

Goldman Sachs Exchange: Great Investors
Blackstone's Kathleen McCarthy on the forces shaping
the real estate industry

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Alison Mass: Welcome back to another episode of Goldman Sachs Exchanges: Great Investors. I'm Alison Mass, Chairman of Investment Banking in Goldman Sachs' Global Banking & Markets business. And your host for today's episode.

Today I'm delighted to be speaking with Kathleen McCarthy, Global Co-Head of Real Estate at Blackstone, the world's largest owner of commercial real estate.

Before joining Blackstone, Kathleen began her career here at Goldman Sachs, starting in the M&A group before moving to the firm's Real Estate Principal Investment business. Kathleen joined Blackstone in 2010 and rose swiftly through the ranks to become the Global Co-Head of

Real Estate in 2018. Under her leadership, Blackstone's real estate assets under management have grown more than 300 percent to over \$330 billion. And today accounts for more than 30 percent of the firm's record \$1 trillion of assets under management.

We'll be talking with Kathleen about her journey to become one of the leading investors in the real estate industry, the forces shaping key sectors of the market, and her advice to the next generation of leaders.

So, Kathleen, welcome back to Goldman Sachs and to the program.

Kathleen McCarthy: Thanks, Alison. Nice to be here.

Alison Mass: So, let's start with your early career. You graduated from Yale where you majored in ethics, politics, and economics. With that liberal arts background, why did you decide to come into finance?

Kathleen McCarthy: Liberal arts is a great place to learn how to process a lot of information and think and write, which probably turned out to be the most important skills

in any career. But coming out of school I really wanted to develop a set of professional skills that could serve me no matter what I do.

At the time, I certainly had no idea of who I wanted to be when I grew up. And I felt like coming to a great investment banking program at a great firm like Goldman would give me this platform to learn analytical skills and persuasion skills and influencing skills. And also, just get the experience of working in teams under pressure and aiming for really high-quality outcomes for your clients.

Alison Mass: As you mentioned, you started your career at Goldman Sachs in the M&A group and later transitioned to the Real Estate Principal Investment group here, which we call PIA or called PIA. So, what drew you to investing in real estate in particular?

Kathleen McCarthy: It was a little bit of an unconventional choice because I think at the time, most of my peers were looking to move to more traditional buyout kind of private equity. Particularly folks who'd been doing M&A banking.

I think I was attracted to the idea of just real assets, things that you can understand in a real tangible way — why people want to live or work or shop somewhere. And I also really liked the kinds of people I started meeting in the real estate sector. There wasn't one type of person. People had all kinds of different backgrounds. Certainly, some coming out of finance. But there were lawyers and engineers and architects. And it led to a really interesting cast of characters on different teams.

And of course, at Goldman, there was just this wonderful group of human beings and the opportunity to stay and stay in that great culture was really appealing to me.

Alison Mass: That hasn't changed, just so you know. So, you were investing in real estate and housing at Goldman Sachs in the mid to late 2000s, which put you front and center of the 2008 global financial crisis. So, tell us what that was like.

Kathleen McCarthy: I feel pretty fortunate, actually, to have been front and center for three sharp downturns before I was 30. So, the global financial crisis, obviously, the biggest and most memorable. But even before that as a

first-year analyst I lived through the dotcom bubble which led to a merger market meltdown. And I was a merger banker. We, of course, had September 11th.

And and I would say that I took out of those experiences really three primary things. One about investing, one just general professional, and three about managing.

On investing, what I've learned is that if you have good quality assets and companies, and a resilient capital structure, you can ride through almost anything. And I would say, and particularly in the global financial crisis, we saw how resilient flexible capital structures mattered so much. And so many real estate investors in particular lost assets because they weren't able to ride through.

On general professional skills, I'd say in each of these experiences I learned that things can change quickly. And you just got to deal. In 2000 and 2001, I had been under the impression that I'd be working on these mega mergers. We had this amazing analyst training program at Goldman where we spent eight weeks hearing about just the gigantic deals we were going to work on.

And my first staffing, I think, was on a \$40 million carve out of a water technology company. And while it was different, it didn't matter. I learned so much. I worked with great people. And I've seen that happen over and over again. I mean, later in my career, in the real estate principles group, I got staffed on writing a private placement memorandum. And that wasn't what I thought I'd be doing as an acquisitions associate.

But that has served me so well in learning how to work with clients, learning how to build fund structures, learning how to think about fundraising and capital management as a business.

So, things change. And that's okay. You just pivot and keep going.

And then the final thing from a management perspective, I think we all are learning lessons as we're being managed and as we're working on our management skills. And I've seen over and over again how transparency in communication is so important. And I heard folks say that the things that are most important to communicate are the things we don't communicate enough about.

And I feel like covid actually was a good example of this. Where, as we were preparing to reopen our office in summer of 2020, we in leadership positions were talking constantly about employee safety and how we were going to bring people back and how we were going to communicate to them about the importance of coming back together.

And, you know, I would get phone calls from our young professionals saying, "Is anybody thinking about how we're going to stay safe?" And I could think was, of course we're thinking about that. That's all we're thinking about. But we weren't telling them that.

