we would be running only a service business dependent on fees. As investors, we would have a much greater share in the financial upside of our work. In private equity firms, general partners identify, execute, and manage any investments on behalf of limited partners (LPs), the investors who entrust them with their money. The general partners put their own capital up alongside the LPs, run the investment business, and tend to be rewarded in two ways. They receive a management fee, a percentage of the capital committed by investors and subsequently put to work, and a share of the profits earned from any successful investments, the "carried interest."

The appeal of the private equity business model to a couple of entrepreneurs was that you could get to significant scale with far fewer people than you would need if you were running a purely service business. In service businesses, you need to keep adding people to grow, to take the calls and do the work. In the private equity business, the same small group of people could raise larger funds and manage ever bigger investments. You did not need hundreds of extra people to do it. Compared to most other businesses on Wall Street, private equity firms were simpler in structure, and the financial rewards were concentrated in fewer hands. But you needed skill and information to make this model work. I believed we had both and could acquire more.

The third and final way we thought about building our business was to keep challenging ourselves with an open-ended question: Why not? If we came across the right person to scale a business in a great investment class, why not? If we could apply our strengths, our network, and our resources to make that business a success, why not? Other firms, we felt, defined themselves too narrowly, limiting their ability to innovate. They were advisory firms, or investment firms, or credit firms, or real estate firms. Yet they were all pursuing financial opportunity.

Pete and I thought of the people we wanted to run these new business areas as "10 out of 10s." We had both been judging talent long enough to know a 10 when we saw one. Eights just do the stuff you tell them. Nines are great at executing and developing good strategies. You can build a winning firm with 9s. But people who are 10s sense problems, design solutions, and take the business in new directions without being told to do so. Tens always make it rain.

We imagined that once we were in business, the 10s would come to us with ideas and ask for investment and institutional support. We'd set them up in fifty-fifty partnerships and give them the opportunity to do what they did best. We'd nurture them and learn from them in the process. Having these smart, capable 10s around would inform and improve everything we did and help us pursue opportunities we couldn't even imagine yet. They would help feed and enrich the firm's knowledge base, though we still had to be smart enough to process all this data and turn it into great decisions.

The culture we would need in order to attract these 10s would by necessity contain certain contradictions. We would have to have all the advantages of scale, but also the soul of a small firm where people felt free to speak their mind. We wanted to be highly disciplined advisers and investors, but not bureaucratic or so closed to new ideas that we forgot to ask, "Why not?" Above all, we wanted to retain our capacity to innovate, even as we fought the daily battles of building our new firm. If we could attract the right people and build the right culture at this three-legged business, offering M&A, LBO investments, and new business lines, all feeding us information, we could create real value for our clients, our partners, our lenders, and ourselves.

Businesses often succeed and fail based on timing. Get there too early, and customers aren't ready. Arrive too late, and you'll be stuck behind a long line of competitors. The moment we started Blackstone in fall 1985, we had two major tailwinds. The first was the US economy. It was in the third year of a recovery under President Reagan. Interest rates were low, and borrowing was easy. There was plenty of capital looking for investment opportunities, and the financial industry was meeting this demand with a supply of new structures and new kinds of businesses. LBOs and high-yield bonds were part of rapid changes in the credit markets. We were also seeing the emergence of hedge funds—investment vehicles with highly technical approaches to managing risk and reward in every class of assets, from currencies to stocks. The potential of all these forms of investment was just emerging and the competition was not yet fierce. It was a good time to be trying something new.

The second major tailwind was the unraveling of Wall Street. Since its founding in the late eighteenth century, the New York Stock Exchange had operated with a fixed-price commission schedule, granting a set percentage of every trade to the broker. That system ended on May 1, 1975, on the orders of the Securities and Exchange Commission (SEC), which determined it to be a form of price fixing. Under the old system, Wall Street's brokerage firms barely had to compete and certainly hadn't had to innovate. Now that commissions had to be negotiated, price and service mattered. Technology accelerated the process, punishing the small, high-cost brokers and rewarding those who could offer better services and lower prices at scale. In the ten years since the SEC's rule change, the firms that succeeded grew larger and larger, while those that stood still eventually died.

This change transformed Wall Street's culture. When I joined Lehman in 1972, it employed 550 people. When I left, Shearson-Lehman had 20,000 (when Lehman collapsed in 2008, it had 30,000). Not everyone liked being part of these giants. You lost the intimacy of knowing everyone by sight, that sense of working for a single, coherent entity. You went from being part of a nimble team to sitting inside a huge bureaucracy. As a new associate at Lehman, I had caught the eye of Lew Glucksman, who yelled at me for not sitting up straight. But that led to someone telling him I had potential and him giving me work. That can happen in a firm of 550. With 20,000 people, it's much harder to find the good, young talent. At Lehman in the early 1970s, we had people from the CIA and the military, all kinds of different fields, who learned finance on the job. They brought a wide range of skills, perspectives, and contacts to our work. But by the mid-1980s, banks were hiring armies of MBAs who could plug in and do the work immediately.

Pete and I believed that these changes to the culture at the big firms would lead to a shake-out of great people and great ideas. If they were anything like us, they would be searching for ways out. We wanted to be ready for them.

For months, we agonized over what to call ourselves. I liked "Peterson and Schwarzman," but Pete had already set up a couple of businesses that included his name and didn't want to use it again. He preferred something neutral so that if we added new partners, we wouldn't have to argue about adding their names. We didn't want to become one of those ungainly law firms with five names on the letterhead. I asked everyone I knew for suggestions. Pete's wife, Joan, talked sense into us: "When I started my business I couldn't think of a name. In the end, we just invented one: 'Sesame Street.' What a stupid name that is. Now it's in 180 countries all over the world. If your business fails, nobody will remember your name. If your business succeeds, everyone will know it. So just pick something, get on with it, and hope you succeed enough to be known."

Ellen's stepfather came up with the answer. He was the chief rabbi for the Air Force and a Talmudic scholar. He proposed we draw on the English translations of our two names. The German *schwarz* means black. Pete's father's original Greek name was "Petropoulos." *Petros* means stone or rock. We could be Blackstone or Blackrock. I preferred Blackstone. Pete was happy to go along.

After months of talking, we had a name and a plan to be a distinctive firm composed of three businesses: M&A, buyouts, and new business lines. Our culture would attract the best people and provide extraordinary value for our clients. We were hitting the market at the right time and had the potential to be huge.

We each put up $200,000 in capital—enough to get started, but not so much that we could be spendthrift. We took three thousand square feet at 375 Park Avenue, the Seagram building just north of Grand Central Station. The building was open, modern, and architecturally significant, designed by Ludwig Mies van der Rohe, the pioneering modernist architect. It was in midtown, far from Wall Street, but near many corporate offices. It was also in the same building as the Four Seasons restaurant, a famous networking location. In 1979, *Esquire* magazine had described it as the birthplace of the "power lunch." It would be easy for Pete to work his many corporate contacts. Had I used us as an exhibit in my business school thesis on the architecture of financial firms, I would have noted that we were straining for prestige.

We bought some furniture, hired a secretary, and divided up our roles. Pete had been a CEO twice before and told me that he didn't want the hassle of running a business again. He asked me to take the CEO role but with the title of president. One of my first acts was to design our logo and our business cards. I hired a design firm, had them come up with alternatives, and spent an enormous amount of time going over them. The design we chose is the one we still have: simple, black and white, clean, and respectable. I thought the time and money we spent when both were scarce were essential to getting this right. When you're presenting yourself, the whole picture has to make sense, the entire, integrated approach that gives other people cues and clues as to who you are. The wrong aesthetics can set everything off kilter. Our business cards were an early step in establishing who we wanted to be.

On October 29, 1985, six months after we had started having our breakfasts at the Mayfair, we took out a full-page ad in the *New York Times* and announced ourselves to the world:


WE ARE PLEASED TO ANNOUNCE

THE FORMATION OF

THE BLACKSTONE GROUP

A PRIVATE INVESTMENT BANKING FIRM

PETER G. PETERSON, CHAIRMAN
STEPHEN A. SCHWARZMAN, PRESIDENT

375 PARK AVENUE, NEW YORK, NY 10152
(212) 486-8500

CALL, THEN KEEP CALLING

To get business rolling, we wrote to everyone we knew—more than four hundred cheerful letters introducing our new firm. We wrote about our track records and reminisced about the business we had done together. We laid out our plans and asked for work. Then we sat back and waited. I was expecting the phone to ring nonstop. But on the few occasions it did ring, it was only to congratulate us and wish us luck.

"How about some business?" I would ask.

"Not right now. But we'll think about you in the future."

The day after our advertisement appeared in the *New York Times*, I heard a knock at the door. I opened it to find a guy in leather pants, a black motorcycle jacket, and a little peaked leather motorcycle hat. We were waiting to hear from our familiar M&A clients, but we got the gang leader from *The Wild Ones*.

"Is there a Steve Schwarzman here?" he said.

"What are you delivering?"

"I'm not delivering anything. My name is Sam Zell. Leah told me I should meet you." In 1979, we had hired Leah Zell at Lehman. She had been an English major at Harvard and had just gotten a PhD. After talking with her for a few minutes, it was obvious she had an exceptional mind. Though she knew nothing about finance, I had decided to give her a chance. She had proved to be a terrific analyst. This biker was her brother.

"What's with the outfit?" I said.

"I left my motorcycle downstairs."

"Where downstairs?"

"I chained it up on Park Avenue," he said. "To a hydrant."

Our first day. *This is some future*, I thought.

He must have thought the same thing looking at me sitting there in my suit in our bare office, the phones silent.

"Look, I'm sorry. We just moved in today. We've hardly got any furniture yet."

"That's okay," said Sam. He sat on the floor, leaned against the wall, against our rolled-up rug, and began to talk. He owned some real estate and wanted to buy some companies, but he didn't know much about finance. "Why don't you teach me?" he said.

I later found out that I shouldn't have been misled by the outfit. Sam's version of "owning some real estate" meant he was building one of the largest portfolios of real estate in the country. All he told me that day was he bought bankrupt properties and wanted to build an empire. We spent two and a half hours sitting on the floor talking. In the years to come, we would do a lot of business together. This one unexpected visitor turned out to be worth more to Blackstone than all the clients we expected in those early days who never came.

To coincide with our launch, the *Wall Street Journal* had planned to run a major front-page article about our new firm—publicity that would have been a huge boost for our new business. The day before it was supposed to run, the reporter called to tell me his editors were yanking it. He apologized. "The Shearson people heard we were doing it," he said. "They called us up and said you were fired for a variety of bad reasons. We didn't feel we could run the piece if Shearson told us on background that you're a bad guy."

I should have known our launch would rile Shearson. I had wanted out of Lehman because the ethics there had become so awful—the greed, the fear, the gutlessness, the hunger for power, the dishonesty. But this counterattack was a new low. I sat there in our bare office with boxes of office equipment scattered around. How could people be so vindictive?

Despite these setbacks, we were still confident enough to think that our reputations, our experience, and those hundreds of letters would bring in a flood of business. Weeks passed. Nothing. Pete had a secretary who was drawing a salary. I was making my own calls and taking deliveries at the front door. Every day I would look around the space we had rented. It felt like watching an hourglass, the money just draining out as the business never came. Not so long ago, people fought to have us work for them. Pete and I hadn't changed, but now that we were out on our own, no one cared about us. As the days ticked by, I worried we would be just another failed start-up.

Finally, Squibb Beech-Nut, a pharma company we had worked with at Lehman, hired us for an advisory job for $50,000. In my previous life, that would have been less than the legal fees on a single deal. It was now a lifeline. Then another small job came in, from Armco, a medium-sized steel company in the Midwest and a client at Lehman. We were covering our rent and other basic costs, but we were still on the edge. By then it was the early summer 1986, and we had been in business for nine months. Pete was away, my family was at the beach, and I was alone in Manhattan working on these two insignificant pieces of business.

One sweltering evening, I went for dinner alone to a Japanese restaurant on the second floor of a building on Lexington Avenue in the thirties. As I was sitting there, I began to feel dizzy, as if my whole body wanted to collapse. I felt I was failing on every count. I was overwhelmed by self-pity. Wall Street loves nothing more than watching other people fail. To see Pete and me, who had been so powerful at Lehman, so sure of our success, take a beating would have given many people pleasure. I couldn't let it happen. I could not fail. I had to find a way.

Here, I realized, was a great truth. For all that we had accomplished, we were a start-up. There would be no easy jobs. What I didn't know was that all the grunt work, the hours I had spent in my career building my own financial models with a pencil and slide rule, learning the craft of finance from my colleagues, was about to prove invaluable.

Shortly after my lonely Japanese dinner, Hays Watkins, the chief executive of CSX, a large railroad company, called us. In 1978, I had overseen the sale of a newspaper company that CSX owned. The standard sale would have involved an English auction—the kind you see in auction houses where the bidders raise their hands, increasing their offers incrementally, until the second highest bidder drops out. All you have to do to win is bid a dollar more than the next bidder. The problem with these auctions is that you never know what the winner might have been willing to pay. Someone might buy a

Van Gogh painting for $50 million, but perhaps if there had been another bidder, the buyer could have been pushed up to $75 million.

For CSX's newspapers, I had staged a two-round sealed-bid auction. In each round, the bidders submitted their bids in a sealed envelope, not knowing what others were offering. The first round weeded out the low bids, the people just fishing. The serious buyers then got to review the target company's financials and visit with management. After that they submitted another sealed bid. The magic of this kind of auction is that if the buyers are desperate to acquire the asset, they won't just try to offer a dollar more than the second-highest bidder. They will offer the highest price they can afford to ensure they win. This style of auction was little known in the M&A world when I began doing it, but it has since become standard practice. Watkins said he remembered me as an innovator and problem solver.

"We have a project," Watkins said. "We're just starting on it. We thought maybe you could work on it." Maybe we could work on it? We were sitting around worrying about going broke. But I knew that he wouldn't have come to us if the situation were simple. There were lots of advisers who could help. Watkins had a difficult problem, and he wanted an inventive solution. As an investment banker and later as an investor, I found that the harder the problem, the more limited the competition. If something's easy, there will always be plenty of people willing to help solve it. But find a real mess, and there is no one around. If you can clean it up, you will find yourself in rare company. People with tough problems will seek you out and pay you handsomely to solve them. You will earn a reputation for doing what others cannot. For a pair of entrepreneurs trying to break through, solving hard problems was going to be the best way of proving ourselves.

CSX wanted to expand into ocean shipping and had made a friendly and generous offer to buy Sea-Land Corporation, a container company. The management of Sea-Land was keen to accept it, but they were being held up by Harold Simmons, a crusty Texan investor. Simmons had no interest in owning Sea-Land. But he had been buying stock in anticipation of an outside acquisition, intending to hold up any sale until he got the price he wanted. He wanted to be overpaid to go away. The finance industry calls this practice "greenmail."

CSX's initial offer was a reasonable $655 million. At Lehman, I'd have had a whole team to support me on a deal this size. Now I had to handle this work alone. Simmons owned 39 percent of the stock in Sea-Land. We couldn't force him to sell, but at the price CSX was offering, Simmons would have made a handsome profit. Still, he was in a strong position to hold out for more. I spoke to him on the phone, explaining how much he stood to make based on the current offer. I can still hear his Texan accent: "Mr. Schwarzman, Ah've told you many times already, Ah am *not* selling my shares. Ah am *not!*" I tried everything to persuade him, until I decided to fly down to see him with our attorney.

Simmons was thin, lanky, with a pock-marked face. He was in his mid-fifties but looked much older. His office gave no hint of his considerable wealth. It was in a cheap building outside Houston, the interior walls covered with peeling wood veneer.

"We'd really like to buy this business, and you're sort of getting in the way," I said. "We'd like you to move aside. We'd like to buy your stock. As you know, we're offering a premium."

"Ah know what you want," he said. "Ah've told you, mah stock is not for sale."

"I thought you were going to say that," I said. "So I've prepared a special arrangement I'm making available for stockholders who don't want to participate in our tender offer." He was the only one. "If you don't want the cash, I'm going to substitute a private issue, PIK [payment in kind, i.e., not cash] preferred stock with no maturity date."

What this proposal meant was that he could either take the cash, or we were going to turn his asset into a serious liability. If he wanted to take CSX hostage, I was going to do the same to him by using the tender offer to force a merger and freeze him out. His preferred stock wouldn't be listed on any exchange, so he wouldn't be able to sell it easily. It would also be junior to corporate debt in the capital structure, so if anything went wrong, he wouldn't get paid until after the creditors. And with no maturity date, he would never even have a chance to redeem his stock because it would never come due. He would just be stuck holding stock that generated ever-increasing tax bills for the indefinite future. The proposition was detestable and highly unusual.

Simmons looked at me, then looked at his lawyer. “They can do this?” Simmons asked.

“Mmmh hmm,” the lawyer said bobbing his head up and down. “They can do it.”

Simmons turned to me. “Get the hell out of my conference room!” My attorney and I walked out, got into the car, and drove back to the airport. From the pay phone in the lounge, I called my secretary. Simmons had just called to tell me he’d be selling his stock.

If the job had been easy, we would never have gotten it. It required creativity and psychological insight to identify Simmons’s weakness and nerve to confront him with our solution to CSX’s problem. This assignment was a breakthrough for us. It was the first major fee we received for our advisory business, and it made Blackstone’s name as an M&A shop.

After we wrapped it up, Hays told me he was bringing in Salomon Brothers for a fairness opinion on the price they had paid. I had written dozens of fairness opinions at Lehman since my first assignment for Herman Kahn. I told Hays he didn’t need Salomon. We could do it for him. I knew Sea-Land and CSX, having just done the deal. Hays agreed. I even waived the fee. Blackstone became the first major boutique advisory firm to write a fairness opinion.

In fall 1986, as we neared our first anniversary, we decided it was time to set about raising our first buyout fund. We would need to convince investors we could take their money; buy, fix, and sell businesses; and return their money to them with a substantial profit after several years. It was step two of our business plan: going from providing advice and transaction services to the more complex but (we hoped) more durable and profitable business of investing. Neither Pete nor I had ever run such a fund, let alone raised money for one. Though we tended to agree on everything, we disagreed on how much we ought to pursue.

I thought we should raise a billion dollars for our first fund, which would make it by far the biggest first-time fund ever launched. Pete thought I was dreaming.

“We’ve never done a single private equity deal,” he said. “And neither of us has ever raised *any* investment money for ourselves.”

“So what?” I said. “I know the guys who do this stuff. I represented them at Lehman. I’ve been in the room.” If they could do it, I assured Pete, we could.

“It doesn’t trouble you that we haven’t done a deal yet?”

“No, it doesn’t.”

“It does me,” said Pete. “I think we should start with a $50 million fund, learn what we’re doing, and then do something bigger.”

I told Pete I disagreed for two reasons. First, when investors put money in a fund, they want to know that theirs isn’t the only money. So if you’re raising a $50 million fund, chances are you’ll have to raise it in increments of $5 to $10 million. And if you’re going to all the bother of raising $5 to $10 million, you may as well save yourself some legwork and ask for $50 to $100 million. Second, investors would expect us to build a diversified portfolio. With only $50 million in hand, we’d have to do a series of tiny deals to get there. Since our expertise was in working with big corporations, tiny deals made no sense.

Pete was still apprehensive. “Why would somebody give us money when we’ve never done anything?” he asked.

“Because it’s us. And because it’s a moment.”

When I began my career, I was like most other ambitious young people: I believed success was achieved in a straight line. As a baby boomer, I had grown up seeing only growth and opportunity. Success seemed a given. But working through the economic ups and downs of the 1970s and early 1980s, I had come to understand that success is about taking advantage of those rare moments of opportunity that you can’t predict but come to you provided you’re alert and open to major changes.

Demand for LBO deals was rising among investors, but the supply was limited and the people who could execute them even more so. It was the perfect scenario for a pair of entrepreneurs with our particular skills. Years earlier at Lehman, we couldn’t get the bank’s executive committee interested in LBOs. We were ahead of their conventional thinking. Now, if we waited any longer, we risked being too late. Others would attract the eager money looking for ways into buyout deals.

“I’m convinced that now is the right moment for us to raise a fund and that moment may never reappear for us,” I told Pete. “We’ve got to hit it.”

As a salesman, I’d learned you can’t just pitch once and be done. Just because you believe in something doesn’t guarantee anyone else will. You’ve got to sell your vision over and over again. Most people don’t like change, and you have to overwhelm them with your argument, and some charm. If you believe in what you’re selling and they say no, you have to presume that they don’t fully understand, so you give them another opportunity. After many discussions, Pete, in his own way, gave in.

“If you feel that strongly, I’ll sign on for it.”

GO WHERE OTHERS AREN'T

We honed our proposal into an offering memorandum—the legal document that explains the terms, risks, and objectives of an investment—and sent it to nearly five hundred potential investors: pension funds, insurance companies, endowments, banks, other financial institutions, and some wealthy families. We made calls and wrote follow-up letters. Once again, our telephones went quiet. We made the mistake of trying out our half-formed pitch on our best prospects, the people we knew best. Rather than being forgiving, they found it all too easy to turn us down. We received just two invitations to meet. Met Life committed \$50 million and New York Life \$25 million, but only if their investments did not exceed 10 percent and 5 percent of the fund, respectively. Until we raised at least \$500 million, their commitments were worthless.

Pete suggested we wait a couple of weeks before making more follow-up calls and refine our approach. This time, I deferred to his counsel. Second time around, we had a better feel for our pitch and arranged meetings with eighteen potential investors.

The Equitable Insurance Company brought us in for two meetings, ten days apart. When we were called back, we hoped it was just a question of signing them up. At the second meeting, the person we had seen just ten days earlier didn't even recognize us. "Blackstone?" he said. He couldn't remember anything about us. It wasn't even a scheduling error. Pete and I left not just deflated but confused. Were we so irrelevant that people couldn't even remember who we were?

Delta Airlines's investment fund agreed to meet us if we came to their office in Atlanta. The night before our 9:00 a.m. appointment, Pete had attended dinner at the White House. I met him at Atlanta's Hartsfield-Jackson airport and we took a cab to our meeting. Pete always had a giant briefcase with him and now also carried a tuxedo bag. When we got out of the taxi, we were still several hundred yards from the Delta building, which was set back from the road. It was hot and humid. I helped Pete lug his bags. By the time we arrived, we were both sweating through our shirts.

A secretary took us down to the second-level basement, not up to the executive floors. The cinderblock walls were painted a bilious green. Pete and I were sticky and disheveled but did our best to straighten up. Inside the small conference room, we were offered coffee. Pete said no; hot coffee on a hot day didn't sound great. *We're in the South*, I thought. *We should be gracious*. So I said yes. Our host went over to a card table with a hot plate and a metal coffee carafe and poured me out a brown cup with a white plastic insert. "That'll be twenty-five cents for the coffee kitty." I dug into my pocket for a quarter.

We were trying to get $10 million from these people. They had read the material and invited us down. We were offering the kind of fund they usually invested in. We went through our presentation with all of our usual enthusiasm, emphasizing our expertise, our contacts, and the opportunities we saw in the markets. When we finished, I asked the executive who had poured me the coffee, "Do you find this of interest?"

"Oh, yes. Quite interesting, but Delta doesn't invest in first-time funds."

"You knew we're a first-time fund. Why did you ask us all the way to Atlanta?"

"Because you're both famous people in finance and we wanted to meet you."

When we left, it was steamier than when we arrived. We dragged our bags back toward the road. Halfway there, Pete looked at me and said, "If you ever do that to me again, I'm going to kill you."

The rejections were horrible and humbling. The setbacks seemed endless. We met people who lied to us or never showed up for appointments even after we had traveled across the country. People we knew well in positions of authority rejected us. Pete and I talked throughout these struggles. He was not someone who failed. He hated failure. But at the same time, he was sixty years old. He was at a different place than I was, with a different mentality. If I had the drive, he had the patience and equanimity. He picked me up and kept me going. He assured me that when you believe in what you're doing, overwhelmed or not, you have to keep moving forward, even when the quest feels hopeless. Which it did.

Pete was from an immigrant family. His parents had come to the United States from Greece and opened a restaurant in Kearney, Nebraska, where Pete worked as a boy. He went to college and graduate school and made his way in business thanks to his intelligence and personal skills. He understood the journey I was on, the need I had to make this work. It had been his journey too. We were just on different schedules.

