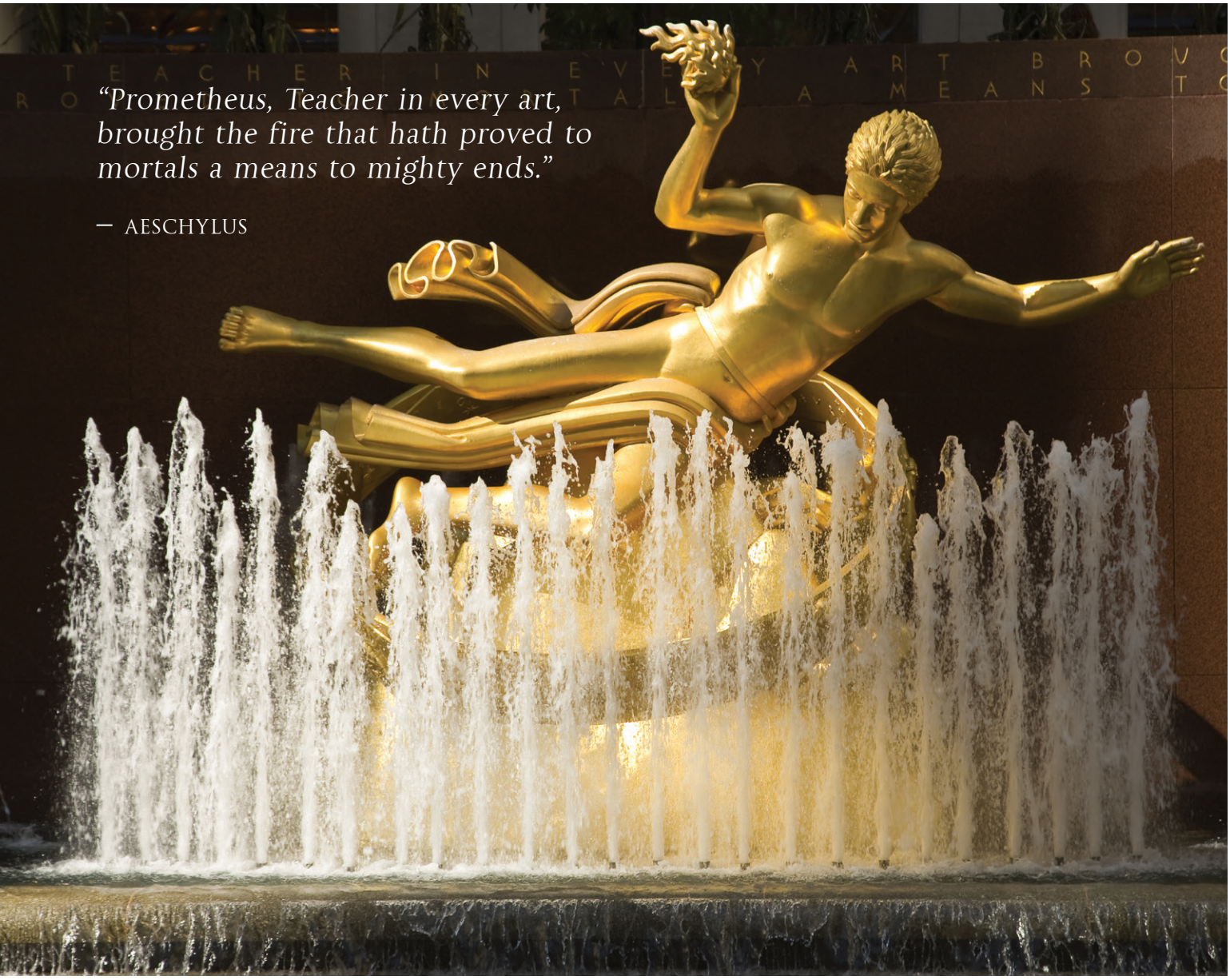
WHITE PAPER



The Pinnacle of Capitalism

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BY **BILL SPITZ**, PRINCIPAL