And I think particularly in moments of uncertainty, it can be about the market, it could be something like COVID, talking to your team about what you know, what you don't know, how you're thinking through tough decisions is so important.

Alison Mass: Yeah, those are absolutely fantastic lessons. And I always say on the deal size, that sometimes there's an inverse relationship between the size of the deal and your experience as a junior banker because on the mega

deals, there could be a team of 12 people.

Kathleen McCarthy: You're totally right. And that was definitely my experience.

Alison Mass: Yeah. So, in 2010, sadly, you moved from Goldman to Blackstone where you took on an investor relations role before you were promoted to global chief operating officer in 2014. In 2018, you were named to your current role of Global Co-Head of Real Estate. Talk about your approach to building up the real estate business during the time you've been at Blackstone.

Kathleen McCarthy: We always start with performance. Where are we performing well? What is creating those distinguishing advantages? And how can we do more of that for more clients?

So, during my time at Blackstone, we really built on the most successful opportunistic real estate investment strategy. And expanded into lending and buying real estate securities. And then more recently into core plus real estate where we buy more stabilized assets.

And in each of these instances, what really happened was we were in dialogue with our clients about what we were doing well and what they wanted more of.

And so, following the financial crisis, we had an opportunity to really get going in the capital markets as a lender, as a securities buyer. And we saw that when we did that, actually expanding what we did gave us more information, more insights, more data and made us better at our original business.

And that kind of experience also then gave us confidence to go into more things in equity investing, which is our core plus strategy.

Most recently, of course, we've also been able to offer more of our products to individual investors. And again, that was just a view that we have a terrific process. We have distinguishing advantages as an investor. And we want to be able to offer that to more people. And by offering it to more people, more clients, that has given us more data, more insights, and that feeds into better outcomes for all of our clients and all of the things we do.

Alison Mass: So, Blackstone is known for its thematic and high conviction approach to investing. So, how do you apply that investing lens to the real estate world?

Kathleen McCarthy: The first thing you do is you step back from what's immediately in front of you in real estate assets and say, what is happening in the world? What are the megatrends impacting how people are living and working and spending their time and spending their money? And which assets are going to benefit from that?

And conversely, which assets are going to be more challenged by those changes? And the greatest example of this in our business is what we've been able to do for our clients with warehouses. One of the fun things that I've experienced in my career, many of my colleagues too, is that all of the rules changed during the last 20 or so years.

Historically, everybody wanted to own a class A office building, or they wanted to own a regional shopping mall. And today, of course, and I'm sure we'll talk about this, those are more out of favor. And instead, the best performing assets are things like warehouses. And it's because technology changed our lives.

E-commerce has completely changed the demand trends for warehouses. And it's done that all over the world. And so, that was a megatrend we invested behind. We said, okay, technology's changing. Where the shopping is getting done, we want to invest our clients' capital into the assets that are benefiting from that. And conversely, try to stay away from things like regional malls. We haven't bought one in over a decade.

And that has been the story of the benefit of investing behind high conviction themes. And logistics isn't the only place. We've done that with rental housing. We've done that with hospitality. Data centers more recently. But it's this idea that we do in real estate, and we really do as a whole firm, of saying what's happening in the world? And let's try to position our capital in the things that are benefiting from that.

Alison Mass: So, Blackstone's chairman, CEO and co-founder Steve Schwarzman has said that great investors are strong at pattern recognition, which is a skill that you've applied throughout your investing career. So, can you reflect a little bit on that and how that skill has helped

you?

Kathleen McCarthy: I think my first reflection is just to think about the benefit of investing alongside people who have just tremendous experience. And Steve, of course, number one for that, probably in the world, and certainly at Blackstone.

And there's also, of course, a huge benefit to having so much data. We own \$600 billion of real estate. It's almost 13,000 assets. And we funnel all of the information we're getting from that real time into all the decisions we're making. Of course, where we're investing. But also, how we're deploying value creation strategies and then also making decisions about what we want to sell.

And I think the art of pattern recognition is being able to quiet noise and look at the information you have, not just about what's going on right now, but what has led to successful outcomes? And conversely, what has led to more challenging outcomes? And reapply those learnings and that information into different situations.

And an example of how we do this, again, goes back to

logistics. We had built up great portfolios and platforms in the US. Starting in 2010, we took that strategy to Europe and to Australia. And one place we hadn't gone was Canada. And we didn't enter Canada in 2018 simply because it was north of the border. It was because we looked at the facts on the ground in Canada and said, "Where have we seen this before?"

At the time in 2018, e-commerce penetration there was half of what it was in the US: 7 percent of sales versus 14 here. We saw that the big e-commerce retailers hadn't really yet entered that market. We had lived through that experience in Australia. And we said, okay, how do we get into this? But let's get into this in a way only we can.

Rather than try to do lots of little things, we took private a company that put us in the best markets, the key markets, with the most demand and the least supply. And I think what we do is just try to bring together that combination of experience and information and find how to reapply that. And that is what pattern recognition means to us.

Alison Mass: And you're clearly at an advantage with that size portfolio and the fact that you're able to use the data

that way.

Kathleen McCarthy: Absolutely.