"This is a high hill," he would tell me before a meeting. "This is really pushing it." But then he'd suck it up, and we'd go off to meet the next investor, where we'd get shot down again.

Six months after we started and had met almost every prospect who would see us, we hadn't raised a dollar since our original pledges from New York Life and Met Life. We were nearing the end of our list of eighteen when we reached Prudential. Prudential was the number one financier of leveraged buyouts, the gold standard. We didn't know anyone there well, so we had saved their meeting to be one of our last. By then we would have our pitch perfected. Garnett Keith, Prudential's vice chairman and chief investment officer, invited us for lunch in Newark, New Jersey.

As I began talking, Garnett took his first bite of a tuna sandwich on white bread, cut diagonally. As I spoke, he would bite off some more, chew, swallow, and not say a word. His jaw would move, his Adam's apple roll up and down. By the time he was three-quarters of the way through his sandwich, I had said all I had to say. Garnett put down the last quarter of his sandwich, stopped chewing, and spoke: "You know, that's interesting. Put me down for 100."

It was so sudden, so casual. There was nothing legal I wouldn't have done for that $100 million. If Prudential thought it was a good idea to invest with us, others would follow. I wanted to reach over and snatch away the last quarter of that sandwich to make sure Garnett didn't choke on it.

We were on our way.

After Prudential's commitment, Pete went to Japan as a speaker at the Shimoda Conference, a gathering of Japan's corporate establishment. He suggested mixing in some fundraising. In 1987, Japanese industrial companies were buying large numbers of American assets. Japan's brokerage firms, we figured, would follow, seeking opportunities in the US capital markets.

There were four large Japanese brokerages: Nomura, Nikko, Daiwa, and Yamaichi. We didn't have contacts at any of them and needed representation. I went to Bruce Wasserstein and Joe Perella, two of the top investment bankers at First Boston. They had excellent relations in Japan. Joe had been a friend since we were in the same class at Harvard Business School. Bruce and I had encountered each other regularly in deals, and we played tennis on weekends in the Hamptons. They set us up with one of their bankers who knew the Japanese market.

But when I laid out my plans to him, he told me there was no point approaching the brokerages because they never invested in our kind of fund. I asked him to try. He refused. Only when I threatened to fire him did he arrange a meeting with Nomura and Nikko Securities, a firm that was opening an office in New York. At Nikko, the Japanese barely spoke English. They looked disoriented. They hadn't a clue about American corporations or investing. I asked them what they were doing here. They told me they were hoping to do some M&A. As respectfully as I could, I told them they had no chance of succeeding in American M&A assignments if they didn't speak decent English. But a thought occurred to me on the spot. Why not form a joint venture? They could bring the Japanese companies to America, and Blackstone could work with them. A fifty-fifty split of revenues on condition they also invested in our first fund.

It was a creative way for both of us to get what we wanted. We needed money for our fund; they needed to build their M&A business. People in a tough spot will often focus on their own problems when the answer may lie in fixing someone else's. By paying attention to Nikko's needs rather than ours, a possible solution had materialized for both of us.

"Right now," I told them, "you're going to get 100 percent of no money. You're going to fail. I can make you successful. All I want is for you to invest in our fund. That's all I care about. You'll make plenty of money with it. But what's important for you isn't the investment. It's what I can do for you." They liked the idea in principle, and we agreed to meet in Japan.

A week later, Pete, a representative from First Boston, and I went to Nikko's Tokyo headquarters to meet with Yasuo Kanzaki, who ran its international business. The prospect of Blackstone working with Nikko to serve Japanese clients coming to America looking for acquisitions delighted him. "I know we will never be successful in America with our own people," he said. I thanked him and told him that in addition to the joint venture, we wanted him to invest in our fund. I explained our investment strategy and said I knew my pitch was most unusual.

"I will talk to my colleagues on our executive committee. I have only one request. Do not go to see Nomura before we make a decision." Nomura was their main competitor, the largest of Japan's brokerages. Nikko was a distant number two. We agreed. The next day Pete and I woke early for the rest of the meetings. Woozy from jet lag, we both fell asleep in the back seat of the car. When we stopped, I woke up and looked out the window and saw the sign on the building: Nomura.

"What are we doing here?" I said to the rep. "Didn't we tell you yesterday we can't go to Nomura?"

"It's on the schedule," he said.

"Then tell us how we handle this situation. We promised Nikko we're not going to meet Nomura. We can't make a promise then break it."

"But you can't insult Nomura. They're the most important broker. You have an appointment with the executive vice president for international business, the same as the other guy."

"We can't be in this position," I said. "What are our options?"

"You could cancel, but that would be bad manners. You could go and have a nonmeeting meeting, and hope that Nikko doesn't find out, where you present nothing, like just a courtesy call. Or you can go make your presentation."

None of these options seemed great. We needed to stop floundering. "We've got to call the guy at Nikko and tell him what's going on and get his advice. We don't know the customs here, and we don't want to offend him," I told Pete. He agreed and made the call. We had one of those giant built-in phones in the car, and we both pressed our ears to the handset, practically kissing each other, so that we could hear Yasuo Kanzaki. We explained that by accident, we were parked outside Nomura. We could hear that sound

Japanese people often make when they don't like something, sucking air in between his teeth.

"You're at Nomura now?"

"It's a mistake," I said. "We're sorry. We haven't gone in, and we're asking your advice. What should we do? Should we just cancel the appointment? Have a nonmeeting meeting? We don't want to do anything that will offend you."

"Okay," Kanzaki said. "Nikko is very interested. How much money do you want for your fund?"

Pete covered up the phone and whispered. "Fifty?"

"A hundred," I whispered. "It's what we got from Prudential."

"We're looking for $100 million," said Pete.

"Okay, no problem. $100 million. We have a deal. Now you can go to Nomura and have a nonmeeting." As we hung up, I murmured to Pete: "We should have asked for $150 million." Recalling this on my sixtieth birthday, Pete said that one of my unique qualities is that my "goals are so demanding and dynamic that sometimes it is even hard for me to accept yes for an answer."

Inside at the reception desk, we asked for Junko Nakagawa, head of Nomura's international investments. There was a lot of muttering and confusion until they found someone who spoke English. "I'm so sorry," he said. "You are not at Nomura headquarters. You are at a brokerage branch."

We were half an hour late for a nonmeeting we didn't want in a country where being late is a gross discourtesy. We raced to the Nomura headquarters, asked for Mr. Nakagawa, and apologized.

Fifteen minutes passed. Very un-Japanese. Finally someone came. "I'm sorry," he said. "Mr. Nakagawa is not in Tokyo today. There must have been a mistake with the appointment. But I'm the general manager. I'm no one really, but I can have a courtesy meeting with you." Which is what we did: a nonmeeting courtesy meeting, during which all we could think of was the $100 million from Nikko.

Their pledge transformed our fortunes. Nikko was the investment bank for the Mitsubishi group, Japan's largest *zaibatsu*, or family of related companies. Once Nikko said yes, all the other companies in the zaibatsu said yes too. Everywhere we made our pitch, people said yes. I loved Japan. After months of rejections, we couldn't stop selling. We flew home with a further $325 million in our fund. Our luck flew home with us.

For months, I had been pitching General Motors's pension fund, the biggest in America at the time. I had come at them five times through different people in different ways, but kept getting the same answer: we lacked a track record. Then one of the partners at First Boston introduced me to Tom Dobrowski in GM's real estate division, whom he knew through his church.

When I met Tom, he was wearing Sunday school medals. Strange for an adult, I thought. But my First Boston colleague was right. Tom was smart, and we hit it off. After listening to Pete and me make our pitch, he said, "Jeez, that's really interesting. Maybe we *should* do something with you guys." GM came through with $100 million.

We were rolling. It was as if all the lights along the way had been switched from red to green. I called my old friend Jack Welch, now CEO of General Electric.

"You guys don't know what you're doing, do you?" Jack said.

"No," I said, "but it's us. We're the same."

"Yeah, yeah, yeah. I love you guys. Listen, I'll give you $35 million. Why? Because you are great, both of you. That way you can use the GE name to help get some other people. Maybe we'll do some business together. Wouldn't surprise me."

When we got up close to $800 million, we began to run short on possibilities. I'd wanted a billion. But it had been a year since we had sent out our initial placement memoranda, a year that had felt like *The Perils of Pauline*, one heart-stopping event after another. We had persevered through rejection, disappointment, and despair.

There is a saying in finance that time wounds all deals. The longer you wait, the more nasty surprises can hurt you. I like to finish work quickly. Even if tasks are not urgent, I like to get them done to avoid the unnecessary risks of delay. I determined to do the same with the fund. By September 1987, stock markets were hitting record highs, and I did not want to get caught if they turned. We decided to push hard to close the fund and wrap up the legal details as soon as possible.

Each of our thirty-three investors had a team of lawyers, and each lawyer wanted everything done right. It was like fighting thirty-three fights in thirty-three foreign countries all at the same time. But we pushed hard to have everything signed and sealed by Thursday, October 15, and we did it. Caroline James, our only associate, who was handling the closing, left soon afterward to become a therapist. She would have a lifetime of case material just from working with me on the closing.

I arrived at the office after the weekend, on the morning of Monday, October 19, with our fund closed and the money committed. That day, the Dow dropped 508 points, the largest one-day percentage drop in stock market history, bigger than the one that triggered the Great Depression. If we had taken an extra day or two to close the fund, we would have been caught in the downdraft of Black Monday. The money could have slipped away, all our efforts gone to waste. Our urgency had saved us. We were ready to start investing.

DON'T MISS THE CAN'T MISS OPPORTUNITIES

Our first leveraged buyout was the kind of large, complex but potentially rewarding deal we had sought. The kind of situation begging for a solution where conventional wisdom had thinned the field. Since we weren't yet either the biggest or the best in our business, we had to pick spots where the problems were toughest and we were the only ones offering a way forward.

USX started as U.S. Steel, the company created in 1901 by J. P. Morgan when he bought Carnegie Steel from Andrew Carnegie and his partners, including Henry Clay Frick, in what was then the biggest leveraged buyout in history. By 1987, U.S. Steel had been an iconic American name for more than three-quarters of a century. But steel production was vulnerable to sharp rises and falls in commodity prices and fluctuating demand from customers. The company had diversified into energy, buying Marathon Oil, and changed its name to USX. But its problems were multiplying. A labor strike paralyzed its plants, and Carl Icahn, a corporate raider in the Harold Simmons mold, had bought enough shares to launch a proxy action or a hostile takeover bid. He had demanded the company make changes to raise the share price. Management decided it would rather pay him off than do what he wanted. To raise the greenmail money, they planned to sell the railroads and barges they used to transport their raw materials and their finished steel, divesting them into a separate company. That was the business we were going to buy.

From the start of Blackstone, Pete and I had agreed that we would never do hostile deals. We believed that businesses were made up of people who deserved to be treated with respect. If all you did as an acquirer was slash costs and take out money until a business collapsed, you would be hurting employees, families, and their communities. Your reputation would suffer, and decent investors would be scared off. But if you invested in improving the companies you bought, not only would their employees benefit from working for a stronger company, but your reputation would be enhanced and you would earn much higher long-term returns—"Friendly Transactions in a Hostile Environment," as we put it in a *Wall Street Journal* advertisement. USX would test that.

If Carl Icahn hadn't come along, USX would not have been trying to sell its transport system. The company depended on this network, from freighters on the Great Lakes to barges in the South, with railroads in between to haul iron ore, coal, and coke into their plants and take the finished steel products out to customers. They wanted the money from divesting it but feared losing control.

To us, the transport system looked like a good asset going through a bad time. The steel strike had idled the railroads and barges. They were generating no income. But the strike would be settled eventually, and we thought the trains and shipping would get back to making a significant profit. The deal could be good for both sides, provided USX trusted us to respect their concerns. Trust would be at the heart of the negotiation.

Roger Altman, who had just joined Blackstone as vice chairman, brought us the deal. He had gone from being co-head of investment banking at Lehman to the assistant secretary in the US Treasury under President Carter, and would later serve as deputy secretary under President Clinton. When Pete, Roger, and I went to the headquarters of USX in Pittsburgh, our main goal was to satisfy the company's managers that we could be good partners. We were not Carl Icahn; we were a friendly buyer. But it was one thing for us to say it, another to demonstrate our intent through the deal's terms.

We proposed a partnership in which we would buy 51 percent of the transportation business and USX would keep the rest. By selling over 50 percent, USX would relinquish responsibility for the business's debts, making their own balance sheet considerably healthier and boosting the value of their stock. But to reassure them that this wouldn't come at the cost of losing control of their essential transport network, we proposed a five-person board with two directors from our side, two from theirs, and an arbitrator, whom we would agree on, would attend all board meetings, and would serve as the tie-breaking vote. They liked our price: $650 million.

Now we had to find the money. Though we had raised an $850 million fund, our intent was to do as many deals as possible with that money. The less equity we used in each deal, the more deals we could take on, borrowing the balance of what we needed from banks. We could use our entire $850 million to buy one $850 million asset, taking on no debt, or treat it as a 10 percent down payment on $8.5 billion worth of assets, borrowing the rest. The second option, assuming we borrowed responsibly, had the potential for much higher returns. Safety also demanded diversification.

I called the banks then financing leveraged buyouts, but all I heard back was, "We don't like steel. We don't like strikes. Everybody in steel goes broke ultimately. Steel is a nonstarter. So, no." I told them they were wrong. We had analyzed the opportunity in depth. Steel was a commodity, vulnerable to shifts in the price of its inputs, iron ore, coal, and nickel, and supply and demand in the market. The price for shipping steel, though, was based on volume, and the Interstate Commerce Commission set the tariffs. For every ton you shipped, you were paid a certain amount. Once steel started moving again, even at lower prices, the transport business would rally. "No," said the banks, still confused by the difference. "It's all the steel business."

If steel was a red flag and strikes were a red flag, so was our inexperience. Only two banks showed the slightest interest: JPMorgan and Chemical Bank. I wanted JPMorgan, the most prestigious commercial bank in the United States. Its name would boost our standing and help build the Blackstone brand. Plus, going back to J. P. Morgan himself, the bank knew steel. They had made their fortune in steel. I was thrilled they were willing to do the deal until I heard their terms: they wanted to charge an unusually high rate of interest and wouldn't put up their own money to underwrite it. When banks issue loans to companies, they typically raise the money by raising money from other banks as well. But they also underwrite the transaction, promising to cover the balance if investors don't buy all the securities. If a bank won't underwrite its own transaction, that hesitation typically signals a lack of faith in the deal.

I challenged them. They said that for JPMorgan to put its name on a deal was as good as underwriting it. But if it's as good as underwriting it, I asked, why not just underwrite it? That would guarantee us the money. They told me not to worry. They were JPMorgan. But their explanation didn't ring true. They were clearly worried about something and not telling me. When I pushed them, they said, "Don't work with us, then. It doesn't make any difference to us. JPMorgan does not change its approach. That's how we do business."

I hadn't wanted to go to Chemical Bank. It was not the prestigious banking partner I had in mind. It was known as "Comical Bank," the sixth or seventh largest bank in the United States, always striving but never quite achieving. But JPMorgan had proved so rigid and condescending, I had no choice. Like us, Chemical had never done an LBO. And also like us, they wanted to get one done. They turned out to be the opposite of JPMorgan: enthusiastic, entrepreneurial, open, and collaborative. At our first meeting, Walt Shipley, the bank's CEO; Bill Harrison, the head of corporate lending; and an investment banker my own age, Jimmy Lee, all greeted me. They had studied our proposal, examined our needs, and lined up an excellent package. The interest rate they planned to charge would fall as the steel strikes ended and the transport business picked up. It made sense. As the business got healthier, the company would seem less risky to lenders, and the interest rate we paid would change to reflect that. They also promised to underwrite the entire deal themselves. "Our underwriting, our money," they said.

I went back to Pete feeling torn. I liked the team at Chemical Bank—their creativity and energy. Their promise to underwrite the whole deal meant we would get all the money we needed the moment we signed. No risk at all. But I was still hung up on JPMorgan. I gave them one more chance to meet Chemical Bank's offer. When they passed, I went back to Shipley, Harrison, and Lee, the three "Comical Bears." We shook hands.

We carved the transportation division out of USX and called it Transtar. Blackstone put in $13.4 million in equity; USX put up $125 million in vendor financing, lending us money to take the division off their hands; and Chemical raised the rest. It proved to be a phenomenal deal. The market for steel did recover, as we predicted. The transport business came back, and the investments we made in Transtar improved its cash flow. Within two years, we had made nearly four times our equity. By 2003, when we sold our final stake in the business, we had made a total return of twenty-six times our investment, or 130 percent a year.

For the next fifteen years, we financed almost every deal with Chemical Bank. Our businesses grew together. The erstwhile Comical went on to swallow Manufacturers Hanover, Bank One, Chase Manhattan, and eventually JPMorgan itself, whose name they adopted. Walt Shipley became CEO of Chase Manhattan, Bill Harrison CEO of JPMorgan Chase, and Jimmy Lee its head of investment banking and my best friend in business. In all our years of collaboration, we never lost a dime together. Pete was happy, I was happy, the three Comical Bears were happy. We had gotten off to a good start. Now we just had to keep doing it.

In spring 1988, I read in the newspaper that one of First Boston's star bankers, Larry Fink, had left. When he was still in his twenties, Larry and a small group of traders had figured out how to package mortgages into securities and trade them like stocks and bonds. Mortgages were the second biggest asset class in the world after US Treasuries. Larry at First Boston and Lew Ranieri at Salomon Brothers controlled around 90 percent of this fast-growing market in mortgage-backed securities. Larry's success had propelled him onto his firm's management committee and put him in line to be its eventual CEO. He was only thirty-five. I had met him through our mutual friend Bruce Wasserstein and found him to be plain-spoken, intelligent, and energetic.

Not long after I heard the news of Larry leaving, we got a call from Ralph Schlosstein, who had run the small mortgage area at Lehman, saying that he and Larry were going into business together. Could they come by and see us? They were in our conference room the next day. Larry looked shocked.

"What happened?" I said. "You're a genius."

Two years earlier, he told me, he had made a bet that interest rates would rise. They had fallen. Mortgage holders had paid down their loans in the hope of refinancing at lower rates, affecting the value of Larry's portfolio. He had hedged his bets perfectly, he thought, so that even if rates went down instead of up, he would be protected. But a guy from the back office who ran Larry's computer models had made a mistake, and the hedges were wrong. Larry had made his calculations based on the wrong numbers. In a single quarter, his department lost $100 million. It wasn't his fault; he didn't control the back office. But he took the blame and he left.

I couldn't believe it. Larry was their most profitable guy.

"What do you want to do now?" I asked. He told me he was done with packaging securities and trading them. He wanted to invest in the mortgage securities market that he had done so much to create. No one else knew it better.

"Sounds like a good idea," I said. "Bring us a business plan. What do you need?"

A few days later Larry and Ralph were back.

Their plan included a list of the assets they wanted to buy and sell, the people they needed, and the profits they could make. They wanted $5 million to get going.

"That's it?" I asked.

"That's it. I want five people from the mortgage department at First Boston, and I need to pay them. I can work for nothing." His financial reward would come from his stake in the new business.

Blackstone didn't have any spare cash lying around at that point and certainly not millions. Our buyout fund was for investing in buyouts on behalf of our investors, not new businesses. But our first new business line had just popped up in front of us, and it ticked all the boxes: an amazing opportunity, beautifully timed, in a giant asset class, with one of the two top people in the world to manage it. We had prepared ourselves to expect the unexpected, and here it was. We would be fools to let it slip. Pete and I decided we would each invest a further $2.5 million personally in Blackstone to fund Larry's new venture. We would own half of the new company, Blackstone Financial Management, and Larry and his managers would own the other half.

Not long after Larry and his team came onboard, we decided to sell a 20 percent stake in our advisory business to Nikko for $100 million, valuing that subsidiary at $500 million, though its revenue was just $12 million. Nikko was already our partner on M&A deals for Japanese firms and had invested in our first fund. We had a good, trusting relationship. We could return their capital in seven years. In the meantime it would help us hire and build our organization more quickly. The transaction validated what we had built and strengthened us as we continued to grow.

By 1991, we had invested most of our first private equity fund and were trying to raise a second fund when a recession broke the momentum of the US economy. Panicked regulators cracked down on the insurance companies that had been the core investors in our first fund and limited their ability to invest in equities. Garnett Keith, the chief investment officer of Prudential, who had invested $100 million in our first fund, called to say that much as he wanted to, the change in regulations meant he could no longer invest with us. He said he might be able to find $1 million to show he supported us. I told him not to stretch and subject Prudential to criticism.

We had to find a fresh source of capital. Our first target was the Middle East. I set off with my colleague Ken Whitney, our treasurer who was also running investor relations for us. We stopped for a day in London. As we rushed out of our hotel to catch our connecting flight, we bumped into Teddy Forstmann, the founder of a rival firm, Forstmann Little, and his beautiful date, both with cashmere sweaters draped over their shoulders and heading to Wimbledon. In the car, I told Ken I wouldn't trade places with Teddy for anything. I wanted to be working, building the firm.

Our meetings in the Middle East were mostly a bust. Late June and early July was the worst time of year to visit. In Kuwait, we took a taxi without air-conditioning in 120 degree heat and arrived at our meeting dripping like we'd just stepped out of the sea. All the senior people knew better and had left for the summer, and the junior staff we met didn't understand what we did. At one meeting, we had presented for an hour when a young Kuwaiti asked the difference between investing with us and buying US Treasuries. Still, we obtained several small commitments. A few months earlier, Kuwait had been liberated from Iraqi occupation by a US-led military coalition. We could see the bullet holes in the buildings.

Next, we headed to Saudi Arabia. After five days of doing six presentations a day, we didn't have a single commitment. Exhausted, on our last day in Dhahran, floating around in the hotel pool, I started telling Ken how successful we would be. I laid it all out for him. To be successful you have to put yourself in situations and places you have no right being in. You shake your head and learn from your own stupidity. But through sheer will, you wear the world down, and it gives you what you want. The money had to be out there. I told him to forget about what had just transpired in Saudi Arabia. It was done. Wasted. We were going to be successful, enormously so.

Ken is a balanced, sensible guy and couldn't hide his disbelief. He told me years later that he didn't want to offend me, but at the time he thought I was out of my mind.

If the insurance companies were out and the Middle East was a bust, we had to keep looking. The next obvious target were pension funds, vast pools of capital, many controlled by states and employees' unions, which had to be invested to generate retirement income. Pension funds were typically conservative and had not yet begun investing in alternative assets. I had never met anyone from a pension fund. They were as foreign to me as Japan had been. Once again, we needed someone to get us in the door.

A few big firms promised introductions, but these placement agents were expensive, and I wasn't sufficiently impressed with anyone we met. We were getting desperate, though, and were about to sign with one of them when Ken brought in a couple of guys just starting out in the placement business. One of them was Jim George, who was wearing a suit but looked as if he would much rather have been out West in jeans and a flannel shirt than stuck in an office in midtown New York. He told me he had never done this kind of work before. He was modest and soft-spoken. I had to crowbar out of him the reason he was sitting in front of me. For years he had been sitting on the other side of the desk as chief investment officer for the state of Oregon, where he had overseen the first investment by a state pension in private equity. A few years earlier, he had invested with KKR. "It worked out nicely," he said. "After that, whenever any other state fund wanted to think about this asset class, they'd call me and they'd come up and see me. I'd tell them what we were doing. You know, that type of thing."

He was barely out of the room when I grabbed Ken and told him Jim was our man. He was the opposite of the smooth placement agents we had seen. He was perfect for what we needed. I didn't care that he was new to the work. Jim George was going to lead us to the promised land, I was sure of it. Another can't-miss opportunity. We put together an offer.

A few days later, I called Jim's partner and invited them both in for another meeting in New York. I was jumping out of my chair promising that if we could agree on a fee, they could get to work immediately. Jim, though, was out of town. His partner said he would try to reach him, but called back later and apologized. Jim couldn't fly up for a meeting the next day.

"This may be the biggest thing in your careers. He can't see me?"

"Jim just got off a Disney cruise in Fort Lauderdale. He doesn't have a suit with him."

"I don't care whether he has a suit," I said. "Just tell him to get on a plane and fly up to New York."

"I told him that, but he won't do it. He only wants to come in a suit."

