Episode 191: "Lessons from the Street: Stephen Schwarzman's Book Prompts Bill to Compare Insights into the World of Money" with John Tamny

Bill Walton (00:00):

Anyway, John, we are branching out with the show. As I mentioned, I'm going to do a show with my wife's pain doctor. He's written a wonderful book about how you deal with that and how people cope. Then I'm going to get one with my golf instructor and my trainer, and they've been incredibly interesting collaborators on getting good at stuff like that. I think that'll be interesting for everybody.

John Tamny (00:23):

Absolutely.

Bill Walton (00:23):

Now we've got you coming in. Instead of talking to the author, we're talking to-

John Tamny (00:30):

We're going to talk behind his back.

Bill Walton (00:32):

We're going to talk behind his back, except he probably-

John Tamny (00:34):

Yeah, we're talking about the author.

Bill Walton (00:34):

... will see this.

John Tamny (00:36):

Yes.

Bill Walton (00:37):

How do you want to structure this conversation? I've got some ideas, but what do you want to-

John Tamny (00:41):

I think we just see where the conversation takes us. That seems best. I've got lots of questions that I'd like to ask you, but I think they can come as part of our discussion of the book.

Speaker 3 (00:52):

The Walton Show, June 2nd.

Speaker 4 (00:58):

Welcome to The Bill Walton Show, featuring conversations with leaders, entrepreneurs, artists, and thinkers. Fresh perspectives on money, culture, politics, and human flourishing. Interesting people, interesting things.

Bill Walton (01:19):

Welcome to The Bill Walton Show. I'm Bill Walton. Well, today I'm back with my friend John Tamny with FreedomWorks and RealClearMarkets. You've seen him on the show many times. He's an extraordinary economist and writer, interesting thinker, great contrarian.

Bill Walton (01:34):

This time, unusually, we're not going to be talking about one of John's books. We're going to talk about a book that we both like a lot. John reviewed it, I guess, two, three years ago. It's a book by Steve Schwarzman, who is the founder and now chairman of Blackstone Group, which is an incredibly successful financial services, financial investment firm. He took it from pounding the streets of Tokyo to raise money to being one of the largest, most successful firms in the world.

Bill Walton (02:06):

He's written a book, What It Takes: Lessons in the Pursuit of Excellence. John has asked me to say about what I think about what's in some of it, and so this is going to be a bit of a twist in that John is going to get the first question today.

John Tamny (02:25):

Well, let's start with the fact that when they were out raising money, that's how I begin my review of the book, Pete Peterson at one point says, "Never do this to me again," as in it was a desperate process of being turned down over and over again. I'm just curious. The numbers you get from the book is 17 nos for every yes in raising the first fund, $880 million.

John Tamny (02:52):

What did you think at the time, or what did you think in reading about this? To raise a fund today, it's a known quantity. Back then, this was remarkably courageous, and they were getting into a field that they hadn't been in, private equity.

Bill Walton (03:07):

Well, back up a bit. Pete Peterson was the very successful CEO of Lehman Brothers. He came out of Lehman Brothers, I think, came to Lehman after the stint at Secretary of Commerce. Before that, he had been president of Bell & Howell, and a very good executive.

Bill Walton (03:27):

Steve was a brilliant star in the M&A department at Lehman Brothers. I think Steve was actually featured when he was 30 years old in New York Times Magazine for putting together a deal where Tropicana was acquired by Beatrice. I don't think he was barely a partner at that point, but he had the chutzpah to go down to take this deal on by himself when nobody else was around, and it was a major, major success.

Bill Walton (03:54):

They'd specialized in working with big companies, financial advisory, and had gone from success to success to success. Steve had gone to Yale, been a member of Skull and Bones, and really never had been in a position where you're going around passing the hat, asking for, in his case, a very modest billion dollars.

Bill Walton (04:19):

I was at Lehman Brothers when it was Lehman Brothers Kuhn Loeb, which was back in the day when it was a private partnership. I was a rung below partner. I was senior vice president, only been in the firm for two, three years, and so I didn't really know the inner workings. But they were a very big deal.

Bill Walton (04:37):

When Lehman Brothers was sold to Shearson, Steve had wanted to go out and do something on his own, but their background was in the M&A business, advisory business. They had no background investing in private equity deals. The discussion they had between the two of them was Pete was being... I think he was 20 years older than Steve. I think Steve was then 37 or 38, and Pete was probably 57, 58.

Bill Walton (05:09):

Steve said, "I want to go raise this fund." Pete says, "Well, let's raise a $50 million fund. We don't really know what we're doing." Steve said, "No, we're going to raise a $1 billion fund." He talked Pete in it. Everybody they went to see hadn't really... In the first place, I think there were only about two or three $1 billion funds in existence at that point. So the idea of people coming out of this with no operating experience, no private equity buyout experience per se, was audacious. If you look at Steve's career, audacious would be one of the words you'd used to describe it.