Alison Mass: Extraordinary.

Kathleen McCarthy: And I think the greatest advantage of our information is the culture around it. So, of course, we and so many others focus on the systems we use to harness the information and the dashboards we build to serve it up to decision makers. But I know a lot of investors who have lots of data. And their question usually for us is how do you get anybody to use it.

And I think that comes down to having a team and a process that values questions about what the information is telling us. So, in our investment committee or in our review committee, you can pretty much guarantee that most of the conversation is going to be about what do we know based on information we have and often uniquely have? And how is that informing choices we're making in our underwriting? And also, trying to use those moments as a moment of real honesty of what's working or what's working better than we thought? And what's working less

well than we thought?

And I do think though it really comes down to how do you talk about the data? How do you use it? And is it valued in your process? And I think that's something we've had long before we had great technology to utilize to harness information.

Alison Mass: Well, talking about the culture of investing and your process, within investing there's always this tension between growing the capital base and the pressure to invest capital. How do you incentivize your people to make good investment decisions versus just rushing to put money to work?

Kathleen McCarthy: I think alignment with our investors is so important. And we do that in a couple of key ways. First is, of course, economics. We and our team invest heavily in all of our investment strategies. So, that just means we have capital on the line, our money, alongside our clients.

And then the other thing we do is we have incentive compensation, which means that we win when our clients

win. And we share that incentive compensation really broadly in our team down to very junior levels. So, those kinds of incentives, that kind of alignment doesn't guarantee perfect outcomes. But it means that you're all heading in the right direction and in the same direction with your clients.

I think the other thing I try to do to create that alignment is really try to draw as many people as possible into the experience of getting to know our investors, spending time with them. I think there's no substitute for looking at client in the eye and understanding their responsibilities and their obligations to the beneficiaries they have because what it does is it makes you realize an institutional investor or an individual considering one of our products isn't a thing. It's a human being. And I think for me personally, I feel great responsibility for the capital we manage because I understand who that's ultimately benefiting.

And I think if we can get our young people, and certainly our folks who have responsibility for committing capital to understand that and know those people, I think it does impact the outcomes. And always for the better.

Alison Mass: You're enormously popular among the investors in the industry. And some have characterized your leadership approach as emphatic and authentic. You've also encouraged your teams to bring their whole selves to work. So, where does the inspiration behind your leadership spring from?

Kathleen McCarthy: We're in the middle of our 360-review process. So, we'll have to check back in a couple weeks to see if my colleagues think I am actually that popular.

Alison Mass: I'm ready.

Kathleen McCarthy: You're very generous. You're being very generous. I'd say all of us through our whole careers are looking at leaders and probably trying to take the best of. And I'm certainly doing that. I continue to do that. I think as far as style, I've learned, particularly in the last five years, that I am my best self when I'm just who I am. And I remember being much younger in my career and being a beneficiary of an incredible training program at Goldman and hearing about how leaders plateau when they try to be something they're not.

And, of course, my young and naïve self is like, "Oh, that'll never be me." But I think the reality is probably five or six years ago, there were a lot of people telling me what my leadership should look like, how I should spend my time, how I should approach things and approach people.

And that advice was all very well intentioned. But I think it led me to be much more stiff and uncomfortable in my own skin. And when I freed myself of that and realized that just being your authentic self, of course trying your best and trying to learn lessons of other leaders, if I do that all along the way, leads to better outcomes.

And as far as bringing my whole self to work or having anyone bring this whole self to work, I just don't really know any other way. And certainly not now. And I think parenting, actually, has been both a humbling and a learning experience in this regard because I realized that people have a huge life outside of work, even our closest colleagues. We may not understand all that's going on with them. And I don't really believe, particularly in these big, intense jobs, that you leave it all at home or you leave it all at work. I think it's all integrated.

And so, I try to approach people and situations assuming positive intent. I hope people will approach me in the same way. And I also try to keep in the back of my mind that they may have a lot going on that goes beyond whatever we're talking about or whatever we're doing in the moment. And that's okay.

And I think that's how we're all going to achieve longevity in our careers and with our teams is just to always be supporting each other in making our ways through tough stuff, and great stuff, at work and in life.

Alison Mass: Which is my answer usually when people ask me how I'm literally still doing this 42 years after I started.

So, let's talk about Blackstone's culture. You know, you've sustained strong performance over the last 30 years. And many of your senior leaders have stayed with the firm over that period of time. So, how has Blackstone been able to maintain that performance within real estate, across geographies, and other strategies over all of those decades? And what do you think makes the platform, and more importantly, the culture so special?

Kathleen McCarthy: It is a really special place. And I think it's because every single person and every single job is oriented around excellence. Doing the very best they can do, we can do, and delivering the very best outcomes for our clients.

And it really is remarkable to work at a place where that is so universally true. And I sometimes describe it as, you know, if you were the kid in high school who did all the work on the group project, you found your place with us.

And I love that because I know I go into work everyday arm in arm with people who are trying to drive to the best possible thing, just like I am. And I think that, and that culture, keeps us all going. Keeps us all motivated. We're fighting always against complacency. And I think behind your question is the point that oftentimes companies as they grow, they lose what made them special in the first place.

