

## Equities

20 April 2012 | 18 pages

# Blackstone Group L.P. (BX)

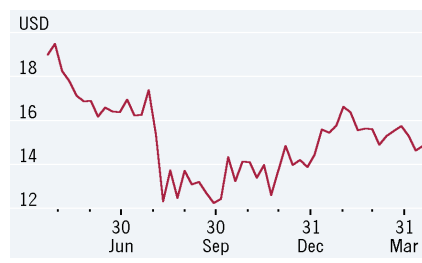
## It Was All Good Until The “Q+A”... But We Remain Buyers

- Company Update
- Estimate Change

- **What is the rub?** — Despite particularly strong underlying fundamentals and positioning, BX stock price increasingly underperformed on 4/19 (down ~5% vs. peers down ~1%) with the underperformance accelerating post 1Q conference call. We point to three issues raised by the call; however, we see the issues as either transitory and/or now fully discounted in the shares. The issues reflect: 1) mixed commentary around the economy; 2) mixed commentary around the PE business; & 3) mixed discussion around realizations. Of these issues, we believe much reflected management conservatism but discussion around BCP V carry potential is most real.
- **The issues** — First, management suggested some weakening in the global economy and again surfaced corporate margin pressures. Second, within PE, management did acknowledge some pricing concessions and elevated deal multiples (given cheap financing), but we do not see either affecting underlying economics/portfolio MOICs. Third and despite favorable commentary in both prepared remarks and in the media, management was uneven around the realization cycle, particularly in RE, though still sees solid to accelerating potential into 2H12/2013-14.
- **What do we think is now discounted?** — Of the issues raised, the most onerous is whether BCP V will be able to provide carry to unitholders. Here, we assume roughly \$0.45 performance fee contribution per unit in 2014. However, with a MOIC of 1.1x at 3/31, management still needs to generate \$5B+ in value to crystallize payout to unitholders. Assuming 50% chance the fund only pays the LP and using a 3-4x multiple, we estimate the foregone (present) value translates into about \$0.60 in the stock price, or 4% of the 4/19 closing price, while the stock dropped 5%.
- **What else did we learn?** — \$10B net inflows in 1Q, or 26% annualized growth, with positive growth in all businesses (RE, PE, Credit and HF Solutions); such growth has continued into 2Q for HF Solutions, including another \$500M in April, or 15% annualized growth. RE metrics are accelerating; PE metrics are solid; allocations are rising and bundled to larger player; GSO/Harbourmaster offers strong growth potential.
- **Affirm Buy; \$19 target; Raise 2013 ENI/trim 2014; raise 2013-14 DE despite call discourse.** Remains on Global Focus Five. Assuming static distributions in 2Q-4Q, BX still offers ~3.5% distribution yield. SOTP increasingly attractive, we think.

<b>Buy</b>	<b>1</b>
Price (19 Apr 12)	US\$14.14
Target price	US\$19.00
Expected share price return	34.4%
Expected dividend yield	4.7%
<b>Expected total return</b>	<b>39.1%</b>
Market Cap	US\$15,972M

### Price Performance (RIC: BX.N, BB: BX US)



EPS	Q1	Q2	Q3	Q4	FY	FC Cons
<b>2011A</b>	0.51A	0.64A	-0.30A	0.40A	1.25A	1.25A
<b>2012E</b>	<b>0.39A</b>	<b>0.28E</b>	<b>0.36E</b>	<b>0.38E</b>	<b>1.41E</b>	<b>1.71E</b>
Previous	0.36E	0.32E	0.35E	0.38E	1.41E	na
<b>2013E</b>	<b>na</b>	<b>na</b>	<b>na</b>	<b>na</b>	<b>1.74E</b>	<b>2.10E</b>
Previous	na	na	na	na	1.71E	na
<b>2014E</b>	<b>na</b>	<b>na</b>	<b>na</b>	<b>na</b>	<b>2.55E</b>	<b>2.53E</b>
Previous	na	na	na	na	2.65E	na

Source: Company Reports and dataCentral, CIR. FC Cons: First Call Consensus.

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See Appendix A-1 for Analyst Certification, Important Disclosures and non-US research analyst disclosures.

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Fiscal year end 31-Dec	2010	2011	2012E	2013E	2014E
<b>Valuation Ratios</b>					
P/E adjusted (x)	11.2	11.3	10.0	8.1	5.6
P/E reported (x)	11.2	11.3	10.0	8.1	5.6
P/BV (x)	1.4	1.5	1.4	1.3	1.2
P/Adjusted BV diluted (x)	na	na	na	na	na
Dividend yield (%)	4.4	3.7	4.7	6.8	9.4
<b>Per Share Data (US\$)</b>					
EPS adjusted	1.26	1.25	1.41	1.74	2.55
EPS reported	1.26	1.25	1.41	1.74	2.55
BVPS	10.37	9.42	9.90	10.69	11.54
Tangible BVPS	4.47	4.79	5.40	6.19	7.04
Adjusted BVPS diluted	na	na	na	na	na
DPS	0.62	0.52	0.67	0.96	1.33
<b>Profit &amp; Loss (US\$m)</b>					
Net interest income	0	0	0	0	0
Fees and commissions	2,557	3,052	3,393	3,998	5,536
Other operating Income	584	232	364	416	472
<b>Total operating income</b>	<b>3,141</b>	<b>3,284</b>	<b>3,757</b>	<b>4,414</b>	<b>6,008</b>
Total operating expenses	-1,561	-1,699	-1,951	-2,204	-2,775
<b>Oper. profit bef. provisions</b>	<b>1,581</b>	<b>1,585</b>	<b>1,806</b>	<b>2,211</b>	<b>3,233</b>
Bad debt provisions	0	0	0	0	0
Non-operating/exceptionals	0	0	0	0	0
<b>Pre-tax profit</b>	<b>1,581</b>	<b>1,585</b>	<b>1,806</b>	<b>2,211</b>	<b>3,233</b>
Tax	-163	-188	-225	-254	-356
Extraord./Min. Int./Pref. Div.	0	0	0	0	0
<b>Attributable profit</b>	<b>1,418</b>	<b>1,397</b>	<b>1,582</b>	<b>1,956</b>	<b>2,877</b>
Adjusted earnings	1,418	1,397	1,582	1,956	2,877
<b>Growth Rates (%)</b>					
EPS adjusted	101.1	-0.3	12.3	23.3	46.6
Oper. profit bef. prov.	118.4	0.3	14.0	22.4	46.3
<b>Balance Sheet (US\$m)</b>					
<b>Total assets</b>	<b>18,845</b>	<b>21,909</b>	<b>23,715</b>	<b>25,612</b>	<b>27,661</b>
Avg interest earning assets	0	0	0	0	0
Customer loans	0	0	0	0	0
Gross NPLs	0	0	0	0	0
<b>Liab. &amp; shar. funds</b>	<b>18,845</b>	<b>21,909</b>	<b>23,715</b>	<b>25,612</b>	<b>27,661</b>
Total customer deposits	0	0	0	0	0
Reserve for loan losses	0	0	0	0	0
Shareholders' equity	<b>4,363</b>	<b>4,671</b>	<b>5,056</b>	<b>5,460</b>	<b>5,897</b>
<b>Profitability/Solvency Ratios (%)</b>					
ROE adjusted	36.6	30.9	32.5	37.2	50.7
Net interest margin	na	na	na	na	na
Cost/income ratio	49.7	51.7	51.9	49.9	46.2
Cash cost/average assets	11.0	8.3	8.6	8.9	10.4
NPLs/customer loans	na	na	na	na	na
Reserve for loan losses/NPLs	na	na	na	na	na
Bad debt prov./avg. cust. loans	na	na	na	na	na
Loans/deposit ratio	na	na	na	na	na
Tier 1 capital ratio	na	na	na	na	na
Total capital ratio	na	na	na	na	na