Bill Walton (05:51):

Is it unusual to get 17 nos for one yes? I'd say that's pretty typical when you're doing a first-time fund, although I think that was the ratio. I think probably he got like 50 nos before he got one yes, and then the averages got better. I guess eventually they got to Japan and were able to raise $100 million from one of the insurance companies in Japan. But it was a humbling experience for them. Being caught in the rain without a coat or a cab was not something Pete Peterson was used to.

John Tamny (06:31):

Just amazing what they went through. I thought it was crucial what he said. People see the success. This book comes out in 2019, when he's one of the richest men in the world. He talks about how, I have in quotes here, grueling. He talks about being alone at dinner thinking, "We're going to run out of money. We just don't have much in the bank. This is not going to last." What a scary thing he did.

John Tamny (07:04):

Did you see it at the time? Did you see it from Lehman Brothers Kuhn Loeb? Was there something about him that you noticed? Could you have predicted it?

Bill Walton (07:13):

Yes-

John Tamny (07:15):

Why?

Bill Walton (07:16):

... in a word. Well, Steve is a highly competitive man. If you look at his background, he grew up fairly... His family, I guess, owned a retail business in Philadelphia, and his father was the successful owner of that business. But even when Steve was 12 or 13 years old, he was telling dad he had to expand to this new location or that new location. His father didn't want to do it.

Bill Walton (07:43):

He was president of his class in his junior year in high school. Surprisingly, you don't think this for a financier on Wall Street, he was an amazing track star. He ran the first leg of the 400-yard dash in high school, and evidently had one of the fastest times in Pennsylvania.

Bill Walton (08:09):

Also, my favorite fact about Steve is when he got into Yale... He wanted to go to Harvard. Harvard, though, had put him on the waiting list. Steve wouldn't accept that as an answer, so he called up the dean of admissions at Harvard. What was this, 1964? You didn't do that.

Bill Walton (08:32):

He told the dean of admissions, he said, "Well, you're really going to want to... You're going to want to have me at Harvard." "Why is that?" He said, "Because I'm going to be very successful, and you'll be proud of me as one of your alumni." Now, it turns out my wife, Sarah, when she was applying to Cornell, said the same thing, and they let her in.

Bill Walton (08:53):

But Harvard didn't let Steve in, so he went on to Yale and had a very interesting career, got into Skull and Bones, which is really remarkable because Skull and Bones is the most prestigious secret society, and you tend to think of people like Averell Harriman and the Harriman family as being in that. I think the Bushes were in Skull and Bones. Steve didn't come from that background, and yet he got in, so he's an extremely socially skilled man.

Bill Walton (09:26):

Another story about him I thought was interesting from the book, between his freshman year at Yale, where he wasn't all that happy, and his sophomore year, he didn't go look for a job as a tennis instructor. He went down to the docks in Brooklyn and got a job on a steamer, a freighter, and signed on to work in the boiler room of a freighter, and then I guess got promoted on another trip to be cook. Here's a kid, 18, 19 years old, Yalie, working on a... I don't know if it was a tramp steamer, but it was a commercial boat. But he took along some things to read, The Collected Complete Works of Sigmund Freud.

John Tamny (10:22):

A varied mind.

Bill Walton (10:24):

When I read that, I thought, "Wow." Now, I have a picture of me in basic training at Fort Knox where I'm reading The Stranger by Camus, but I didn't think about-

John Tamny (10:32):

Oh, you show-off.

Bill Walton (10:32):

I didn't think about-

John Tamny (10:32):

You show-off.

Bill Walton (10:35):

Well, yeah, I did it too. Anyway, so Steve had this ability to figure out what he wanted to do and make a connection. So am I surprised that he ended up getting his fund done? Not really.

John Tamny (10:50):

Your views on the book evolved. You liked it more the more you read it.

Bill Walton (10:57):

I did.

John Tamny (10:58):

Why?

Bill Walton (10:59):

Well, in the first place, it shows who he is. If you look at the construction of the book, in the first place, it's not a warts-and-all, tell-all, "I did this when I was in fourth grade" kind of book. He talks about the highlights of his life, the track team, Yale, Skull and Bones. I think he recruited a popular group to sing at his high school. Do you remember the name of that?

John Tamny (11:25):

Oh yeah. There's a picture in the-

Bill Walton (11:31):

A picture of them. Yeah, the-

John Tamny (11:31):

Always a doer.

Bill Walton (11:32):

Little Anthony and the Imperials, he recruited, when they were big stars, recruited them to sing it as high school prom or something like that.

Bill Walton (11:42):

I wasn't sure. I started liking it a lot, and then it went into the normal getting up through the ranks in investment banking, or getting through Yale and then the Harvard Business School. Then you see, when you look at this, that this man has thought through so many things. He's got 14 pages of acknowledgements in this book. He probably had 12 people working on it. I think it took him 10 years to write it.

Bill Walton (12:14):

It really tells you a lot about what it was like to build this business, what it was like to manage a company going through the financial meltdown of 2008, 2009. I don't know, it's hard not to see lots in there. If I'm a young man or a young woman who wants to make it in business, or for that matter, any field, I think this would be a great place to start learning about what it takes.

John Tamny (12:43):

Well, so let's talk about the-

Bill Walton (12:44):

By the way, I'm not on commission.

John Tamny (12:46):

That's right.