Beginning in the early 1970's, there was an evolutionary change in the prevailing view as to the role of corporations in our economy and society. The new ethic was captured in a statement by the Nobel Prize winning economist Milton Friedman who wrote: "The social responsibility of business is to increase its profits." Building on that view, economist Michael Jensen argued in a series of articles that management compensation should be more closely tied to the return earned by a company's shareholders leading to the widespread use of stock options and other forms of equity based incentive plans. And, this focus on stock performance contributed to the proliferation of stock buybacks, activist investors, compensation consultants, proxy voting advisory firms, and many other features of contemporary capital markets. The net result of all of this is what some call the "financialization" of our economy in which everything seems to revolve around trading pieces of paper. To be fair, I believe corporate performance has improved by virtue of increased focus and accountability on the part of managements and boards of directors. And, most executives would vigorously dispute the notion that they are focused on the return on their stock to the detriment of other objectives.

But, rather than debate that issue, I would like to describe what I believe to be the crowning achievement of a different corporate ethos which some have labeled "enlightened capitalism." The development by John D. Rockefeller, Jr. of what came to be known as Rockefeller Center entailed great courage, considerable foresight, and an incredibly long time horizon. Most important, it ultimately benefited a large number of constituencies and remains an icon of art, architecture, and urban life as well as a powerful economic engine for the City of New York.

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A Very Condensed History

There are two superb books that chronicle the development of Rockefeller Center: *Great Fortune* by Daniel Okrent, and *Rockefeller Center* by Carol Herselle Krinsky. Since I cannot do justice to the history of this project in a short paper, I particularly recommend Okrent's book because it is more recent. But, I will provide a summary of the key milestones and events as described by them knowing that I am only scratching the surface. These two books focus on the detailed development of the Center, its architecture, and the personalities of those involved. Later in this paper, I hope to add another dimension to the discussion by virtue of the fact that I look at it through the lens of investing and finance.

Initiation of the Project

In December of 1928, Mr. Rockefeller (Commonly known as Junior or Mr. Junior) signed a lease with Columbia University which had owned since 1814 the land under what would become Rockefeller Center. The original lease term was for twenty-four years with three renewal options of twenty-one years each and annual rent that began at $3.4 million. To place that number in perspective, it is roughly equivalent to $51 million in today's dollars and represented 25% of Columbia's operating budget at the time. Mr. Rockefeller is arguably the most prolific philanthropist in history having contributed to among many, many others: the creation of Colonial Williamsburg, the renovation of Versailles, the creation of Spelman College, the University of Chicago, and Rockefeller University, the creation of Grand Teton and Acadia National Parks, and the construction of Riverside Church and the Cathedral of St. John the Divine. Some insight into his values is provided by his statement that, "For every right implies a responsibility; every opportunity, an obligation; every possession, a duty." So, it was not a surprise that a group of New York business and social leaders approached him to provide a new site for the Metropolitan Opera which was housed in inadequate space at 39th Street and Broadway. His solution was to lease the Columbia land and create a new opera house and plaza. Unfortunately, the Stock Market crashed in October of 1929 and the Opera quickly lost the philanthropy of many of its donors. Since Mr. Rockefeller was unwilling to be the sole supporter of the project, the Opera withdrew. That left him with a long term lease on a property without a specific purpose or goal. And, to make matters worse, it only generated about $300,000 in annual rents as compared to his $3.4 million obligation to Columbia. Ironically, the Opera remained at 39th and Broadway until it moved in 1966 to Lincoln Center, a project that was spearheaded by John D. Rockefeller III.

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In an act of incredible courage, Junior decided to "go it alone" and began developing a commercial project on the Columbia tract. Notwithstanding the fact that he was the wealthiest person in the world, it is hard to overstate the fortitude that he demonstrated given the market crash and onset of the Great Depression when there were few available tenants and significant excess space. Carol Krinsky described the Center as "the only large private permanent construction project planned and executed between the start of the Depression and the end of the Second World War." Preliminary estimates provided by the architects suggested that the project might cost $125 million which is equivalent to $1.85 billion in today's dollars! Even given his vast wealth, Mr. Rockefeller entered into the project with some anxiety as demonstrated by his statement that "I feel all right, but I don't sleep so well. I walk the floor nights, wondering where I'm going to get the money to build these buildings."