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# The Off-Script Discourse Presents Opportunity

## Investment Summary

Coming into earnings, we were tactically positioned defensively on BX despite strong LT support as we were concerned around a potential ENI miss to consensus. And while this thesis proved correct, the stock sharply underperformed. However, we believe much of the relative erosion followed seemingly uneven commentary from management during the post quarter recap rather than the 1Q miss, which to be fair, was slight (at least to consensus). From our vantage point, we believe much of the issues are either transitory in nature and/or fully discounted following the approximate 5% blow-off in the shares on 4/19 and creating an (even more) attractive entry point.

We address the real economic impact of management commentary, yet the call reinforced BX's increasingly superior positioning among Asset Managers – both traditional and alternatives – in our view, with many key positives.

We affirm our Buy rating, maintain our \$19 sum-of-the-parts (SOTP) 12-month price target and tweak 2012-14 ENI estimates – and despite call discourse, actually raise our 2013-14 DE forecast.

## What Are The Issues?

We highlight three key issues that cumulatively added to the negative momentum to the stock on 4/19:

1. **Management commentary around the global outlook was mixed.** Two sub-issues. First, management noted some erosion in the global economy...or did they? Second, management once again pointed toward corporate margins under pressure – a theme our own strategists have been highlighting of late.

Around the economy, President and COO, Mr. Tony James indicated some softening in the global economy from 12/31. However, in refining his remarks, he subsequently noted that the global economy is recovering albeit at a low clip – the latter more in-line with the consensus view, we believe. We believe these uneven comments spooked investors around portfolio IRRs and realization potential/timing though believe greater diversification versus prior years could partially offset (Figure 1).

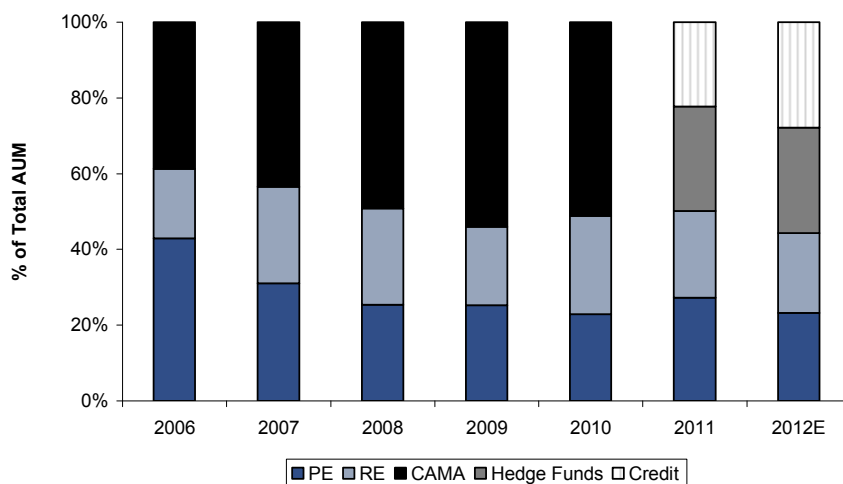
Management noted that portfolio company revenues were up ~5% in 1Q but that: a) growth was slower in the quarter on a Y/T/Y basis while EBITDA growth lagged revenues due to margin pressures around pricing and commodity costs.

However, the carrying value of PE increased 4.9% in 1Q, and the portfolio (unrealized and cumulative realized proceeds) is marked at a 1.5x MOIC (multiple of invested capital) at 3/31 versus 1.4x at 12/31/11 and PE segment revenue were in-line with our forecast. Importantly, management noted that underlying portfolio company economics continue to track toward long term assumptions, limiting adverse mark impact, in our view.

Here, we clearly believe it is well too soon to panic around underlying PE

marks, particularly as underlying economic data continue to point toward further recovery, shallow as it may be.

Figure 1. Greater Diversification Should Partially Offset Any Realization Timing Concerns



Source: Company reports, Citi Investment Research and Analysis

- Management commentary around PE was a bit mixed, but did anything really change?** Ultimately, we do not think so. Here, there were also two issues. First, around pricing; second around implied deal IRRs. Around pricing, management noted some break points for particularly large accounts, continuing a trend for the last 10-20 years. However, the market only seems to have focused on this price concession and glossed over: a) the discussion is for only very large sized AUM; b) such give up tends to come with long to longer lock ups – in fact, 70% of AUM have 10+ year duration; c) many traditional managers have break points, at far lower AUM levels, particularly in mutual funds; and, d) BX's superior track record likely mitigates such erosion in fee rates. That said: a) the \$86M in 1Q base management fees within the Private Equity segment were \$3M ahead of our forecast; and, b) the recently raised BREP VII fund did not lower overall fee rates versus prior quarters within the RE segment. We recently highlighted potential economic impact from lower fees, so also our 4/12 note, [Alternative Asset Managers - Potential Changes In Fee Structures May Not Alter Net Economics, We Believe](#).

Turning to deal IRRs, management noted that financing remains well attractive, particularly as demand for HY and Bank Loan funds remains strong (as measured by ICI/retail MFs, for instance). However, management also noted that deal pricing has bubbled up. Yet, we believe such dynamics are counterbalancing, and we suspect BX remains selective around opportunity. Still, management put \$2.7B to work in 1Q, with another \$800M already deployed into 2Q suggesting they are still seeing attractive deals, particularly in energy where the firm has \$3B in deal backlog at 3/31. Indeed, management did not back off its \$3B-4B per year deployment goal with seemingly attractive potential in US/non-US and across industries still.

- Mixed commentary around realization cycle.** Management started out the conversation incrementally upbeat around realizations indicating that

cycle could pick up into 2H12 and run for a few years into 2014, but the enthusiasm seemed to wane, particularly when discussing the potential in RE as the call unfolded. Several elements to the discourse: a) two funds (BREP International II and BCP V) may not fully pay carry based on current MOICs; b) management noted that the IPO window is opening a bit but strategic M&A remains slow; and, c) management seemed to push out RE cycle given surging fundamentals and worry around not maximizing returns – here, we think senior officials were particularly conservative based on follow on conversations post the call.