Bill Walton (12:46):

I haven't Steve in 40 years, or however long it's been.

John Tamny (12:51):

Well, I threw it big bouquets in my review. I thought it was very interesting and insightful in a lot of ways, and I've used it over and over again just for my own writing.

John Tamny (13:02):

One of the things that most interested me, and I thought about you at the time, is that he has this admonition throughout the book, "Don't lose money." That was what he told the people at Blackstone, "You do not lose money."

John Tamny (13:17):

Private equity, at least to an outsider, is all about taking big risks on companies that aren't doing too well and operating them better on the way to an eventual exit. You read the book, and there's one deal where he admits to losing money, where he thought, "I actually want to write a check to the people we lost money for." Is there such a scenario where you could never... Aren't you losing money a lot of the time?

Bill Walton (13:49):

Well, not on purpose.

John Tamny (13:50):

Not on purpose, but because you're taking big risks. It just struck me that we're not hearing about a lot of bad deals. Am I incorrect?

Bill Walton (14:02):

This is not warts-and-all book. We're reading mainly about the ones that worked in this book. I would guess there are probably 10%, 15%, 20% of the deals in the Blackstone portfolio where they might have lost some money. I think the message that I took away is you want to structure things so that you do incredible due diligence. You want to run down what...

Bill Walton (14:25):

I was a baby, but when I was a baby banker in a commercial bank, Jay Pritzker was my biggest client. I worked very closely with him. He took me into his arms as a protege. He called them the horribles. Anytime you go into a deal, you want to say, "Okay, here are the three things or five things that could cause this to blow up or end up badly," and you mitigate that.

Bill Walton (14:50):

You say, "Okay, well, here's this bad thing. Maybe there's a regulatory risk. How do we deal with that? Or maybe we've got a key customer who, if we lose, would be a big problem. How do we think about that? How do we protect ourselves if that happens?" You try to think all that through before you go in.

Bill Walton (15:07):

"Don't lose money" is a mindset, and it makes you much more careful than you would be. If you're thinking about 10 deals and you're saying, "Well, look, I'm going to do..." Venture capital is more like this. You go into 10 deals. The way that business works is you get one massive winner, and it makes up for the other nine where you do lose money, so it's a different mindset.

Bill Walton (15:32):

In private equity, you're typically buying fairly established companies. Maybe they're a turnaround. Maybe they're already successful and you just want to take it further. But you shouldn't be thinking about the possibility of a wipeout, because you're betting on something that already has some commercial success.

Bill Walton (15:57):

I think I would say that to... I'm sure he says that to everybody who worked for him, to give them the same kind of mindset he had. One of the things I liked in his rules, and he's got 25 rules here in the book, and I think my favorite, a lot of them are the standard self-help, is rule number 21, "Worrying is an active, liberating activity." I saw that and I thought, "Absolutely." He says, "If channeled appropriately, it allows you to articulate the downside in any situation and drives you to take action to avoid it." I think what it... I interpreted "don't lose money" to say "worry about all the bad stuff that happened, and don't find it acceptable that you could lose things."

Bill Walton (16:56):

One moment.

Bill Walton (16:57):

You're watching The Bill Walton Show. I'm talking with John Tamny, and we're talking about Steve Schwarzman and Steve Schwarzman's life, his book, and his investment philosophy. We're working to figure out what we like best about it, and maybe some of the things that we don't like about it.

Bill Walton (17:15):

John.

John Tamny (17:16):

Well, so continuing on that, I thought it was interesting. As you describe, you were a baby banker. You were a senior VP while he was partner, head of M&A at Lehman. He talks about, at Blackstone, about a very collegial atmosphere, as in, from analysts on up, we want everyone's opinion on the way to making a deal. We want everyone's opinion about what could go wrong. How true did that read to you? Do you think he grew into that? Was that the way it was at Lehman? Was it a truly collegial atmosphere, or is there a bit of showmanship there?

Bill Walton (17:58):

Well, again, collegial after you get to a point where you trust everybody in the room, and their judgment and their ability to deliver time after time after time. I used to say about private equity, "Many are called, but few are chosen," because the amount of things you need to know to be successful in private equity is a lot.

Bill Walton (18:23):

I remember being in New York in the '80s, and people would say, "Oh, I want to go into private equity. Everybody is making billions in leverage buyouts." Well, but you had to know a lot to do that. You needed to understand how businesses operated, how to pick people, how to structure things, how to get financed. Most people don't have that talent.

Bill Walton (18:43):

Lehman Brothers Kuhn Loeb, Lehman Brothers, when it was still a private partnership, was hardly what you'd call collegial. It was a very sharp-elbow environment. The joke about Lehman is, "Nobody will ever stab you in the back. They'll stab you in the chest."

Bill Walton (19:05):

I'd been a banker at Continental Bank in Chicago, and I had a really terrific career. I was the star banker in the commercial lending division. That's where I got to know Jay Pritzker very well. Then they made me head of strategic planning when I was 30 years old, which at the time, that was a pretty big deal. Now, I'm not responsible for the plan that got Continental Bank into bankruptcy. I'd left before then.