And I think we are always fighting against that by trying to continue to enrich this value of aiming at excellence, doing that as a team, and keeping people super connected and connected to the mission of the work.

And I think the connectivity is important. And it goes to the importance of being able to have a team that everywhere in the world and every function has consistent culture. Some of that is attracting people who really believe in that and want to work in that way. There's no kind of lone wolves in our system.

But it's also talking about and valuing the rewards of that behavior in terms of the outcomes we can generate. It's a really special place.

Alison Mass: Blackstone's a really big organization. And continuing on the theme you were just talking about, how do you encourage a culture of innovation and decide to move into new growth areas?

Kathleen McCarthy: I think, first of all, you have to be encouraging innovation in absolutely everything you do. And I spend a lot of my time on the noninvestment areas of our business, as well as our investments. And I think there's definitely a benefit of being in an investment culture, because when you're an investor, the things that worked in the past or even yesterday aren't going to work

the same way again. And so, you're always having to innovate your approach.

But I think particularly in an organization that's growing and then gets big, you have to make sure people have the freedom and actually the encouragement to keep evolving and innovating how we do things. And I try to really push this with our team.

Any time I hear someone's frustrated with a process or feels like what we're doing is hard on the system or isn't having the impact we want, I try to help drive change in that because I feel like if people start feeling like the process has calcified, that is very discouraging. And you just feel like you're inside a bureaucracy. We are not a bureaucracy. Like I said about excellence, we have the opportunity every day to show up and try to make things better. And that's not just about our investing, it's also about how we're operating our business.

And so, I think the innovation has to be in everything you do. But I think it really is, I think, sometimes folks get afraid to talk to a leader about something that isn't working because all kinds of stories build up about an analysis or a

process that was very important to a leader, for example, in my life. I will get calls from people sometimes who say, "In 2015 after our investor conference, you said the following should be done a different way." And I don't even remember that conversation from 2015. And I say, "Okay, if it's not working for us anymore, let's just stop doing it or let's change how we do it."

And so, I've now started saying to people, "If you hear something is important to me or to a senior leader, first ask if you heard that directly. And second, ask when you heard that. If it's more than about two months ago, let's try to revisit it." I think that kind of innovation is so important.

I think the other part of innovating is, again, thinking about what are needs of your clients and how are those changing. And we have a front row seat to this both with institutional and individual clients. And I think we have the opportunity and we certainly have had them in the past, to bring new concepts and new ideas that meet the new challenges.

So, for example, part of the reason we were able to grow a core plus business was our institutional clients were really

struggling with reinvestment in high quality real estate. And we said, okay, we can do that for you with perpetual capital vehicles. It doesn't have to look like the same opportunistic draw down fund we've had in the past. And so, we evolved to meet those needs.

Alison Mass: So, you co-lead the real estate business with Ken Caplan. And not all co-leadership roles work and partnerships work. But it really works well with you and Ken. So, why do you think that is?

Kathleen McCarthy: It starts with deep trust. We trust each other immensely. And that solves almost all the problems that could arise in co-leadership, I think. We also trust that each other can be a surrogate as we often are. And we have a tremendous amount of communication all the time to continue building that trust.

I think the other benefit we have is that we've really tried to divide our roles functionally. We're not trying to do all the same things everyday. I think about it as we're swimming in the same lane all the time, but maybe not always doing the same stroke.

And the one thing we definitely do together is talent management. Thinking about where our team needs greater reinforcement. Where we need to be in touch with individuals or teams to really help them do what they're doing, continue to build skills and deliver the outcomes we're trying to deliver?

But beyond the talent, our roles somewhat mirror what we were doing as we were growing up through the Blackstone system. So, Ken had been the chief investment officer. Which means today he wakes up everyday focused on what we're buying, what we're not buying, our asset management strategies, our disposition plans. And that's his kind of major, if you will.

His minor is all of the other things that come in an investment business around our team development and what the business of Blackstone Real Estate looks like.

My story, my majors and minors are the opposite. So, I wake up everyday really focused on our clients, how we're engaging with them, the products we're delivering for them, our team structure. Do we have all the right people in the right places to do the things we need to do?

And I spend a lot of time with external engagement every beyond investors. And so, I think the combination of dividing the world into this kind of idea of majors and minors, where it's really clear for the team and it's really clear for us what needs our focus has been enormously helpful to our co-leadership.

Alison Mass: So, I want to talk about the macro.

Blackstone's done a really good job of getting the macro right. Focusing on sectors, as you mentioned, that are poised for outperformance and avoiding the ones that are not. For example, you mentioned logistics, one of the strongest performing sectors in real estate.

So, what are the areas that you're focused on now that you expect to drive performance over the next 10 years?

Kathleen McCarthy: I think top on that list is data centers. It's really hard to overstate the explosive demand happening for data centers. Data is a physical asset. It is created. It is stored. It relies on enormous amount of power for the computations that are happening.

And we took private a company called QTS about two years ago. And we did that because we saw the explosive demands just from cloud computing and content creation. And we wanted a company where we could really continue to grow and meet client and tenant demand in that space with a great platform that had operational expertise and a land bank to continue to grow with its most important tenants.