Of these issues, we are most concerned around commentary by the CFO that BCP V (\$17B to \$18B in AUM at 3/31, or ~9% of total, we believe) may not pay carry to the unitholders (the BREP International II fund represents about \$1.5B in AUM, or ~1% of total AUM, and is a rounding error in our view). BCP V is currently marked at 1.1x MOIC at 3/31, and relatively unchanged from 12/31. Management noted the change in TEV needed to cross the carried interest threshold is about 11%, down Q/Q from 12%, but translating into ~\$5B in portfolio appreciation, we estimate – on a base of approximately \$17B to \$18B, we believe. Management ultimately sees a 1.8x to 1.9x MOIC though timing is clearly key given 8% annual hurdle rate in the fund.

However, we believe such uncertainty around whether BCP V will pay carry to the unitholder is fully discounted. Why so? In Figure 2, we lay out our math. In our model, we have been assuming BCP V would get into carry paying status in 2014. However, with management saying the fund may or may not get back into carry, it is fair to re-think such assumption. In turn, should the fund not get into carry, our performance fee estimate for 2014 would decline from \$1.72 to \$1.26, or indicating about \$0.46 related to BCP V.

Based on current valuations for the sector/BX, investors seem to be putting a 3-4x P/E on performance fees, we estimate. If we assume the midpoint of this range, we get potential hit on the stock of around \$1.60 per share. However, two offsets. First, there is the time value of money, and we need to discount by roughly 11% cost of capital. Second, investors need to also contemplate that the fund could very well get into carry. Assuming a 50% probability that the fund does not pay carry to unitholders, we ultimately get about \$0.60 of (present value) haircut to the stock price. On 4/19, the stock fell \$0.70 – though we note the SPX was down about 50 bps on the day. As such, we believe the risk is fully discounted.

**Figure 2. The Risk BCP V Does Not Earn Carry Appears Fully Discounted, In Our View**

Fund	2014E			Per Unit Impact		PF @ 3-4x multiple	50% probability	Discounted @ 11%
	Accrued Carry <sup>1</sup> (\$M)	Comp (40%)	Net	PF	DE			
BCP V	864.4	345.8	518.6	\$0.46	\$0.19	\$1.61	\$0.80	\$0.62

<sup>1</sup>includes estimate for accelerated catch-up and 2012-14 market change

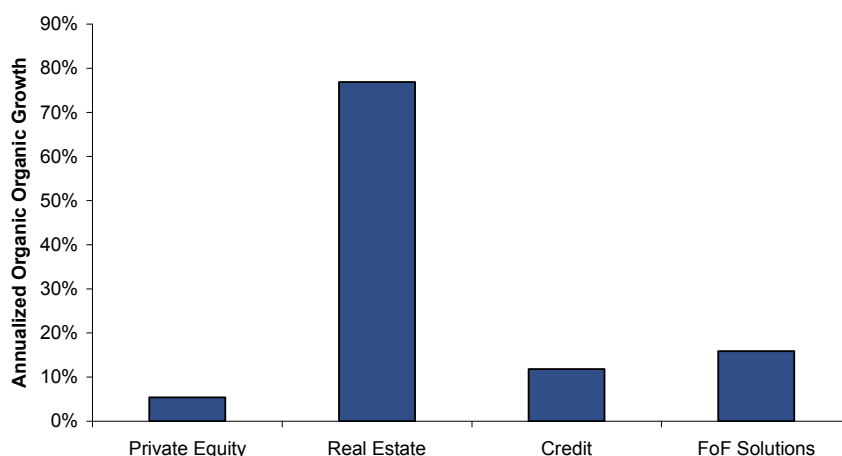
Source: Company reports, Citi Investment Research and Analysis

## Not All Lemons

Despite the discourse of these three topics, there is much favorable trends underway as well, in our view. We highlight a few key takeaways:

1. **Organic growth strong and diverse:** Management put net inflows at \$10B in 1Q, or 6% unannualized, with positive growth in all four key businesses, including \$6B in real estate; \$500M in private equity; \$900M in credit and \$1.5B in HF solutions (Figure 3). No question the \$6B in RE is not fully repeatable, but lead indicators across all four segments are strong, we believe.
2. **Lead indicators are strong, we believe:** We note: a) based on management commentary, the HF Solutions business generated \$500M net inflows for April, or 16% annualized growth; b) BREP VII, is expected to bring in another \$2B-3B in 2012, potentially bringing the fund to \$13B; c) the GSO Capital Opportunities II fund (mezzanine) closed at 2x prior level, and turned away AUM to protect return potential; and, d) management sees significant areas of growth across sector and region specific areas, boding well for subsequent growth, we believe.
3. **Europe remains a great growth area:** As Basel 3 requirements continue to marginalize other intermediaries. Here, BX's prior mezzanine fund generated a 23% annualized IRR, or consistent/superior to PE metrics, at lower risk. In turn, the recently closed Harbourmaster Capital deal gives BX strong presence in credit, with over 80% overlap in specific credit exposures but only 5% LP overlap, creating strong growth potential, we believe. Per management, they see significant single credit opportunities over the next few years, perhaps larger than sizeable pools also expected to come to market as financial firms potentially downsize to meet more stringent capital requirements.
4. **Portfolio performance strong across all businesses:** The carrying value of Private Equity increased 4.9% in 1Q12; Real Estate appreciated 4%; Credit HFs +4.6%; rescue lending +7.5%; mezzanine +6.5%; and HF Solutions +4%;
5. **Ample dry powder and deployment momentum** – Dry powder totals \$39B at 3/31 including \$17B in Private Equity, \$13B in Real Estate and \$6B in Credit. Management sees energy, Europe, middle market credits, and select real estate providing attractive investment targets; and the slack competition from banks and private RE firms are providing ample opportunities and/or favorable supply/demand imbalances.

Figure 3. Organic Growth Is Positive Across Each Business And Lead By Real Estate



Source: Company reports, Citi Investment Research and Analysis

## Refine ENI Outlook AND Raise DE Estimates

We are maintaining our 2012 ENI estimate of \$1.41 as we lower performance fee assumptions but also reduce the ratio of comp to performance fees. For 2013 these same dynamics add \$0.03 to our prior forecast to \$1.74. We trim 2014 \$0.10 to \$2.55 on lower BCP V NAV compounding.

Moreover, we raise our 2013-14 distributable earnings estimates from \$0.79, \$0.98, and \$1.39 to \$0.77, \$1.03, and \$1.41.

In 1Q, comp related to carry totaled 28% of carry, versus our 40% estimate. The variance reflects where the carry is being generated, with much coming from pre-IPO legacy funds which have lower comp ratios, such as BCP IV (PE) and BREP V and BREP VI. Here, the compensation payouts are much lower as BX employees gave up points for equity at the time of the IPO. Going forward, we expect a moderately lower blend than 40% prior as we do expect strong growth in new RE + credit + HF.