Bill Walton (19:33):

I didn't want to stay in a big bank, and I wanted to get out and do something more entrepreneurial. I wanted to be on Wall Street. I'd gone to Indiana, and Wall Street was not recruiting people from Indiana. There was a guy that ran the Goldman Sachs office in Chicago, and I'd go see him every two or three weeks, saying, "You've got to hire me at Goldman Sachs, Goldman Sachs, Goldman Sachs." Well, he never did.

Bill Walton (19:58):

Then I got a call from Lehman Brothers, and they said, "We'd like to hire you as a business development guy." That was my chance to get into the street. I said yes, but I said yes with a little bit of trepidation because Lehman was known for a very tough culture, but a really interesting culture. They had all kinds of people from the CIA. They had Europeans from noble families who were great business development people. It was a very, very colorful group of people. We still had Bill Lehman's art collection there, so we had these fabulous Matisses and Manets and that sort of thing.

Bill Walton (20:46):

You go to work at Lehman Brothers. At the time, we were at 55 Water. It was just this really interesting culture, but you didn't do very well there unless you could deliver. It wasn't a nurturing environment in any sense at all. You needed to get a rabbi. They also didn't think they needed to spend a lot of time training you.

Bill Walton (21:06):

I'll never forget. I had similar experience with Steve. They say, "We want you to take a look at this bond deal that's coming up. It's a convertible preferred whatever." I'd come out of commercial banking. I had no idea what they were talking about. They threw me this prospectus on the table, and I'm supposed to figure it out. I remember spending three or four really, really tough days and nights trying to figure out how this thing worked. That was the culture. You had to figure it out and you had to make things happen and then prove you could do it.

Bill Walton (21:42):

Then Steve also talks about a culture at Lehman, I guess one of his early experiences, where... Back in the day, we had pitch books. I'm sure they still do. You'd go visit the CEO of some major corporation; every single word in that book had to be right, every single number. You dot your I, cross your T, and you get it exactly right. Well, Steve, I guess, showed up at one of those pitch book meetings where he'd made a mistake, and the partner in charge just absolutely... He had a very bad day. So he learned the standard of being perfect.

Bill Walton (22:23):

When he talks about hiring people, he talks about hiring tens, and he's talking about getting people who can get it exactly right. I think the other word he uses in the book is, you can make mistakes... Well, actually, he doesn't put it that way. He says, "The word for you to be thinking about is 100%. I want you to get 100% right." what do they have at Blackstone now, 20,000 applicants for every job?

John Tamny (22:53):

Yeah, I'm so glad you brought that up, because it's kind of a digression, but it's a question I've been wanting to ask you. The number that I got in there was 14,000 applicants. This was for, I think, 2018, around when the book was published. They hired some microscopic number relative to that. He says it is harder to get a job at Blackstone than it is to get into Yale or Harvard. They hire tens. That's it.

John Tamny (23:26):

It leads to a question. I want to get back to the process of investment, but I found myself reading that wondering about this woke capitalism thing. Steve Schwarzman has to get the best people. That's his deal. That's the Blackstone deal. Do you ever think that sometimes the Goldmans, the Blackstones of the world, the BlackRocks do some of this woke stuff, not because they care a lot about it, but because for the people they want to get in modern times, for whatever reason, they care about it, and this is a way of recruiting the tens, that you couldn't necessarily recruit without it? Am I nuts?

Bill Walton (24:08):

You're saying kids you'd recruit when they're 23, 24 years old are big devotees of woke capitalism, and they believe in diversity, equity, and inclusion over making money-

John Tamny (24:23):

All that nonsense. They believe in making money. Oh, of course they do. But they want to think that they're-

Bill Walton (24:28):

Well, those two are not... Those two don't hang together very well.

John Tamny (24:32):

But invariably, they do. These kids from the Harvards and Stanfords that he hires from, whatever their politics, they're good at making money, and he hires these tens. Is there something to maybe they touch on some of this stuff to placate them?

Bill Walton (24:52):

Okay, this is The Bill Walton Show. I'm here talking with John Tamny, and I'm stalling for time to figure out how to answer his question. We're trying to figure out whether you can be woke while at the same time being successful in the private equity business and on Wall Street.

John Tamny (25:09):

I told you it was a digression.

Bill Walton (25:11):

We are digressing. I'll come up with an answer. John, the thing that's fascinating is how the culture has changed. American culture has changed, and I think not for the better.

Bill Walton (25:26):

I found working on Wall Street, and then later on with Allied Capital in the '90s and the early 2000s up through 2010, just so energizing and stimulating because you're really pursuing excellence. You're trying to get the best deals done. You're trying to not lose money. You got to work with amazingly smart people.

Bill Walton (25:49):

My shop was in D.C. In D.C., we could pay a fairly good salary, basically New York salaries in D.C., so we got the best and the brightest. I guess one of the things I miss about that the most is the investment committee we had, where we had 12 or 15 people in it that were just so smart and so many different points of view, and you just learned so much.