And what we have seen in that time has just been absolutely incredible. Since then, of course, the biggest technology companies have made a trillion-dollar commitment to their digital infrastructure. Really so that they can propel their own businesses through this AI revolution.

So, QTS when we bought it was the fifth-largest data center provider in the country. And today, because of the development pipeline we've been able to propel through the combination of capital and relationships and expertise, the company's on track to be 10 times larger than it was when we bought it. And it feels to me like every three-year look back period we can say that more data has been created in those past three years than the rest of human history

combined. You just see it in the last 10 years. There's been something like a 50 times increase in data creation.

So, I think we're going to continue to see numbers like that. And that's going to continue to drive demand. And as a real estate investor, you have to always though be thinking not just about the demand side of things, but also supply.

And this is a sector that has tremendous capital needs, power needs, all of those are constrained particularly in an environment like we're in today with so many capital constraints. And so, I think the supply and demand fundamentals also set up really well for successful outcomes for folks who do have a platform like we have.

Alison Mass: What is your view now, I want to pivot to the office market, in light of remote work policies? And I know those don't really exist at Blackstone or Goldman Sachs. But out there in the general population. What does that mean for Blackstone and bigger cities more generally?

Kathleen McCarthy: The office market is certainly under pressure and remote work is part of that. Although, I think

some of these pressures existed long before remote work and before covid. In 2015 and 2016, just for example, as we always do, we were looking at what was happening in our portfolio. And trying to use those experiences to inform our future investments. And what we were seeing was that capex as a percentage of net operating income was increasing pretty dramatically as landlords were needing to transform spaces to be much more attractive, much more flexible.

I think at the time I might have joked that every office building lobby started to look like a hotel lobby. And what that was meaning particularly with the higher capital costs, with lower tenant retention as tenants went to the higher quality buildings, was that you had a very low or no cash flow asset in offices. And that was concerning for a number of reasons, and particularly because we were looking out and thinking that if we ever found ourselves in a higher rate environment, an office building which was starting to look like a zero coupon bond, would not perform particularly well if cap rates were going up and you didn't have cash flows to offset that.

And so, we really deemphasized office starting then. Just to

give you a dimension, when Blackstone went public in 2007, 61 percent of our equity book was traditional office buildings. And today it's 2 percent.

Alison Mass: That's phenomenal.

Kathleen McCarthy: Yeah. And again, it goes back to looking at the data, looking at what we're really experiencing. And letting that inform our investment decisions.

I think today, with remote work, we're still kind of midstream in the era of experimentation of office. And I'm sure by the time this podcast is on air, more companies will have announced bringing people back to work more days in more places.

But I think what we're seeing is that it's really favoring dynamic locations, newer buildings, highly amenitized office product. And that is really tough on the older assets. You combine that operational reality with a dramatically changed capital market where capital costs are high and everyone's reevaluating what the value of assets of all types should be.

And no asset can hide from higher rates. But I think it's particularly tough in the office sector for the older assets.

Alison Mass: So, Kathleen, what do you think about the commercial real estate market given the banking stresses and interest rate environment we've seen over the last year?

Kathleen McCarthy: Headwinds in real estate are feeling stronger. And that's both from an operational perspective as the work the Fed and other central banks are doing is slowing the economy. And certainly, what they're doing on the capital market side of the equation, driving rates higher means there's upward pressure on cap rates and it's just the equivalent of downward pressure on multiples.

So, headwinds feeling stronger in real estate certainly. But I think we continue to see that not all real estate is created equally. And not all of it's traveling at the same speed.

So, if you just look at our portfolio, about half of the portfolio's concentrated in warehouses and student housing and data centers. These are sectors that are

having high cash flow growth. And cash flow growth is really the strongest mitigant against a higher rate environment, higher cap rate environment.

At the other end of the spectrum, it would be the older office buildings where they're operationally challenged. And now as capital is repricing, I think there are meaningful headwinds that will be hard to overcome when you don't have the cash flow to offset those changes in valuation.

Alison Mass: All right, so, I want to talk about another post pandemic trend, which was a surge in travel and experiences. You've been bullish on hospitality properties, like resorts, casinos. But in an inflationary environment that's likely to curtail consumer spending, how is that affecting investment opportunities?

Kathleen McCarthy: Hospitality and hotels have been probably our longest-term conviction theme, really since the very beginning of Blackstone Real Estate, we have always been a hotel investor and have continued to look at different types of hotel investments. And that probably really gets us laser focused on certain aspects of the hotel market that we find most interesting.

Our portfolio today is really characterized by three different types of things. Really special assets in highly supply constrained locations. So, coastal assets in places like Hawaii and southern Spain, the Balearic Islands.

On the other end of the spectrum, we have Great Wolf Lodge or Bourne Leisure in the UK where we offer a very affordable, recession resilient, family holiday vacation. Something like 90 percent of America can drive to a Great Wolf Lodge in under four hours. And so, that is a great business in any environment. But I think also very recession resistant.

Where we're seeing the impact of inflation probably most is on the most price sensitive traveler. And that would be in something like extended stay hotels where it's a business where we offer a very attractive room rate. And we feel the economy probably most quickly when it's moving in either direction.

