Interview

The BlackRock Model

An Interview with Laurence D. Fink,
Chairman and Chief Executive Officer, BlackRock, Inc.

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EDITORS' NOTE *In 1988, Laurence Fink and some friends founded BlackRock, an investment management firm that manages $3.35 trillion, as of December 31, 2009. He started his career at First Boston Corporation after graduating from the University of California, Los Angeles (UCLA), and earned an M.B.A. at the UCLA Graduate School of Management in 1976. Fink also serves on the board of trustees of New York University and the NYU Langone Medical Center.*

COMPANY BRIEF *Headquartered in New York, BlackRock, Inc. (www.blackrock.com) is a premier provider of global investment management, risk management, and advisory services to institutional and retail clients around the world. The firm manages assets across equity, fixed income, cash management, alternative investment, and advisory strategies. Through BlackRock Solutions, the company also offers risk management, strategic advisory, and enterprise investment system services to a broad base of clients with portfolios totaling more than $9 trillion. The firm maintains offices in 24 countries around the world, including in Asia, Australia, Europe, the Middle East, and countries in North and South America.*

Did the severity and speed with which the economic crisis hit surprise you, and where are we now on the road to recovery?

What surprised everybody was how every non-correlated trade became correlated, which created an extreme breakdown in the markets and led to many corporate failures.

At the moment, the private sector has taken a new approach to credit, and now everyone is screaming at the banks for not lending. Yet their regulators are saying they have a lot of balance sheet risk already. So the lending community is getting a mixed message. And we have a very large housing and mortgage problem in the United States. It is improving, but there are many homeowners who have negative equity in their homes, unsecured debt on their credit cards, larger second mortgages than first mortgages, and they're struggling. We need to find a way to help those consumers so they have a brighter outlook and the opportunity to spend money, which will re-stabilize the economy. Right now, I don't see any movement by our government to truly address the housing problem in our country.

This is not going to be a normal recovery; it's not a V or a U, but more like the Nike Swoosh – slow, elongated, and drawn-out. People have suggested that we're going to have a jobless recovery, and there is a lot of evidence to that point. But I think we're going to see a slow, gradual improvement in our economy, around 2 percent growth. We're also going to have a lot more volatility, so it will be a lot harder than the past nine months of '09 during which it was pretty one directional.

One of the strong pieces of evidence that gives me comfort that the healing process will continue is that the balance sheets of corporations are stronger than they've been in years. There is $1.2 trillion sitting on companies' balance sheets because they're frightened of growing, so they're frightened of hiring and adding inventory. The banks themselves have more than $1 trillion of excess cash because they're frightened of lending. There is a lot of money sitting around, and we could improve rapidly because that money could be put to work quickly.

The biggest lesson we need to learn coming out of the financial crisis is about the use of leverage and a more systematic approach to underwriting risk. That is going to take time and is part of the healing process.

Is there such a thing as a jobless recovery?

Yes, 2 percent growth produces jobs, but not enough to overcome the seven million that were lost. In every other recession, we've had spikes of 5 to 7 percent GDP, which stimulates 500,000 to 700,000 jobs per month; a 2 percent GDP is 50,000 to 75,000 jobs. So we can have positive GDP without having much job growth.

Despite the volatility and challenges, BlackRock's business has remained strong. What is the secret to your success?

Our model is simple: We do investment in management and risk management, and we always put our clients' interest first. That is a very different business model than most financial institutions. We're a fiduciary to every client. So whether it is an individual client, an insurance company, a sovereign wealth fund, a pension plan, or the Federal Reserve, everybody has to be treated with the same proprietary structure. We cannot make scale or size differentiation.

If you think about the problems associated with our economy, most of it has been the breakdown in the client relationship. In many instances, unfortunately, we have seen institutions put their balance sheet in front of their clients' interest. But we have kept our relationship with our clients very simple and consistent.

Why was the Barclays Global Investors (BGI) acquisition a good fit, and will that in any way change your business model?

The combination of the BlackRock and BGI platforms has allowed us to offer the most complete and comprehensive product profile of any firm out there, and it is helping us develop even deeper and more robust relationships with our clients.

If you look back, BGI was one of our great competitors. It had a great legacy, history, and standing in terms of its strength in the investment management business. We had conversations with them in late '02 and early '03, but we both came to the conclusion that it was not the right time to do a deal. I didn't believe BlackRock had the DNA to do an integration of that scale at that time. Over time, both firms gained a deeper appreciation for each other, and through that process, BGI hired BlackRock for our Aladdin product. They became one of our large clients and we formed a relationship.

The attraction for us was that about 80 percent of BGI businesses were additive to BlackRock, so although it was the largest investment management merger ever, we are talking about businesses that possessed a whole different product mix. For instance, BGI's legacy was indexing, and BlackRock was just starting to migrate into indexing as we saw that more clients were interested in beta products. We were one of the top five in indexing, but being fifth meant we were hundreds of billions behind the leaders – we had about $80 billion in indexing, and BGI had close to $1.2 trillion, so the combination of our platforms has put BlackRock in a different league.

BGI also had developed and nurtured the leading ETF platform called iShares®, which has the largest market share of any ETF platform and a great brand name. Although many firms are following the iShares lead and are trying to develop their own ETF platform, just as many firms are walking away after they try; it's a very hard business to get into. Investors buy ETFs for their simplicity and liquidity, but it's very hard to develop liquidity when there are already one or two leaders.