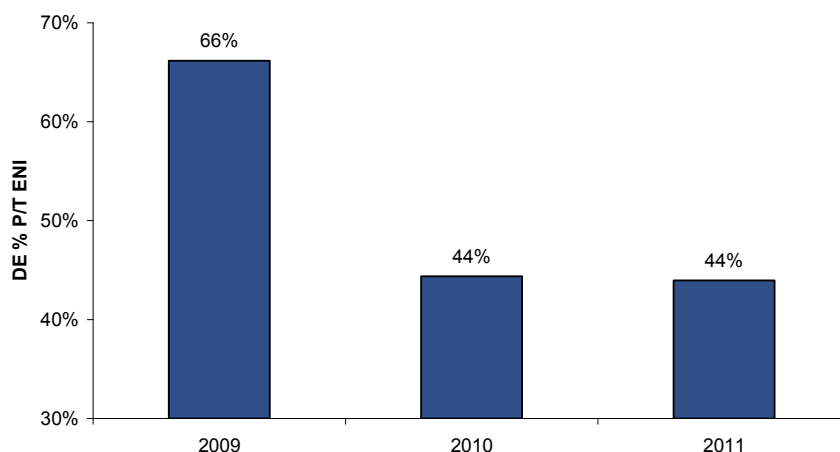
## How Can We Possibly Raise DE Estimates After That Call?

In Figure 4, we array BX's ratio of DE to ENI between 2009 and 2011. Here, the ratio ranged from 66% in 2009 and held at 44% in both 2010 and 2011, while totaling 39% in 1Q. For 2012-14, our assumptions translate into DE/ENI ratios of 47%; 51%; and 48%. Given further upward migration in the equity markets, reasonably stable spreads, and growing mix of business – including more contribution from: a) credit book + b) HF Solutions, our assumptions seem reasonable, even as management contradicted itself during the call. We note, approximate 26% of the HF Solutions FPAUM are now above high water mark, up from 8% at 12/31, with rising AUM balances, which increased from \$38B at YE to \$41B at 3/31. We also note, Credit accounts for 27% of FPAUM at 3/31 versus 22% at 12/31/11, providing a more stable source of potential carry based AUM, we believe.

In all, BX now has \$120B in performance fee-based AUM, with \$49B already generating performance fees.

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Figure 4. DE As A Percentage Of ENI Ranged Between 44% And 66% Between 2009-11



Source: Company reports, Citi Investment Research and Analysis

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## Some Final Thoughts Around Valuation

Investors clearly were not pleased with management commentary; however, if we conservatively assume static quarterly distribution of \$0.12, the \$0.48 translates into nearly a 3.5% distribution yield – better than all traditional managers except 8% for AB, a business facing much more uneven flow/positioning prospects, in our view. Our work suggests investors are now discounting particularly low distributions ad infinitum which seems onerous to us.

In contrast, we see a SOTP valuation that is much more attractive. Applying 15x P/E on \$0.54 in 2014E FRE (up from \$0.53 prior), we get \$8.10 in value. We calculate B/S impact to be \$3.14 at 3/31, leaving ~\$3.00 stub value per unit. Our 2012 and 2013 performance fee only ENI are \$0.74 and \$0.94, or essentially 4x and 3x implied P/E multiples. We view this valuation as attractive. Put another way, the 3x to 4x residual P/E multiple implies a 7%-8% implied NAV in PE and RE portfolios, we estimate, a seemingly low assumption when considering TROW price trades at 19x FTM EPS. While we believe TROW is a great company – but overvalued – we find it intellectually difficult to see how TROW can sustain such a premium valuation to most global financial services companies and against low implied P/E on performance fees. Something has to give, and while we think TROW is overly rich, we also believe BX (and Alts generally) are inexpensive.

Companies mentioned: (TROW.O; US\$61.76; 3)



Figure 5. BX Summary Model

Blackstone (BX)  
Earnings Results and Forecasts  
(\$ Millions, Except As Noted)

