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The Carlyle Group's David M. Rubenstein: Expanding Horizons, Doing What He Loves

"It's the rate of return. Everything is the rate of return," said David M. Rubenstein, cofounder and co-executive chairman of The Carlyle Group, summing up what has fueled the growth and success of the modern private equity business.

The noted financier and philanthropist covered a range of topics—and earned many audience laughs—in a lively and candid conversation with ICI President and CEO Paul Schott Stevens on the opening day of ICI's 60th annual General Membership Meeting (GMM), which began yesterday in Washington, DC, and runs through Thursday, May 24.

Private Equity Today

Stevens and Rubenstein kicked off the discussion by focusing on the biggest trends in private equity today. "It's easier to raise money today than any other time I've been in the business in the last 30 years or so," revealed Rubenstein.

Where is this liquidity coming from? Though US public pension funds are still the largest source of capital for private equity, Rubenstein predicted that they will soon be replaced by sovereign wealth funds. Third on the list as a big source of capital are individual investors coming in through family offices or through feeder funds. Though prices are high, people are willing to pay these prices, he said.

In addition, as the public has learned more about private equity, its opinion of the business has evolved. "We are no longer called locusts anymore. We're not seen as barbarians at the gate. People are not embarrassed to say they're in the private equity industry," Rubenstein explained. Because US private equity companies have outperformed public market averages by anywhere from 300 to 600 basis points on average, more people have concluded that they should try private equity, he said.

Rubenstein remembered that private equity was a "mom and pop" business in the early days, because partnership agreements allowed firms to have only one fund at a time. "I decided to ignore that, and used the model of the mutual fund industry—have multiple funds; centralize the accounting, operations, and administration; and globalize it. People made fun of me: 'Well, he's making a McDonald's out of Carlyle.' But if you like Fund A, there's a reasonable chance that you'll like Fund B and C—and that's how we grew the firm."

The Effect of Private Equity

Stevens noted that the number of public companies in the United States has been on a decline since its peak in the late 1990s, when it totaled more than 7,300. “There haven’t been 5,000 stocks to include in the Wilshire 5000 index since 2005,” he pointed out. Rubenstein offered two reasons why fast-growing companies are moving away from the capital markets and changing the way they’re financed. The first, he said, is because it’s easier to raise private capital than it used to be, so companies can grow longer before tapping the public markets. The second involves the high regulatory burdens associated with going public.

As a result, he explained, many firms are waiting longer to go public. “There is more access to capital, smaller investors can come into these stocks and trade in and out of them as they want, and there are a lot of regulatory issues,” he said. Rubenstein especially stressed that something should be done to address the problems posed by regulatory burdens. “Public markets offer a lot, but something is clearly not working if there are only half as many public companies today as there were 20 years ago,” he warned.

One way to do this would be to expand access to private equity. America’s current system of accrediting investors is “ass backwards,” he joked, suggesting that the government should allow everybody to participate in private equity for a small percentage of their portfolios. “I don’t think the world would fall apart and civilization would come unglued if 5 percent of a 401(k) or IRA were allowed to go into an illiquid private equity investment. We should enable workers who aren’t able to participate directly in private equity to participate through these funds.”

Emerging Markets

Stevens then turned to the world of emerging markets, asking Rubenstein about the rise of funding outside of the United States. Rubenstein predicted that the biggest increase in terms of geographic area over the next five to 10 years will be in the emerging markets. But, he noted, those markets can be very challenging, due to accounting problems, issues with corruption and the quality of management, and an inability to exit investments quickly and easily. “You don’t see as much money going there [now], but eventually that’s where the growth will be,” he said.

When asked about the rise of foreign private equity firms, Rubenstein joked that Americans still dominate the private equity scene because “Americans feel they have a manifest destiny to conquer the world—Europeans are taking weekends and summers off.” He noted that Europe has some very good firms, but that few are truly global. Chinese firms would struggle in the United States, he said, because the US government is not welcoming to Chinese-controlled private equity firms. “But 15 years from now? Who could predict?” he asked.

Hard Work, Perseverance…and Luck

Turning to his philosophies around personal achievement, Rubenstein shared the qualities that he thought were most important: a willingness to work hard, be entrepreneurial, and be passionate about what you’re doing. “Nobody ever won a Nobel Prize by hating what they do. If you don’t have a passion for it, it’s not going to work.” How did he achieve success? Through persistence, which he called “everything in fundraising. You can’t take it personally if they reject you. Rejection is a large part of life.” All of this is tied together with a little luck, he said.

Stevens and Rubenstein wrapped up the conversation with some thoughts on Rubenstein's generosity to the nation, which he calls "patriotic philanthropy" and involve gifts of historic documents (such as the Magna Carta, Declaration of Independence, and the Emancipation Proclamation) to the National Archives, as well as support for historic landmarks (such as Monticello and the Washington Monument).

"My theory is, if people can see originals of these documents, people might learn more about American history. I think a more-informed democracy is a better democracy," he said. Building on this theme, he lamented that the average American could likely not pass the US citizenship test.

He reflected on the four things that the wealthy can do with their money: Hold it all and be buried with it; pass it along to children; give it away while alive; or give it away after death. "I wanted to give it away while I am alive," he concluded with a smile. "It's more fun giving it away than making it. I love doing it."