I think though for us, when we look at the environment, while we are seeing some softening off of the post-pandemic highs, because again, like you were saying, travel has been

a winning theme, a post-pandemic winner, we've tried to look through the immediate term of some dislocation because of the environment and say this is going to create some great opportunities.

Hospitality is a cyclical business. We've been through this before. We've been investing for over 30 years in hotels. We bring expertise, not only how to operate, but how to invest capital. And we're not afraid to invest when the environment gets rocky, and sentiment turns negative. In fact, when sentiment is most negative is usually where the values will decouple from what we see as the long-term intrinsic opportunity in the business. And we can do some of our best work.

Alison Mass: Speaking of Great Wolf Lodge, one of my biggest regrets is I never did that trip with my children. And my children are now adults. So, I'm going to have to wait to do that with my grandchildren.

Kathleen McCarthy: Maybe you can borrow some children right now.

Alison Mass: Yeah. I can borrow--

Kathleen McCarthy: I think we have some colleagues who are, like, themselves maybe are not into the water side. But if you want to take their kids, they'll take you up on it.

Alison Mass: All right, so, I want to turn to the residential market. Rising rates are increasing the cost of homeownership. And how is that affecting the housing market and the calculus to buy or rent properties in your view?

Kathleen McCarthy: Our focus is on rental residential. And we own rental product in a lot of different categories. So, market rate rental apartments. Single family rental homes. Affordable, meaning rent regulated rental homes. And student housing as well.

And what we're seeing now is that higher mortgage rates is making it 50 percent more expensive to buy versus rent. And so, that is sustaining demand for rental housing. And I think it's happening against a backdrop of a long-term structural under supply of residential housing pretty much everywhere in the world. And it's extremely pronounced

here in the US.

So, since the financial crisis because the country really never got back to building at levels that keep up with household formation and population growth, we think we're 4 to 5 million units short of the amount of housing we need in the country to have a healthy housing market. And you're seeing that show up in some of the affordability pressures, both for sale and for rent housing.

I think the good news in the short-term for that equation is that we are going to have elevated levels of new supply for multifamily housing this year, next year. That will put some pressure on rents, downward pressure on rents.

What we're seeing now is there's a sharp pullback again in supply. And that's because of the capital markets. It costs so much to build it. And the borrowing costs against that are high too. And so, I think that sets up for really favorable fundamentals in the medium to long term, which is part of what I think sustains our investment strategy in this space.

Alison Mass: So, I want to get your perspectives on the

global environment. And how do you look at your portfolio today, globally? How does it sit today? And what are your views on the biggest opportunities globally moving forward, US, Europe, Asia, etcetera?

Kathleen McCarthy: We do have established business US, Europe, and across Asia. And in Asia, it's both developing and developed markets. We have a lot of consistency in the themes that we like. And it just goes back to this concept of investing behind macro trends and the assets that are going to benefit from that.

So, today's environment reinforces our desire for assets and asset classes with higher cash flow growth, ideally with short-term leases. We want to be able to capture that higher growth. Having a very long-term lease doesn't really help you in a higher rate, higher inflation environment because you may not be able to get to the higher rents when you buy assets where the in-place funds are below market.

So, we want to have that, what we call, reversionary rent capture. And that does favor the asset classes we're in today. So, our best weather sector is our favorites today:

data centers, student housing, warehouses. I'd say that's pretty universally true. So, for example, student housing, I was just in Brisbane, Australia last week. We are under contract to buy a platform, including three assets of student housing. In Australia, similar to the UK, similar to Canada, education is really an export. And what we have seen is that as the universities are offering an English language, high quality education, they're garnering interest from students from around the world. And there is not enough housing for those students.

And similar to your question about housing, there's not enough housing of all forms. And there's certainly not enough student specific housing. And so, we're investing behind that theme. And that is a global phenomenon and a global opportunity for us.

Alison Mass: Australia is one of my favorite places to visit. But it's so far.

Kathleen McCarthy: It's so far. Oh my gosh. I go all the time and I feel like it's getting farther with each trip.

Alison Mass: I know. The only time I will say in my entire

career I almost missed a plane because I was in an airport lounge in San Francisco, and I fell asleep in between my flights. But they did let me on because I had checked a bag.

Kathleen McCarthy: Oh, because they want you with your bag.

Alison Mass: Correct.

Kathleen McCarthy: They find you.

Alison Mass: And I was like, "You don't have to open the door. But you've got to get my bag off." All right. So, let's talk about the fundraising environment, investors. Against this more challenging environment, how are institutional investors thinking about investing in real estate?

Kathleen McCarthy: Investors today are highly selective. They are more capital constrained. The combination of the denominator effect, and also just themselves trying to make sure they're really prepared to withstand what we expect to be a continued volatile dislocated environment.

And in real estate, probably like all asset classes, it's really favoring managers who have long-term track records of good performance in lots of environments. I think for us, part of the reason we've been able to raise \$30 billion of capital for our flagship fund is because we've been doing this since 1991. We have a 16 percent net return. And the wind wasn't always at our back through that.