Bill Walton (26:13):

One of the things that Steve talks about is adding businesses to Blackstone where you learn about the world. If you learn about this business, the hedge fund business, or maybe it's a real estate business, where you get into this, that, and the other, the knowledge you get from deal after deal after deal about the way the world really works is extraordinarily exciting.

Bill Walton (26:35):

You're now asking me if Blackstone is now hiring kids out of Harvard Business School who are 25 years old, who've been through all the new age, politically correct, woke approaches to business, does that work in his model? I don't know. I don't know. It's a good question. That's really a cultural change.

Bill Walton (27:03):

I don't think you can measure success in terms of... Certainly, your private equity success, your investors are going to say, "Well, we're glad you're focused on diversity, equity and inclusion, but how much did you return from our investment in the fund?" That's the tension. You get some people arguing that, "Well, that's good business." Well, it's not really very measurable business, and it's certainly not measurable in the private equity or hedge fund business.

John Tamny (27:33):

Can I ask you... I thought, very interestingly, the way Schwarzman put it was China is now a market economy overseen by the Communist Party. He's obviously doing a lot in China, not just from a private equity perspective, but he's funding a university. Did any of his commentary on China change your point of view? I don't ask that... Was it compelling to you? What did you think about that?

Bill Walton (28:05):

China is a very thorny issue for people like me who've been on Wall Street, been investing, who came up in the world where, once we opened China up, we were supposed to all go into China. We're going to make China prosperous. We're going to help their economy succeed. We're going to help them build their businesses. We're going to do all sorts of things with China. In return, the expectation was China is going to become more like us, a liberal democracy, join all the Western institutions. That seemed to be happening up until the last five or six or seven years when Xi began to ascend and get more and more powerful.

Bill Walton (28:52):

I think the China that Steve went into 20 years ago is a different China than the China we have today. There are now a lot of people in the private equity business... Chinese private equity investors are beginning to say China has become uninvestable because it's no longer a capitalist economy with the Communist Party in charge. The Communist Party now is taking much more of a direct involvement in businesses in China, and so it's changing.

Bill Walton (29:26):

I know he's got a massive... Steve created something called the Schwarzman Scholars with, I think, the largest, most prestigious university in China, one I didn't know about. He's got a major investment, and it's been very successful. It's kind of like a... It's equivalent almost to a Rhodes Scholarship with the Schwarzman Scholars.

Bill Walton (29:50):

His acknowledgements, which I think mentioned, goes on for page after page. He's got a couple pages just thanking the people he did business with in China. I know you're a big fan of China, and you say they love the West. Five years ago, I would've been mostly there with you. Five years ago, I was a unilateral free trader. Let's open it up, no tariffs. Let's do business back and forth. I don't think that's what we're dealing with now. I don't think it's a competitor. I think it's an enemy.

John Tamny (30:24):

Do you think he thinks that?

Bill Walton (30:27):

Steve, if you're watching, we'd love to have you on to talk about how your views about China have changed. I think everybody has to be thinking about it differently.

Bill Walton (30:39):

I've been noisy about Larry Fink and BlackRock and what they're doing in China. I think they're still plunging ahead in China because they see that 450-million-person investment market and they want all those savings dollars. They want BlackRock to be managing all that. I think he's not hearing the music, as I see it, but maybe they know more than we know. Maybe they've got some deeper insights into the workings of the Chinese Communist Party. I don't think so.

John Tamny (31:16):

It's one of the ones that Schwarzman acknowledges that he got wrong, was BlackRock.

Bill Walton (31:20):

Well, that was interesting, wasn't it?

John Tamny (31:22):

Yeah, that was-

Bill Walton (31:23):

Isn't that a good story?

John Tamny (31:24):

That was. Yeah.

Bill Walton (31:25):

Larry Fink, bond department guy, knew how to put together a complicated bond deal on the planet, set up a shop. What did they want to call it? Black Pebble?

Bill Walton (31:38):

Steve had Blackstone. They wanted to have something Black in it, and so they started out with Black Pebble. That lasted a day or two. Then they ended up with BlackRock, which is a better name. I think Blackstone had like a 40% interest in BlackRock, which today would be worth, I don't know, $1 trillion? I don't know. Some huge number.

Bill Walton (32:05):

I guess Larry Fink went back to Steve and said, "Look, we made this deal. You invested in us. On the other hand, we're doing all the work, and we think your stake is too high." Steve said, "A deal is a deal. We're going to stick with it." Well, instead, they came apart, and he now owns 0%. That's one he missed. He didn't lose money. He didn't lose money.

John Tamny (32:24):

No, but it was one of the two things where he said, "Boy, I really blew it here," and so something he regrets.

John Tamny (32:31):

I've got to ask you, mark-to-market accounting, 2008. I have something underlined in here. He looks back on that, and the view inside Blackstone was that Lehman's real estate portfolio was a mess. This was before the meltdown. You sold massive amounts of real estate in 2005 because you noticed something amiss. He talks about something amiss here.

John Tamny (33:05):

He says this, but then he says, "Well, mark-to-market accounting was a bad thing." I think any accounting rules are bad, but I find myself wondering, would it have made any difference for Lehman Brothers? By his estimation, the portfolio is a mess. I guess my question is, does Lehman die either way? What's your assessment of that?