The project also required great vision to imagine what would become a commercial and retail hub of New York because that area of Manhattan consisted of modest brownstone homes and businesses including a number of speakeasies. (There were more than thirty on one block of West 52nd Street) And, the west side of the project fronted Sixth Avenue which was dominated by elevated train tracks and generally considered quite seedy.

Design and Initial Construction

Rather than hire a single architect, Junior decided to work with a number of firms operating what he called "architecture by committee." His goal was to involve as many points of view and skills as possible and to moderate what he viewed as the strong wills of some creative types. Membership in this group assured both prestige and financial success in that the shared architect's fee of 4% would approximate $5 million which represents $74 million in today's dollars. In keeping with the notion of enlightened capitalism, Mr. Rockefeller gave the following instructions to his team: "While the prime consideration in this enterprise must be its financial success, the importance of a unified and beautiful architectural whole must be constantly kept in mind." Later in this paper, I will describe some of the many progressive architectural features of the Center. But, in a nod to globalism that was way ahead of its time, a portion of the Center was conceived for international tenants, and five of the original fifteen buildings so designated were: the International Building and International Building North, La Maison Francaise, the British Empire Building, and the Palazzo d' Italia.

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While the architectural committee labored to produce a number of designs during 1930 and 1931, demolition of 228 buildings took place beginning in 1930. In the excavation process, 556,000 cubic yards of rock were removed and used to create among other things the Great Lawn in Central Park. The process of clearing the property also required the relocation of some 4,000 tenants. Rockefeller was forced to buy out the leases of many tenants, and there were a small number of holdouts who would not move at any price thereby forcing changes in the project's design and layout. One humorous sidebar is that he and his associates were forced to negotiate with a number of speakeasies and brothels which is very poignant given that he was both a teetotaler and rather straight laced. Another interesting fact is that one of the speakeasies whose lease he purchased was moved a short distance and became the famous 21 Club that is still very much in operation. Once the design of the project was finalized, 1860 separate blueprints were filed with the City's Department of Buildings.

Some of the initial risk of the project was mitigated when RCA contracted for approximately one million square feet of space at an annual lease payment of $4.25 million. RCA was the parent of NBC and RKO which was one of the Big Five Movie Studios during Hollywood's Golden Age. Interestingly, one of the key principals of RKO was Joseph Kennedy, father of future U.S. President John F. Kennedy. This lease allowed the Center to take out a $65 million mortgage from the Metropolitan Life Insurance Company in March of 1931. However, as a condition of the loan, Junior was forced to personally guarantee the entire amount! Construction of the first buildings commenced in September and November of 1931 and the RKO Building was completed in September of 1932 followed by the Musical Hall, British Empire Building, and RCA Building in May of 1933. NBC began broadcasting from its new quarters in November of 1933 featuring famous stars of that era such as Fred Allen, Ed Wynn, and Arturo Toscanini.

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It is noteworthy that the onset of the Depression decimated the construction industry in New York. Work had stopped on many projects including the West Side Highway and Triborough Bridge, and 64% of construction workers were unemployed. This allowed Mr. Rockefeller to drive hard bargains with suppliers although it is generally agreed that he used the cost savings to enhance the project rather than reduce the size of his investment. While he did demand wage cuts from workers, he apparently was much less aggressive in doing so than other employers, and most of his employees were extremely grateful for their jobs.

Between 1925 and 1931, the inventory of office space in Manhattan had increased by 92% and the development of the Empire state Building and Rockefeller Center added another 56%. When combined with the Depression, this created a great challenge in terms of leasing space. Rockefeller Center got off to a slow start, but a very organized and aggressive leasing effort ultimately generated enough momentum that only 70% of the Metropolitan Life loan was ever drawn.