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KEY FORECAST VARIABLES:	1Q11	2Q11	3Q11	4Q11	1Q12	Forecast:			2010	2011	Forecast:			% Change			
						2Q12E	3Q12E	4Q12E			2012E	2013E	2014E	2Q12/1Q	2Q12/2Q	12E/11	14E/13E
<b>Management Fees</b>																	
Base Management fees	305.6	316.5	322.4	336.8	395.5	385.2	398.3	405.5	1,069.5	1,281.2	1,584.5	1,685.2	1,853.4	-2.6	21.7	23.7	6.4
Advisory fees	70.3	102.2	86.2	123.6	75.8	100.0	110.0	125.0	426.1	382.2	410.8	451.9	488.1	31.8	-2.2	7.5	10.0
Transaction & Other fees, net	58.4	103.6	41.8	43.8	38.5	38.4	40.9	41.4	137.7	247.5	159.2	225.6	205.6	-0.2	-62.9	-35.7	41.7
Management Fee offsets	-8.5	-8.7	-7.7	-8.5	-13.1	-2.5	-3.0	-3.1	-2.3	-33.4	-21.8	-24.6	-19.2	-80.6	-70.8	-34.8	13.1
Total Management Fee	425.7	513.6	442.6	495.6	496.8	521.0	546.2	568.7	1,631.0	1,877.5	2,132.8	2,338.2	2,527.9	4.9	1.4	13.6	9.6
Realized Performance Fees	95.6	60.2	7.9	64.2	18.8	28.3	86.2	93.8	361.7	227.9	227.1	525.1	1,012.1	50.4	-52.9	-0.3	131.2
Unrealized Performance Fees	505.2	612.8	-465.2	293.7	366.9	170.7	235.5	260.0	564.6	946.6	1,033.1	1,135.0	7.0	-53.5	-72.1	9.1	9.9
Total Performance Fees & Allocations	600.8	673.1	-457.3	358.0	385.8	199.1	321.7	353.7	926.3	1,174.5	1,260.3	1,660.1	3,008.1	-48.4	-70.4	7.3	31.7
<b>Investment Income (Loss)</b>																	
Realized	23.5	30.7	31.6	16.7	23.5	26.8	27.9	28.9	46.9	102.6	107.1	73.1	83.3	14.2	-12.7	4.4	-31.7
Unrealized	102.6	106.8	-165.8	39.0	59.9	54.2	56.4	58.6	501.6	82.7	229.1	309.6	355.2	-9.5	-49.3	177.0	35.2
Total Investment Income (Loss)	126.1	137.6	-134.1	55.7	83.4	81.0	84.2	87.5	548.5	185.3	336.2	382.8	438.5	-2.8	-41.1	81.5	13.9
Interest Income	9.4	9.3	10.1	10.0	9.3	6.8	6.8	6.8	36.1	38.8	29.7	35.2	35.2	-27.5	-27.1	-23.6	18.8
Other	2.3	1.1	-1.7	5.7	-1.2	-0.3	-0.3	-0.3	-0.6	7.4	-2.0	-2.0	-2.0	-79.3	-122.2	-126.4	0.4
Total Segment Revenues	1,164.2	1,334.6	-140.3	925.0	974.1	807.7	958.6	1,016.5	3,141.4	3,283.6	3,756.9	4,414.3	6,007.7	-17.1	-39.5	14.4	17.5
<b>Expenses:</b>																	
Base Compensation	224.5	272.4	238.2	225.4	254.8	260.6	273.9	287.1	859.1	960.6	1,076.4	1,141.6	1,220.1	2.3	-4.3	12.1	6.1
Performance Fee related	177.1	145.8	-100.9	94.7	109.5	77.5	117.7	128.4	357.0	316.7	433.0	598.6	1,067.4	-29.3	-46.9	36.7	38.2
Compensation & Benefits	401.6	418.2	137.3	320.2	364.3	338.1	391.6	415.5	1,216.1	1,277.3	1,509.4	1,740.1	2,287.5	-7.2	-19.2	18.2	15.3
Other Operating Expenses	103.0	99.4	96.9	122.1	109.5	109.6	110.6	111.6	344.5	421.3	441.4	463.7	487.2	0.1	10.3	4.8	5.1
Total Segment Expense	504.6	517.6	234.2	442.2	473.8	447.7	502.2	527.1	1,560.6	1,698.6	1,950.8	2,203.8	2,774.7	-5.5	-13.5	14.8	13.0
<b>Economic Net Income (Loss)</b>	659.7	817.1	-374.6	482.8	500.3	360.0	456.4	489.4	1,580.8	1,585.0	1,806.1	2,210.5	3,233.0	-28.0	-55.9	14.0	22.4
Tax	86.2	107.5	-38.3	32.9	67.9	43.2	54.8	58.7	163.1	188.3	224.6	254.2	355.6	-36.4	-59.8	19.3	13.2
After-Tax ENI	573.5	709.6	-336.3	449.9	432.3	316.8	401.7	430.7	1,417.6	1,396.7	1,581.5	1,956.3	2,877.4	-26.7	-55.4	13.2	23.7
Weighted-Avg ENI Adjusted Units	1,115.9	1,109.2	1,110.6	1,116.1	1,120.2	1,121.2	1,122.2	1,123.2	1,126.6	1,113.0	1,121.7	1,125.7	1,129.7	0.1	1.1	0.8	0.4
<b>After-Tax ENI per diluted unit</b>	<b>0.51</b>	<b>0.64</b>	<b>-0.30</b>	<b>0.40</b>	<b>0.39</b>	<b>0.28</b>	<b>0.36</b>	<b>0.38</b>	<b>1.26</b>	<b>1.25</b>	<b>1.41</b>	<b>1.74</b>	<b>2.55</b>	<b>-26.8</b>	<b>-55.8</b>	<b>12.3</b>	<b>23.3</b>
<b>Fee Related Earnings</b>	98.5	143.6	107.6	152.3	138.0	147.4	158.2	166.6	442.3	502.1	610.1	726.2	813.9	6.8	2.6	21.5	19.0
Distributable Earnings	201.9	190.9	125.7	178.2	162.1	191.1	239.5	253.9	701.8	696.7	846.6	1133.8	1551.8	17.9	0.1	21.5	33.9
After-tax FRE/unit	0.09	0.13	0.10	0.14	0.12	0.13	0.14	0.15	0.39	0.45	0.54	0.65	0.72	6.7	1.5	20.6	18.6
Distributable Earnings/unit	0.18	0.17	0.11	0.16	0.15	0.17	0.22	0.23	0.64	0.63	0.77	1.03	1.41	17.9	0.1	21.5	33.9
Performance Fees/unit	0.38	0.48	-0.32	0.24	0.25	0.11	0.18	0.20	0.51	0.77	0.74	0.94	1.72	-56.0	-77.2	-4.3	27.9
Investment income/unit	0.11	0.12	-0.12	0.05	0.07	0.07	0.08	0.08	0.49	0.17	0.30	0.34	0.39	-2.9	-41.7	80.1	13.4
Other	-0.07	-0.09	0.04	-0.02	-0.06	-0.03	-0.04	-0.04	-0.11	-0.14	-0.17	-0.18	-0.27	-45.3	-65.4	24.2	7.1
<b>Margins</b>																	
Base Comp % Management Fee	53%	53%	54%	45%	51%	50%	50%	50%	53%	51%	50%	49%	48%				
Other Expense % Management Fee	24%	19%	22%	25%	22%	21%	20%	20%	21%	22%	21%	20%	19%				
Perf Fee Comp % Perf Fees	29%	22%	22%	26%	28%	39%	37%	36%	39%	27%	34%	36%	35%				
Expense % Revenue	43%	39%	-167%	48%	49%	55%	52%	52%	50%	52%	52%	50%	46%				
FRE (after-tax) margin (% mgmt fee)	23%	28%	24%	31%	28%	28%	29%	29%	27%	27%	29%	31%	32%				
ENI (after-tax) margin	49%	53%	240%	49%	44%	39%	42%	42%	45%	43%	42%	44%	48%				
Tax Provision	13%	13%	10%	7%	14%	12%	12%	12%	10%	12%	12%	12%	11%				
<b>AUM (\$M)</b>																	
Private Equity	43,955	46,728	42,967	45,864	47,624	47,714	48,427	49,199	29,319	45,864	49,199	50,831	52,455	3.8	8.3	7.3	3.3
Real Estate	34,991	37,606	40,710	42,853	48,323	49,736	51,054	51,287	33,165	42,853	51,287	54,933	64,958	12.8	38.1	19.7	7.1
CAMA	N/A	N/A	N/A	N/A	N/A	N/A	N/A	N/A	65,640	N/A	N/A	N/A	N/A				
Hedge Fund Solutions	39,542	40,578	40,373	40,535	43,351	45,459	47,345	49,260	N/A	40,535	49,260	56,828	65,067	6.9	9.6	21.5	15.4
<b>Credit Businesses</b>	<b>31,475</b>	<b>33,791</b>	<b>33,649</b>	<b>36,977</b>	<b>50,776</b>	<b>50,999</b>	<b>51,727</b>	<b>52,459</b>	<b>N/A</b>	<b>36,977</b>	<b>52,459</b>	<b>52,837</b>	<b>56,283</b>	<b>37.3</b>	<b>61.3</b>	<b>41.9</b>	<b>0.7</b>
Total	149,963	158,703	157,698	166,229	190,074	193,909	198,553	202,205	128,124	166,229	202,205	215,429	238,763	14.3	26.7	21.6	6.5
<b>FPAUM (\$M)</b>																	
Total FPAUM	124,033	129,001	132,934	136,757	156,261	159,861	163,889	166,853	109,500	136,757	166,853	186,017	202,898				
Net Flow	N/A	4,952	7,202	3,657	1,493	2,856	3,249	2,149	10,264	29,033	9,746	15,733	12,855				
Annualized Growth Rate	N/A	16%	22%	11%	4%	7%	8%	5%	11%	27%	7%	9%	7%				
Revenue Yield	100.7	100.2	97.3	97.6	103.1	98.0	97.9	97.5	104.8	98.9	99.1	95.5	95.3				
<b>Miscellaneous</b>																	
Distributable Earnings Per Unit	0.18	0.17	0.11	0.16	0.15	0.17	0.22	0.23	0.64	0.63	0.77	1.03	1.41				
Distribution per unit	\$0.10	\$0.10	\$0.10	\$0.22	\$0.10	\$0.10	\$0.10	\$0.37	\$0.62	\$0.52	\$0.67	\$0.96	\$1.33				
Net Cash + Inv per unit	\$3.00	\$3.59	\$3.40	\$3.42	\$3.14	\$3.38	\$3.65	\$3.94	\$2.28	\$3.43	\$3.95	\$5.12	\$6.70				
<b>LP Capital Deployed (\$M)</b>																	
Private Equity	653	667	1,415	1,093	643	1,050	1,550	1,550	1,654	3,828	4,793	4,100	4,100				
Real Estate	654	2,785	1,706	996	1,144	1,241	1,491	1,541	4,073	6,141	5,417	6,101	4,750				
<b>Credit</b>	<b>154</b>	<b>153</b>	<b>1,314</b>	<b>1,029</b>	<b>928</b>	<b>700</b>	<b>800</b>	<b>800</b>	<b>0</b>	<b>2,650</b>	<b>3,228</b>	<b>1,500</b>	<b>1,320</b>				
Total	1,658	3,605	4,435	3,406	2,720	2,991	3,841	3,891	7,134	13,509	13,439	11,701	10,170				