I think the other thing our investors are looking for is managers who really have the ability to find opportunities and execute on them in this environment. For our investors, what we offer is this experience and this comfort with scale and complexity and a practice of moving quickly so that we can capture opportunities without necessarily competing on price. And we've already been able to do that a lot in the last year as we see sellers who are under some liquidity pressure. And we can then pick assets that we like to buy. And we just think a lot more of that is coming.

And so, that combination of track record and positioning for the environment ahead, I think, is really where investors are focused.

Alison Mass: I want to talk a little bit about the Blackstone

talent pipeline and also philanthropy. So, in the real estate group, Blackstone has doubled the number of women in managing director and senior managing director positions over the last five years, which is phenomenal. So, what else do you think can be done to promote more women and diverse talent in our industries and keep them in senior level positions?

Kathleen McCarthy: One of the things I'm really happy we're doing more of at Blackstone is offering training and development and mentorship specifically for our women at different stages in their career. This was something that I benefited from enormously when I was at Goldman. In my 10 years here, I joked that I either got the most enrichment or remediation than anyone else. And it was programs that were designed, for example, for associate women recognizing that was a place women were getting discouraged, where they were not addressing some of the gaps in their tendencies or capabilities.

And I felt like I got what I needed to keep going and propel through. And so, it's been important to me and important to us at Blackstone to really understand that the experience women are having in finance and real estate is

different than their male colleagues. And we want to meet them where they are and support them through it.

And I think we all as an industry have to keep doing more of that, which is saying, "I see you. I'm going to be really specific about your development. And I'm going to support you through a whole career journey."

We also at Blackstone are making sure that we're bringing in, particularly coming out of college, much more diverse analyst classes. When I started at Blackstone, we weren't necessarily doing that. But like, with anything, if you bring focus to it, things change.

Alison Mass: Yep.

Kathleen McCarthy: And so, I think we have to keep that focus going. And then like I said, as they're at our firm, try to support through the different levels of getting up into leadership.

The fact that in the real estate industry leadership teams across the industry don't look at diverse as we'd like is because people weren't making investments 15 or 20 years

ago. And so, it's important as leaders to be making those investments today to change the complexion of our organizations over time.

Alison Mass: So, your impact also stretches beyond the world of real estate. You're a member of the Blackstone Charitable Foundation board. And you're also a board member at City Harvest and have found a way to connect the food rescue pantry with your colleagues at Blackstone. So, can you talk about the impact of both of those efforts?

Kathleen McCarthy: I think I spent a lot of time in my early career thinking about how was I going to make an impact, and should I leave a career in finance at Goldman Sachs to go do something where I would have direct impact at a not for profit or at an NGO or something like that?

And what has been really rewarding to me is to realize that by developing all those skills that brought me to Goldman Sachs in the first place, those professional skills, the networks, the knowledge and capabilities, I've been able to share those onto organizations that can have impact at scale.

I found City Harvest through a Blackstone volunteer day. And what I've been able to do there is bring not only things I know about real estate, we just opened a new facility in Sunset Park. I know you and your family are finally spending time there. But I have also been able to draw the power of our whole organization and other organizations you work with into it.

And so, what's been meaningful to me is to not just have a personal impact, but to have a scale impact. And to see that my career and the positive outcomes I want to deliver for my community can come together, and it also makes me just really joyful to know that I work alongside people that care about these things.

We just came through at Blackstone, our global fight hunger month where all around the world every single office picked a hunger charity to raise money for, to volunteer at, and to see that tie binding all of us together is just really very meaningful to me.

Alison Mass: And that's an amazing effort. And you're right, the Mass family is doing a repack, all 30 of us, on Saturday morning. So, we'll be there at 9:30. I can't tell

whether people are more excited about the repack or the pizza that follows.

Kathleen McCarthy: They're both important.

Alison Mass: We have a lot of young family members. So, let's rewind the clock and go back to your early years. You grew up in Middletown, New Jersey. The oldest of three sisters. And grew up in a family that wasn't necessarily defined by traditional gender norms. Describe what that was like and how it informed your drive.

Kathleen McCarthy: I think you're referring to the fact that my dad worked for a cosmetics company, Avon products, whose motto was “The company for women.” And where when I went to Take Your Daughter to Work Day, I would see many women leaders. There was a female CEO for the longest time. My dad routinely had female managers.

Alison Mass: What did your dad do for Avon?

Kathleen McCarthy: He did purchasing. He bought all of the packaging, the mascara tubes and brushes. Still to this

day, although he's been retired for a while, he knows a lot more about my makeup than I do, which is so fun.

And on the flip side, my mom was a chemistry teacher. And so, I think the potential norms that emerge in a lot of families where dad's helping you with your math homework was just not the case in our house.

I'd say my dad also was making lunches every day and cleaning up the dishes because my mom was working. And both of them had to pitch in to all aspects of life. And so, I think that set expectations, not only for my career, but also even my marriage and the support I should expect from my partner. Which I have. Tremendously.

But I will say that experience of watching my dad, learning from my mom, I think, did a couple things. One is I just never questioned that I could be analytical or that math should be a strength. And so, that turned out to be a great asset in life generally, but particularly when you're intrigued by a career in finance.