Bill Walton (33:28):

I think, had we not had FAS 157, which was the mark-to-market, we wouldn't have had the meltdown we had in 2008, 2009. I think that accounting rule was so destructive because all these companies, and mine was in that group... We didn't have FAS 157. We had some SEC rules. But most of them were in the business of long-term investing, medium-term investing, holding assets for a period of time. There's an investment cycle.

Bill Walton (34:01):

If you're you and me sitting there investing our dollars, and we're saying, okay, we've got a portfolio of $100 million here, but this is in real estate, and we're expecting to hold this for five to 10 years, and there'll be cycles and things like that, and so we end up with a down cycle, we don't all of a sudden say, "Well, this thing is worthless." We say, "Well, let's ride it out through the next piece of it."

Bill Walton (34:25):

What mark-to-market did essentially was it says, "Well, let's mark this thing to the most pessimistic view about the market right now in this moment in time," and it mismarked a lot of the portfolios of all the big banks. And your favorite, it was exacerbated by short selling and the use of derivatives, where people were trying to drive these companies out. If you start short selling, you drive the value of the assets down; you use derivatives to amplify that.

Bill Walton (34:55):

Lehman Brothers, let's pick a big number, maybe their assets were $3 billion. And maybe with the problems in the real estate market, maybe they were worth $2.8 billion or something like that. I don't know what the actual numbers were, maybe 2.5.

Bill Walton (35:10):

With mark-to-market, remember, everything was marked based on public. I think S&P fell 50%. Instead of marking it down just some, they went all the way down to what you could trade things are in that moment. Mike Milken has one of his axioms, which I think is absolutely true, liquidity, access to credit. You're big on that one. It's never there when you want it, never.

Bill Walton (35:41):

Liquidity had driven up. It was at zero. Nobody could get access to credit, the big insurance companies, the big banks. What were things trading? Well, they're trading close to zero. But is that where you want to put your books and that's where you want to create panic? There could have been somebody that stepped in and said, "Look, guys, this is a massively successful country. We've got these long-term successful firms. We're going to pull back on marking everything to zero and wait to see until the dust settles to find out how much underwriting losses we're actually going to have."

John Tamny (36:18):

Couldn't an investor have done that anyway?

Bill Walton (36:20):

Who?

John Tamny (36:20):

What was keeping an investor from saying, "Accounting is theory"?

Bill Walton (36:26):

Well, if you're running a public company, you've got to pay attention to the accounting rules. If you're Dick Fuld or you're the guy that's running Citibank or Bank of America or any of these big things, they didn't have a lot of options.

John Tamny (36:42):

I'm not doubting their lack of options, but an investor could say, "Okay, well, mark-to-market says it's worth some very low number. We disagree." I can't get away from the fact that Schwarzman's view was that the portfolio was a mess. So if you take away-

Bill Walton (37:02):

I wouldn't hang yourself too much... I wouldn't hang on that sentence too much.

John Tamny (37:07):

Really?

Bill Walton (37:07):

That was one sentence. When people characterize a thing as a mess, it doesn't mean 100% of it was a mess. It meant that 10% of it may be a mess, or something at the margin, but not the whole thing-

John Tamny ([37:18]):

What if there's no accounting-

Bill Walton ([37:19]):

I think he said later on there was only some damage there, not all damage.

John Tamny ([37:25]):

Well, because that was the other thing that I thought was interesting that he pointed out, was that if you look at the housing investment, people to this day say, "Well, it was a bunch of sloppy loans made." Well, as he points out, over 90% of them performed. These were generally good loans, that, over time, they worked out. This wasn't banks just throwing money at bad idea after bad idea, that they performed.

Bill Walton ([37:53]):

Well, we had a lot of bad underwriting. One of the great ironies of history is we've got Dodd-Frank, which was put in place to cure the ills of the meltdown, where Barney Frank and Chris Dodd were two of the principal proponents to have the banks drop their underwriting standards to put more money out to promote housing. It got to the point where you could buy a house, and they would lend you more than the purchase price to give you some extra money to fix it up. You remember those days. It was crazy. A reasonable banker doesn't do that unless they're being encouraged to do it.

Bill Walton ([38:39]):

Then you got a lot of really bad actors. I can't remember all the names, Countrywide Finance. There were a lot of them. A guy shows up at an investor conference with a deep tan and chest hair and jewelry, and you're thinking, "Why do we..." It was pretty obvious that some of these guys were crooks.

John Tamny ([39:02]):

When we were emailing before this, you talked about the investment process really interested you in this, but we never got beyond that. What stood out? Did you find yourself learning things? Did you find yourself fascinated?

Bill Walton ([39:19]):

Well, there's a lot of recognition. One of the things that he points out that I struggled with was that... He was, I'm looking at his book, chairman, CEO, and co-founder of Blackstone. He was also the chief investment officer. When you're deploying capital, and a lot of capital, the chief executive officer's role has many pieces. The chief investment officer has a different role.