Source: Company reports, Citi Investment Research and Analysis

Figure 6. BX Summary Model (cont)

Blackstone (BX)		William R. Katz															
Earnings Results and Forecasts		(212) 816-5394															
(\$ Millions, Except As Noted)		william.katz@citi.com															
KEY FORECAST VARIABLES:	1Q11	2Q11	3Q11	4Q11	1Q12	Forecast:			2011	Forecast:			% Change				
						2Q12E	3Q12E	4Q12E		2012E	2013E	2014E	2Q12E/1Q	2Q12E/2Q	12E/11	13E/12E	14E/13E
Private Equity Funds																	
Total Management Fee	107.4	127.0	100.5	103.1	100.1	108.5	109.6	110.1	437.9	428.3	441.5	442.0	8.4	-14.6	-2.2	3.1	0.1
Total Performance Fees & Allocations	114.9	188.6	-288.0	55.4	38.0	10.8	55.1	65.6	70.9	169.4	327.3	1,358.0	-71.6	-94.3	139.0	93.2	314.9
Total Investment Income (Loss)	47.0	80.0	-101.1	28.6	30.4	38.7	40.3	41.9	54.5	151.4	173.5	199.6	27.5	-51.6	177.9	14.7	15.0
Interest Income	3.5	3.2	3.4	3.7	2.4	1.4	1.4	1.4	13.7	6.5	9.5	9.5	-43.3	-57.1	-52.5	45.2	0.0
Other	0.8	0.7	0.1	0.2	-0.2	0.3	0.3	0.3	1.8	0.5	0.5	0.5	-216.3	-62.4	-70.4	0.0	0.0
Total Segment Revenues	273.7	399.4	-285.1	190.9	170.7	159.6	206.6	219.2	578.8	756.1	952.4	2,009.6	-6.5	-60.0	30.6	26.0	111.0
Total Segment Expense	96.8	124.1	32.6	84.2	80.7	84.4	93.8	96.2	337.7	355.1	403.6	754.9	4.6	-32.0	5.1	13.7	87.0
Economic Net Income (Loss)	176.8	275.3	-317.7	106.7	90.0	75.2	112.8	123.1	241.1	401.0	548.8	1,254.7	-16.4	-72.7	66.3	36.8	128.6
Margins:																	
Base comp % Management Fees	51%	51%	52%	44%	52%	50%	50%	50%	50%	51%	50%	51%					
Segment FRE (after-tax) margin	23%	26%	22%	24%	19%	24%	24%	24%	24%	23%	23%	22%					
Segment ENI (pre-tax) margin	65%	69%	111%	56%	53%	47%	55%	56%	42%	53%	58%	62%					
Real Estate																	
Total Management Fee	116.5	146.0	116.6	120.3	153.6	139.0	144.6	144.5	499.3	581.7	634.5	681.1	-9.5	-4.8	16.5	9.1	7.3
Total Performance Fees & Allocations	370.7	450.3	-114.9	243.4	238.0	136.0	202.7	215.9	949.5	792.6	1,006.6	1,248.0	-42.9	-69.8	-16.5	27.0	24.0
Total Investment Income (Loss)	555.6	648.5	-15.2	392.4	427.2	314.8	388.6	403.3	1,581.3	1,533.9	1,839.1	2,154.9	-26.3	-51.5	-3.0	19.9	17.2
Interest Income	3.3	3.0	3.2	3.4	2.6	3.0	3.0	3.0	12.9	11.6	12.0	12.0	17.6	0.4	-10.5	3.9	0.0
Other	0.9	0.5	-1.4	-1.0	-0.7	0.0	0.0	0.0	-1.1	-0.7	0.0	0.0					
Total Segment Revenues	555.6	648.5	-15.2	392.4	427.2	314.8	388.6	403.3	1,581.3	1,533.9	1,839.1	2,154.9	-26.3	-51.5	-3.0	19.9	17.2
Total Segment Expense	193.7	194.0	50.2	141.6	159.9	146.1	175.6	181.2	579.5	662.9	810.3	932.7	-8.6	-24.7	14.4	22.2	15.1
Economic Net Income (Loss)	361.9	454.5	-65.4	250.8	267.2	168.7	213.0	222.1	1,001.8	871.0	1,028.8	1,222.2	-36.9	-62.9	-13.1	18.1	18.8
Margins:																	
Base comp % Management Fees	49%	48%	47%	44%	45%	45%	45%	45%	47%	45%	45%	45%					
Segment FRE (after-tax) margin	28%	36%	32%	31%	35%	34%	34%	34%	32%	34%	34%	35%					
Segment ENI (pre-tax) margin	65%	70%	430%	64%	63%	54%	55%	55%	63%	57%	56%	57%					
Hedge Fund Solutions (BAAM)																	
Total Management Fee	76.2	80.0	79.8	81.7	81.6	88.7	93.7	97.8	317.7	361.8	430.8	499.6	8.7	10.9	13.9	19.1	16.0
Total Performance Fees & Allocations	20.1	4.1	-14.1	2.1	26.5	12.8	21.0	25.6	12.2	85.8	110.5	133.6	-51.8	210.6	600.7	28.8	20.9
Total Investment Income (Loss)	8.5	0.0	-9.0	-0.8	8.9	3.5	3.6	3.6	-1.3	19.6	14.9	16.0	-60.6	N/A	-1,596.2	-24.1	8.0
Interest Income	0.5	0.5	0.5	0.5	0.4	0.5	0.5	0.5	2.0	1.9	4.0	4.0	29.5	5.9	-6.9	112.1	0.0
Other	0.1	0.0	0.0	7.8	-0.1	0.0	0.0	0.0	7.9	-0.1	0.0	0.0					
Total Segment Revenues	105.4	84.5	57.2	91.4	117.2	105.4	118.8	127.5	338.5	468.9	560.2	653.2	-10.0	24.8	38.5	19.5	16.6
Total Segment Expense	46.8	51.0	40.1	59.9	50.8	55.5	61.0	64.7	197.8	232.1	264.1	293.1	9.2	9.0	17.4	13.8	11.0
Economic Net Income (Loss)	58.7	33.5	17.1	31.5	66.4	49.9	57.7	62.8	140.8	236.8	296.0	360.2	-24.8	48.8	68.2	25.0	21.7
Margins:																	
Base comp % Management Fees	37%	40%	38%	47%	35%	41%	41%	41%	41%	40%	37%	35%					
Segment FRE (after-tax) margin	44%	38%	41%	34%	45%	40%	41%	41%	39%	42%	45%	48%					
Segment ENI (pre-tax) margin	56%	40%	30%	34%	57%	47%	49%	49%	42%	51%	53%	55%					
Credit Businesses (GSO + CEFs)																	
Total Management Fee	55.3	58.2	59.5	67.1	85.5	84.9	88.3	91.4	240.0	350.1	379.5	417.1	-0.7	46.0	45.8	8.4	9.9
Total Performance Fees & Allocations	95.0	30.1	-40.3	57.0	83.3	39.6	43.0	46.7	141.8	212.5	215.6	268.5	-52.5	31.4	49.8	1.5	24.6
Total Investment Income (Loss)	5.8	8.7	-5.0	1.1	9.9	1.8	1.8	1.8	10.6	15.2	7.4	8.0	-82.3	-79.8	44.0	-51.3	8.0
Interest Income	0.5	0.9	1.4	0.6	2.4	0.5	0.5	0.5	3.4	3.9	4.0	4.0	-79.4	-44.6	16.5	1.9	0.0
Other	0.1	0.0	-0.1	-0.8	-0.2	0.0	0.0	0.0	-0.9	-0.2	0.0	0.0					
Total Segment Revenues	156.7	97.8	15.4	125.1	180.9	126.7	133.5	140.4	395.0	581.5	606.5	697.6	-29.9	29.6	47.2	4.3	15.0
Total Segment Expense	95.4	56.1	31.5	70.4	93.7	75.7	79.1	82.5	253.4	331.0	343.8	384.1	-19.2	34.9	30.6	3.9	11.7
Economic Net Income (Loss)	61.3	41.7	-16.1	54.7	87.2	51.0	54.4	57.9	141.6	250.5	262.7	313.5	-41.5	22.4	76.9	4.9	19.3
Margins:																	
Base comp % Management Fees	53%	57%	68%	38%	43%	50%	50%	50%	54%	48%	48%	47%					
Segment FRE (after-tax) margin	18%	24%	14%	37%	33%	25%	26%	26%	23%	27%	28%	29%					
Segment ENI (pre-tax) margin	39%	43%	-104%	44%	48%	40%	41%	41%	36%	43%	43%	45%					