"Please," I said, "just buy him a suit and get him up here."

Jim's personal dignity was unimpeachable. It was why people trusted him. He had rules, and wearing a suit to a business meeting was one of them. When we met, I told him how much I intended to pay him. He was shocked. It was a big leap from his government salary in Oregon. "You deserve it," I told him. "You've given great service to Oregon and to the other pension funds in the country. We're going to see every one of the state funds. And we're going to sweep the table." He agreed to help us.

What Jim had was far more important than a business card from one of the big placement firms: he had the credibility and temperament for the work. Visiting pension funds with Jim turned out to be like going around Japan after Nikko invested with us. When the pension managers saw him, they saw one of their own, from the smallest to the biggest of all, the California State Public Employees Retirement System, which has invested with Blackstone ever since. With Jim leading us, we raised $1.27 billion for our second fund, the biggest private equity fund in the world at the time.

At around the same time we were raising our second private equity fund, we also began considering another new opportunity: real estate. In the late 1980s and early 1990s, the US real estate market collapsed. First, bad loans overwhelmed the savings and loan associations. These small financial institutions across America had lent more than they should have to fuel a nationwide building boom. Then in 1989, when the extent of their problems emerged, the federal government created the Resolution Trust Corporation (RTC) to liquidate their assets, their mortgages, and the buildings these loans had been used to build. But when the country tipped into recession in 1990, the value of all those newly built offices and homes collapsed. The RTC came under pressure to move the assets off their books at almost any price they could get, forcing massive amounts of real estate onto the market.

In 1990, all I knew about real estate came from my personal experience as a home owner. One of the partners at Blackstone suggested I meet Joe Robert, a real estate entrepreneur from Washington, DC, who was looking to raise money. I had read in the newspapers that the market was frozen: the buyers had all fled. Joe, though, saw the market differently. He had built a property management firm in Washington and developed close ties to the government. Watching the RTC's struggles, he had lobbied hard for them to involve private sector investors and real estate experts to help work through their backlog of distressed property. In 1990, his efforts resulted in a deal with the RTC for him to sell a $2.4 billion portfolio of property acquired by the government from collapsed savings and loans during the 1980s.

"I'm selling $5 to $10 million buildings to doctors and dentists," he told me. "They have savings and enough credibility in their communities to borrow whatever they need from the banks." What he wanted from Blackstone was the money to buy these buildings for himself. He had done well enough on brokerage fees, but now he saw the chance to make much more as an owner and developer. It seemed a perfect match: our money and his expertise. He proposed working together on the next RTC auction, which was coming up in just a couple of weeks. "Trust me," he said. "The country's in a complete mess. There won't be many people bidding."

When the RTC released the details of the auction, it included a package of garden apartments in Arkansas and East Texas, about three years old and 80 percent occupied. As investments go, this collection of buildings couldn't have been further from the deals I was used to working on. It would not require a lot of capital and the risk seemed modest. It seemed a great way to learn the business and probe for a bigger opportunity in the future.

I called Bob Rubin, then CEO of Goldman Sachs and a future US treasury secretary, and proposed working together. Goldman had significantly more experience in real estate than we did. He agreed.

When Joe and I went to meet Goldman's real estate team, though, we found they had a different view of the risks of this deal. Goldman wanted to bid as low as possible to avoid overpaying. For me, the biggest risk was not offering enough and missing out on a tremendous opportunity. I wanted to make sure we beat Bankers Trust's expected bid. You often find this difference between different types of investors. Some will tell you that all the value is in driving down the price you pay as low as possible. These investors revel in the transaction itself, in playing with the deal terms, in beating up their opponent at the negotiating table. That has always seemed short term to me. What that thinking ignores is all the value you can realize once you own an asset: the improvements you can make, the refinancing you can do to improve your returns, the timing of your sale to make the most of a rising market. If you waste all your energy and goodwill in pursuit of the lowest possible purchase price and end up losing the asset to a higher bidder, all that future value goes away. Sometimes it's best to pay what you have to pay and focus on what you can then do as an owner. The returns to successful ownership will often be much higher than the returns on winning a one-off battle over price.

At the price I suggested, I calculated that we would lock in a 16 percent annual yield. That meant every year we would receive 16 percent of our purchase price back in profits from rental income. And that was just the start. These apartments were producing a steady flow of cash. They were almost new, so we wouldn't have to spend a lot of money fixing them. If we added some debt to the acquisition, we could lift the return on our investment to 23 percent a year. This concept will be familiar to anyone who has taken out a mortgage. Let's say you paid $100,000 for a house by putting down 40 percent in cash and borrowing 60 percent. If you sold the house immediately for $120,000, your profit would be $20,000, or 50 percent of the $40,000 in cash you initially put down. Alternatively, if you paid for the same house by putting down only $20,000 in cash and borrowing the remaining $80,000, then the return on your original $20,000 investment would double to 100 percent. Taking on debt, assuming you can pay it back, can substantially increase your return on equity.

In addition, we thought we were close to the bottom of the real estate cycle. In 1991, we felt real estate had bounced off the bottom. As the economy recovered, the vacant 20 percent of apartments would fill up, lifting the 23 percent return to 45 percent. And rents would then rise, taking the 45 percent to 55 percent. If all we had to do for this 55 percent compound return was buy the asset, I reasoned, we shouldn't be worrying about getting the lowest possible price at the auction. I told Goldman, "I'm happy with 55 percent a year. I don't need 60." They conceded, we placed our bid, won, and over time our first investment in garden apartments yielded a 62 percent annualized return, even better than I'd imagined. After that auction, I asked Joe how much of this stuff was out there. "There's a whole country full," he told me.

We were new to the real estate game, but that was our edge. We came without baggage, no failing properties or underwater loans. I could scarcely believe it. A country full of value and no competition. But as we prepared for the next auction, Joe told me that Goldman Sachs had offered him the chance to invest a billion dollars. Though he had committed to us, he wanted to take them up on it.

"The only way you know these people is thanks to me," I said to him. "How can you just run over there?" He said he felt bad about it, but Goldman was offering him what he wanted. If I could raise a similar-sized fund in the next month, though, he'd reconsider.

Under the terms of our main investment fund, we could use the money for real estate deals. But I wanted our investors' consent before we committed such a significant portion of their money to this new strategy. I felt it was our duty to explain what we were doing. At our annual investors' meeting, I laid out the opportunity, expecting our limited partners to jump at it. But to my surprise, all except General Motors turned it down. One after the other, our investors told me, "We know you're right. But we're loaded to the gills with these terrible real estate deals." They all agreed with us that prices were low and must eventually go up. But still they couldn't act. We had a huge opportunity but no money for it. I could have held Joe to his promise to keep working with us, but since we could not offer him a competitive platform, the right thing to do was to let him go.

We were determined not to give up, even without Joe. A few times in every investor's life, an immense opportunity appears. I asked Ken Whitney to find me someone else to develop our real estate business. We needed a 10 to build a great new business. As I worked through a list of names, checking references, I spoke to a man in Chicago, John Schreiber, whom Ken had identified as a reference. We talked for a while about the candidate he was supposed to be recommending. (He wasn't enthusiastic but was too polite to say so.) And the longer we talked, the more I was intrigued. In the 1980s, John had worked for JMB, a real estate investment firm in Chicago, which had been an active and aggressive buyer. Over the previous decade, he had bought more real estate than anyone else in America. He had seen the collapse coming and told JMB to sell everything. They told him he was crazy and paid him out so he could leave. Then came "the thousand year earthquake" that proved him right.

"So why don't you come and work with us?" I said. He had worked so hard in the 1980s, he told me. He had eight kids and his family wanted to see more of him.

"You built the largest real estate firm in America and had eight kids? When did you ever get to see your wife?"

"Obviously I found the time," said John.

I kept pressing, and eventually he promised to give us twenty hours a week. He said he'd hire a couple of younger guys and mentor them for us, and use his connections to open some doors. We'd see how it went. In no time, his twenty hours were seventy hours. It was the 1980s all over again for him. I wasn't sure how his wife felt about it, but we were delighted to have him. He stayed in Chicago, working from home, an éminence grise to those who didn't know him. But he did much more than just hire a couple of younger guys and oversee them. He went in person to check out every single property we contemplated buying. Blackstone's partners were investing their personal money, and the deals were so good they had us talking to ourselves. But months in and without a fund, we couldn't get to real scale. It was driving me crazy.

Even as the real estate market began to recover, investors still felt burned by the crash. We needed to come up with a sweetener, some incentive to calm their fears and help get them over their misunderstanding of the risk. In the same way I had used a sealed bid auction for CSX's newspapers and pressured Harold Simmons with an endless flow of taxable yet unredeemable stock, we invented a novel structure designed to address a particular psychological state. It had to convey our confidence in the opportunity while giving investors a safety valve if they felt scared. We decided that for every three dollars an investor pledged to our real estate fund, two dollars could be discretionary. They could make a pledge, but if they didn't like the specific deals we were presenting, they could hold back two-thirds of it.

The first investor to express interest was a friend of Jim George. Steve Myers ran the public pension fund for the state of South Dakota. Jim told us Steve was a clever, courageous investor. Jim, Pete, John Schreiber, and I flew out to see him in Sioux Falls, South Dakota. When I explained what we were trying to do, Steve lit up. Real estate had come off the bottom, and the market was rising. It was a great time to get in. He persuaded his board to commit $150 million.

For the first time in my life, I was nervous about taking money. It was a big check for South Dakota's $4 billion pension fund, a lot for a single investment representing a lot of people's retirement funds. I asked Steve if he was sure. Under the terms of the deal, he said, he was only committed to investing $50 million of his pledge. He could invest the remaining $100 million if he liked the deals he saw and hold back if he didn't. For an opportunity with this kind of potential, that was a risk he could take. Steve's decision gave us our second new business line, real estate, which would eventually become Blackstone's largest business.

CYCLES: INVESTING THROUGH UPS AND DOWNS

The success of any investment depends in large part on where you are in the cycle when you make it. Cycles can have a major impact on the growth trajectory of a business, the valuation, and, of course, the potential rate of return. We routinely discuss cycles as part of our investment process. Here are my simple rules for identifying market tops and bottoms:

1. Market tops are relatively easy to recognize. Buyers generally become overconfident and almost always believe "this time is different." It's usually not.
2. There's always a surplus of relatively cheap debt capital to finance acquisitions and investments in a hot market. In some cases, lenders won't even charge cash interest, and they often relax or suspend typical loan restrictions as well. Leverage levels escalate compared to historical averages, with borrowing sometimes reaching as high as ten times or more compared to equity. Buyers will start accepting overoptimistic accounting adjustments and financial forecasts to justify taking on high levels of debt. Unfortunately most of these forecasts tend not to materialize once the economy starts decelerating or declining.
3. Another indicator that a market is peaking is the number of people you know who start getting rich. The number of investors claiming outperformance grows with the market. Loose credit conditions and a rising tide can make it easy for individuals without any particular strategy or process to make

> money "accidentally." But making money in strong markets can be short-lived. Smart investors perform well through a combination of self-discipline and sound risk assessment, even when market conditions reverse.

All investors will tell you that markets are cyclical. Yet many behave as if they don't know this. In my career, I have seen seven major market declines or recessions: 1973, 1975, 1982, 1987, 1990–1992, 2001, and 2008–2010. Recessions happen.

Market bottoms can be difficult to detect as markets are declining and the economy weakens. Most public and private investors buy too early and underestimate the severity of recessions. It's important not to react too quickly. Most investors don't have the confidence or discipline to wait until a cycle fully plays out. These investors suffer by not maximizing the profit they would have otherwise made from executing the same idea at a later point.

Timing the bottom of a cycle isn't easy, and it's often a bad idea to try in any case. The reason is that it typically takes a year or two for an economy to really emerge from a recession. Even when a market starts turning around, it still takes time for asset values to recover. This means you could be investing at the bottom with no return for some period of time. This happened to investors who started purchasing Houston office buildings in 1983 after oil prices collapsed and the market hit bottom. Ten years later, in 1993, these investors were still waiting for prices to recover.

The way to avoid this type of situation is to invest only when values have recovered at least 10 percent from their lows. Asset values tend to increase as economies gain momentum. It's better to give up the first 10 to 15 percent of a market recovery to ensure that you are buying at the right time.

While most investors say they are interested in making money, they are actually interested in psychological comfort. They would rather be part of the herd, even when the herd is losing money, than make the hard decisions that yield the greatest rewards. Doing what everyone else is doing seems like a way to avoid blame. These investors tend not to invest aggressively near market bottoms, but instead do it at market tops, where it makes little sense. They like the comfort and reassurance of watching assets go up. The higher prices go, the more investors convince themselves that they will continue appreciating. This same phenomenon explains why it's almost impossible to bring an IPO to market near the bottom of a cycle. But as a cycle grows riper, the number, size, and valuations of IPOs explode.

Cycles are ultimately powered by all types of supply and demand characteristics. By understanding and quantifying them, you can be well positioned to identify how close you are to a market top or bottom. In real estate, for example, building booms are stimulated when existing buildings are being valued at significantly more than replacement cost because developers understand that they can build a new building and sell it for more than they paid. This is a brilliant strategy if only one building is being constructed. But almost every developer can see the same opportunity to make what they think will be easy money. If a large number of them start building at the same time, you can easily predict that supply will overwhelm demand and the value of buildings in that market will decline, most likely precipitously.

The idea that no one can see bubbles, as one former chairman of the Federal Reserve once announced, simply isn't true.

THERE ARE NO BRAVE, OLD PEOPLE IN FINANCE

As Blackstone was expanding, we hired a young banker from the corporate finance division at Drexel Burnham Lambert. He was smart and ambitious and soon after he arrived in 1989, he had a deal for us. Edgcomb, based in Philadelphia, bought raw steel and milled it into products for car, truck, and airplane manufacturers. This young partner had worked on a couple of Edgcomb deals at Drexel, so he knew the company, and its executives knew him. Now it was up for sale, and we got an exclusive first look at buying it.

An exclusive always warrants attention, and the deal looked promising. Edgcomb was making a lot of money. Its customer base was growing, and the company looked as if it could expand. They were asking around $330 million, which, based on our analysis, seemed like a decent price. I was ready to offer. Before I did, though, another of our new partners, David Stockman, came into my office spouting doom. David was a hybrid of Washington, DC, and Wall Street and had been director of the Office of Management and Budget under President Reagan. He had been with us less than a year, and had a fierce intellect, analyzed deals closely, and expressed his opinions without reservation.

"This Edgcomb thing is a disaster," he said. "We absolutely cannot do it."

"The other guy thinks it's great," I said.

"It's not great," David said. "It's awful. The company is worthless and poorly managed. All of its profits are coming from the increase in steel prices. They're one-time profits, and the basic business just has the illusion of profitability. It's going to end up going bankrupt. If we leverage it the way we're going to, we're going to go bust ourselves. It's a disaster in the making."

I called Edgcomb's champion and chief critic into my office to debate the investment, so I could hear them argue it out face-to-face and then make a decision. I sat there and listened to their pitches as if I were King Solomon. I thought the younger man got the better of it. He had worked with Edgcomb for years. He had an insider's knowledge and could answer all the questions. Stockman was analyzing the deal as an outsider. He had a strong argument but didn't have the same level of information. We thought we understood steel after our success with Transtar, the transportation business we had bought from USX. And somehow we thought we could now predict the commodity cycle, so I decided to go ahead. We made the offer, gathered money from investors, and closed the deal.

And right on cue, a few months after we closed, steel prices began to nosedive. Edgcomb's inventory was now worth less than they had paid for it and dropping in value every day. The profits we anticipated, which were to pay our borrowing costs, never materialized. We couldn't make our debt payments. Edgcomb was imploding, just as David Stockman predicted it would.

I got a phone call from the chief investment officer of Presidential Life, which had invested in our fund. He wanted to see me. I took a cab to his office in Nyack, on the Hudson above New York. He asked me to sit down and started screaming at me. Was I a complete incompetent or just stupid? What kind of imbecile would squander his money on something so worthless? How could he have given a dime to someone as inept as I was? As I sat there absorbing the punishment, I knew that he was right. We were losing their money because our analysis was flawed. I was the person who had made the decision. I don't think I have been as ashamed as that in my life before or since. Even messing up those deal book numbers for Eric Gleacher as a first-year associate at Lehman didn't compare. I wasn't capable. I wasn't competent. I was a disgrace.

I also wasn't used to being yelled at. My mother and father never raised their voices. If we did something wrong, they let us know about it, but they never screamed or shouted. I felt tears welling up and my face turning red and hot. I had to force myself not to cry. I said I understood, and we would do better in the future. As I found my way to the parking lot, I vowed to myself, *This is never, ever going to happen to me again*.

Back in the office, I worked like a demon to make sure that even if Blackstone and our investors lost money on Edgcomb, our creditors—the banks we had borrowed from to fund part of the deal—didn't lose a nickel. Edgcomb was just one deal in one fund. We would make other deals with the money from that fund and ensure that, overall, our investors did well. But our creditors lent us money deal by deal. If we failed to repay them even once, I feared, it would damage our reputation. Banks would lend us less money on stricter terms, making business harder.

We then examined our decision making. For all our entrepreneurial strengths, our drive, our ambition, our skills, and our work ethic, we still weren't building Blackstone into a great organization. Failures are often the best teachers in any organization. You must not bury your failures but talk about them openly and analyze what went wrong so you can learn new rules for decision making. Failures can be enormous gifts, catalysts that change the course of any organization and make it successful in the future. Edgcomb's failure showed that the change had to start with me and my approach to investing and evaluating potential investments.

I had fallen into a trap common to many organizations. When people have to pitch ideas, they tend to address the great man or woman sitting at the end of the table. If their idea is no good, the great man or woman rejects them. Regardless of the quality of their proposal, they leave the room with their heads down. A few weeks later, they go through the same routine with a new proposal and leave the room even more slowly than before to show what they think of the decision. The third time, they're gritting their teeth. The fourth time, the person at the end of the table now feels bad. The proposers aren't horrible employees, just not that good. But if that fourth idea is near-okay, the boss will end up green-lighting it just to keep everyone happy.

In my enthusiasm to give a new partner a shot with the Edgcomb deal, I had made myself and the firm vulnerable. I had succumbed to a good sales pitch. I learned later that one of the analysts on this new partner's team had opposed the deal. He couldn't see it ever working. But the partner had told him to keep his doubts to himself.

I should have been more wary of my emotions and more scrupulous with the facts. Deals aren't all math. But there are a lot of objective criteria to consider, and I needed to do that at length, in peace, not with two people pushing their views, and me sitting there deciding between them.

Finance is full of people with charm and flip charts who talk so well and present so quickly you can't keep up. So you have to stop that show. Decisions are much better made through systems designed to protect businesses and organizations than through individuals. We needed rules to depersonalize our investment process. It could never again rely on one person's abilities, feelings, and vulnerabilities. We needed to review and tighten our process.

I had always been maniacal about not losing money, and the trauma of Edgcomb pushed me further. I began to think of investing as like playing basketball without a shot clock. As long as you had the ball, all you had to do to win was just keep passing, waiting until you were sure of making the shot. Other teams might lose patience and take those off-balance, low-percentage shots from behind the three-point line, the way we had done with Edgcomb. At Blackstone, I decided we would keep moving and passing until we could get the ball into the hands of our seven-foot center standing right underneath the basket. We would obsess about the downside of every potential deal until we were certain we could not miss.

We decided to involve all of our senior partners in our discussions of investments. We would never again allow one person single-handedly to green-light a deal. During my career, I had gotten things more right than wrong, but Edgcomb had shown that I was far from infallible. My colleagues had decades of experience. By working together, arguing and applying our collective wisdom to evaluate an investment's risks, we hoped we could examine our deals more objectively.

Next, we insisted that anyone with a proposal would have to write a thorough memorandum and circulate it at least two days before any meeting so it could be carefully and logically evaluated. The two-day requirement would give readers time to mark up the memo, spot any holes, and refine their questions. No additions could be made to the memo at the meeting unless there was a significant subsequent development. We did not want extra sheets of paper going around the room.

The senior partners would sit on one side of the table and the internal team presenting a deal on the other. Around us would be the junior members of our teams, who were expected to watch, learn, and contribute.

These discussions had two fundamental rules. The first was that everyone had to speak, so that every investment decision was made collectively. The second was that our focus should be on the potential investment's weaknesses. Everyone had to find problems that hadn't been addressed. This process of constructive confrontation could be challenging for the presenter, but we designed it never to be personal. The "only criticism" rule liberated us to critique each other's proposals without worrying that we might be hurting someone's feelings.

The upside of the potential investment should be included as well, but that was not the focus of our early investment committee discussions.

Once this group dissection process concluded, whoever was running the deal now had a list of problems to address and questions to answer. What would happen to the company they were proposing we buy if a recession hit? Would its profits decline gently or plummet? Were the best managers likely to stick around following a buyout? Had we thought hard enough about the likely response from competitors? Or the effect on profitability if commodity prices collapsed, as they had after we bought Edgcomb? Did their financial model take account of all these eventualities? The presenter's team would go back and find answers to our questions, and in doing so, they could implement fixes or figure out how to manage the downside, or they might uncover new risks, new probabilities of loss that they might never have seen before. And back they would come for another round of discussion. By the third round, we hoped, there would no longer be any nasty surprises lurking in the deal.

I also resolved that I would never talk to just the lead partner on any potential investment. If I had detailed questions, I would call the most junior person, the one working the spreadsheets and closest to the numbers. If I had done that on Edgcomb, I might have heard from the analyst who hated the deal. Breaking through the hierarchy would allow me to get to know the junior people at the firm and get a different read. The risk may not be obvious on paper, but it came through in the analysts' tone of voice when I asked them, "Just walk me through this deal from your perspective." You could hear if they liked it or felt anxious. Psychology would be one of my strengths as an investor. I didn't need to remember each number in an analysis. I could watch and hear the people who knew the specifics and tell how they felt from their posture or tone of voice.

The final change we made to depersonalize and derisk our investment process was to encourage a greater sense of collective responsibility. Every partner on our investment committee needed to participate in assessing the risk factor of a proposed investment. In this way, the internal team presenting could not target the senior person at the table or lobby him or her for a positive decision. Everyone in attendance would share responsibility for whatever decision was made. And we made every decision in the same predictable manner.

As we have added new businesses to Blackstone and ventured into new markets, we apply this same process to all our investment decisions. Everyone contributes to the discussion. Risk is systematically broken down and understood. Debate is full and robust. The same small groups of people, who know each other well, go over each investment applying the same rigorous standards. This unified approach to investing has become the backbone of the Blackstone way.

For all that was going on at Blackstone in its early years, the rest of my life didn't stop. Ellen and I divorced in 1991, but we continued to raise our children, Zibby and Teddy, together. It had been a painful decision to separate. Before we did, I remember going to see my internist, Dr. Harvey Klein, for a checkup. Physically I was fine, but at the end of our meeting, Harvey asked me how I was doing. I told him I was under a lot of stress at work, and I couldn't make a decision on my marriage. I was unhappy but frightened by the prospect of divorce. Harvey jotted down a telephone number and handed it to me.

Dr. Byram Karasu is a psychiatrist who spent twenty-three years as department chair at the Albert Einstein College of Medicine in New York. He is the author of nineteen books; runs a small, private practice in Manhattan; and is regularly called on for his opinions in Washington. When I stepped into his office for the first time, I made it clear that I wasn't there for therapy. I just couldn't make my mind up about divorce. He asked me what was holding me up. Four fears, I told him: the fear of losing my relationship with my children, the prospect of signing away half of what I had worked so hard to make, the fear of losing half my friends, and terror at having to date again.

Four reasonable anxieties, Byram said, but all ultimately unjustified. My children were well past the imprinting stage of childhood, when divorce might traumatize them. If I wanted a good relationship with them and worked on it, they would want the same. As for my money, yes, it would be a big check to have to write, but if it cleared the way for a new chapter in my life, I would soon forget about it. The friends we had made as a couple would likely split fifty-fifty, and that was just a fact of life. And as for dating? As a wealthy, single man in Manhattan, I wouldn't be short of options.

Byram was warm, thoughtful, insightful, experienced, and convincing. His advice changed the direction of my life in the most positive way. I have been to see him once or twice a week ever since to talk about work mostly, and he always thinks with that same objective clarity he showed me at that first meeting. He understands my brain, the intensity with which I experience and respond to the world. He helps me test my intuitions and strip away the psychological, social, emotional, and intellectual filters that can obscure the truth.