Bill Walton ([39:51]):

As chief investment officer, you're supposed to be more or less gimlet-eyed about what the opportunity is, weighing risk, so on and so forth, and being really pretty rough about saying, "No, this is a dumb idea. We shouldn't do it." But when you're the chief executive officer, there's always the personnel part of it, where you get a guy that you really like, he comes to you with a deal, you say no; comes to you with another deal, you say no; third deal, now a fourth. Pretty soon you've got an employee who's pretty dispirited.

Bill Walton (40:20):

As a chief executive officer, you want to say, "Well, let's give him a chance to do something with this," and so you go for something because you're trying to support the person who's bringing you the deal, when in your heart of hearts, you may think it's not that great. He recognized that.

Bill Walton (40:38):

I think I recognized it to a certain extent. I tried to fill seats in my investment committee with some of the most negative people in the firm, because I tend to see things as half full, and I wanted people that would tell me that there's not only not half full, but the glass is empty, so we'd have that balance of opinions. It's always tough when you're trying to manage personalities while at the same time managing how you allocate capital.

John Tamny (41:05):

What's your speculation along those lines? Do you think he's got people inside Blackstone willing to tell him what he doesn't want to hear? That would be-

Bill Walton (41:15):

I do. One of the things that struck me about Steve was the people he recruited early on were very independent, tough-minded people out of Lehman Brothers Kuhn Loeb. These were very bright people. They were tens. They were people that could have probably run their own company, but he recruited them in to help him run divisions. Tom Hill was one of them, Steve Bushad. There's several other names that spring to mind. He brought in people that would tell him good idea, bad idea. It gets back to...

Bill Walton (41:50):

I'm here with John Tamny. This is The Bill Walton Show. We're talking about allocating capital and personalities involved with that, and how Steve Schwarzman did it at Lehman Brothers, but now at Blackstone Group.

Bill Walton (42:10):

The thing that Steve... He says in the book that his strong suit was not numbers, not finance. That surprised me. I didn't know that.

John Tamny (42:21):

Oh, really?

Bill Walton (42:21):

He saw his strong suit as being how to read people, how to take a lot of information out of a conversation with somebody. This gets to your investment process question. He wanted people sitting in the room so he could hear the way they talked about the deal. He developed a real knack for being able to read confidence or doubts or considerations. I think a lot of his ability to deploy capital successfully was his ability to get good people who did all the analytical work, and he would then leverage off of the way they presented it to him.

Bill Walton (43:05):

It gets back to that story I've mentioned about him sitting there as a cook on a tramp steamer reading Sigmund Freud. What's that about?

John Tamny (43:19):

You were in the business. What was Blackstone's reputation, looking back?

Bill Walton (43:26):

Oh, I think it's got a great reputation.

John Tamny (43:28):

How did you feel in 1990, 2000? Was it the pinnacle?

Bill Walton (43:36):

Well, not then. You had Goldman. KKR had been in the buyout business. There were a lot of very successful buyout firms. At that point, I think Blackstone was considered to be one of the top players, but it wasn't at the top of the heap. It took a while. But I think they were always considered highly, very smart, highly ethical, very aggressive, able to make smart deals. In that world, that's the gold standard.

John Tamny (44:11):

Was there anything in the book that made you skeptical or that you felt didn't read right?

Bill Walton (44:20):

Well, I think the story of the way Lehman got sold to Shearson was a version of the story. It didn't get into all the personalities and aspects of the things you saw in a book like Greed and Glory on Wall Street. There was a lot more sturm und drang. It wasn't quite as clear-cut as he made it in the book. There are a lot of interesting, juicy details left out of it, but I don't think they were necessary for the book he was writing.

Bill Walton (44:52):

I wouldn't say skeptical, but I just thought, "Well, this is Steve's version," and I'm okay with that. His deal he did with Tropicana, sort of the same thing. There were a lot of annoyed people at Lehman Brothers when he did that deal, because he was this junior guy and he stepped over all sorts of people to put himself in a position to do that, and it worked for him. There's a little bit of the blowback that he got from things he did, I don't think is in this, but I don't think it should be. They can write their book.

John Tamny (45:29):

Yeah. Not as many people will buy it.

John Tamny (45:32):

One of the things that I thought was so great in it was that he gave a lot of credit to Tony James, just as an... Now, Tony James was very high up at Blackstone. I think he's just retired.

Bill Walton (45:44):

He ran it. He was the day-to-day-

John Tamny (45:45):

Yeah, tip-tip top. One of the things that I underlined was that Tony James said, "Success breeds arrogance and complacency." It's something that Howard Marks at Oaktree Capital has similarly said, that the seeds of recession are actually laid during the good times and the seeds of recovery are laid during the bad times. I liked that he threw such bouquets to some of the other people. He must be a great hirer.

Bill Walton (46:22):

Schwarzman?

John Tamny (46:23):

Yeah.

Bill Walton (46:23):

Oh yeah. I think he is. What's not in the book are all the mistakes I'm sure he feels that he made, but why get into it? He talks about the people he hired who turned out to create big parts of his business.