I think also I came into this world never really even thinking about gender in the workplace. And it took an

embarrassingly long time for me to pop out of my cube at Goldman and be like, hey, wait a minute, there are not so many Alison Masses. There are not so many women in corner offices. And it frankly didn't bother me that much. I just didn't really think about it. I focused on the fact that I was working alongside amazing people that were investing in me, investing in my female colleagues, and giving us great opportunities. And so, I think I just worked through it.

And I would say, I really feel like I have had wonderful female mentors and managers. But also, just tremendous male managers and mentors. And so, I just felt like always supported and able to keep going. And again, it did start from a baseline that was, I think, different than maybe some other families and helped me through.

Alison Mass: And today, you're the mother of two daughters. So, as a trailblazer in a male-dominated industry, what are some of the lessons that you hope to pass along to your daughters, and younger women more broadly?

Kathleen McCarthy: I hope my girls see how rewarding

and interesting my career has been. I hope they know how much I enjoy my work. And they see how it has continued to evolve and stay interesting over multiple decades.

One of the things that makes sad, frankly, when I meet, often it's men, dads who have daughters who themselves are just starting their careers, and those dads say to me, "Oh, I would never want my daughter to do what I've done in trading or banking." I think that's so sad. I think that's sad for them. The dads too. That they had that kind of career experience that they wouldn't wish on their children.

I wish for my girls all of the magic of this career. And I would say what has just been stunning to me, because again, I came to Goldman thinking I was going to come for a couple of years, build professional skills, and go do something else. What is just amazing is when you have the opportunity to work with such smart people who challenge you in all the best possible ways, you keep learning, and you keep growing and you keep wanting to do more. And the career itself keeps evolving and staying really interesting.

Alison Mass: So, something I didn't know about you. You

and your husband are long-time Coachella fans?

Kathleen McCarthy: Yes.

Alison Mass: Where did that come from? Okay, so let's just talk about how many times have you been there? And where did it come from? And what do you enjoy most about that music festival?

Kathleen McCarthy: This comes from my husband being much cooler than me on all dimensions. And he loves music. He's always loved music. We actually just had this conversation with a friend this weekend about-- she told me her 14-year-old son, she finds him laying in his bed listening to music. And my husband overheard this conversation and he said, "You guys didn't lay in your bed just listening to music when you were 14?" We're like, "I don't think so."

Alison Mass: Not really.

Kathleen McCarthy: But he did. And so, anyways, so Coachella started when Matt was in business school at UCLA. He drove out to the desert. It was a much smaller

festival then. There were no celebrities and pink walls for Instagram like there are today. And he called me, and he said, "This is amazing. The whole experience is amazing. And there's so much interesting music."

So, the next year I started going. And I have now been to Coachella, I think, 14 times. 2015 I skipped. I had had my second daughter three weeks before. Matt did not skip, I will note.

Alison Mass: Wait, I thought you were talking about that partnership.

Kathleen McCarthy: The partnership. Yeah. No. That was definitely a moment where he was like, "You'll be good here with grandparents. I'm going out."

But actually, coming back to what do I love the most about it, of course it's super fun to find new bands or see the ones you already love. But what I enjoy most is just three days in beautiful weather wandering around a polo field with my husband with the only distraction being the stress he's feeling over the conflicts, two bands he wants to see at the same time on different stages. If that's our biggest

problem over those three days, we have no problems.

Alison Mass: That's great. So, I want to do a little lightning round before we finish. So, we're going to run through a couple of questions and just a quick answer.

All right, so my first question is what was your first investment?

Kathleen McCarthy: A portfolio of grocery anchored shopping centers in Austin, Texas.

Alison Mass: Okay, and what is your biggest lesson you've learned as an investor, knowing that sometimes the best lessons are from investments that didn't go so well?

Kathleen McCarthy: I think having a durable capital structure and a high-quality underlying business is most important.

Alison Mass: So, what's the best piece of investment advice you can give to our listeners that you wish someone had given to you when you were younger in your career?

Kathleen McCarthy: Cheap is not a strategy. If you are getting something cheap, but you have to assume that everything goes right for you in a way that it's not going right in the world or for everyone else, it's unlikely to be a great risk-adjusted return.

Alison Mass: Yeah, that's a great piece of advice. And while it's a very complicated time in the world, geopolitically, I want to end by asking you what you're most excited about in the world right now.

Kathleen McCarthy: I'm super excited about the investment opportunities that I think are just beginning to unfold. In moments of dislocation where capital's pulling back, where there's a lot of negative sentiment, and there is a lot of negative sentiment today about real estate in particular, I think that's when we found the best opportunities and when we do some of our best work.

Alison Mass: So, Kathleen, it was such a pleasure talking to you this morning, having you on the show. And thank you for joining us and sharing your perspectives.

Kathleen McCarthy: Thanks, Alison. So fun.

Alison Mass: So, thank you all for listening to this special episode of Goldman Sachs Exchanges: Great Investors. This podcast was recorded on October 26th, 2023. If you enjoyed this show, we hope you'll follow us on Apple Podcasts, Spotify, or Google Podcasts, or wherever you listen to your podcasts and leave us a rating and a comment.

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