Byram was also right about my divorce clearing the way for a new chapter in my personal life. My friends were kind enough to set up dates for me, and one was with a recently divorced attorney, Christine Hearst, who had a job lined up and her boxes packed to move to Palo Alto. Not the most promising setup. We were both busy, and Christine was already thinking about her new life on the West Coast. But my friends were insistent that I meet her, and I had promised I would try.

I thought our first date was great. She thought it was weird. She was expecting me to pick her up, but I was working late and we were going to a party close to my office, so I sent a car over to get her instead. She looked surprised when I finally did get in the car. I glanced over and said, "Hi, I'm Steve." And then proceeded to flip down the visor mirror and run an electric shaver over my face. We went from a book party at Rockefeller Center to see George Michael perform at the new Sony Plaza building on Madison Avenue to a dinner party with friends. Debbie Bancroft, the mutual friend who introduced us, called me the next morning to ask how the date went.

"Great," I told her. I liked Christine and we had done all these exciting things. Christine, though gregarious, is a private person. She had told Debbie she felt like an accessory as we went from place to place, socializing with lots of people I knew and she didn't. She had had a miserable time. The date was so busy that we never had a proper chance to talk at all. Debbie told me I was to call Christine, apologize, and invite her out for a quiet evening at a restaurant, someplace where we could actually get to know each other. I did as she suggested, and our next date was a long dinner at an Italian restaurant on First Avenue. I had such a good time that by the end of the dinner, I had my trusty calendar out. Christine looked surprised as I ran through various dates and tried to schedule when we might meet again. She wasn't used to anyone in finance as precise as I can be.

"We can do this thing fast or slow," I said. "I prefer fast."

Thankfully, I didn't put her off. Once we started dating, one of her first orders of business was to bring some order to my bachelor habits. I was living in an apartment at 950 Fifth Avenue with my son, Teddy, and had hired a chef, Chang. Night after night we'd have those familiar father–teenage son conversations over dinner. "How was school?" "Fine."

The first time Christine came over, she went into my kitchen and opened the fridge. It was more than I ever did. There she found box upon box of Stouffer's ready meals all stacked up. For two years, Chang had been heating them up and serving them to me and my son, and we hadn't even noticed.

A couple of years later, after Christine and I were married, I wanted to hire a chef. Christine has many skills, but none of them include meal prep. And everyone who knows me knows that after a long day's work, I like a proper dinner. So we put out an ad and were particularly impressed by a résumé from a chef called Hymie. We invited him for an interview, and Christine recognized him the moment she opened the door. It was Chang! He had simply changed his name and hoped we might have forgotten the bad Stouffer years. That's New York for you.

DON'T LOSE MONEY!!! DEVELOPING AN INVESTMENT PROCESS

People often smile whenever they hear my number one rule for investing: Don't. Lose. Money. I never understand the smirks, because it is just that simple. At Blackstone we have established, and over time refined, an investment process to accomplish that basic concept. We have created a framework for assessing risk that has been incredibly reliable. We train our professionals to distill every individual investment opportunity down to the two or three major variables that will define the success of our investment case and create value. At Blackstone, the decision to invest is all about disciplined, dispassionate, and robust risk assessment. It's not only a process but a mind-set and an integral part of our culture.

This is how we do it:

The concept of an investment committee is commonplace across Wall Street and other industries. A handful or more senior leaders from a given firm invite deal teams to present a new opportunity that has usually already been summarized for them in the form of a memorandum. The deal team will try to sell a potential investment to the committee, listing all the reasons a deal is great and quantifying the potential for profits. If the committee members like what they hear, they bless the deal, and the presenting team is relieved to know they can proceed. If not, it feels like a loss, and the deal team usually skulks out of the room feeling defeated, memos in hand and perhaps muttering to themselves. Not at Blackstone.

We structure our investment process to democratize decision making and encourage intellectual engagement by everyone involved—the deal team and committee members. There is no "us" and "them," no seeking of approval from a group of elders. Instead, there is only a collective sense of responsibility for identifying the critical drivers of a deal and analyzing the extent to which those drivers could affect the financial performance of an investment in various scenarios.

Everyone around the table, from the most junior to the most senior person, is expected to have an opinion and participate. No one person, or subset of people, dominates the conversation or holds the power for approval. It's team ball. Everyone must debate and agree on the variables and decide the range of possible outcomes. In some cases, the variables are obvious, and in others, it takes a few rounds of rigorous debate and discussion to determine what they are. But we don't move forward without agreement.

It's a subtle point, but this approach removes a lot of the noise and emotion that often affects investors' ability to make sound decisions. It also eliminates individual risk and the pressure for a deal team to be "right" on the ultimate outcome. In instances when we talk about investing billions of dollars, this pressure can be psychologically intense and overwhelming if concentrated on just a few people. You could ruin the firm or your reputation with one bad investment.

At Blackstone, investment committees are about discussion and discovery, not about getting a deal approved. Because the decision to move forward or not is made together, no one feels pressured to sell a deal just because he or she brought the idea. Similarly, there is no pressure to approve a suboptimal deal as consolation for a deal team's hard work in sourcing and analyzing the investment in question. If we make an investment and it goes wrong, we all got it wrong, and we are all responsible for fixing it. And when we are right, which is more often the case, we reap the rewards together.

Our process forces every person, no matter anyone's seniority, to act like an owner of the firm, as if our LP's capital was their own. This arrangement results in an extremely powerful alignment of incentives, and it also turns every deal evaluation into a teaching moment. The success of our process speaks for itself.

SPINNING THE WHEEL FASTER

Pete and I always resolved to hire 10s. Today, Blackstone gets to choose from the very best young graduates. For our 2018 class of junior investment analysts, we received 14,906 applications for 86 spots. Our acceptance rate is 0.6 percent, much lower by far than the most selective universities in the world. If I had to apply for a job at my own firm today, I seriously doubt I'd be hired.

But it took many years of trial and error to get here. Early on there were challenges to finding and keeping the people we wanted. The first was not our fault. Under the terms of my departure from Lehman, we could not hire our former colleagues. These were the people we knew best, whom we trusted, and with whom we had worked well. They would have been the ideal partners in our new venture. The second problem was that the big firms on Wall Street at that time were more like tribes than businesses. For someone to leave Goldman Sachs to join Morgan Stanley was like a Comanche leaving to join the Mohawks. And back then, Blackstone barely constituted a hunting party, let alone a tribe. The scale and systems at Lehman had largely spared me from having to fish through Wall Street's hiring pools. But now there were no bureaucratic layers to protect me from the truth that finance is an industry that encourages self-delusion. People think they're great and tell you they're great, never that they failed at their last job, only that they are looking for "more opportunity." You hire them, and they often fail. So then you have to fire them and go looking for more candidates. Then you have to work through that second group as well, until with the third group, you might just have the people you want. Then the first and second groups go around telling everyone how difficult your firm is as a place to work, making hiring even more difficult.

The third problem was me. While I was good at raising money and doing deals, scrambling to keep the cash flowing into the firm, I was hopeless when it came to hiring and managing people in our first five years. Pete was bringing in friends even when we didn't have work for them. The partners who did have work would do their own deals with no sense of what the rest of the firm was up to. Information came to me, but I didn't always make sure to pass it on. We were more a collection of individuals than a team. I excused myself on the grounds that we were in a hard, competitive business with little time for worrying about people's feelings. I was wrong.

I saw the opportunity to begin optimizing our hiring and training in 1991 when we hired our first class of MBA graduates. I knew at this moment that Blackstone would succeed. These promising young people, who were entrusting their careers to us, would be Blackstone's future. In return, we owed them a culture in which they could realize their ambitions.

The Wall Street culture that I had grown up in was not going to work. At Lehman, people were smart and tough, and they made a lot of money. But everyone had complex relationships with each other. They were sometimes verbally abusive. In the early years, Blackstone's culture echoed the places we had all come from. Despite our efforts to create a new kind of firm, we still had a few midlevel people who were exceptionally hard on their staff. They would occasionally shout at them, insult them, and push them around. They would wait until the last moment on Friday to give people work, ensuring their subordinates lost their weekends. One young analyst got so frustrated that he kicked in a photocopying machine and destroyed it. When I heard about it, I thought, *This is insane*.

To purge the firm of its worst behavior, we turned to Respect at Work, a group that came in and interviewed people throughout the firm to find out what was going on. They put on skits to small groups, showing them what their behavior looked like. They made our employees take roles as bullies or victims. I went to every one of these performances and sat in the front row. To see these actors playing my colleagues was shocking, absurd yet horribly undeniable. Confronting our shortcomings was the first step to eradicating this kind of behavior. We made clear that if there was any more of it, the perpetrators would be fired. It was up to me to say what I believed, to stand behind it and show everyone at the firm that I was serious.

Just as we had rethought our investment process in the wake of Edgcomb, we now put ourselves in the shoes of these young people joining Blackstone and considered what they would want from us. At DLJ, I was never trained properly. I would cower in my office hoping no one noticed me, scared I would be found out as ignorant or incompetent. I must have been the biggest buyer of antiperspirant on the East Side of Manhattan. At Lehman, I had to learn from my own mistakes. Learning in that environment was a slow, uncertain undertaking that led to a high rate of burnout and attrition. So at Blackstone we invested in a thorough training program to make sure our recruits knew what to do before we put them to work. We expected them to be active and useful as soon as possible, flawless on the basics of finance and deal making, alert to our culture, not hiding to conceal their ignorance. The cost of an efficient, effective training program was minimal compared to the benefits of having our newest people, our greatest resource, feeling informed, confident, valued, and ready to work.

We formulated a clear set of expectations, which I laid out in a welcome speech to our new analysts. It boiled down to two words: *excellence* and *integrity*. If we delivered excellent performance for our investors and maintained a pristine reputation, we would have the opportunity to grow and pursue ever more interesting and rewarding work. If we invested poorly or compromised our integrity, we would fail.

To ensure my message got through, I defined excellence in narrow, practical terms: It meant 100 percent on everything. No mistakes. That is different from school or college, where you can get an A with 95 percent. At Blackstone, that 5 percent of underperformance can mean a massive loss for our investors. It is a lot of pressure, but I suggested two ways to relieve it.

The first was focus. If you ever felt overwhelmed by work, I said, pass on some of your work to others. It might not feel natural. High achievers tend to want to volunteer for more responsibility, not give up some of what they have taken on. But all that anyone higher up in the firm cares about is that the work is done well. There is nothing heroic or commendable about taking on too much and then screwing it up. Far better to focus on what you can do, do it well, and share the rest.

The second way to maximize your chances of achieving excellence was to ask for help when needed. Blackstone is full of people who have worked on a lot of deals. If you are spending all night trying to solve a problem, chances are there is someone a few offices away with more experience who could solve it in far less time. Don't waste your time trying to reinvent the wheel, I advised. There were plenty of wheels all around you, ready-made, just waiting for you to spin them faster, further, and in new directions.

As for integrity, the easiest way I could explain it was in terms of reputation. To earn a great reputation, you think long term. I had been building my reputation since growing up in suburban Philadelphia, true to those middle-class values of honesty, hard work, respect for others, and always doing what you say you will. If those values sound simple, it is because they are. Anything more complicated can get lost amid the traps and temptations of our work. So my message to our new analysts was simple: stick to our values and never risk our reputation.

During my career, I had brushed up against the worst of Wall Street. I had seen people compromise their integrity with disastrous consequences for themselves, their firms, and their families. In the early 1980s, when I was running M&A at Lehman, Dennis Levine had the office next door. Dennis was a banker with a young family and seemed like the rest of us. But in 1986, he pleaded guilty to insider trading, securities fraud, and perjury. He had been taking confidential information on planned corporate takeovers and bought stock in the target companies. When the takeovers were announced to the public, the stock went up, and Levine made large, illegal profits. His most famous conspirator was Ivan Boesky, a trader in a three-piece suit who had made millions of dollars sitting at the heart of Wall Street. Everyone knew Boesky, and everyone spoke to him.

One day in the early 1980s, Boesky had invited me for a drink at the Harvard Club on Forty-Fourth Street. He began by asking me how I liked Lehman. I told him I enjoyed the work and the size of the deals. Then he asked me, "Wouldn't you like to earn more money?" I said I was earning plenty, and more would come. "But wouldn't you like to get it a lot sooner?" he said. I thought he was offering me a job, so I told him I was happy where I was. But he kept on with this same weird and ill-defined proposition: "Wouldn't you like to have more?"

Finally, I asked him if he had anything else to discuss. He said no and gave me a lift home. I didn't think much of it until Boesky was arrested in 1986 based on Levine's testimony. The *Wall Street Journal* ran a story about how Boesky had lured another conspirator, Marty Siegel, the head of M&A at Kidder Peabody, with a meeting at the Harvard Club and that same odd language: Wouldn't you like to have more money sooner?

Boesky, Siegel, and Levine, as well as a more junior banker, Ira Sokolow, all went to jail. Though, reading the news, I realized that Levine must have been getting some of his inside information straight from my desk. He must have been coming into my office, taking it, and passing it on to Ivan Boesky.

I tell our first-year associates at Blackstone this story as a warning. These men—Boesky, Levine, Sokolow, and Siegel—looked like any of us. They walked, talked, and acted like us. And they went to jail for trading on inside information. If I ever caught anyone at Blackstone doing what they did, I warned, I would take them to jail myself. I didn't say it to frighten anyone. I said it to help them, to eliminate doubt and make their decisions simpler.

When we hired the class of 1991, Pete and I were looking decades ahead. We hoped that one day, this would be the group to which we could turn over the firm. They would ensure that Blackstone thrived long after us. They represented our future. We were training them not just to be great players, but future coaches for the classes that followed them. All the theories we had about building an information machine, adding new business lines and achieving significant scale, depended on these twenty-somethings living up to the promise we saw in them. Only time would tell if we had made the right bets.

And as it turned out, we did. Many in that first class, and the ones that immediately followed, stayed with us for years, becoming some of the most successful investors and managers in our industry.

SEEING AROUND CORNERS

EXPAND

By 1994, Larry Fink had raised two big funds for Blackstone Financial Management and was managing around $20 billion of mortgage-backed assets. But as the Federal Reserve began raising short-term interest rates more than expected, long-term rates also moved up sharply and many bond investors were caught off-guard. Bond prices crashed in what subsequently became known as the "great bond massacre," driving down the value of Larry's funds.

Larry wanted to sell the business. One of the funds was maturing soon, and he was concerned that investors wouldn't want to reinvest with him given the downturn in performance. I tried to reason with him. It was true that we, along with the rest of the market, were having a tough time, but in the case of Larry and his team, I thought we had the best in the business and I wanted to continue growing. Even if performance decreased for a while and there were redemptions from investors, I was sure the asset class would eventually recover. Give it time, I told Larry. I have no problem selling an asset or business when the time is right, but this wasn't the right time. This business could be huge if we stuck with it.

But I couldn't persuade him. "Why do I have more confidence in you than you have in yourself?" I asked him. He told me that the business represented 100 percent of his net worth, but only 10 percent of mine, hence our differing appetites for risk. We went back and forth for months.

The other disagreement we had was around equity in the business. Under our original agreement, Blackstone owned half of Blackstone Financial Management, Larry and his team the rest. We had agreed to reduce our stakes to 40 percent each, leaving 20 percent to be distributed as stock to employees. If there was any further dilution to be had after that, it would have to come out of Larry's side. That was the deal. But before long, they asked us to give up more stock. I refused. Larry and his team were furious, saying they did all the work. I believed that once you signed something, you stuck to it, but in retrospect, I should have put the contract aside and accommodated Larry's request.

Blackstone, Larry, and his team ended up selling its stake in Blackstone Financial Management to PNC, a medium-sized bank in Pittsburgh. The only humor in it all came from the process of renaming the firm once it was owned by PNC. It could not be called Blackstone anymore. Larry thought there might be a way of retaining some institutional connection through a new name. He suggested Black Pebble or BlackRock. Black Pebble sounded puny to me. We settled on BlackRock.

Selling that business was a heroic mistake, and I own it. Larry's troubled funds recovered from their lowest point in 1994, and PNC has made a fortune from its investment. Larry has done what I always imagined he would and built a huge, successful business, the largest traditional asset manager in the world. I see him often, and he's an unbelievably happy man. It's extraordinary to think of what Blackstone and BlackRock have become. Two firms, hailing distance from each other in midtown Manhattan, starting with a few people in the same office. I often imagine what we might have been together.

If I were in the same situation today as I was in 1994, I would have found a way not to sell Blackstone Financial Management. Larry was an 11, and his business was exactly the kind we wanted to build at Blackstone. Not only did it have the opportunity to be huge and highly profitable, it also generated the kind of intellectual capital that would inform and strengthen everything we did. Moreover, Larry's skills were complementary to my own, and he was an extraordinary talent and manager. I specialized in illiquid assets; he knew liquid securities. We could have worked both sides in the same business.

But I made the mistakes of an inexperienced CEO: I let the differences between us brew. I stood my ground on the dilution of our equity because I considered it a moral principle to respect the terms of the original deal. Instead, I should have recognized that when a situation changes and a business is doing extremely well, sometimes you have to make accommodations.

When we first thought of adding business lines to Blackstone, our idea wasn't to enter just any area. We wanted to build businesses that were great in their own right but also made our whole firm smarter. We believed that the more we learned from different lines of business, the better we would become at everything. It was the one thing they taught at Harvard Business School: everything in business is connected. We would see opportunities and markets in unusual and different ways from our competitors. Our perspective would broaden and deepen. The more feeds we had running into the firm, the more we'd know, the smarter we'd be, and the better the people who'd want to work with us.

In 1998, we did our first big deal in Europe, buying the Savoy Group in the United Kingdom, owners of four treasured London hotels: the Savoy, Claridge's, the Berkeley, and the Connaught. We had no permanent presence in London at the time, and it was a difficult deal because the owners had been fighting for years. So I flew over for the signing. Afterward, I went to Claridge's in Mayfair, sat down on a sofa, and sank so far into it that my knees were up around my ears. The whole place desperately needed an overhaul.

Who were we to do it? The British press greeted us as barbarians, Americans who would ruin these national treasures. I knew we were going to be judged in London by how we handled the redecoration of Claridge's, one of the grandest and most traditional of the city's hotels, a favorite of the Queen Mother. If we did a beautiful job, it would make our future there much easier. It would be better than any advertising. I considered it so important, I took on the task of overseeing the revival and redecoration myself. I like having a hand in creating beautiful things.

The best way to make the English happy, I figured, would be to hire an English decorator to renovate the hotel. I called Mark Birley, who had created a succession of stylish and popular clubs and restaurants in London, including Annabel's and Harry's Bar, and suggested he open a club at Claridge's. He warned me off a collaboration, saying, "I'm very unreasonable." When he was creating Harry's Bar in London, he told me, a supplier sent him the wrong sconces for the main dining room. The project was already months behind schedule, and his family and business partner were all pushing to get it finished. Put up something temporary, they urged. Don't hold up the opening for the sake of a few sconces. But Birley wouldn't budge. He didn't want to open until everything was perfect. "We lost a lot of money," he told me. "But I don't care about money. I care about perfection. That compromises the way I look at things." I told him I understood his choice of excellence over an easy life.

I then got the names of the five top English decorators and invited them to present to a panel of society women who I thought would know good taste from bad. It took nine months of planning to get the decorators and the panel together. At the end of the day of presentations, I told the panel that we would have a vote. One of the women put up her hand and asked, "Do I have to vote for any of them?" The verdict was unanimous. They didn't like any of what they had seen.

The next day, I got a call from one of the panelists, my friend Dorrit Moussaieff. The person I needed wasn't English at all, she said. He was French, and lived in New York. *Not the ideal pedigree for an English hotel in London*, I thought, but I was out of ideas.

A few days later, Thierry Despont came to my office, immaculately dressed and charmingly French. He gave me two books of his designs and said, "Thierry does not do auditions. If you want to hire me, just hire me. Also, I do not do commercial work, so zees project is ze wrong one for me."

Naturally I was intrigued. This was going to be a very different kind of negotiation, so I started sending out probes, searching for a way past this formidable facade. If Thierry didn't do commercial work, I asked, what did he do?

"I do ze big house. The library of one of ze houses I just do is bigger zan ze lobby of ze Claridge hotel." And he added with emphasis, "I work wiz no budget."

"Sounds fun."

"It is very fun."

"Out of curiosity, have you ever done any commercial work?"

"Yes, for my friend Ralph Lauren." Ralph had been redesigning his store on New Bond Street and asked Thierry to copy the stairwell at the Connaught. "I told Ralph I could not copy the stairwell of ze Connaught, but I can give maybe ze essence of ze stairwell." While he had been going back and forth to London to create that essence, he told me, he had stayed at "ze Claridge" on seventeen separate occasions. It was a "confused hotel," some of it Georgian, some Victorian, lacking any sense of a whole. He had redesigned the entire hotel in his head because "zat's how I zink. If I stay in some place, I zink how it should be better."

In any conversation with someone you don't know, you should always be patient and keep asking questions until you find a place of common ground. That Thierry had not only stayed often in Claridge's but thought about its design told me that his initial salvos about not doing commercial work were true, but perhaps not accurate in this situation. He had the confidence it would take to fix up Claridge's against potentially hostile public opinion. Now I had to persuade him.

"I know you don't do commercial work, but it sounds like this wouldn't even be work," I said. "You've already redesigned the place in your head." What is more, it would be the greatest advertising any decorator could have. I knew a lot of designers and decorators, but I had never heard of him. His reputation could be transformed with one project. "Every wealthy person visiting London will know you did Claridge's, and if they like it, they'll try to hire you."

"Thierry will zink about it and call you."

Two weeks later, he was back in my office. "I have zought about what you said and it would be easy for me to do zis. It could be a good project." I asked if he had any storyboards or preparatory drawings to show me. "Thierry does not do zis. Here is the rule. I will talk to you about colors and concepts and show you what I'm zinking. I'll lay it out and you can say if you like it or not. I'll work with you, you can veto any-zing, and we'll come up with ano-zer solution."

Then I dropped my bomb. Given how much we had ended up paying for the hotels, there wasn't much left over to pay an expensive decorator. The cash mattered to us, because we were trying to squeeze a profit out of the deal, but that mattered less to him. The hotel would be terrific advertising for him. Fair for him and fair for us, the perfect outcome.

"Do you talk to everyone like zis?" he asked.

"It's just the reality of this particular situation."

"Zere is only one answer I should give you. It is no. But I shall say yes."

Thierry did a beautiful job. Not long after the renovation, I received a letter from the exiled king of Greece who lives in London. After we had bought Claridge's, he had written to one of the British newspapers saying these uncouth Americans would destroy his favorite hotel. Now that he had seen what we and our French decorator had done, he was kind enough to write to me to tell me he had been wrong.

The success of our London hotels deal was one reason we decided to open our first overseas office there. In the late 1990s, many of our competitors began opening international offices. The most pressing argument for global expansion was that it would give us access to more investment opportunities. We could raise new funds and find new ways to reward our investors. If the United States entered another recession, we could turn our focus to other developed markets such as Europe or the developing markets of Asia, Latin America, and Africa. But even though we began doing a few deals outside the United States, like the Savoy Group, we did not move faster for two reasons.

First, our most important investment rule: don't lose money. We were comfortable in the United States, where there were plenty of deals to do. We understood the risks and knew how to minimize them. In new markets, we would have to learn much of this from scratch.

Second, overseas expansion risked compromising the investment process we had developed after Edgcomb. Its success depended on the same people being in a room together scrutinizing dozens of deals over time, reading each other's levels of confidence. I needed to hear a deal explained to me in person before I reached a conclusion. Hearing the nuance in someone's voice or seeing that person's body language told me as much as anything he or she said. I couldn't see us retaining the rigor our investment process demanded if we spoke only by telephone from offices scattered around the world. The evolution of videoconferencing technology changed my mind. By 2001, you could interact with people thousands of miles away in real time. That year, we opened an office in London.