Bill Walton (46:38):

The thing that was interesting to me was when he had the first strategic plan for Blackstone right at the beginning, he said, "We're going to be in the advisory business," which is what Pete and Steve had been doing forever there, big deals, very, very, very respected, "and we're going to be in the buyout business." This is this $1 billion fund that they... They must have had a... I think probably the way Steve got that sold is, "We may not have the specific skills you're talking about, but we know how to find those people. We've worked with this person and that person, and they're all going to be part of this," and he executed on that.

Bill Walton (47:20):

Then there was this third part of the plan, where he said advisory buyouts and other ventures. He proceeded very opportunistically trying to find related industries where he could get the right people with the right opportunity. He didn't shut that down. You can be guilty in the business "let's just stick to what we know." Instead, he was looking at hedge funds or the real estate business, residential housing, all these things, that if you'd looked at Steve Schwarzman in 1985, you would've said, "What do you know about that?" But he had the intellectual curiosity and interest, and this sounds a bouquet, but I'm impressed. What's he have, 500,000 employees now? I don't know, $10 billion? I don't know what the revenues are.

Bill Walton (48:17):

I think the way he built it, finding, as he calls them, 10s, and also finding businesses that were adjacent to what they already knew, but would add something new to their knowledge base, allowed them to make much better decisions than a lot of people who cut themselves off from those new opportunities. I think there's a lot to learn from that.

John Tamny (48:42):

What do you think drives him? You can't spend all this money. What do you think... He's still doing this. What do you think drives him?

Bill Walton (48:50):

Well, you remember the story DLJ wanted to hire him-

John Tamny (48:54):

Yeah.

Bill Walton (48:54):

... out of Yale? He was talking to the top partner. The top partner says, Bill Donaldson, or whichever one, "Steve, you're amazing. We want to hire you. You're just out of Yale, $10,000." Steve said, "Well, I won't come to work for you for $10,000." "What? You're kidding."

Bill Walton (49:18):

He said, "No. I heard that somebody else from Yale got an offer for $10,000, and I want mine to be $10,500." He said, "I won't take the job unless you do it," and so he left. I guess three days later, they called him back and said, "Okay, we'll pay you $10,500." Who has that?

Bill Walton (49:38):

He wants to be the very best, the very biggest numbers. You can see that with MIT. I don't know what other places he's endowed, but he's dropped about $150 million into all these prestigious universities. I think it really matters to him. In his 14 pages of acknowledgements, he's got the president of France and Kissinger and-

John Tamny (50:05):

Yeah, he's well-connected.

Bill Walton (50:07):

... Colin Powell and all the five presidents. It's a long list of people. He's very interested in being a player at the highest levels. I have less appetite for that personally. But I think if you want to know what drives him, it's to be the best among the best.

John Tamny (50:26):

Ken Auletta, he didn't write this in Greed and Glory on Wall Street, but he wrote about New York City. He said, "It's the final test for the talented." I would have to believe that he wants to... His final test is to be the richest person in the most important city on Earth, and I think he's close, if not there, at this point. Just a remarkable man.

Bill Walton (50:48):

Yeah. I have met Steve. I haven't seen Steve in years, but I would bet Steve could be pretty prickly at this point. He's got like 53 people that work for him personally. But that's okay. That goes with the territory. I don't begrudge that-

John Tamny (51:10):

You can't be him unless you're prickly.

Bill Walton (51:12):

You, of all people, who admire success for people who create biggest things like that, their trappings go with it. I think Steve likes the trappings.

John Tamny (51:21):

I hope so. Yeah. I just-

Bill Walton (51:23):

Why don't we get some-

John Tamny (51:24):

... want to follow him around.

Bill Walton (51:25):

I could use a few more trappings.

John Tamny (51:25):

Yeah. No, I want to see it all.

Bill Walton (51:29):

Well, John, how have we done on your questions? Are we-

John Tamny (51:31):

Oh, we could ask so many more.

Bill Walton (51:33):

I know. We can keep going.

John Tamny (51:35):

I hope I asked the right ones, because there's so many things that... You've got to have so many opinions on this book. This was fun, though.

Bill Walton (51:45):

Well, I found it really enjoyable, and it was a great summary of a lot of things that I think people ought to know about. If you want to understand how private equity works, this would be a good place to start as well.

Bill Walton (51:59):

This has been, alas, The Bill Walton Show, and we're here with my favorite guest, Bill Walton.

John Tamny (52:06):

Wait a second.

Bill Walton (52:08):

No, my favorite guest, John Tamny. John Tamny has been asking me some very hard questions about Steve Schwarzman and his book and the industry. I've got to get you on a plane to head off to-

John Tamny (52:20):

Yeah, somewhere.

Bill Walton (52:21):

... give a speech.

John Tamny (52:22):

That's right.

Bill Walton (52:23):

Well, you'll be back. We're going to be talking-

John Tamny (52:25):

We'll be back.

Bill Walton (52:25):

... about this. Much to cover.

Bill Walton (52:28):

Bill Walton Show. You can find us on all the major platforms, YouTube, Apple, Spotify, wherever you get your podcasts. This is one of the many shows we'll be doing on finance and personalities. Hope you enjoyed it. Back to you next time. Thanks.

Bill Walton (52:48):

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Bill Walton (53:08):

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