So the acquisition of BGI has allowed us to have a much more comprehensive dialogue with our clients, and it has really set us apart, because no firm has the same magnitude of beta and alpha products today. Five years ago, beta was considered a very separate product; today, clients say they don't need alpha products – they can asset allocate just in beta or in ETF products. So if you asset allocate properly through beta products, you can have huge returns. Many other clients are saying they want to have a higher percentage of beta products so they're close to their benchmark, but they want to have them with a stronger base of beta product that allows them to have more volatile, risky alpha products. So you barbell that risk.

Having the ability to acquire the leading beta provider in the world with very little redundancies to what BlackRock already did was a unique, one-time opportunity. We were not in the market to do another acquisition – they are tough and painful, and take years of hard work. We have done some very successful mergers, but you have to be totally committed for a number of years as a management team to assure their success. It doesn't matter if the merger looks good on paper; if you can't bring the synergies together and make it work for your clients, the deal will be a failure.

How critical was it for the cultures of BlackRock and BGI to mesh, and is that a concern for a merger?

That is one of the biggest concerns of any merger. You have to think about culture in two ways: First, you never change your core values. You change those values, and you change the whole firm. For us at BlackRock, our core values are teamwork, partnership, and communication, and that is never going to change. Fortunately, these are many of the same core values that were at the heart of BGI's own culture and business.

But second, you have to be both global as a firm and local in the community. How that culture and those values may manifest – whether in a beta or alpha style, or the peculiarities of how things are done in New York versus San Francisco, London, Tokyo, or Hong Kong – is a people thing. Every firm has different legacies and histories, and therefore, those firms have different styles. So we need to make sure those styles can be compatible with, and part of, the BlackRock culture and style.

Of course, our style and beliefs have had to change and evolve with the globalization of our business. So if we want to export American values in China or Japan, that may not work; you won't be local. But we have to bring our global information and insights to those regions. Globalization presents as many difficulties in terms of how one evolves culture, and a merger just brings it all to a head. You have to work on it.

BGI is a wonderful community in which people care about each other, so the value systems between us are similar. But they were manifest in different ways. I think the majority of our new partners truly appreciate what it means to be part of a monoline investment management firm, rather than part of a larger financial institution – like Barclays or Merrill Lynch – that had multiple businesses and products. It is a lot easier to bring a shared culture together when the business we do day in and day out touches every employee at the firm. For us, we're only absorbing organizations that are in the same business we are; they may be in different products, but it's the same business. I think that helps us forge a stronger culture and stay true to our values.

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As BlackRock has grown to a certain size, have you been able to give up some control?

That is a big issue. We are currently looking at how we navigate information and control in a firm of this scale. We have an incredibly talented team at BlackRock, and it's even stronger with the addition of our colleagues at BGI. I believe we have to be empowering more people in this firm, we have to have more leaders, and we have to have more people taking on responsibility and accountability. That is maturation and growth. When key people take the time to try to be part of the decision process, generally the decision is better, but we're not growing our leaders if we have to be involved in every one of these decisions. As you allow more people to grow, you have to accept that you might not always get the maximum result, but you have to give them the opportunity. You have to give your leaders the ability to fail or do well, but you have to monitor them – if they're about to fail, you have to come in and try to mitigate it. It's no different than being a parent to children. If you protect your children too much, they're never going to grow up. You have to give your leaders the ability to be decision-makers. You have to give the accountability to those leaders so they can grow too. The people we have given that sort of leadership and responsibility to have done exceedingly well, and have made the firm better than what the founders ever could have done.

Looking back 22 years when you started the firm, could you have imagined that it would have worked this well, and do you ever step back and appreciate what you've been able to achieve?

I don't pause to look back that often. I do appreciate what we've done at BlackRock, what our entire team has accomplished together. But I'm focused on the future, and on the issues and challenges I'm seeing in front of me today. Every day, you're reminded how fragile a firm can be; if you don't focus on fixing, mitigating, and cauterizing issues, they become bigger. So that's where I spend my time – looking forward. I don't have time to look backwards.

You come across as someone who is not easily frazzled. Is that part of your make-up, or do you just hide the stress well?

I think it's part of my make-up. As long as you can tell your clients you're doing the best you can, you're doing what you can do, that is all you can ask of yourself.

In terms of these macro-global problems, you have to look at them in a holistic way. I don't think it's fair for people to point fingers at bankers. Yes, the banking community was the nexus of a lot of the problems – we all get that. But it was a societal problem. It was not opaque that Lehman Brothers had 40:1 leverage – we knew that, the regulators knew that. We just assumed wildly that they may have had the proper risk management to manage leverage at that level. So when you tackle these problems, let's talk about what society as a whole did wrong, and how the moral fabric broke down. It's very hard to navigate a societal problem. You need to identify it, you need to understand it, you need to take responsibility, and you need to be accountable. Right now, there is too much finger pointing and not enough assuming of responsibility for this problem. We all contributed, and until you accept responsibility, you can't fix the problem. But like in history, even in the early days of our Founding Fathers, it's always convenient to blame it on the bankers. I think it would be more productive for everyone – the industry, regulators, Congress – to work together toward a solution that makes sense for the financial system as a whole. That's what is most important at the end of the day. ●