

The Blackstone IPO: \$4 billion payday for private equity bosses

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An initial public offering of stock in the Blackstone private equity firm raised more than \$4 billion June 22, the bulk of it going to the firm's two founders, Stephen Schwarzman and Peter G. Peterson.

Blackstone partners sold 133.3 million shares at \$31 each to preferred customers, for a total of \$4.1 billion. The shares were repeatedly resold with heavy demand from institutional investors and pension funds, driving the price up to between \$35 and \$38 by the close of trading, with a total of 113 million shares changing hands after the initial offering.

Schwarzman, the firm's CEO and largest shareholder, sold shares worth almost \$700 million. He retains 24 percent of the total stock, worth about \$8.8 billion at the trading price. Even before his staggering windfall, Schwarzman was one of the highest-paid executives on Wall Street, raking in \$398 million last year.

Peterson, who is 81 and expected to retire from Blackstone later this year, sold most of his shares in the IPO, collecting \$1.8 billion in a single day. The balance of nearly \$1.6 billion was collected by others of the 48 Blackstone partners, including the company's president, Hamilton James, who netted \$148 million and retains a 5 percent stake worth nearly \$2 billion.

Blackstone is the largest IPO on Wall Street in five years, since the collapse of the dot-com bubble. The \$4.1 billion valuation on shares amounting to 12 percent of the total stock puts the company's overall market value at nearly \$40 billion, making Blackstone overnight one of the largest financial corporations in America.

The company, founded by Peterson and Schwarzman in 1985, was for more than 15 years a relatively minor player on Wall Street, managing capital for a handful of well-heeled investors. It took off over the last five years, going from \$14 billion under management in 2002 to \$70 billion in 2006, and an estimated \$88 billion today. The partnership reported profits of nearly \$2.3 billion last year and was involved in takeover deals totaling \$102 billion.

This mirrors the exponential rise of private equity companies and merger and acquisition activity, the driving force of the current stock market boom. In 2003, according to the newsletter *Private Equity Analyst*, buyout funds raised \$28 billion, doubling in 2004 and 2005 to reach \$113 billion, then rising

another 53 percent in 2006 to hit \$173 billion. Overall, mergers and acquisitions reached a staggering \$4.1 trillion worldwide, with much of that activity generated by private equity funds, hedge funds, and other new forms of finance capital.

Among the companies that Blackstone has taken over in recent years are the Chicago-based Equity Office Properties Trust, acquired in February for \$39 billion, Pinnacle Foods (with brands like Duncan Hines, Vlasic and Aunt Jemima), Freescale Semiconductor, Michaels Stores, Celanese, Foundation Coal and New Skies Satellites. It also has significant minority shareholdings in major telecommunications companies, including Deutsche Telekom (\$3 billion), and owns several software, healthcare and media companies.

Blackstone-controlled companies employ more than 350,000 people, making it an economic entity comparable in that respect to General Electric or Citibank, although the actual payroll employees of Blackstone itself number only 770, mainly at its midtown Manhattan headquarters.

Private equity firms represent a new form of capitalist organization, in which individual capitalists, possessors of wealth to the tune of tens of millions and more, pool their resources under the management of the partners who run the firm. Typically, the managers collect fees of up to 2 percent of the total assets in their charge, plus an additional 20 percent of all profits above a targeted minimum rate.

Such firms have had three principal advantages over traditional joint-stock companies. They are largely unregulated by any level of government; they do not face share market pressure to meet quarterly or annual earnings targets; and they have easy access to capital, both from the private investors they represent and in the form of debt, at the relatively low interest rates which have prevailed over the past six years.

From the standpoint of society as a whole, the operations of a private equity firm are parasitic. Its few employees do not produce anything, and their "work" is largely destructive: eliminating jobs, wages and benefits in the companies targeted for restructuring, closing down and selling off factories and other facilities.

From a class standpoint, a private equity firm is a shameless form of exploitation, as a few dozen capitalists join forces to plunder the assets of hundreds of thousands of working people,

destroying their livelihoods and their economic future to make the already insanely wealthy even more so.