Continued Development

The Center's famous Christmas tree was first erected in 1933 and a total of six buildings were opened by July of 1934 rapidly becoming 80% leased. Several more buildings were constructed in 1934-36 with the underground pedestrian mall opening in 1935 and the ice skating rink in 1936. By 1937, a total of eleven buildings were open at a total cost of more than $100 million which is roughly equivalent to $1.8 billion in today's dollars. Four more buildings were added between 1938 and 1963 bring the total number to fifteen. Most important, the Center earned its first operating profit in 1941 with the Center 87% leased rising to more than 97% in 1944. In the late 1940's, the Center was essentially fully occupied with a long tenant waiting list and it had become quite profitable. That would have been an opportune moment to sell, but on behalf of Junior's five sons, Nelson Rockefeller (A future Governor of New York and Vice President of the U.S.) petitioned his father to keep the Center in the family. In 1948, ownership was transferred to them. Various estimates suggest that Junior had invested somewhere between $75 and $125 million of his own money. The Center made the final payment on the mortgage to Metropolitan Life in 1950.

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The International Style Buildings

Rockefeller Center then acquired land on the west side of 6th Avenue (now Avenue of the Americas) and constructed four modern office buildings which were occupied by Time Life, Exxon, McGraw Hill, and the Celanese Corporation between 1959 and 1974. While they are not built in the Art-Deco style that characterizes the original complex, they do incorporate some of its features including large plazas, broad promenades, and an underground concourse system. The completion of these projects created the footprint that remains in place today covering a total of twenty-two acres.

Later Financial Transactions

While the annual lease payment to Columbia had risen over time, it only provided a modest return on the estimated value of the property which motivated the University to sell the land to Rockefeller Center in 1985 for $400 million. The proceeds of the sale doubled the University's endowment just in time to enjoy the major Bull Market in stocks that had begun in 1982 ultimately leading to its current market value of approximately $10 billion.

In 1985, the Rockefeller Group, the family entity that held the complex, mortgaged the property to the tune of $1.3 billion in order to provide liquidity to some family members and to reduce the concentration in a single investment. This was followed by the sale of a majority interest in the Center in 1989 to the Japanese company The Mitsubishi Group for $1.4 billion. In the depths of the early 1990's recession, Mitsubishi made a decision to maintain their ownership in the more modern buildings on the west side of Avenue of the Americas while allowing the landmark portion of the Center, which was owned in a publicly traded REIT structure, to enter bankruptcy. That portion of the Center was then purchased by a consortium that included Goldman Sachs, Gianni Agnelli, Stavros Niarchos, and importantly, David Rockefeller (One of Junior's sons and the longtime Chairman of Chase Manhattan Bank). Importantly, Mitsubishi maintains an ownership to this day in approximately six million square feet of space in the center including 745 Seventh Avenue which was co-developed with the Rockefeller Group. Finally, a consortium that included the real estate firm Tishman Speyer and the Lester Crown Family purchased the original fourteen buildings from the Goldman Sachs/ David Rockefeller Group for $1.85 billion in 2000.

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Rockefeller Center Today

The current complex consists of the original fourteen Art Deco Buildings, a standalone building built in 1947 and acquired by the complex in 1963, and the four towers built on the west side of Avenue of the Americas. As previously mentioned, the complex covers twenty-two acres and has some 17 million square feet in rentable office space. According to its owners, it is 98% leased. Famous amenities include the Radio City Music Hall which seats 6,000 and has been visited by more than 300 million people since its creation, the Plaza/ Ice Skating Rink, and Top of The Rock Observation Center which receives more than 3 million annual visitors. An average of 470,000 people visit the complex on weekdays and that number increases to almost 800,000 during the holiday season. There are more than one hundred retail shops and fifty restaurants to serve them. The most prominent structure is 30 Rockefeller Plaza which was originally the RCA Building and has since been renamed several times including its current moniker as the Comcast Building. It houses a number of NBC studios as well as the Rainbow Room and Top of the Rock Observation Center. Perhaps the most famous feature is the lower level Plaza which becomes an ice skating rink in the winter and houses the statue of Prometheus which is depicted at the beginning of this paper. It is also the site of the famous Rockefeller Center Christmas Tree. This year's (2018) tree is a 72 foot tall Norway Spruce from upstate New York that will contain more than 50,000 LED lights.