The United Kingdom was an obvious choice for our first foreign outpost in private equity. It was the most active country for deals in the European Union, and we had done a few of them, like the Savoy Group, without moving a team there. The language, the legal system, and the general environment for doing business made it an easy place for an American firm to expand. But still, I felt we needed something to help us stand out. We looked at the American deal makers there, masquerading as Brits in their custom suits and shoes. And we looked at the Europeans, with centuries-old animosities. And then we decided that our edge was being unabashedly American, unabashedly Blackstone. We would offer the connection to American money and American business know-how, no cultural baggage attached. Just straightforward Americans, there to do business.

Most firms looking to start a new venture put a senior person in charge, someone with gravitas and experience. As we weighed our ambition to grow with our need to retain our culture, we decided it was much more important that we send someone who embodied our culture. Someone we could trust absolutely, someone hungry to build a business of his or her own within Blackstone.

David Blitzer had joined us in 1991 straight out of Wharton, a member of our first class of graduates. He had been one of the junior analysts I used to surprise with calls as I dug into the details of a deal. He loves Coca-Cola, hamburgers, and the New York Yankees and would never wear a custom suit. He is likable and sociable, smart and entrepreneurial.

The only problem was that David didn't want to go. He and his wife, Allison, were newlyweds and hadn't had any children yet, and they were worried about the care in British hospitals. So Christine and I took them out to a French restaurant on Central Park South. I promised David and Allison that we would fly them back for any medical care they wanted, even bring them over for a month before any child was born. It was a lot of money for the firm at the time, but I wanted David there. And I assured them that everyone I knew who had ever moved to London loved it. So off they went.

David chose Joe Baratta to go with him as his associate. Joe had also come to Blackstone in his twenties after working at Morgan Stanley. Joe had a strong entrepreneurial streak and a fascination with business, not just finance. He was a fierce worker who had suffered under some of our worst-behaved partners. But he had come through it all and was developing a great reputation. Like David, he understood our investment process and our culture intuitively.

They arrived in London with capital but no office and squeezed into a space sublet from KKR. The deals they pursued built on our unusual expertise in both private equity and real estate. They bought pubs, hotels, and theme parks and expanded into the rest of Europe. They were creative and aggressive and did some of the most successful deals in our history, building our first global outpost without sacrificing the culture and discipline central to our firm. As it turned out, David and Allison ended up having five children in London.

At around the same time back in New York, we were expanding as well. I asked Tom Hill, whom I had known since the Army Reserves and worked with at Lehman, to build out a new hedge fund business, Blackstone Alternative Asset Management (BAAM). Tom took over our nascent operations in this area and developed them into the largest discretionary investor in hedge funds in the world, increasing assets under management from less than $1 billion when he started, to more than $75 billion when he retired in 2018.

Within a year of David and Joe's arrival in London, Blackstone had outgrown its shared office space there. When you enter a market, you send signals with every choice you make, from the people you hire to the offices you rent. They are an important piece of your brand. I was determined that our new European headquarters exude the values of the firm: excellence, integrity, and care for all the people associated with us, those we employ and those whose money we invest.

I was on vacation in France when the realtor we had hired called and said he had five locations in London for me to see. I flew up and still wearing jeans and a polo shirt went to see five dark, dingy sets of offices, all with low ceilings and small windows. I told our realtor they were dreadful. He said they were the best to be found in London, outside of the City. I can see him now, with his slicked-back hair, his tightly fitting, blue, chalk-stripe suit, and taps on his wingtips, which clicked as he walked.

But as we were driving through Mayfair in central London, I noticed a construction site in Berkeley Square, covered in barriers. It was a great location.

"How about that?" I asked the realtor.

“Not available,” he said. It was a hole in the ground. But the realtor asserted that the owners were refusing to sign any leases until the building was finished. Still, I insisted we take a look.

I stopped the car, and we walked back to the construction site office, where I found the site manager. I told him it looked like he was working on a terrific project. He said they were proud of it. I asked him who owned it. I wanted to figure out if it was an insurance company or a couple of smart entrepreneurs. It turned out to be the former.

At the time, London real estate seemed to be going down in value. Rents were down to £60 per square foot. I guessed that the owners probably started out expecting rents of £70 per square foot. If the market kept falling, this building would soon be a money-losing project. I asked the site manager to call the owners and tell them that I would take at least half the project at £80 per square foot. If I paid £80 for half, assuming the world did not melt down, they could rent the other half at £60 and still get the £70 per square foot they had in their projections.

“I know I don’t look like a proper businessman,” I told the site manager. “But I don’t report to anybody. If I tell you I’ll pay £80, it’s just me. We’ll pay. So please let the owner know. If he wants us to take more than half, we’ll take more than half.”

As we walked away, the realtor started criticizing me for my manners. He said he had told me the owners weren’t ready to sign leases and I’d wasted his time, not to mention ruined any chance we might have had of getting space in the building. Fortunately, he was wrong on both counts. The owners called back the next day and said they liked my offer. We could have half the space. Today we have every floor but one.

I was never going to settle on offices that were less than perfect. The rewards of having a beautiful space that attracted the best people and gave our clients greater confidence in our abilities would far exceed the cost of paying a little extra to close the deal. And the best way to get what you want is to figure out what’s on the mind of the person who can give it to you. By addressing the developer’s concern about falling rents, we got the space I wanted.

We delegated the decoration at first to our facilities department. They hired a design firm who came to present to us in New York. This firm proposed putting a giant piece of natural wood in the lobby. We would look like a branch of Timberland.

"We are not a shoe store," I told them. "This is awful."

"What don't you like?" they asked.

"Everything."

"We can fix it."

"No, you can't. If you came up with this design, you can't fix it. The concept is so wrong. I don't want you even to try and fix it. You might be able to half-fix it. But I think we should settle up and move on."

One of the best features of the office was the amount of space and the large windows. I sent Stephen Miller Siegel, a designer I knew in New York, who came up with a beautiful design that we have to this day in all of our offices around the world: a thin ribbon of stainless steel running through walnut paneling. The only difference between London and New York is the light, so we have slightly different carpets, adjusted to the light, that in fact look the same. You never see decor this pretty in finance. Back then it was really something.

At Lehman, I had realized that I spent more time at the office than at home, so I wanted a beautiful environment. It made me feel happier. I wanted the same for everyone at Blackstone: warmth, elegance, simplicity, balance, and natural light pouring in from huge windows. When people come to a Blackstone office to work or for meetings, I want them to feel as blown away as I am by the experience.

One night in 2004, I was traveling in eastern France. My driver couldn't speak English, and I was exhausted from a European trip. My cell phone rang and it was a headhunter who asked if I would have an interest in being chairman of the Kennedy Center for the Performing Arts in Washington, DC.

The call surprised me; at the time I didn't even know what the Kennedy Center did. She said it was Washington, DC's version of Lincoln Center. The role was part time. I told her that much as I loved the performing arts, I had a full-time job running Blackstone. But she insisted on sending me some information.

Several days later, Ken Duberstein, who had been Ronald Reagan's chief of staff, called me. He told me that in Washington, the Kennedy Center, named in honor of President John F. Kennedy, is an incredible place to meet people. There are cabinet members on the board, and I'd get to meet the president whenever he visited. Lobbying was not permitted, so the center was bipartisan. It was also the social capital of Washington. The chairman must bridge the many worlds of Washington—politics, business, law, and culture—to bring the best of America and the world to the capital.

I had always been fascinated by politics, as a student running for office in high school to my meeting with Averell Harriman to my interviews at the White House when I was preparing to leave Lehman. From Blackstone's perspective, we were facing an increasing number of issues related to regulation and taxation. Our investors now included state, national, and international investment funds, so politics at every level was of increasing relevance to our business. Having an official position in Washington would allow me to meet new people and learn more. I called my old friend Jane Hitchcock, a playwright and novelist who lives in Washington, for advice. "Stevie," she said, "you have to do this."

Ken arranged for me to meet the board. I asked them about the center: its goals, its challenges, and what it needed from a chairman. Ken called me later and said the board was surprised. They thought they were supposed to be interviewing me, but instead I had interviewed them. My objective, I told Ken, had been to learn. I wasn't trying to persuade anyone I was right for the job. It was the same way I thought about interviews at Blackstone. If both sides could be easy, open, and direct with each other, the fit, or lack of it, would become apparent. From our conversations that day, it seemed the fit was there.

Next, Ken asked me to meet Senator Ted Kennedy, who had to approve any new chairman on behalf of the Kennedy family. He came to see me in New York and told me that after his brothers Jack and Bobby were assassinated in the 1960s, the family divided their public legacy. Ted looked after the Kennedy Center, and Jack's daughter, Caroline, the Kennedy Presidential Library in Boston.

"I have a simple rule with the Kennedy Center," he told me. "I'll support you and make sure you get the funding you need from Congress. I'll support you even if you screw up. And anything you need here in DC, call me and I'll make it happen for you." I had imagined there would be more political complexity in the process. Ted's promise pushed me closer to accepting.

One more thing, I told Ted. I wanted Caroline to get involved. She represented the next generation of Kennedys, but she never came to the Kennedy Center. He said he'd speak to her. A few days later, Caroline called, and we set up a meeting. I told her I wanted her to be the symbol of change and new life at the Kennedy Center. I realized that this wasn't something she wanted to do for herself, but it would be right for the institution. Her absence would be a deal breaker for me. Happily for me, she agreed and began a run of hosting each year's Kennedy Center Honors television show wearing her mother's famous diamond earrings.

The Kennedy Center also put me back in touch with George W. Bush, who had been a year ahead of me at Yale. I had met George's father, who became the forty-first president, at Parents' Day in 1967. To mark my appointment, the first lady, Laura Bush, hosted a lunch in the private quarters of the White House complete with a cake baked as a replica of the Kennedy Center. The building itself was frosted in chocolate, the stage made of sorbet, the orchestra members slices of peach, and the audience raspberries.

Another time at the White House, George and I were waiting for an event to start and had a moment to ourselves.

"How did you get here?" I asked.

"What?"

"How did you get here?"

"I'm president. That's how I got here."

"I mean, how did *you* ever get to be president?" He laughed and agreed that if you'd met us both in the late 1960s at Yale, you would have been surprised to find either of us at the White House, decades later, pillars of the establishment. It was a real pinch-me moment and another reminder of how people you meet accidentally early in life keep popping up to surprise you.

Being in Washington on a regular basis turned out to be more fulfilling than I had imagined. It gave me the chance to meet almost everyone of importance in our government, from Supreme Court justices to the leaders in Congress and members of the administration.

The role of chairman satisfied the producer in me. Whenever I was at the Kennedy Center, I had to go onstage and introduce the performance. And when we handed out awards, I welcomed and hosted our honorees. During my tenure, these included Dolly Parton, Barbra Streisand, and Elton John, among others. But the highlight for me was in 2005, when we awarded Tina Turner the Kennedy Center Honors. I had loved Tina's music since I was in college. Now I had the opportunity to host her and four other honorees for an entire weekend of celebrations. Tina came with her good friend Oprah Winfrey, who toasted her at an event at the State Department and came with us on a tour of the White House. As we walked around, Tina kept saying, in her surprisingly small voice, "I can't believe I ever got to the White House from where I came from." For the main event at the Kennedy Center itself, Beyoncé and a group of backup singers sang "Proud Mary," wearing the original short dresses that Tina and the Ikettes had made famous. Looking along our row in the balcony, with the other honorees and the president, I could see tears in Tina's eyes.

Several years after that night, I was at a charity event at Cipriani on Forty-Second Street in New York when I saw someone at a nearby table waving at me. I couldn't quite make out who it was because of the lighting, but my wife nudged me to go say hello. It was Beyoncé and her husband, Jay-Z. We talked for a few minutes, reminiscing about her Kennedy Center performance in 2005. It turns out that night was just as memorable and special for her as it was for me. As I walked back to my table, I shook my head in disbelief. What a remarkable life I was privileged to be living.

It's important to always be open to new experiences, even if they don't completely fit your agenda. My role at the Kennedy Center allowed me to use my experience—running organizations, fundraising, hiring talent—to give back to an important American cultural institution. In return, I learned more about Washington, DC, and developed interesting new relationships in almost every area of the entertainment business: comedy, theater, music, movies, television, opera, and dance. This included meeting the stars, directors, choreographers, musicians, and writers involved with each relevant art form. For someone from the financial world, chairing the Kennedy Center was a once-in-a-lifetime opportunity. Although I didn't know it at the time, the connections I made would eventually prove immensely important to me, even leading to several future opportunities to develop institutions in this area.

ASK FOR HELP WHEN YOU NEED IT

As the firm grew rapidly, the burden of maintaining a zero-defect culture and managing our expansion was crushing. By 2000, Pete was in his late seventies and spending most of his time running the Council on Foreign Relations and focusing on domestic and international economic issues in Washington. When we started the firm, he told me he didn't want to be involved in the investment area. He said he would help us raise money, stay involved in the advisory business, and help in any way I asked him. Watching me now try to do everything, he told me, "Steve, you're going to drop dead; you're just working too hard." He was right. The day-to-day management of the business was not my strength. I needed help.

I had known Jimmy Lee since the late 1980s, when we had hired him at Chemical Bank to finance our first deal, Transtar. We had done a huge amount of business together since. He was exceptionally high energy, a model of integrity, a great friend, and someone I trusted. He knew capital markets, M&A, and the buyout business and was a great salesman. I felt we could achieve a lot together at Blackstone and have a lot of fun doing it.

The first time we discussed it, he told me he loved the idea, but it would be tough to leave his colleagues at JPMorgan. I told him to think about it. A while later, he came back to me. "I want to do it," he said. "I want to make the change."

As we were negotiating the legal arrangements, I got a call from Bill Harrison, the CEO of JPMorgan, another great friend. "Jimmy came in to see me about the discussions he's been having with you. You know it's my job to fight to keep him."

"Of course, Bill, I know that," I said. "Jimmy's incredibly loyal to you. I asked him to think this through, without any pressure from me, because it's about what he really wants to do with his life. This isn't just a job. The bank's been his life, as Blackstone's been mine. He's got to figure it out."

"Whatever he decides, we'll both have to live with it," said Bill. "I just wanted to give you a heads-up that he and I talked." A few days later I was at the Ritz Carlton in Sarasota, Florida. The legal agreement and press announcement between Jimmy and Blackstone was finalized. We were going to make the announcement the next day. I was walking on the veranda when my cell phone rang.

"Steve," said Jimmy, "I can't do it."

"You can't do what?"

"I can't leave the bank. I know I'm totally disappointing you. You gave me all the rope anybody could need, and I told you I'd do it. But I realize I just can't."

"Jimmy, we've spent months on this, and I really want you to do it. But I said at the beginning that it was your call, your life. You don't need to be emotional. If you are going to join, you have to be all in. If you can't do that, it's not a good thing. You definitely shouldn't join us because you feel guilty about me. If you need more time to think, that's absolutely okay."

"No," he said. "I've thought about it. I have to stay."

It was a terrible setback and disappointment. But I knew Jimmy's strengths, and I knew his weaknesses. A man who in many ways dominated Wall Street was at heart a modest, dutiful Catholic boy who had to do the right thing.

It took me a year to muster the energy for another search. When the search company gave me their list, I saw the same tired old names. Of the couple of new ones, one stood out. A decade or so earlier, we had agreed to buy Chicago Northwestern Railroad for $1.6 billion. DLJ, my first employer, had given us a bridge loan to pay part of the purchase price. We planned to issue bonds to pay it back. But as credit seized up in the late 1980s, we would have to pay a higher rate on the bonds than we wanted just to get the deal done before the markets slammed shut.

Early one morning, a violent storm was raging outside. I had to catch a flight to London a few hours later. Pete, Roger Altman, and I were sitting opposite the team from DLJ arguing over the rate. DLJ wanted a floating rate with no limit. I couldn't agree because the interest rate could theoretically go extremely high if the company got into difficulty. DLJ countered by proposing a floating rate that could range between a minimum and maximum based on what some Wall Street experts would determine was fair. I knew that the rate would never float down, only up to that high cap. They argued it was necessary to sell the bonds. We wanted a fixed lower limit on the rate, so we could be sure we could pay it back. We weren't getting anywhere, and our flight was waiting, assuming the weather didn't ground us entirely.

"I'll bet a million dollars of my personal money that whatever higher cap you set on the rate, that's where these bonds will end up. Anybody willing to take me up on that?" I asked, knowing full well that they wouldn't. Nobody.

"Half a million?"

Nobody. These DLJ people assumed I didn't know we would end up as victims under the structure they were proposing. They weren't confident they could sell the bonds without the cap.

"How about a hundred thousand? No? Anyone in for ten thousand?"

One hand went up, Tony James's. To move forward, I agreed to the structure they wanted, but sure enough, the bonds were eventually reset and their rate floated up to their highest possible point. I told Tony he could send his $10,000 to the New York City Ballet. And I always remembered him as the only person ready to stand by his firm's position.

I asked the headhunter for his file. At DLJ, Tony had run corporate finance and M&A and started the firm's private equity business. Over the past decade, DLJ had the best-performing private equity funds, and Tony had been the trigger puller, its head investor. Everything we did at Blackstone, he had been doing at DLJ. In many cases, he had done it better. I invited him for dinner at my house.

Tony is tall, patrician, and reserved. He had grown up in a wealthy suburb of Boston and gone to all the best schools. He had spent most of his professional life at DLJ, but since its acquisition by Credit Suisse, he had become frustrated. I could empathize, having gone through a similar experience when we sold Lehman. He didn't like the new hierarchy and bureaucracy. His record at DLJ was remarkable, but he didn't boast. He laid out the facts, what he had done, why and when.

Over the next few weeks, we had a succession of meetings and meals. Getting to know each other went well beyond the usual hiring process. I knew this decision was going to be the most important hire I ever made. We kept talking about interesting deals, the complexities, the decisions, why we had made one rather than another, whether that had been right or wrong. We talked about deals neither of us had been involved in and how they had been handled. What did he think? What did I think? How should it have been handled? We agreed on almost everything.

I called some of my old friends at DLJ, including Dick Jenrette. And they all said the same thing, as if they had met and drawn up a script: "Tony is perfect for you, absolutely perfect. He's the smartest guy we've had here. He's a completely dedicated, loyal, hard-working person. Nobody works harder. He doesn't have a political bone in his body. He'd be a perfect complement to you. He'd never undercut you. He'd be a great, great partner." I trusted my friends, I trusted him, I trusted myself. I was done.

As Tony and I finished our discussions, I told him, "Listen, we agree on virtually everything. There's only one disagreement we'll ever have. I only like to do big things. I don't like getting diverted. I like taking on huge opportunities and making them happen. You have a different philosophy. You like doing what works. You'll do huge things and small things. You don't care as much about scale, as long as they're well constructed and you can make them work.

"You'll be unhappy with me when I don't want to do things that aren't consequential, things you know you can set up and that are going to make money. You won't understand why I won't do it. But I'm always going to want to keep our firepower for something that's worthy."

Tony joined as my partner and chief operating officer in 2002, and, as predicted, those are the only type of disagreements we have ever had. Every other aspect of running Blackstone, every personnel question, every management problem, every deal decision, every investor issue, where we go, where we do not go—we talk, we figure it out, and we always agree. It is an amazing partnership.

I'm not a natural manager, but I've improved over the years. Tony, by his own admission, is the opposite. He is a great manager. I phased him in so that our partners could get used to his style and his direction without creating the kind of resentment that proud insiders often feel toward a person brought in from the outside. First, he was chief operating officer; later he became president. It took a year of introducing him into an important role in each of our businesses. But by the time we finished, everyone understood his capabilities and accepted his leadership. In time, he was running the business, directing investments and handling the day-to-day managerial challenges of a growing organization.

When he arrived, he found a culture in need of a refresh. It had been over a decade since the sweeping changes we had introduced after Edgcomb. We had just avoided the excesses of the dot-com bubble. Despite our younger partners urging me to invest more aggressively in technology firms, I had resisted. Investors seemed to have abandoned all logic in valuing tech firms. Our investment discipline kept us from joining the herd.

There were many other great aspects to our culture. Every Monday morning, for example, all of our investment teams gathered to talk about their deals and their context, starting at 8:30 a.m. and running until early afternoon. We discussed the global economy, politics, conversations with our investors, media, any issues that might affect the business. Then we went through a list of live deals, sharing our insights and ideas from our different activities around the world. Everyone could attend. Those who had something relevant to say were encouraged to say it, whatever their age or rank within the firm. All that mattered was the quality of their thinking. To this day, Monday mornings remain the clearest demonstration of our commitment to transparency, equality, and intellectual integrity.

But our reputation as a place to work had suffered as a result of personnel turnover. Many of our partners had become complacent. Sometimes they didn't work on Fridays or refused to spend enough time training and mentoring their junior people. In 2000, I had tried to reenergize the firm by adding five new partners, all in their early thirties, to our existing twelve. Many of the support functions of the firm, from HR to compensation, weren't working the way they should and I had been too busy to fix them.

Tony started by literally breaking down walls. He took down the partitions shielding the partners' offices from the rest of the firm and replaced them with glass. Sunlight now poured in where the analysts and assistants sat. Tony kept his own door open, and he expected others to do the same. He reached out to families and invited our employees to bring their children to work to learn about what their parents did all day. He instituted 360-degree performance reviews to assess everyone at the firm. He overhauled the compensation system toward one based on group bonus pools, written feedback, and open reviews.

Knowing the machinery of the firm was now operating properly and that Tony had their backs, our people felt more confident to speak up, especially young people. The number of people now attending our Monday morning meetings made our lawyers nervous. They worried that too many people knew too much. But Tony and I refused to change what we were doing. If we started eliminating people, how would they ever absorb our investment process? Almost everyone else in finance was stovepiped: they could see only what was going on in their own narrow slice of the industry. Our Monday morning meetings allowed people from every part of the firm to see how the specialists in other parts thought and acted, and we've never had a breach in confidentiality.

A few years after we introduced the 360-degree reviews, I learned that one of our most senior people was yelling at and demeaning people, behavior I had tried to eliminate years before. I realized that I could not delegate this problem. I met privately, one by one, with the fifteen people who worked most closely with the person under review and guaranteed the confidentiality of what they told me. I wanted them to trust this process and know that by being open, they were helping the whole organization reaffirm our core values. I learned that the partner was deceitful and vindictive. I called him to my office and explained what I had done. Every single person who worked with him was scared. Given his position, I assumed he could not help himself. It must be something out of his control. I was ready to give him one chance.

"I know you're appalled by this meeting," I told him. "That's either because you've been discovered or because you're learning about yourself. But if I ever see or hear about this kind of behavior again, you're gone. Regrettably, because I don't want you gone." He did change, for about a year. But then he reverted back to his old self. We let him go.

I was never a founder who needed to hang on to power at all costs. Lifting the day-to-day management burdens energized me for the deal making I loved. Tony brought a discipline and orderliness to each of the firm's functions that we had not had previously. I knew that bringing in and empowering someone of Tony's caliber would institutionalize the firm and give us an edge to complete some of the largest deals in Wall Street history.

In 2006, Angela Merkel invited me to meet her at the German Chancellery in Berlin. We had made substantial investments in German companies, but the country's vice chancellor, Franz Müntefering, had called private equity investors "locusts" who devour companies. This began a national debate for Germany that dominated daily headlines and television news.

"I've read some things and want to learn more," said the chancellor, who, thankfully, wanted to hear the other side of the critics' argument. "They say you are locusts," and she raised her fingers above her head and waggled them like a locust's feelers.

"But I'm a good locust," I said, making the same gesture.

"But why would they call you a locust?"

I gave her the explanation I give to everyone who asks what we do. We are in the business of buying, fixing, and selling. We are managers and owners as much as we are investors. We try to improve the companies we buy and help them grow faster. The faster a company grows, the more someone else will pay for it. The perceived problems arise when we buy a company that is poorly managed and we have to fire people to make room for better ones, or change strategy. Even once we've improved the company, grown it, and hired more people than it ever had before, the people we fired tend to stay angry at us and become our critics.

Merkel told me that when she was growing up in East Germany, she had never learned about business or finance. Her father had been a pastor. She had trained and worked as a physicist. But she was a quick study. Why, she asked, aren't all companies run like private equity–owned companies? Some, I said, need access to bigger pools of capital, which exist only in public markets. A mining company, for example, has to invest huge amounts in exploration and extraction before it can earn any cash flow. As for the rest, maybe they should.

The chancellor's questions cut to a frequent debate on private equity, and one that would intensify with the financial crisis. Do investors like us help or harm the economy? The argument against us has always been that private equity is no more than financial engineering practiced by a small bunch of people far removed from the factories, shops, buildings, and labs where the real work is done. That is not us.