Source: Company reports, Citi Investment Research and Analysis

## **Blackstone Group L.P.**

### **Company description**

Established in 1985, The Blackstone Group is a leading, NY-based global and diversified alternatives manager with \$190B in AUM at 3/31/12 including \$48B in Private Equity, \$48B in Real Estate, \$43B in Hedge Fund Solutions, and \$51B in Credit Businesses, along with an independent financial advisory practice. The Blackstone Group was founded by Mr. Stephen A. Schwarzman and Mr. Peter G. Peterson and the company launched its first Private Equity fund, Blackstone Capital Partners two years later. Over time, the business model evolved from a leverage buyout firm to a global provider of alternative investments across multiple assets classes. In 1990, Blackstone Alternative Asset Management (BAAM) was established and has become one of the leading managers of funds of hedge funds and other institutional investment vehicles. Over the last 20 years, Blackstone has expanded its capability by adding real estate & credit investment functions, by growing its international presence and by delivering strong investment results to its investors. Blackstone became a publicly-traded company in 2007 through an IPO, raising \$7.6 billion, including a \$3 billion investment from the China Investment Company (CIC).

### **Investment strategy**

We rate Blackstone Buy. We believe BX has a diversified and high powered financial model that is well positioned to capitalize on a rebounding economy at a favorable point in the private equity/real estate cycle. We believe the units are undervalued when considering the depth of franchise and performance fee potential, where investors appear to be ascribing a low valuation, despite an impressive LT track record.

### **Valuation**

We value BX using a sum-of-the-parts (SOTP) approach that combines target P/E, book value, and NPV. In turn, our \$19 12-month target factors: 1) 15x target multiple applied to our 2012 FRE estimate of \$0.54, or ~\$8.20 in value; 2) ~\$8 for the net present value of performances across Private Equity, Real Estate, Credit, and Hedge Fund Solutions segments; and, ~\$3.10 in net cash and investments and unrealized carry (discounted by 20%).

### **Risks**

The three central risks to our price target reflect slowing investment performance, slowing organic growth, and adverse carried interest legislation.

Additionally, if the impact from any of the following factors proves to be greater than we expect, the unit price may have difficulty reaching our target price. If market conditions improve faster than anticipated, the unit price may outperform our target.

Financial market risk — Changes in markets will impact the comps used in the valuation of BX's portfolio companies. Such values will have a direct impact on AUM and IRRs.

Performance risk — An inability to generate an adequate return sought by clients could result in prospective clients choosing to invest with competitors.

Performance fees — The lack of positive IRR's in BX's private equity funds would limit the company's ability to generate carried interest.

Financing — Private equity firms use funding from the capital markets, both large commercial and investment banks. Financing will vary regarding: 1) interest rates; 2) equity commitments; 3) debt covenants. Generally, when more capital is available, private equity portfolio companies have greater access to financing with acceptable terms. When capital markets become more restrictive, it can be more challenging for portfolio companies to refinance debt and/or for sponsors to arrange acquisition funding, thus limiting deal activity.

(TROW.O; US\$61.76; 3)

## T Rowe Price Group Inc

### Valuation

We value the shares of T. Rowe price using the Target P/E method. Our \$56 12-month price target is derived by applying a 17x target multiple to our 2012 EPS estimate. The 17x multiple compares to a historical 21x FTM P/E multiple in light of lower industry multiples at present.

### Risks

If the impact from any of the following factors proves to be greater than we expect, the stock price may have difficulty reaching our target price. If market conditions improve faster than anticipated, the stock price may outperform our target.

Financial market risk — Changes in markets have a direct impact on AUM and investment advisory and services fees.

Performance risk — An inability to meet relevant investment benchmarks could result in clients withdrawing assets and in prospective clients choosing to invest with competitors. This could also result in lower investment management fees, which could result in a decline in revenue.

Redemption risk — Investors can redeem their investments without notice. A significant increase in redemption rates could have a material adverse effect on revenues, financial condition, results of operations and business prospects.

## Appendix A-1

### Analyst Certification

The research analyst(s) primarily responsible for the preparation and content of this research report are named in bold text in the author block at the front of the product except for those sections where an analyst's name appears in bold alongside content which is attributable to that analyst. Each of these analyst(s) certify, with respect to the section(s) of the report for which they are responsible, that the views expressed therein accurately reflect their personal views about each issuer and security referenced and were prepared in an independent manner, including with respect to Citigroup Global Markets Inc and its affiliates. No part of the research analyst's compensation was, is, or will be, directly or indirectly, related to the specific recommendation(s) or view(s) expressed by that research analyst in this report.