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Visionary Architectural Features

I will describe a number of progressive design and architectural features shortly, but it is worth noting at the outset that Rockefeller Center has served as a model for mixed use developments all over the world that contain significant open spaces and welcoming features such as promenades, fountains, gardens, and specially commissioned art. World famous architect I. M. Pei called the Rockefeller Center Plaza "perhaps the most successful open space in the United States, perhaps in the world."

Among the many innovative design features of the complex are:

- The construction of lower density buildings (setbacks) on Fifth Ave. to create a more welcoming façade and maximize light
- The use of high speed elevators and escalators. After steel, the elevators were the largest single expense item in the project accounting for 13% of the total cost
- An underground loading dock to reduce street congestion; even today, there is less truck congestion surrounding the Center than in other busy mid-town streets
- The creation of the Lower Plaza and sloping promenade to it
- The construction of the lower level mall with shopping, restaurants, and subway access. The strategy for the Center was to create a total entertainment and shopping experience. Interestingly, that is the same strategy that is currently being espoused to rescue troubled malls
- The complex represented one of the first in Manhattan to be fully air conditioned
- The Center was built with underground parking that represented the first garage contained within an office building in New York
- Roof gardens were created on a number of the buildings, the largest of which was .75 acres. While many were ultimately removed, gardens remaining atop three buildings were renovated in the late 1980's. Some of the former gardens now hold solar panels

And, deserving special mention are the Radio City Music Hall and the Center's amazing collection of art.

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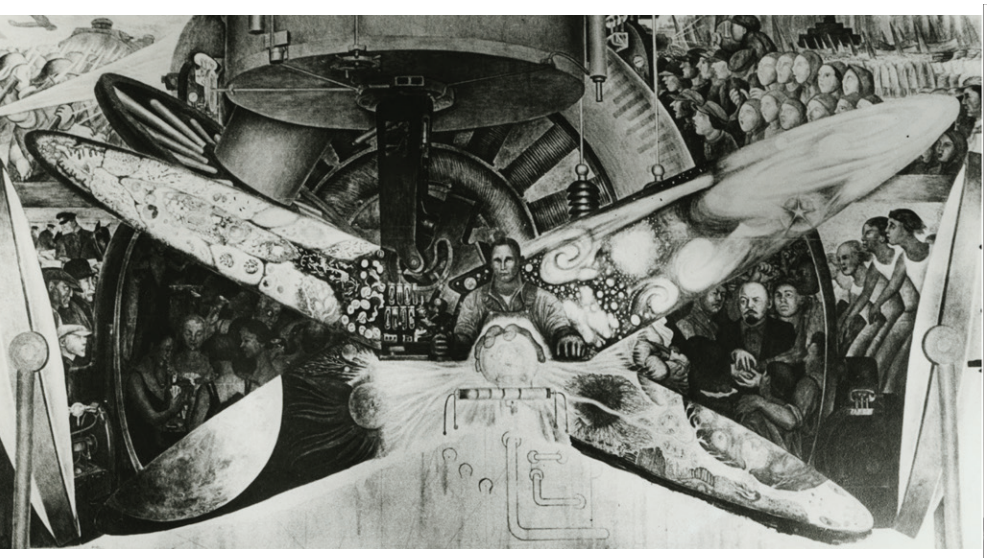
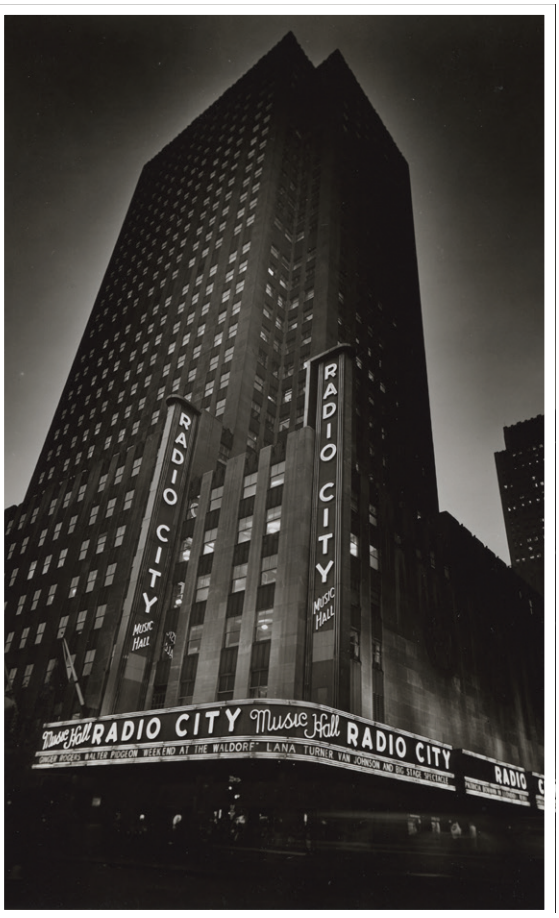
Art and Music