We step into markets when we see a dislocation. A great company hits a rough patch and needs financing and operating intervention to help it through. An infrastructure project needs capital. A corporation wants to sell a division and invest its capital elsewhere. A terrific entrepreneur wants to expand or acquire rivals, but banks won't lend to him or her. We enter these situations with financing, a strategy to transform the business, and expert operating professionals, and we invest the time needed to turn them around.

ENTREPRENEURSHIP: NO ONE TELLS YOU ABOUT THE PAIN

I once attended a meeting of student entrepreneurs at a top American university. A professor of entrepreneurship showed a slide illustrating all the steps a start-up must take, from hiring people and raising money to developing a product and going to market. His slide showed the business on a predictable, upwardly curving trajectory hitting various milestones. *If only*, I thought to myself. My experience of entrepreneurship was anything but a smooth, upward curve. It was so grueling that I have never understood the idea of people wanting to be "serial entrepreneurs." Doing it once is hard enough.

By the time the professor stopped talking and passed the microphone to me, I had decided these students needed a reality check. If you are going to start a business, I told them, I believe it has to pass three basic tests.

First, your idea has to be big enough to justify devoting your life to it. Make sure it has the potential to be huge.

Second, it should be unique. When people see what you are offering, they should say to themselves, "My gosh, I need this. I've been waiting for this. This really appeals to me." Without that "aha!" you are wasting your time.

Third, your timing must be right. The world actually doesn't like pioneers, so if you are too early, your risk of failure is high. The market you are targeting should be lifting off with enough momentum to help make you successful.

If you pass these three tests, you will have a business with the potential to be big, that offers something unique, and is hitting the market at the right time. Then you have to be ready for the pain. No entrepreneur anticipates or wants pain, but pain is the reality of starting something new. It is unavoidable.

Real companies don't just happen. Raising money and recruiting good people is very hard. Even when you are small, though, and your resources most constrained, finding the right people is the most important thing you can do. You typically won't have access to the best, who are working elsewhere at much higher compensation levels. You have to make do with the people you get. That means, at a minimum, you must reduce your criteria to a simple question: Does this person have the same zealous commitment to the mission of this business as you do?

When Phil Knight was building Nike, he hired other distance runners to work with him because he knew that whatever they lacked in terms of business knowledge, they made up for in stamina. They would never give up. They would take the pain and make it to the end of the race despite the difficulties.

When you start a company, you are usually happy to find anyone of quality willing to go on the journey with you. But as you grow, you realize that some people are like wide receivers in football with hands of stone. You throw to them, and the ball just bounces off them. Others have hands like glue. As a decent person you think your role is to coax the bad ones along, to find workarounds. As employees, these are 6s and 7s out of 10. If you keep them, you will end up with a dysfunctional company, where you do all the work, staying up all night with the few people who can make it happen.

You have two options: either run a middling company going nowhere or clear out the mediocrity you created so you can grow. If you are ambitious, you have to fill your company with 9s and 10s, and give them the difficult tasks to do.

Finally, to succeed as an entrepreneur, you have to be paranoid. You always have to believe your company, regardless of size, is a little company. The moment you start to become big and successful, challengers will appear and do their best to take your customers and defeat your business. You are never more vulnerable than at the moment you think you have succeeded.

Many founder-led companies stumble trying to make the transition from scrappy start-up to a well-managed machine. Entrepreneurs often prefer to trust their instincts rather than the more orderly systems that professional managers use. Entrepreneurs often resist any limits placed on those instincts and the energy that brought their company into existence. But eventually it is those limits that create the foundation for the next phase of growth. The turbulence of starting a firm must at some point permit systems to be implemented that allow other people to help drive the organization forward.

LISTEN FOR DISCORDANT NOTES

One Monday in fall 2006, I settled into my seat at the long conference table that fills the boardroom of our New York office. Colleagues filled every seat, even the benches along the walls. Video screens embedded in the walls showed our teams in London, Mumbai, and Hong Kong. We talked about politics, the macroeconomy, and trends in our businesses. Forty-three stories above the streets of Manhattan, these meetings always gave me the sense of manning a mission control center, navigating Blackstone through a fast-changing and uncertain environment. What I heard that morning scared me.

The discussion had turned to Spain, where we were looking at buying several blocks of condominiums. Someone said that there was now so much construction going on in southern Spain that you could move most of Germany there and still have units to spare. Developers were ignoring the basic laws of supply and demand.

As our European team laid out their concerns, a disembodied voice interrupted us. “We’re seeing the same thing in India. Raw land here is up ten times in eighteen months.” I almost choked on my coffee.

“Who is that?” I said, looking around the room. I thought everyone was connected via monitor, and it took me a moment to realize the voice was coming from a telephone speaker.

“This is Tuhin Parikh,” said the voice. “I recently joined the firm to look at real estate in India.” We had opened our India office only a year before and had made no investments in real estate there. It was a surprise to hear from him. The line had static. But what Tuhin said was so startling, I asked him to repeat it.

“Yes, Steve,” he said. “In the past eighteen months, we’ve seen land prices multiply ten times. Prices were much too high already. And now they have gone completely crazy.” India was a fast-growing, emerging economy, which was why we had decided to open an office there. But it was not growing at anything like the rate that would have justified that kind of explosion in land prices. In fifteen years of real estate investing, I had never seen anything go up ten times in eighteen months.

Even more concerning, this was just raw land. When you buy land, you are betting that you can build something valuable on it. But that could take years. You are betting that you can get the approvals you need from the government; that construction goes smoothly; that there will still be demand for whatever you build whenever you finish it; and that the economic conditions remain strong enough for you to earn a yield higher than your cost of borrowing. When land prices are skyrocketing ten times in a year and a half, you know that investors have succumbed to a kind of madness, blinding themselves to all the obvious risks.

On the spot, we decided that we would not be doing the Spanish housing deal. There were some confused looks around the table. What did land prices in India have to do with Spanish condos? In an increasingly globalized economy, you had to be able to make connections that a decade or two earlier might not have existed. Cheap, readily available credit was now virtually borderless, flowing around the world in pursuit of opportunity. If we were seeing real estate bubbles in Spain and India, chances were that it was happening elsewhere. This was no time to reach for high-priced real estate deals in overheated markets.

The following weekend, I was at my house in Palm Beach reading the newspapers over breakfast and spotted a story about Palm Beach house prices rising 25 percent. The population growth in Palm Beach could not have been more than 1 or 2 percent a year. Yet here was the local paper describing the abnormal strength of the local real estate market. As in Spain and India, the basic link between supply and demand was broken.

All my life, I have been looking and listening for patterns. It is like the old TV show, *Name That Tune*. The more songs you know, the more likely you are to be able to identify the song from just one or two notes. You become like an experienced clinician, who can tell what's wrong with a patient long before seeing the results of all the tests. The suspicions raised by that real estate meeting earlier in the week now grew into outright fears of an imminent collapse. As I sat there in the Florida sunshine, I began to have serious concerns about the risk of a global collapse.

The Monday after I returned from Florida, I opened our 8:30 a.m. private equity meeting by asking about the environment for doing deals. It was tough. There were interesting opportunities to buy companies, but the prices were far too high. "It's not like we're losing the deals by a few dollars," one of the team told me. "People are bidding 15 to 20 percent higher than our highest valuations. We're not even close."

We had been doing private equity deals for almost two decades. Either we were missing something, which seemed unlikely given our experience and expertise, or other investors were taking too much risk.

I asked what kind of deals we were looking at. When they told me we had just been approached with two deals for home-building companies, I almost jumped out of my seat.

"We're not touching housing," I said. If home builders were trying to sell us their companies, they were probably seeing what I was seeing. It would be a terrible time for us to buy.

At the 10:30 a.m. meeting with the real estate team, I said we had to eliminate any exposure to housing, not just condos in Spain, but anything, anywhere—in the United States too. Later, I instructed our credit group to reduce their positions in any real estate loans or mortgage-backed securities they might own and not buy any more. Our hedge fund team got the same directive. They listened to my warnings, and my partner, Tom Hill, the head of our hedge fund investment business, bet that the value of subprime mortgages, home loans made to the least creditworthy borrowers, would fall. He was right, and we made more than half a billion dollars for our investors.

If I had walked out of the office that morning onto Lexington Avenue, I would have seen an economy operating at full throttle. Shops were busy, the stock market was hitting all-time highs. People had gotten used to the value of their homes going in only one direction: up. Even in my own industry, all the talk was of endless growth. Our competitors kept outbidding us on deals. They saw a rosier future than we did.

Changing your behavior in the face of changing information is always hard. But when people are doing well, they don't want to change. They choose to ignore the discordant notes and the tunes you are hearing. They feel threatened by bad news and dread the uncertainty of change and the hard work it demands. This tendency makes them passive and rigid at the very moment they should be most active and flexible.

I have always regarded worry as an active, liberating kind of activity. Worrying allows you to articulate the downside in any situation and leads to action to avoid it. We had set up Blackstone to give us reasons to worry, to absorb reams of raw data, so we could develop our intelligence by looking for anomalies and patterns. At its best, worrying is playful, engaging work that requires that you never switch off.

My concerns about eliminating risk rippled across our portfolio. We did not just get out of Spanish housing; we got out of Spain entirely. The oversupply in condominiums identified by our real estate team suggested a credit bubble that could overwhelm the entire economy. No business, however robust, could compete against a systemic collapse.

Not long afterward, I was in Madrid visiting friends and had gone to look at Picasso's *Guernica*. We were about to close a giant deal to buy Clear Channel Communications, an American media company, in partnership with two other firms, Providence Equity Partners and KKR. I remember thinking as I looked at the painting that we shouldn't be doing it. Perhaps it was just being in Spain, and all the doubts I was having about its economy. Or maybe it was Picasso's gruesome subject matter, the bombing of the small town of Guernica during the Spanish Civil War. But I felt uneasy. As I came down in the elevators outside the Reina Sofía Museum, my feelings grew stronger, a physical sensation provoked by the evidence. By the time I got back to my hotel room, I had decided we had to pull out of the deal. I called Jonathan Nelson at Providence. It wasn't just nerves, I told him. It was judgment. All of us were in deal heat and eager to get something done. But if this deal went wrong, it could seriously damage our investors and our firms.

Across the firm, we were selling assets we had bought following the collapse of the tech bubble in 2001 and owned through a robust recovery. These were cyclical companies whose fortunes rose and fell based on the health of the overall economy. In 2003, we had bought Celanese, a big German chemical manufacturer, which had grown unwieldy and inefficient through multiple acquisitions. We shut the German headquarters and moved it to the United States, where it was making 90 percent of its sales. Just making it an American company transformed its multiple. By the time we sold our last shares in Celanese in May 2007, we had made nearly five times our money. It was our single most successful investment up to that point.

In 2005, 70 percent of our investments had been in cyclical businesses. By the following year, this share had fallen to 30 percent. We effectively closed shop for private equity deals, cutting our deal volume in half. I was determined that if the markets did collapse, our people wouldn't be tied up trying to clean up messes from bad deals. But of course, just as we were locking down the firm, we ran straight into a situation that embodied another of our investment principles: don't miss a can't-miss opportunity.

We weren't the only ones seeing trouble. In October 2006, we got word that our old friend Sam Zell, our first visitor to Blackstone, was thinking of selling his office property business. Since the day when we had sat on the floor of our empty office and talked, we had stayed in touch. In 1994, we bought a company from him, Great Lakes Dredge and Dock, and our real estate team in particular had watched him closely. Sam is a true entrepreneur and never one to settle for the status quo. Since the early 1990s, he had been arguing that the public should be able to buy and sell shares in portfolios of commercial real estate, the way they can with other companies. He had created Equity Office Properties (EOP) as a real estate investment trust (REIT). It was the first of its kind to be traded as part of the S&P 500 index. By the time we were evaluating it, the EOP REIT was the largest office company in the world, with over 100 million square feet in nearly six hundred properties across the United States, many in prime urban locations. Everyone in the real estate business knew it was a rare collection of assets.

Sam wanted to get out of real estate at the top. If he felt the time had come to sell, you could bet something bad was on the horizon. The only way we thought we could make a profit on the deal was to break up the company before the crash we all felt coming.

Our real estate business by this time had grown beyond all recognition. Since that first deal for apartment buildings in Arkansas, we had raised and invested billions of dollars. We had also had to apply our own culture, focused on reputation and integrity, in an industry used to very different standards.

A few years after we began investing in real estate, we were in a meeting trying to price an asset with a team leader who had come to work for us from a pure real estate firm. When I asked him for the numbers, he said, "Which numbers do you want?"

"What do you mean?" I said.

"Well, there's the set of numbers for the bank, there's the set of numbers for taxes, there's the set for when you're raising equity. Then there are the numbers you believe."

I looked at the guy. "You've got four sets of numbers? You would actually tell somebody something you don't believe? At Blackstone, we have one set of numbers. For the banks, for the limited partners, for taxes. They're what we believe. We tell them what we believe. We're not in the con job business. We do the right thing. Get out of here. And if you come back with your team, it's what you believe. That's all I ever want to see."

When he left, I said to the partner who was running our real estate group, "Where did this person come from? You train this person or else we're going to shoot him out of a cannon."

Another common practice we found in real estate was retrading. Late in a deal, after terms had been agreed, even at the closing, we found buyers would threaten to pull out unless they got a lower price. This behavior put sellers in a terrible position. To get to the table, they may have agreed to terms requiring that the deal close by a fixed deadline, or spent a lot of money in transaction costs and turned away other potential buyers. Now they would have to start again from scratch or accept the lower price.

If I had tried that as an investment banker, I would never have had a career. In corporate deals, you agree on your price, and unless something big changes, you stick with it. You don't screw around, or else no one will ever take your word again. In real estate, guys who had been in the business forever told me that it was normal to make a high bid to get the deal, then slash it at the closing. That didn't work for me. We were going to do our real estate deals to the same standard we demanded in our private equity business:

the same analytical rigor, the same discipline, the same level of trust. We might lose some deals in the short term. But in the long run, we would maintain our reputation as a firm that meant what it said.

Jon Gray joined Blackstone in 1992. By 2005, at just thirty-four years old, he was running our real estate business. He had started in private equity. But in 1995, we were bidding on Worldwide Plaza, an entire city block of mixed-use property on Eighth Avenue in Manhattan, and the real estate team needed help. We sent them Jon, who excelled in navigating a deal's complex details and helped push it to a successful close. He forged a close relationship with John Schreiber, and his prodigious run as a real estate investor began.

In the years after that, Jon developed two major insights that accelerated the growth of our real estate business. The first was to use collateralized mortgage-backed securities (CMBS) to make bigger acquisitions. CMBS were new securities. Traditionally, if you needed a loan to buy a commercial property, you borrowed from a bank or another big institution. With these new securities, a lender could package your loan with other loans into a tradable security and sell them to investors. It turned your loan into a more liquid and tradable asset. The easier it became for banks to sell their loans, the more loans they made and the less they charged us to borrow money. In practice, we could borrow more money at lower rates to make bigger acquisitions.

Jon's second insight was that public companies containing lots of properties were frequently valued at less than the sum of their parts. Real estate investors tended to be individual proprietorships or small family firms without our intellectual or financial resources. They might have accumulated lots of buildings over decades that had different uses and were in different states of repair. If you offered a good price for the whole lot at the right moment, they might take it because they did not have the people or patience to go through the entire portfolio, putting precise values on every piece of it and finding different buyers willing to pay the highest price. We had experts who could value a piece of real estate, fix it up, and then find the perfect buyer from our network of relationships. We also had the financing available to be patient. By doing all the work that other owners either couldn't or wouldn't, we could earn the difference between the "street value" of these properties and the "screen value," the value we could establish through our disciplined analysis. This increased our reward while lowering our risk.

When we appointed Jon co-head of our global real estate business, we were once again putting our faith in our next generation. He may have been short on years and experience compared to his peers at other firms, but he embodied our culture and had earned his chance. In June 2006, he closed our fifth and largest-ever real estate fund, $5.25 billion in committed capital.

As Sam Zell's Equity Office Properties deal developed, we would need Jon's leadership, our unique culture, our approach to financing, our flair for deal making, and a large chunk of that $6 billion fund. We were about to go straight into the eye of the gathering financial storm.

TIME WOUNDS ALL DEALS

Equity Office Properties was six or seven times larger than any other real estate deal ever done. This deal was so big that a miscalculation could be disastrous: we risked being stuck with buildings we couldn't sell and debt we couldn't pay. But if we got it right, the upside could be tremendous. Jon understood the pressure and moved quickly. We had to get inside the company and understand it before our competitors did, which meant we had to make a serious opening bid. On November 2, 2006, we offered a premium of 8.5 percent over the market price, and EOP opened their books to us. The whole real estate industry lit up, with various consortia of investors assembling to try to top us. Sam had what he wanted: an auction with multiple bidders.

Ordinarily in deals like this one, potential buyers will negotiate a breakup fee with the seller, meaning that the seller will agree to compensate a potential buyer for all the expense of a bid—the time and the legal, accounting, and diligence work—in case he decides to sell to someone else. If there is not much interest, the seller might agree to pay a high breakup fee to attract risk-averse buyers. But if there is a lot of interest, the seller can insist on a low breakup fee. The standard fee in transactions like this is 1 to 3 percent of the total deal size. There was so much serious interest in EOP that Sam was able to insist on a break-up fee of just one-third of 1 percent.

As the bids went up, we looked for ways to stay in the contest. The higher the price, the more resourceful we would have to be to turn a profit. We asked Sam for permission to presell properties from the company. If we could lock up buyers now for certain assets, we could feel more confident about paying a higher price for the whole portfolio. He refused. He had decided to unload EOP in its entirety, one large check for his decades of work, and he did not want us unraveling his firm before the sale was complete. We asked him to raise the breakup fee from $100 million, $\frac{1}{3}$ percent of the deal, to a more reasonable $1\frac{1}{3}$ percent, which was about $550 million, to cover all the costs we were incurring and deliver a return for our investors. He agreed, grudgingly. Just as we needed justification for a higher price, he needed to keep us at the table.

For a deal this big, we needed a lot of financing from the major banks—around $30 billion. We couldn't get a sum that large from just one bank, so we had gone to several, as is standard practice, committing them exclusively to our bid and tying up their resources. When Sam heard that other bidders couldn't get money from the banks that had agreed to lend to us, he summoned Jon to the Waldorf Astoria and explained in the most vivid terms what he would do to him personally if we locked up the banks.

Eventually almost all the other bidders dropped out. It came down to us and Vornado, a large, publicly traded real estate company owned by Steve Roth, a friend of Sam's. Jon, Tony, John Schreiber, and I met to decide whether we should just take the $550 million breakup fee and walk away or if we should stay in the competition. After all, $550 million was a good payday for our investors. But a successful deal for EOP could be worth much, much more. We decided to raise our bid to $52 per share, 9 percent higher than where we had opened, but with one big caveat. "This deal is so dangerous," I told Jon and his team, "I want to sell half of it immediately at a profit to make the price for the rest of it more conservative. I want to sell it on the day we close. I don't want any daylight. We need to execute the exact same day we buy." Everyone around the table froze. Who did that? Even thinking about doing it was surreal. But I wasn't kidding. This deal could bankrupt us.

"How are we supposed to do that?" someone said. "Sam's never going to agree to let us shop assets in advance. He already said he wouldn't let us presell the properties."

I had known Sam for twenty years and seen him in action. I knew that he wanted the highest payday possible. Now that we were so close, he wasn't going to quibble over details. Whatever he had said earlier in the process was a matter of tactics, not principle. A request like ours was essential for us and would land well within his zone of fairness.

"Go and tell him," I said. "If he wants us in this, he's got to let us presell. What does he care if we presell anyway? Give the guy a little more money, and he'll go for it."

He went for it. On the next round of bids, Vornado topped us. But our right to presell changed everything. Harry Macklowe, a New York real estate magnate, offered to buy seven prime office skyscrapers in the city for $7 billion, which would cover nearly 18 percent of our offer price. Buyers came to us from all over the country, from Seattle to San Francisco to Chicago, all hungry for pieces of Sam's empire. They didn't share our view that the market had peaked or that a thousand-year flood was brewing. They saw the breakup of EOP as a rare chance to acquire trophy real estate.

We and Vornado went a couple more rounds until February 4, Super Bowl Sunday. Vornado had bid the same as us, but with a few sweeteners. Jon got the call that we needed to improve our offer in the opening minutes of the game. He grew up in suburban Chicago and is a lifelong Bears fan. They were playing the Indianapolis Colts and the Bears' Devin Hester had just returned the opening kick for a touchdown. He had to pry himself from the television to attend to business.

On Monday morning, Jon, Tony, John, and I decided to go up to $55.50 per share, around 24 percent higher than the market price when the bidding started. Our best and final offer remained all cash, valuing EOP at $39 billion including its debt. Vornado's offer was part cash and part stock. We knew Sam's purpose in selling EOP was to get out of real estate. The last thing he wanted was stock in another real estate firm. Jon submitted our offer that afternoon. Vornado folded. We had won.

There wasn't a moment to celebrate.

I had insisted on no daylight between closing and selling a significant portion of the portfolio. Every single member of the real estate team was packed into meeting rooms waiting for this moment. They had been there for days, lining up buyers and preparing documents. Now that the deal with Sam was closed, it was time to finalize the sale of billions of dollars' worth of property. No one was going home, and no one was sleeping until we were done.

These weren't small deals. Each one of them was big, and together they were shaking the market. We had closed the biggest acquisition in real estate history, and on the same day, we were trying to pull off a series of huge sales.

The smell in the meeting rooms was overpowering. People hadn't showered for days. Messengers ran back and forth, up and down the elevators.

We closed our deal with Harry Macklowe. The timing meant that Harry bought these properties directly from EOP, without Blackstone ever actually owning them. We sold 11 million square feet in Seattle and Washington for $6.35 billion. Nearly $3 billion worth of space in Los Angeles and the same in San Francisco. Another $1 billion or so in each of Portland, Denver, San Diego, and Atlanta. We had quickly recouped more than half of what we paid at a very big profit, relative to the value we'd attributed to those properties.

And then for two days, we rested. Everyone went home, cleaned up, and slept. But throughout those two days, my mind continued to churn.

The week after we closed on EOP, I turned sixty. On my friends' birthdays, I call them and sing them "Happy Birthday." If they're not there, I leave my singing on their answering machine. My grandfather died in his forties, and I often thought I'd go early. As a teenager, I was in two near-fatal accidents in cars. In 1992, I got tuberculosis on a trip to the Middle East. Without modern medicine, it would have been fatal. In 1995, I developed phlebitis, which had killed my grandfather. In 2001, I had a 95 percent blocked artery in my heart, which was solved by inserting two stents to relieve the blockage. Every day since, I have taken an anticoagulant drug, Coumadin, that keeps me alive. Each birthday is a reminder of how glad I am still to be alive and in good health. It certainly beats the alternative.

Christine brought a great deal of joy into my life and loved organizing parties and holidays with family and friends. We decided we would mark my sixtieth in New York and make it one to remember. No cake, no toast, but a celebration with six hundred people we cared about. Christine loved dancing, so she hired Patti LaBelle and persuaded our favorite singer, Rod Stewart, to perform. My mother and father, my children, my brothers and their families, friends from high school, college, and New York all dressed up and came. It was a great night despite unfavorable media coverage, which created some controversy around the event.

As a gift, Christine put together a book of recollections from family and friends. My daughter, Zibby, recalled that in seventh grade, her school had assigned her the Communist Manifesto to read. I put aside my ideological reservations and we went through it together line by line. My son, Teddy, remembered me coming in to say goodnight, making sure the sheets were tucked in tight and shaking his entire bed for about thirty seconds. We called it the "milkshake." When Teddy played sports at school, he said his teams were often terrible, but I would still show up to watch them play, sitting down in a beach chair and talking nonstop on the phone.

As a parent, you strive for balance between doing enough at work to succeed and being there in person for your family, emotionally available for your kids. At the time, you never know if you're doing a good job. The reckoning comes years later. Looking back on the night of my sixtieth and the memories of those closest to me, I didn't think I'd done so badly.