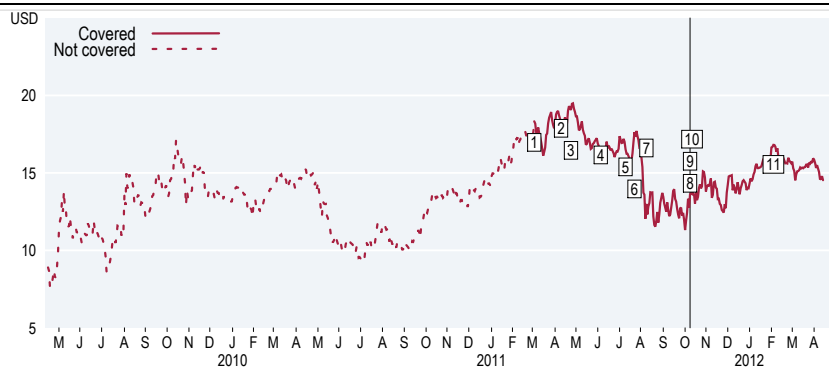
## IMPORTANT DISCLOSURES

### Blackstone Group L.P. (BX)

#### Ratings and Target Price History Fundamental Research

Analyst: William R Katz

Covered since March 3 2011



	Date	Rating	Target Price	Closing Price
1	3-Mar-11	*1M	*23.50	18.33
2	11-Apr-11	1M	*24.00	18.00
3	25-Apr-11	1M	*25.50	19.06
4	6-Jun-11	1M	*23.00	16.16

\* Indicates change

	Date	Rating	Target Price	Closing Price
5	11-Jul-11	1M	*22.00	16.53
6	22-Jul-11	1M	*24.00	17.63
7	9-Aug-11	1M	*20.00	13.00
8	8-Oct-11	Stock rating system changed		

	Date	Rating	Target Price	Closing Price
9	8-Oct-11	*1	20.00	12.75
10	12-Oct-11	1	*18.00	14.33
11	3-Feb-12	1	*19.00	16.81

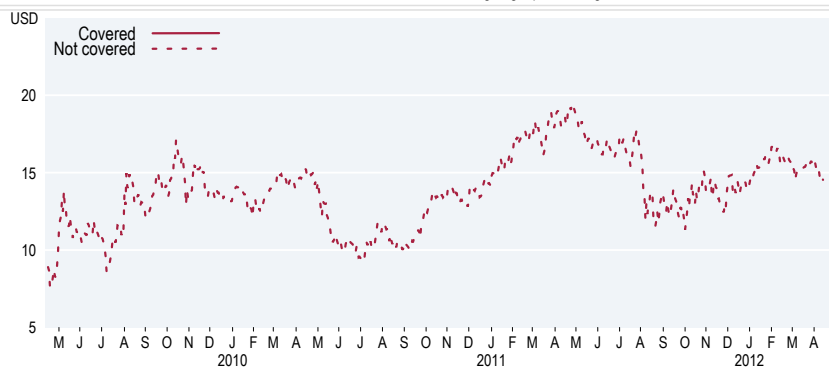
Rating/target price changes above reflect Eastern Standard Time

### Blackstone Group L.P. (BX)

#### Ratings and Target Price History Best Ideas Research Relative Call (3 Month)

Analyst: William R Katz

Covered since March 3 2011



\* Indicates change

Rating/target price changes above reflect Eastern Standard Time

### T Rowe Price Group Inc (TROW)

#### Ratings and Target Price History Fundamental Research

Analyst: William R Katz

Covered since March 31 2010



	Date	Rating	Target Price	Closing Price
1	8-May-09	2M	*39.00	40.94
2	2-Jun-09	*1M	*48.00	41.95
3	26-Jul-09	1M	*52.00	45.45
4	13-Oct-09	1M	*54.00	44.41
5	26-Oct-09	1M	*63.00	53.65
6	31-Mar-10	*1L	*62.00	54.97
7	23-Apr-10	1L	*66.00	58.88
8	27-May-10	1L	*60.00	51.47
9	18-Jun-10	1L	*57.00	49.34

\* Indicates change

	Date	Rating	Target Price	Closing Price
10	23-Jul-10	1L	*56.00	47.85
11	8-Oct-10	*2L	*53.00	51.62
12	14-Oct-10	2L	*54.00	52.52
13	22-Oct-10	2L	*57.00	54.89
14	21-Dec-10	2L	*63.00	64.27
15	28-Jan-11	2L	*67.00	65.85
16	11-Apr-11	2L	*70.00	67.30
17	19-May-11	2L	*67.00	63.73
18	6-Jun-11	2L	*63.50	58.04

	Date	Rating	Target Price	Closing Price
19	23-Jun-11	2L	*60.00	57.08
20	26-Jul-11	2L	*63.00	60.06
21	9-Aug-11	2L	*53.00	51.99
22	19-Aug-11	2L	*47.00	46.44
23	28-Sep-11	2L	*49.00	48.42
24	8-Oct-11	Stock rating system changed		
25	8-Oct-11	*2	49.00	49.06
26	1-Feb-12	*3	*50.00	58.62
27	16-Apr-12	3	*56.00	62.05

Rating/target price changes above reflect Eastern Standard Time

# T Rowe Price Group Inc (TROW)

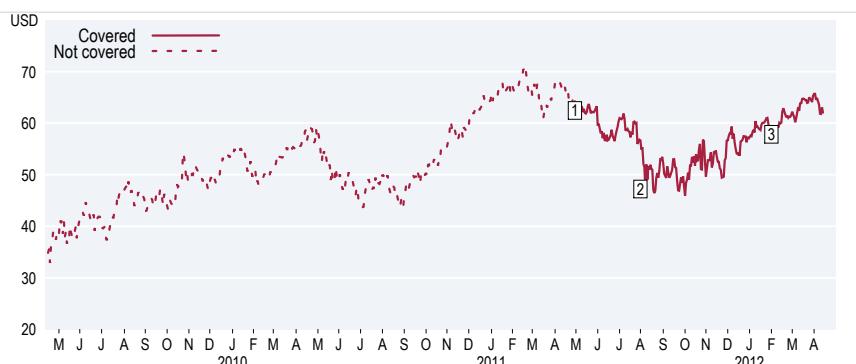
## Ratings and Target Price History

### Best Ideas Research

### Relative Call (3 Month)

Analyst: William R Katz

Covered since March 31 2010



	Date	Rating	Target Price	Closing Price
1	29-Apr-11	*ADD LP	-	64.25
2	1-Aug-11	*REM LP	-	56.67
3	1-Feb-12	*ADD LP	-	58.62

\* Indicates change

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### Data current as of 31 Mar 2012

	12 Month Rating			Relative Rating		
	Buy	Hold	Sell	Buy	Hold	Sell
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