Schwarzman and Peterson personify the deepening class chasm in 21st century America. Schwarzman, a heavy contributor to the Republican Party and the Bush presidential campaigns, has an 11,000-square-foot Palm Beach home that was profiled in the *Wall Street Journal*, which reported that his private chef frequently spends \$3,000 for a single weekend of food for the CEO and his wife—more than many low-income families spend for food in the course of six months. For his 60th birthday party earlier this year, Schwarzman rented the Park Avenue Armory in Manhattan, where Rod Stewart and Patti Labelle performed for hundreds of invited guests.

While his partner flaunts his wealth, Peter Peterson, former CEO of Lehman Brothers and secretary of commerce in the Nixon administration, devotes much of his time to the Concord Coalition, which lobbies for austerity in federal budgeting, incessantly demanding an end to “overspending” on Social Security, Medicare, Medicaid and other programs that underwrite the health and financial survival of tens of millions of elderly and impoverished Americans.

This hypocritical combination of private money-grubbing and public moralizing is underwritten by working class taxpayers. A key element in the financial success of private equity firms, as well as hedge funds, is that the enormous fees collected by the partners are not taxed as income, at a rate of up to 35 percent, but as capital gains, for which the rate was slashed to 15 percent in 2001 as part of the Bush administration’s tax cuts for the wealthy.

The *New York Times* reported that Blackstone earned \$1.1 billion in operating income in the first quarter of 2007 and paid only \$14 million in taxes, about 1.3 percent.

As plans for the Blackstone IPO were made public over the past two weeks, there was a round of predictable posturing by congressional Democrats. They suddenly discovered the gross unfairness of taxing billionaires at a much lower rate than day laborers, and vowed to do something about it (secure in the knowledge that anything they propose will be vetoed by Bush).

Congressmen Dennis Kucinich of Ohio and Henry Waxman of California wrote to the Securities and Exchange Commission, which regulates the stock market, urging its chairman, Christopher Cox, to delay the Blackstone IPO. They claimed to be concerned that the unusual financial structure now assumed by Blackstone—as the first private equity firm to become a publicly traded company—could present “potential investors and the public with new and undisclosed risks.” Their request was turned down, as they knew it would be.

Democrat Max Baucus and Republican Charles Grassley, the chairman and ranking minority member of the Senate Finance Committee, introduced legislation to require private equity firms to pay taxes at the 35 percent corporate rate if they follow Blackstone’s example and go public.

Baucus and Grassley co-authored the Bush tax cut in 2001,

with Baucus playing the key role in rounding up enough Democratic support to insure passage—including approval of the 15 percent capital gains rate which he now claims is unfair. The bill is a publicity stunt, since, even if enacted, it would cushion the impact on Blackstone by providing a five-year grace period.

Another bill was submitted by Democratic congressman Sander Levin and backed by 13 other leading Democrats, including Charles Rangel, chairman of the House Ways and Means Committee, and Barney Frank, chairman of the Financial Service Committee. It would impose the corporate tax rate of 35 percent on most partnerships, including hedge funds, regardless of whether they launched IPOs. Levin downplayed any punitive intent, saying, “I am not trying to soak the rich; I am trying to find tax equity.”

All of these lines of attack on the Blackstone IPO are media hocus-pocus, aimed at striking a populist pose before the congressmen and senators go back to doing the bidding of the corporate oligarchy behind closed doors. There is only one threat to Blackstone that could prove more than play-acting—an effort by Senator James Webb, a Democrat of Virginia, to whip up chauvinism and anti-communism.

Webb noted that Blackstone recently agreed to sell a \$3 billion stake, about 9 percent of the firm, to the Chinese government, and suggested that this might give China access to sensitive information and technologies in companies controlled by Blackstone, which include high tech and telecommunications firms which do work for the Pentagon.

Left unstated was the more serious concern that the Chinese government, currently holding \$414 billion in US Treasury debt, might be shifting some of these assets. Such a move would have a triple effect, putting greater pressure on the US dollar on world currency markets, undermining the ability of the US government to continue financing military aggression with money borrowed from China and other Asian countries, and raising the prospect of major American firms being targeted for takeover by Beijing.



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