When we came back to work, I gathered the real estate team back together in our main conference room. The cleaners had been to work, and the room smelled fresh for the first time in days. "You put in an absolutely unprecedented effort and achieved something no firm in history has ever achieved," I said. "A totally different scale. It's unbelievable what you have done. Congratulations!"

I paused to let them enjoy the moment.

"And now. We're going to do it again."

A hundred sets of eyes were staring at me.

"We need to offload half of what we have left. We'll make less money in the long run, but we'll be safer. We should aim at keeping only $10 billion worth of the best properties. At this point, we are already in the market. The market is red hot now, so let's keep feeding it. Because you know when the market's this heated, something bad's bound to happen."

Over the next few weeks, we sold the additional $10 billion. In two months, we had bought $40 billion and sold almost $30 billion, a total of $70 billion in real estate transactions in eight weeks. By the time we were done, we had managed to sell about 65 million square feet at a price of $461 per square foot. By contrast, the final cost to us of the 35 million square feet we kept was just $273 per square foot. We had acted at a scale and speed no one else in global real estate had ever done. We had reduced every bit of risk we could to protect and deliver for our investors.

LOAD THE BOAT

Around the time Sam called, we were going through another big change at Blackstone. Michael Klein, one of the heads of investment banking at Citibank, had called one Saturday morning in May 2006 with an idea. It was so exciting he wanted to tell me in person. I told him to come right over to my house at the beach. As we sat on my porch, finishing breakfast, Michael proposed that Blackstone go public.

Up to that point, no private equity firm had gone public. KKR had come closest that May, raising capital for an investment fund by issuing stock in that fund in the Netherlands. It was an innovative move. Firms like ours had traditionally raised money from institutional investors with the promise to return it after a few years. Now KKR had raised $5.4 billion from the public markets, capital they could invest but would never have to return. By going public in the Netherlands, they had also avoided some of the reporting required in the United States.

Every one of KKR's peers and competitors had studied the deal and wondered if some version of it might be right for them. Michael suggested that we go further: We shouldn't simply try to raise money for an investment fund. We should offer stock in Blackstone itself, the company that managed all these funds, as well as our businesses lines offering advisory, credit, and other investment services. This decision would be big, a transformation for the company that Pete and I had founded in 1985. A successful IPO would raise permanent capital to invest in the firm and expand our reach. If the markets turned, we would not have to worry about keeping the lights on. And it would allow our partners to sell their ownership stakes over time if that's what they wanted to do.

But there would be issues of control and ownership. We would have to open ourselves to public scrutiny. Up to now, we had enjoyed the flexibility and discretion afforded private companies. We were answerable only to ourselves and our limited partners. As a public company, if we missed earnings in a single quarter or our share price fell for any reason, we would be scrutinized, questioned, even attacked, no matter our long-term performance. We would be subject to the irrational pressures of the public markets, which can force companies into poor, short-term decision making. But if we pulled this IPO off, we would put ourselves ahead of our rivals.

I kept Michael's proposal to myself for a while as I mulled it over. Nikko had been wonderful partners for more than a decade, but in 1999, they had to sell their stake for regulatory reasons. We then sold a 7 percent stake in Blackstone to AIG, one of our most reliable investors, for a price that valued the entire firm at $2.25 billion. In 2006, Michael's calculations valued Blackstone at $35 billion. If that was true, the value of AIG's investment had risen by more than fifteen times in seven years.

When I told Tony, he was immediately supportive. He saw that we could use stock to make acquisitions and attract and retain the best people. We could reward our teams with stock in the firm rather than provide bonuses linked to their individual area of the business. This structure would reinforce our "one firm" culture. The money would give us financial and psychological comfort during the financial storm we both saw coming soon and allow us to reward Pete as he approached retirement.

The next person at the firm I spoke to about going public was our chief financial officer, Mike Puglisi. He said that we didn't have the internal systems in place to become a public company. Building them would require more work from people already stretched to their limits. If we were serious, he suggested we assemble a small team to work in secret away from our main office.

We had a lot of thinking to do about the right structure. As a private firm, we had fiduciary duties to our limited partners—the people who gave us their money to invest. These were sophisticated investors with clear strategies and long time horizons. But as a public firm, we would have an added duty to our shareholders. The limited partners were used to investing their money and waiting years while we put in the work. Public shareholders would track the value of their holding every second of every day. The interests of both wouldn't always be aligned.

Tony insisted we figure out the technicalities dispassionately and in private. He didn't want anyone getting distracted from their work by the prospect of an IPO windfall. Nor did he want to incite months of office politics and gossip. He suggested we invite Bob Friedman, our general counsel, to meet with us and Mike. I told them that I was still undecided. But if we did start to explore an IPO properly, I had three nonnegotiable terms that I believed would strike the right balance in our varying interests.

First, there could be no conflict between our duty to our limited partners and our public shareholders. Second, Pete and I had created billions of dollars of value out of our initial $400,000 investment, and I didn't want the world telling us how we should be running the company. We now had a firm that combined my entrepreneurial energy with Tony's gift for organization. Our culture was sacrosanct, and if going public risked disrupting it, we should not even consider it. Third, I knew I wanted to retain 100 percent control. In addition to ensuring my strategic vision for Blackstone as founder, I saw this as the surest way to keep the firm together and prevent it from fracturing into warring factions, the way Lehman had. If I kept the final word over people and compensation, I believed Blackstone would stay together and thrive. If we met these three terms, we could consider an IPO. Without them, we couldn't. I asked Tony, Bob, and Mike to try to figure this out in secret. If they had to reach out to people outside the firm, they should say we were investigating the idea for a portfolio company. Any leaks, I feared, would be fatal.

A few weeks later, Mike and Bob came to see Tony and me. They were smiling. To resolve the two issues of control, they found we could remain a limited partnership while issuing publicly traded units, the equivalent of stock. Outsiders wouldn't be given a vote on appointing the general partner or the board. That would be up to me. We would need to appoint independent outside directors for the audit committee. But otherwise I could keep the company united and running as I saw fit.

On the issue of prioritizing our commitment to our limited partners, the answer was even simpler: disclosure. We would tell prospective shareholders that our foremost duty was to investors in our funds. If we fulfilled that duty, the shareholders would do well. Since I would be the largest shareholder, they need not worry about my interests diverging from theirs. That alignment was more powerful than any complex legal promise. I had set some high hurdles for the IPO and was a little surprised that Mike and Bob had cleared them. It still felt like a long shot. But it seemed as if at least we should try.

I insisted we adopt the same approach we used for all of our investments. Start with an idea. Discuss it, criticize it, and question it. And only when we were as certain as we could possibly be, make a decision. There was a mountain of work. Our accountants would have to reorganize our financials to meet the regulatory standards for public companies. Our lawyers would have to restructure the entire company. We would have to draft materials for investors, get approval from the SEC, then hit the road with our sales offering. It would be a year at least.

We weren't the only ones looking at an IPO. If we were going to go public, we had to be the first. The first to hit the market would attract the most money. Everyone else would be fighting for leftovers.

I wanted us to keep running the firm as we always had, privately and quietly, while moving forward, developing the numbers and the legal structure of an IPO. Day to day, we were evaluating major deals in every sector—in private equity, real estate, alternative credit, and hedge funds. We had to retain our focus even while in the background we were reimagining our future. Mike dispatched a couple of members from his team to work with our accountants at Deloitte & Touche, while we had our lawyers working at Simpson Thacher out of sight of the rest of the firm.

Toward the end of 2006, Tony said we should start thinking about one of the hardest aspects of the process: figuring out the value of what each of us owned. Up to that point, Blackstone had been a confederation of some one hundred partnerships linked to our different lines of business. Some overlapped, some didn't; some had an expiration date, others didn't. All of the businesses were on different trajectories, most growing strongly, some flat, some occasionally shrinking. We had money either in or pledged to various funds that had yet to be invested. All of that had to be valued and assigned to the right owners. Everyone at the firm had to be considered, from me to the messengers, from senior managing directors who had been with us for twenty years to the latest class of associates, fresh out of college.

It was a monumental task, and Tony did it all, alone and in private. If anyone found out, he feared he would end up chewed to pieces. His goal was to ensure that once we had gone public and everyone's stock had vested, we had a compensation system that was transparent and competitive, benchmarked against our peers. One that would ensure the long-term health of the business. He wanted to reward past and present partners and employees, yet leave enough in the pot for generations to come. It required a lot of analysis, but also a lot of judgment, understanding what people thought and felt and smoothing out any perceived differences. He had run a similar process before at DLJ, a firm with ten times the number of employees we had. But the complexity and novelty of our situation made this task ten times harder. It was the kind of multidimensional problem he excelled at solving.

In February 2007, as Tony was deep in his calculations and our lawyers and accountants were at work, another much smaller asset manager filed to go public. Fortress was a hedge fund that also did some principal investing. It managed just $30 billion in assets, around a third of what we were managing at the time. But its IPO proved successful. There was a strong appetite in the market. Fortress's success forced us to move even faster. I could imagine our rivals now all pushing toward the same goal, to be the first of us to file. I couldn't bear to be runner-up.

We informed the SEC of our intentions, and I called Morgan Stanley to discuss underwriting. We had been relying on Michael Klein's original, arm's-length estimate of our potential market value. Now I wanted another opinion. Morgan Stanley had old-fashioned corporate finance people and had done excellent work on a couple of our debt deals. They sent over two senior bankers, Ruth Porat, who later became Google's chief financial officer, and Ted Pick. Ruth and Ted both said the deal looked great and produced some thoughtful work to support their advice.

Everything was now in place: the legal and financial structures; the internal changes and compensation plan; and the underwriters—Morgan Stanley, Citibank, and Merrill Lynch. I had written a section for the prospectus myself, titled "We Intend to Be a Different Kind of Company." I described our intention to keep the culture of the firm as it was, with our long-term perspective, our partnership management structure, and widespread employee ownership. I also promised we would put $150 million of equity into a new Blackstone Charitable Foundation to oversee our corporate giving in the years to come. "Because of the nature of our business and the long-term focus we employ in managing them," I wrote, "our common units should only be purchased by investors who expect to remain unit holders for a number of years."

As the date of our public filing loomed, I went one evening to see *In the Heights*, Lin-Manuel Miranda's first musical, before he wrote *Hamilton*. It was spectacular, I'm sure, but my mind was elsewhere. The final draft of the Blackstone prospectus had arrived just as we were leaving and I was so eager that I tried reading it in the dark of the theater. Finally I took it out into the lobby. It was 221 pages of numbers, charts, and clear, persuasive language. When I finished, I thought to myself, *What a marvelous company. I'd buy stock in a minute*.

Before we revealed our plans to the firm, I needed to talk to Pete. We had been working together for the better part of thirty-five years. We had conceived Blackstone during those long breakfasts at the Mayfair Hotel. We had endured the agony of raising our first fund, and deal by deal, we had built the firm together. Pete had been active in our M&A work from the beginning, and he was always there if I needed advice. In recent years, he had pulled back. He was writing books about his favorite cause, cutting the federal deficit, and spending an increasing amount of time in Washington where he was creating an institute dedicated to international economics. I hadn't included him in our IPO plans yet because I had always handled the financial aspects of the firm, and Pete often had trouble keeping secrets. I knew what he would say: "Really? Do you think that's a good idea?"

He listed the arguments against going public, the ones we had been wrestling with for months. The duty to shareholders and the exposure to public scrutiny. He added one more: I would now become a target, and I would hate the unpleasantness of being a public figure.

I told him he was right. Going public would give us permanent capital, stock to buy both assets and security. It would transform us into a global brand and bring us deals, new limited partners, and new opportunities. It would reinforce our "one-firm" culture even as it enabled us to develop new lines of business. Finally, because my antennas were telling me that the world was getting so crazy, we would do well to load up with cash sooner rather than later, I didn't feel we could wait any longer. If I had to become a public piñata to make this happen, so be it.

"We started this business together twenty-two years ago with almost nothing," I said. "And this is going to mean wealth for our families. It's a good economic event."

His math skills had always been good.

On March 21, 2007, the day before we filed, we held firm-wide meetings to describe what we were doing. It was a lot to absorb. The news had not leaked and people were stunned. Once we pushed the button, the financial world began to light up.

The plan for our IPO was to raise $4 billion at a valuation of $35 billion. That changed with a single phone call. One evening, soon after we filed, I was sitting at home watching *Law & Order*, reading through investment committee memos, when Antony Leung called. We had hired Antony a few months earlier to be our partner in China. He had been chairman of Asia for JPMorgan and head of China and Hong Kong for Citigroup before becoming the equivalent of treasury secretary in Hong Kong. He had relationships rather than deal-making experience, but I had a feeling about him. We settled on the idea that he start an asset management business for us in China.

I had first visited China in 1990 with my family. It was a different country then, still feeling its way toward a market economy. The roads were choked with bicycles, not cars. In 1992, when Blackstone looked at a deal in China, I was amazed to learn that there was still no national money transfer system. You couldn't write a check in one place and cash it in another. We passed on the deal. I watched China's subsequent development with increasing interest over the next decade and a half, but as a firm, we had our hands full in the United States, Europe, and Japan. Antony, who joined us in early 2007, was our first real stake in the ground.

That evening, he told me that he had just come from the board meeting of ICBC, the Industrial and Commercial Bank of China, the most valuable bank in the world. Two former senior government officials had approached him and said the Chinese government was planning to create a sovereign wealth fund, a government-owned investment fund, and wanted Blackstone to be their first big investment. They liked what we did and what we stood for. They wanted to invest $3 billion in our $4 billion IPO. We were being adopted by the world's next great superpower and hadn't even made a pitch. I went in to see Tony the next morning at 8:30, and said, "I got a whopper for you."

If one of the main reasons to go public was to load the boat with capital, more capital had to be better. Tony didn't hesitate: "Take the money." We could increase the IPO to $7 billion and use the extra cash to pay down Pete and the other partners, then invest the rest in the firm. We proposed that in exchange for their $3 billion, the Chinese take nonvoting stock for just under 10 percent of the company and hold it for at least four years, at which point they could sell their stake in thirds over each of the next three years. This strategy would align them with our own and our fund investors' interests. The deal required the approval of China's State Council and premier, both of whom, to my astonishment, took just a few days to reply. In the United States or Europe, it could have taken months or longer. The speed with which official China acted showed me that this decision was more than just financial. This had profound political and diplomatic ramifications.

We were the Chinese government's first foreign equity investment since World War II. They had come in before their new state investment company was even operational.

I was about to get my first taste of the public scrutiny Pete had warned me about. In early June, Senators Chuck Grassley and Max Baucus introduced a bill that would change the tax laws for partnerships that went public after January 2007. People started calling it "The Blackstone Tax." If it came into effect, it would force us to reexamine all the risks of going public. At best, we would have to redo all the tax calculations we had been making for a year leading up our filing. At worst, we would have to yank the IPO. But after Tony and I talked it over with Wayne Berman, our longtime government relations adviser and then vice chairman of Ogilvy & Mather, we felt the bill was unlikely to pass. And even if it did, it would be a long while before it became law. It shouldn't hold us up.

A few days later, John Sweeney, the head of the AFL-CIO, wrote to the SEC demanding it hold off on our IPO until the union had investigated the treatment of employees at our portfolio companies. The SEC then chimed in themselves, saying that they were changing the accounting rules so our restructuring to go public would look more like we were buying a new company. That would lead to substantial new costs.

The SEC said that the way we were swapping our employees' interests in all the different Blackstone partnerships and entities into shares of a single firm looked as if we were buying them out. This wasn't a buyout. If we were buying them out, I'd know about it, as I'd have written the check. The owners were still the owners of the firm. What the SEC was doing made no sense to me, but they made it clear that they had the last word.

There was more. Senator Jim Webb of Virginia challenged the Chinese taking a stake. Although we had ticked every legal and regulatory box for foreign investments, he said the stake might pose a threat to national security. His challenge went nowhere.

As we fought these political wildfires, we still had to sell the Blackstone story to potential investors. The way this process typically works, which Wall Street refers to as a "road show," is that a team of senior managers goes out and pitches investors one by one or in small groups. We decided to do ours differently. We wanted to hit the world all at once. We hit the cities home to major investor accounts together—New York, Boston, and other cities—and then split up. Tony led the team for Europe and the Middle East. Mike Puglisi, our CFO, took Asia. I handled the largest accounts in the United States and Tom Hill and Jon Gray took the smaller ones.

At the first event I did, at the Pierre Hotel on Fifth Avenue in New York, we filled the ballroom as well as several overflow rooms where people could see me on video screens. Balloons everywhere added to the circus atmosphere. As I began my presentation, my cell phone rang. It was Zibby, my daughter, calling from the hospital. I had just become a grandfather of twins. It seemed like I had just been helping her with her elementary school homework by slithering across her bed to show her how glaciers moved and sending her postcards every day she was at summer camp. I left the stage to Tony and went straight to go see her. So much for a carefully choreographed launch.

The hoopla followed us to Boston and then to Chicago. Investors didn't seem to care about the issues in Washington. Within days, Morgan Stanley said there was more than enough demand to issue more stock.

As I was in Chicago riding to an event, one of Tony's team called to tell me that Tony had been taken to the hospital in Kuwait. He was in excruciating pain, but the doctors hadn't figured out what it was. I called David Blitzer, our senior partner in London, and told him to drop everything and fly to Kuwait. Rent a plane if necessary. Just make sure Tony was being taken care of. The road show could wait. I called Tony's number, and to my surprise, he picked up.

"I'll be fine," he said, phlegmatic as ever. "Don't worry."

"Tony, I'm sending Blitzer. I don't want you straining yourself for a road show."

"Steve, I don't need that. I'm telling you, I'm fine."

But he didn't sound fine. I phoned David again. "Just tie the guy down," I said. "I don't want him hurting himself."

David was on the first plane to Kuwait, but by the time he got there, Tony had checked himself out of the hospital. The doctors had diagnosed a large kidney stone, agonizingly painful but not life threatening. It still hadn't passed through his system, but Tony had been discharged with a box full of syringes filled with morphine so he could numb the pain while he waited. He was determined to press ahead.

With Blitz now in support, they finished their presentations in Kuwait, then moved on to Saudi Arabia and Dubai. Tony refused the morphine, preferring to gut through the pain. It was torture for him, but over the course of those three days, he never missed a meeting. In Dubai, he checked himself back into the hospital, and then when he was ready, he chartered a plane to fly him and his team back to London.

Just as I was about to relax, I got another call. There was a problem with Tony's plane. One of its engines had failed over Iranian airspace, but the pilot hadn't filed for permission to fly over Iran. His manual told him to make an emergency landing at the nearest airstrip, but he didn't like the idea of putting down in the middle of the night somewhere in Iran with a plane of Americans who had been flying through Iranian airspace without permission. The other option was to press on to Athens on one engine and hope they could make it. Tony, lying on a cot in the back of the plane still in awful pain, urged him to try.

Now I had visions of my colleagues and friends crashing or making an emergency landing in Iran, which was led at the time by Mahmoud Ahmadinejad, who hated the United States and Israel. He believed that the United States planned the 9/11 attacks as a pretext for the war on terror and that the Holocaust was a myth. We all agreed that the pilot should fly on to Athens. The plane just made it on the single engine. Tony and team took another charter to London and completed a full day of meetings before finally flying back to New York. Upon his return, Tony admitted in his understated way that even he had been rattled. "That was a tough trip," he said.

By the middle of June, we had done only half the presentations we had planned, but the IPO was oversubscribed by fifteen times. We priced the offering at $31, the top of our expected range, and increased the number of shares we put out to market. On June 24 we sold 133.3 million shares and raised more than $7 billion, including the investment from China. It was the second largest IPO of the decade after Google.

The night we priced the deal, I went home to an empty apartment. Christine was traveling in Africa with her daughter, Meg, and her nephews and nieces. I was drained. I took a hot shower; changed into jeans, a polo shirt, and slippers; and slumped down in a chair with my dinner on a tray. I turned on the television, and to my horror, there I was. The channel had been left on CNBC. I was too tired even to change it, and just sat there, mesmerized, staring at myself, wondering if I was ever going to escape this IPO madness.

The *New York Times* wrote that the stock had "an almost Google-like mystique," and observed that all the challenges that would have derailed many market debuts hadn't affected us. "The Blackstone juggernaut kept going," the journalist wrote. The morning of our first day as a public company, I could have gone down to the stock exchange to ring the opening bell but asked Pete and Tony to do it without me. Instead, I went to the office and sat in my conference room alone.

It was strange to feel this way at what should be a high point in any entrepreneur's life. In the early 1990s, we had seen the opportunity to buy real estate when prices were at historic lows but been restricted by our lack of funds and our investors' anxiety. Their irrational fears had held us back, and we had missed opportunities while we raised the money. We weren't going to have the same problem now. We had plenty of capital in our investment funds locked up for years, and the money we raised through the IPO meant we could keep investing in our business to ensure we had the people and resources to pursue the most attractive opportunities wherever and whenever they arose.

That day, there wasn't the usual hum of activity around the office. The corridors were empty, the whole place hushed. I turned the TV to CNBC to watch the market open. "Good morning. Today we're bringing you all-day coverage of the Blackstone IPO." I stared at it for an hour, semicomatose. There I was again, inescapable. I couldn't even remember doing the interviews they were showing. I shut it off. It was nuts, an absolute blur. I thought I had understood what I was getting myself into. But I had no idea.

Soon after we went public, we received a call from Bennett Goodman, co-founder of GSO Capital Partners. Ever since Tony had joined Blackstone in 2001, he had been interested in expanding our relatively small credit business. For several years, we had tried to recruit Bennett's group from DLJ but were turned down. But after the IPO, Bennett called to say he was ready to merge GSO with Blackstone. He and his partners were stunned by how rapidly we were growing, as well as the breadth of our relationships. They thought they might be able to supercharge GSO's growth by teaming up with us, and as it turns out, they were right. By merging, we created one of the largest credit platforms in the alternative asset management business, and GSO ultimately grew more than fifteen times in the decade following the IPO.

SPRINTING DOWNFIELD

BE A FRIEND TO THE SITUATION

By the time we became a public company, the market's nerves were beginning to fray. In February 2007, Freddie Mac announced that it was no longer buying subprime loans, the mortgages given to less creditworthy borrowers who had pumped up the housing market. Mortgage lenders that specialized in subprime lending were increasingly in trouble. Their problems would eventually infect the entire credit market.

Several weeks later, I got a call from Jimmy Cayne, the CEO of Bear Stearns. He needed help. Two of his hedge funds were in trouble, and he wanted an outside opinion. I sent over a couple of our people who understood these funds. They returned with troubling news.

The first fund had bought only securities collateralized by subprime mortgages. These weren't publicly traded, so it was hard to determine their value. As people started defaulting on their mortgages in increasing numbers, you could assume these securities would plummet in price and no one would buy them. Yet under the terms of the fund, investors could withdraw their money once a month.

You couldn't make this up: an opaque and fast-depreciating fund that was still promising monthly liquidity to investors. The second fund was the same as the first one, but with leverage: if the first fund was broke, the second was astonishingly broke.

I called Jimmy and told him the funds were going to blow up and there wouldn't be any equity for investors. I advised him to take the hit and write the investors a check to cover their losses. This concession was not necessary from a legal perspective, but it would be less expensive than the hit to Bear Stearns's reputation from the failure of these two ill-conceived funds.

"I love you, Steve," said Jimmy. "But what the hell are you talking about? I'm not writing any checks. This game is for grown-ups. We've got a prospectus. People take risks. Sometimes you win, sometimes you lose."

I told him that such logic did not apply to a firm as big as Bear Stearns, with so much else at stake. He had its broader reputation to think about. His best brokers had recommended this product, under the supervision of Bear Stearns's president. If the funds collapsed, the firm's sales force would be damaged. If investors felt mistreated, he had to make it up to them or risk the failure contaminating the entire company and the livelihoods of thousands of employees.

"I don't have to write a check to anybody," he said. "This is the way markets work."

"I don't know about markets," I said. "But there are times when you just have to stand up and write a check. You have to show customers that you own this, because if you don't, they're not going to trust you ever again." I had felt the pain of this dilemma after our experience with Edgcomb, I had made sure we paid back the banks that lent to us. It would have cost us a lot more to earn back their trust on later deals if we had not made them whole right then.

At Blackstone, our adrenaline was still pumping after the EOP deal and the IPO. Stock prices continued to rise, with most investors still locked into their position of psychological comfort, refusing to absorb the changes, draw conclusions, and act based on the negative data in the credit markets. But as we saw the coming dislocation in markets getting closer, we got ready. Many people make the mistake of thinking the moments when markets collapse are the moments of highest risk. They are the opposite.

Entering the crisis, Blackstone had $4 billion in cash from the IPO and a $1.5 billion revolving credit line to draw on if we needed it. As a fundamental operating tenet, Tony and I had insisted on having no net debt. It was part of our aversion to risk. We had more than $20 billion in committed funds locked up for ten years, so we could ride out a storm without worrying about a run by our clients on their money. Thanks to our strong capital position, we were open for business, but our disciplined investment process kept us out of another major deal that would eventually become a financial disaster.

Between the late 1990s and early 2000s, we had begun taking a harder look at the US energy sector when we saw two forces changing the industry. The first was steady deregulation, which was driving more and more of the energy industry into the hands of smaller, private firms. The second was the collapse of Enron, which forced many companies to sell assets, from drilling rights to refineries to pipelines, at low prices under financial duress.

We had started modestly and spent years building up our knowledge, experience, and relationships so that we could maximize our rewards and minimize our risks over the course of multiple turns in the cycle.

In 2004, we had partnered with three other private equity firms, Hellman and Friedman, Kohlberg Kravis and Roberts, and Texas Pacific Group (TPG), to buy Texas Genco, a set of power plants in Texas. A year later, we sold the company and split a gain of around $5 billion on our equity. It was one of the most profitable private equity investments ever made. The source of our profit was the rising price of electricity, which regulators had pegged to the price of natural gas. Texas Genco produced electricity mostly from much cheaper sources, coal and nuclear, so as electricity prices went up along with the price of gas, so did its profits in greater proportion. KKR and TPG went back to that trough in 2007 for a much bigger deal, offering $44 billion for TXU, another Texas power company. I asked David Foley, the head of our energy fund, why we were missing out.

I had recruited David out of business school. He had had no background in energy when he launched our first fund, but he had immersed himself in the industry. He talked the investment committee through the math of the TXU deal and explained why it made no sense. Energy, like real estate, is an industry dictated by cycles. As an investor, you have to understand that the troughs can be deep and long, and you cannot get carried away when the markets peak. The buyers of TXU were borrowing over 90 percent of the $44 billion purchase price, which left them little margin for error. They were betting that the price of gas, and thus the regulated price of electricity, would remain high. In that scenario, they would have years of strong profits, on the difference between the high price of electricity charged to consumers and the low cost of producing it from their coal-fired power plants. But if gas prices fell, so too would the price of electricity for consumers. TXU's owners would be stuck selling electricity for dwindling profits and struggling to service their debts. David was emphatic that we shouldn't put in a bid.

It took a little while to play out, but by 2014, TXU was bankrupt, producing electricity from coal as the price of natural gas and electricity collapsed. Investors had been caught buying at the top of a cycle and paid a heavy price.

It was just as we were passing on most of the deals in the marketplace that Steve Bollenbach, the CEO of Hilton, called us. A few months earlier, we had looked at his company and made an offer, which Steve had rejected. But now he was ready. He wanted to retire, and a sale would be the capstone on his career, both financially and personally. And perhaps like Sam Zell, he saw that if he hesitated now, he might have to wait years before the market rebounded.

We had been buying and selling hotels since 1993, from chains like La Quinta and Extended Stay in the United States to the Savoy Group in London. We knew when to buy them and how to operate them. We also understood labor relations, a big part of owning hotels. Hilton had interesting domestic and international businesses. For years, the two had been run separately. They had recently been reunited, but the stitches holding them together were still fresh. The domestic business was headquartered in Beverly Hills. Its properties were aging, not having been renovated as frequently as they should have been. Costs were being duplicated across four separate divisions, and Hilton's margins were smaller than those at its competitors. Its managers seemed to have lost a step. Their corporate offices closed on Fridays at noon. And to top it all off, they kept an expensive fleet of corporate airplanes. We could see a lot of ways to increase value.

The international business, headquartered in London, was even more intriguing. Hilton International, we believed, was the Rip Van Winkle of the hotel business, fast asleep while the world boomed around it. It had not added any new properties in twenty years and had barely cracked the fast-emerging markets of China, India, and Brazil. Anyone could see that international business and tourist travel was growing as emerging economies became richer. Hilton was one of the most recognized brands in the world, up there with Coca-Cola. If it got this right, its runway looked endless. It already owned some of the best hotel properties in the world: the Waldorf-Astoria, the Hilton New York, the Hilton Park Lane in London, the Hilton Morumbi in São Paulo. Add all these individual properties up, and they were worth far more than the market cap of the whole firm. Combining Hilton's domestic and international businesses, though, had done little to wake either business from its slumber. They missed opportunities to grow, and the stock price had languished.

Based on our analysis, Hilton would cost $26 to $27 billion, after we'd just invested over $10 billion, net of all our sales, in EOP. But the way we looked at it, Hilton was already throwing off $1.7 billion a year in profit. If we could get that up to $2.7 billion through better management, organic growth, and selling noncore assets, we could offer more than our rivals and still make more money. But if EOP had been the hare, a deal done at breathtaking speed to maximize value in a white hot market, Hilton would be the tortoise, requiring years of diligent work.

One of our first steps was to recruit Chris Nassetta, then CEO of Host Hotels and a longtime friend of Jon Gray, which owned Marriott among other chains. Chris is a master of his craft. If anyone could improve Hilton, he could. His promise to join as CEO if Blackstone won boosted our confidence. There were still risks, of course: another major terrorist attack like 9/11 freezing travel; an international virus like severe acute respiratory syndrome (SARS). But if the whole world had to stop traveling, we would all have bigger problems.

Even contemplating Hilton after EOP felt like finishing one Olympic final, then lining up for another. But you don't get to choose the timing of these moments. You just have to be ready. We offered a 32 percent premium over Hilton's stock price, and Bollenbach accepted, barely two weeks after we went public. We invested $6.5 billion in equity from Blackstone funds and co-investors and borrowed $21 billion from more than twenty lenders. We now had to chew our fingernails until we closed.

Bear Stearns led our group of lenders for the Hilton deal. While we waited to close, the hedge funds I had discussed with Jimmy Cayne imploded. Bear lent the two funds $1.6 billion to keep them going, but by late July, there was nothing more to be done. The funds were forced into bankruptcy.

On August 9, the French bank BNP Paris halted redemptions from three of its funds, which were invested heavily in subprime American mortgages. They said there was no liquidity left in the market. That same day, Countrywide, America's largest originator of mortgages, filed its quarterly report with the SEC, citing "unprecedented market conditions." Within days, it was drawing down its credit lines and two weeks later accepted a $2 billion investment from Bank of America to keep the lights on.

Around this time, I got a call from Jimmy Lee. He told me I couldn't tell anyone, but for three days, JPMorgan hadn't been able to roll over its commercial paper. These are the loans that corporate America lives on, the most liquid kind of debt, used to run their operations. It's the closest debt gets to cash. And it wasn't just JPMorgan. Bank of America and Citi couldn't roll theirs over either. Jimmy told me they had sorted it out by offering extra protections to the other banks and institutions that lent to them. But if the biggest banks in the country had to hustle to get short-term loans to pay their bills, this problem had gone way beyond subprime mortgages.

We closed Hilton on October 24, almost twenty years to the day since we had closed that first Blackstone fund on the eve of Black Monday. We had once again come in just in time. The same day, Merrill Lynch announced a quarterly loss of $2.3 billion. Citi later said it was writing down $17 billion of mortgage holdings. By the first week of November, the CEOs of both firms, Stan O'Neal at Merrill and Chuck Prince at Citi, had resigned. The entire financial system was entering cardiac arrest.

Starting in late 2007, I received an unusual crash course in the foundations of the financial crisis by attending a series of lunches at the Federal Reserve Bank of New York on Liberty Street. Hosted by Tim Geithner, then head of the New York Fed, they often included Ben Bernanke, chairman of the Federal Reserve; Hank Paulson, secretary of the treasury; the CEOs and chairmen of New York's biggest banks; Larry Fink of BlackRock; and me.

For all I knew about finance, what I learned at these lunches astounded me. I knew that Fannie Mae and Freddy Mac, the two government-sponsored mortgage giants, bought and securitized half the residential mortgages in the country, to the tune of around $5 trillion. What I didn't know was that they were nearing bankruptcy. It was a given to everyone else in the room, but it made my jaw drop.

There were two chronic problems in the system. First were subprimes. For years now, the market for mortgages had become more liquid, thanks to securitization. Since the 1980s and thanks to people like Larry Fink, mortgages had been packaged and bought and sold like other securities, such as stocks and bonds. Successive administrations had been pressuring banks to make more loans to people who could not previously afford to buy their own homes. Many politicians considered home ownership the first step toward fulfilling the American dream. This combination of financial innovation and political pressure led to new kinds of mortgages requiring low to zero down payments, or ultralow interest rates for the first few years. Poor regulatory oversight led to unscrupulous lenders that took advantage of borrowers by offering loans without insisting on the proper documentation, such as proof of income or assets. The increase in the number of buyers pushed up the price of homes, causing the market to overheat. In the mid-1990s, subprime mortgages had made up 2 percent of the entire US mortgage book. By 2007, they were 16 percent. You didn't have to be a genius to see that if the economy tipped into recession or home prices fell for any other reason, a housing market fueled by subprime lending would collapse.

The second chronic problem had been created by regulators. Technically, the problem was a regulation, FAS 157, that had been intended to ensure so-called fair value accounting. The problem was that it was neither fair, nor did it lead to the proper accounting of value. One of the most important lessons from the collapse of Enron in 2001 and then the telecoms giant WorldCom in 2002 was that companies could obfuscate what they owned and what they owed. They could use accounting tricks to pump up the value of assets and hide liabilities. The solution, said a group of influential academics, was more transparency. If everyone knew everything all the time, we wouldn't have scandals like Enron. Marking assets and their liabilities to their market prices every day was considered the cure-all to corporate chicanery.

What made sense in theory, though, made no sense in reality. Imagine owning a stock. You buy it for your retirement, which is still twenty years off. You buy ten shares at $100 each. The price of the stock rises to $120, then falls back to $80. But you don't care, because you have a twenty-year horizon and you consider the stock a good long-term investment. All it means is that the numbers on your quarterly statement change.

But what if every time the stock rose or fell, you received a check for the difference in any increase or had to write a check to cover any shortfall? And furthermore, you had to inform every single one of your creditors, from your mortgage lender to the company that lent you money to buy a car, and they reassessed your creditworthiness based on this new value? You would be working on a twenty-year horizon, but they would be evaluating you on what happened today, holding you accountable for the latest shifts in the market.

In the late 1930s, the US government, scarred by the Great Depression, prohibited mark-to-market accounting. They saw that in any normal year, almost any asset class, including stocks and bonds, will go up or down by 10 to 15 percent. In a boom or crisis year, it could be even more. It would be terrible for the health of the economy if companies acted like Chicken Little, constantly rebalancing their assets or liabilities based on that day's movements in the markets instead of coolly managing for the long term.

During the second half of the twentieth century, it was typical for a bank to borrow twenty-five times its equity to lend money to customers. If it could lend at a higher interest rate than the one at which it borrowed, it could make a profit. Since successful banks tended to be good at lending, choosing customers who would pay back what they borrowed, regulators didn't require them to hold a lot of emergency cash. If there were an emergency, though, the answer would not be to demand they unload all their assets in a fire sale to raise cash.

I had started my career in finance in 1972 and watched in 1975 as the Federal Reserve and the Comptroller's Office managed twin crises in real estate and shipping loans. They didn't force the owners of troubled loans to mark them to market. Instead they gave them time for the loans to recover or to be charged off quarter by quarter over several years. That's how real life works. If you're faced with a problem, you don't panic and declare immediate catastrophe. You call for quiet and give everyone time.

FAS 157 required the opposite. In the name of transparency, it made the balance sheets of financial institutions look insanely volatile. Portfolios of assets that had been built up to be held over long durations now had to be priced when their values were collapsing. Institutions were required to hold more cash at the moment when cash was scarce. The combination of irresponsible subprime lending and FAS 157 was leading to the market's hysteria and driving the banks to insolvency.

In early 2008, I had dinner with John Mack, the CEO of Morgan Stanley. He was miserable, having just reported a quarterly loss of $7 billion. How had he managed to lose so much money? He hadn't, he said. It was all on paper. He had portfolios of subprime securities dating back four years. The underlying mortgages on the securities for 2004 were defaulting at a rate of around 4 percent, for 2005–2006 at 6 percent, and for 2007 around 8 percent. But the market for these securities, even with default rates below 10 percent, had evaporated. No one would buy them. Fewer than one in ten Americans were defaulting on the mortgages backing these securities, yet they were considered untouchable. Under Sarbanes-Oxley, the financial reform act introduced in 2002 to protect investors after the accounting scandals at Enron and WorldCom, you couldn't take the risk of misrepresenting the value of any assets. So John had brought in BlackRock to value its portfolio. They estimated the loss to be somewhere between $5 and $9 billion. He simply split the difference, reporting a vastly larger loss than the value of the securities that were actually defaulting. And suddenly everyone was panicking about the health of Morgan Stanley.

At Lehman Brothers, my old employer, the problems were piling up even more. Its CEO, Dick Fuld, and I had come up together in the early 1970s and both became partners in 1978. Dick had been a C student at college, where he spent most of his time skiing and partying. He then earned his MBA at New York University. Dick would joke that the only reason Lehman appointed him CEO in 1994 was that all of the smart guys had left while he had stuck around. We weren't close, but we saw each other at different public events and had dinner with our wives perhaps once a year.

Sadly, people inside Lehman rarely saw the warm, self-effacing side of him. Dick was an autocratic leader, feared more than loved. And by 2008, he had put his company in a tough spot. That spring, my real estate team saw that Lehman's real estate portfolio was in a mess. They were holding a large block of bad mortgages alongside some good residential assets, such as Archstone, a major investor in apartment buildings. They owned a lot of commercial real estate they had bought but failed to sell before the crisis bit. Now the debt on those commercial properties was putting pressure on them. In a healthy market, the total portfolio might have been worth $30 billion. But the buyers had fled and values were impossible to estimate. We offered $10 billion to take it off Lehman's hands. We could be more patient about selling the assets over time. Dick turned us down. He preferred to stagger on than to take the hit to his equity.

Shortly afterward, on March 16, JPMorgan, under government orders, agreed to buy Bear Stearns. Now all eyes were on Lehman, wondering if it would be next. Dick was looking for a buyer as the deepening crisis in mortgages made his task ever more difficult. And despite the way he joked about his improbable ascent at Lehman, he had a strong, sentimental attachment to the firm. He struggled to accept how little it was now worth. In early August, Dick told me that out of his $675 billion of assets, around $25 billion was linked to bad real estate loans. The remaining $650 billion was healthy and making plenty of money for the firm. So why not separate the two? I suggested. Call the $650 billion "Old Lehman" and let it carry on, uncontaminated by the real estate book. Then move the $25 billion pool of assets into a new firm, Lehman Real Estate, and give it enough capital to survive the cycle. It might take five years, but real estate would come back. It always does. Shareholders would still own 100 percent of the assets in both firms, but their risks and rewards would be decoupled to take account of what was happening to real estate. The government would likely have no objection if this split lifted some of the uncertainty Lehman was inflicting on the markets.

Dick liked the idea and asked if Blackstone would buy a couple of billion dollars' worth of Old Lehman if he executed the split. With the appropriate diligence, I said yes. But our discussions were proceeding slowly. Worry paralyzed Dick. His quarter was due to end on September 30, when he would be required to mark down his real estate assets to their current value. In the end, his agonizing meant we ran out of time to complete the diligence, file a proxy, and get the SEC to accept the split we'd discussed. I felt terrible for him. He had been out there trying to sell his company and haggling over price when price wasn't the issue. Short sellers were punishing Lehman's stock. If Dick had been able to create two separate securities—one for real estate, one for the rest of Lehman—he could have saved the firm. The financial meltdown would have continued, but good Lehman would have been cordoned off. Instead, Lehman became the largest bankruptcy in US history, and Dick an emblem of all that went wrong.

Lehman went bust on Monday, September 15. The next day, money market funds, normally viewed as a very low-risk investment and virtually equivalent to cash, dropped in value for the first time in recent memory. Every dollar invested in one of these funds fell to 97 cents. On Wednesday, September 17, the yield on Treasury bonds turned negative. People were so panicked they were now buying government securities knowing they would take a loss. It just seemed safer than any alternative.

Thanks to the IPO and vigorous fundraising leading up to the crisis, Blackstone was in a strong financial position. But the week Lehman went down, I called down all of our bank credit lines. Before I hunkered down for what was bound to be a nuclear winter, I wanted all the cash we could lay our hands on. There would be a lot of people in trouble and trying to sell. I was determined that we would be ready to buy.

At 3:30 p.m. Wednesday, September 17, Christine called.

"How has your day been, dear?" And as usual, she asked, "What do you feel like having for dinner?"

"My day has been terrible," I said.

"Oh, I'm sorry . . . why?"

"Well, everything's collapsing. Treasuries have a negative yield. Mutual funds have broken the buck. Companies are drawing down their bank lines. The whole financial system is going to collapse."

"That's awful," she said. "What are you going to do about it?"

"What am I going to do about it? I'm drawing down my bank lines."

"No, I mean what are you going to do to stop the whole thing?"

"Sweetie, I don't have the ability to stop it."

"Do you think Hank knows all of this?"

"Yes, I'm sure he knows."

"How do you know he knows?"

"Because if I know about it, he knows about it. He's the treasury secretary."

"But what if he doesn't actually know? And he does nothing and the system collapses?"

"It's not possible that he doesn't know," I said.

"But what if he doesn't and you could have done something, like warn him? I think you have to call Hank."

"Sweetie, I'm sure Hank's in meetings. It's a crisis. He's not reachable."

"What's the harm of trying to call him?"

"But it's a ridiculous call."

"But you should call him."

By now I'm realizing that I'm never going to get off this call unless I agree to phone Hank.

"Okay," I said. "I'll call him."

"Oh, by the way," Christine added. "When you call him, you ought to have some solutions to help him. Also, we're having your favorite—curry!"

I called.

"I'm sorry, Mr. Schwarzman," said Hank's assistant. "Secretary Paulson's in a meeting." That was hardly a surprise.

"Here's my number," I said. "Please tell him I called."

An hour later, quite unexpectedly, he called back. When Hank had been chairman and CEO of Goldman Sachs, Blackstone had been a major client and sometimes a competitor of his. I had always found him intelligent, logical, determined, tough, and fair with a deep understanding of finance. He was a very good listener as well as having excellent sales abilities. Most important, he was highly ethical, someone to trust.

"Hank," I said, "how's your day?"

"Not good," he said. "Whaddya got?"

Throughout the crisis, Hank and his team were in constant communication with senior financial executives across Wall Street like me in an effort to develop real-time knowledge of what was happening. We were closer to the markets than he was by virtue of the companies we ran. I knew he would appreciate honest, straightforward observations and advice.

I told him companies were drawing down their bank lines, and at the rate things were going, the banks were going to fail. There was a good chance they wouldn't be able to open for business on Monday morning.

"How can you be so sure of that?" he asked.

“Because this panic is gaining such momentum that it’s all going to be over.

“You need to stop the panic,” I said. I described the situation like an old Western movie, where the cowboys had just come into town after a cattle drive. The cowboys are drunk, shooting their guns in the streets. The sheriff was the only one who could stop them. Hank was the sheriff. He had to put on his hat, pick up his shotgun, walk out into the street, and shoot straight into the air. That’s how you stop a panic, I told him. You freeze the mob in their tracks.

“And how do I do that?” said Hank.

“First, you need to eliminate the ability to short financial stocks,” I said. People might say it’s bad policy, but it would signal to people that the rules of the game are no longer reliable. Every hedge fund and short seller trying to make money by driving down bank stocks would worry what the Treasury was going to do next.

“Okay,” said Hank. “I like that. What else?”

“Credit default swaps,” I said. People were putting pressure on financial institutions by effectively buying insurance in the hope that banks would default on their obligations and collapse. Hank should make these credit default swaps nonactionable.

“That’s a great idea,” he said, “but I don’t have the legal ability to do that. What else?”

I had learned that since Lehman filed for bankruptcy earlier in the week, investors were frantically trying to move their brokerage accounts over to the one bank everyone thought would survive: JPMorgan. They were closing their accounts at Morgan Stanley and Goldman Sachs, pushing these institutions toward failure, while JPMorgan was struggling to process all the requests. I suggested that Hank stop allowing people to transfer their accounts.

Again, he did not have the authority. “Anything else?” he said.

More than anything else, I told him, the market needed to be reassured that the system wasn’t going to collapse. The only way to stop the panic was for someone to show up with so much money, such brute force, that it shocked the market into submission. That someone had to be the US government. That would stop all the dysfunctional behavior. And Hank needed to do this tomorrow.

"If you don't announce tomorrow, it'll be too late. The banking system will collapse and you won't be able to open the banks on Monday," I said. This was on Wednesday at around 4:30 p.m.

"I don't trust the system anymore." I said. "In the last few days I've witnessed the downfall of Lehman and Bank of America saving Merrill Lynch through a last-minute merger. AIG would have gone under yesterday had it not been for your intervention, and Fannie and Freddie had to be bailed out in August. Nothing is sacred. Everyone believes the same thing. You've got a financial system that won't be able to survive this level of mistrust. You need this large pool of capital to give people confidence that the system won't collapse. It's all happening so fast that every hour you wait, the more money you're going to need. You have to announce it tomorrow, the earlier the better."

"Are you going to be around for the next hour or so?"

"Sure. The world's ending. Where else do I have to go?"

I later learned that Hank was already working to persuade the SEC to put a moratorium on short selling. But as for the rest, the Treasury needed congressional approval to intervene at the speed and scale now required. For months as the crisis deepened, Hank had considered asking for that approval but feared that a Democrat-controlled Congress would refuse to hand so much power to the Republican-controlled executive. On the night Lehman failed, there was no longer any choice: Hank and his team had to act. They decided to ask for what they needed.

On Friday, President Bush announced from the Rose Garden that the treasury secretary had asked Congress to appropriate emergency funding of $700 billion to stem the crisis. The legislation was called the Troubled Asset Relief Program, or TARP. I wished it were bigger, but $700 billion was pretty big. It would probably be enough to stop the madness. That same day, the SEC also banned short selling.

That should focus people's attention, I thought. The shorts and others busy exploiting the chaos now had to ask themselves whether they wanted to be in a game where the government was playing against them, where the government would put anything on the table in order to protect the system. Once Congress passed the TARP, we would be on the road to survival.

Ten days later, on September 29, I was in Zurich, Switzerland. I had just checked into my hotel and turned the television on to watch the House vote on the TARP legislation. I saw the votes coming in, 228 to 205 against the program I thought could save the country. Not enough Democrats voted for it, and the Republicans killed it. The panic was going to start all over again.

I sat there wondering how this could have happened. At Congress's request, Hank's team had prepared a three-page outline of the TARP legislation soon after it was announced, with the expectation that it would be fleshed out into a much fuller document. Their critics, though, portrayed it as an inadequate, entitled approach to securing and spending $700 billion of taxpayer money. As Hank wrote in his memoir, *On the Brink*, "We were pilloried for the proposal—not least because it was so short, and hence appeared to critics as if it had been done offhandedly. In fact, we'd kept it short to give Congress plenty of room to operate."

The eventual hundred-plus page of TARP legislation arrived in a challenging political environment. We were only five weeks from the presidential and congressional elections. Politicians were staking out their territory. The vote to reject it reflected ideological rather than national interests.

I was so freaked out I called Wayne Berman, our government relations advisor. As an insider's insider, I hoped he might have some thoughts on what could be done to save the situation.

"Wayne, we must get the TARP passed," I said. "It's the survival of the system. We can't let it get bogged down in some horrible political mess." I suggested we assemble all living US presidents—Jimmy Carter, Bill Clinton, and George H. W. Bush—to deliver a national address on television urging Congress to pass the TARP legislation. Wayne said he would work on it. I fell asleep that night thinking that everybody involved with the crisis at Treasury and the Fed must be so exhausted and sleepless that they could use help. They had a million things on their minds: short- and long-range fiscal and economic consequences and implications, political posturing and egos,