Construction of the Music Hall began in 1931 and the venue opened in 1932. It consists of the Grand Foyer, the Main Auditorium that seats approximately 6,000, and a variety of support facilities including carpenter and scene shops, and dressing rooms for 600. At the time it opened, the stage was the largest in the world and it contained some very innovative machinery including rotating and rising and falling sections. For many years, the entertainment format consisted of a movie followed by a stage show, and in its heyday, the Hall presented four shows per day, seven days a week. But the original model has long since given way to periodic concerts as well as the traditional Radio City Christmas Spectacular featuring the Rockettes. The Music Hall contains noteworthy art including a 2,400 square foot mural in the Grand Foyer called the "Quest for the Fountain of Eternal Youth." There are also several prominent sculptures and many of the rest rooms have an attached lounge which is decorated with murals and other wall coverings. The famous artist, Georgia O'Keefe, was hired to paint one of these murals but suffered a nervous breakdown on her first day on the job and was hospitalized for several months. The work was actually painted by Yasuo Kuniyoshi.





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More broadly, Rockefeller Center is home to more than 100 significant pieces of art including murals, sculptures, and mosaics created by thirty-nine different artists and governed by the overriding theme which is "The March of Civilization." There are many sources of information on the Center's art including tours guided by knowledgeable docents and books such as Christine Roussel's The Art of Rockefeller Center. Given my total lack of expertise, I will defer to them and only mention three interesting anecdotes related to the art program. First, Henri Matisse and Pablo Picasso were both asked to create pieces for the RCA Building. Matisse declined as a result of prior commitments to the Barnes Foundation in Philadelphia, and Picasso did not even bother to respond. Second, the Mexican muralist Diego Rivera, who had strong Socialist/Communist leanings, was commissioned by Nelson Rockefeller to create a fresco for the lobby of the RCA Building. "Man at the Crossroads" contained scenes from May Day in Moscow and also a portrait of Vladimir Lenin, both of which were quite offensive to the Rockefellers. The fresco was papered over during considerable back and forth between Rivera and Nelson, and when no compromise could be reached, it was removed, destroyed, and replaced by a mural by Josep Maria Sert titled "American Progress." Finally, Junior was very much of a traditionalist and something of a prude. As a result, he refused to use an entrance to 30 Rockefeller Plaza that was (and is) flanked by two very large sculptures by Leo Friedlander containing a number of nude figures.

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Enlightened Capitalism

I don't believe there is a generally accepted definition of this concept so I will provide my own as it relates to investments. So, an enlightened investment would be characterized by:

- Patient money/ a long time horizon
- The assumption of prudent risk
- A reasonable return that is consistent with the risk assumed
- Active participation and engagement on the part of the investor
- A global view
- Ethical behavior
- Concern for constituencies other than the investor
- Concern for the environment
- Benefits to the local/national/global community

At the outset, I asserted that Rockefeller Center may represent the pinnacle of enlightened capitalism, so let's go through the list to see how it stacks up. I will deal with the financial criteria first since they are relatively straightforward, and then focus on the community and social issues because I believe they are particularly powerful.

Financial Criteria

The Rockefeller Family's involvement in the complex spanned the period 1928 to 2000, and Junior funded it to the tune of approximately $100 million from its inception until 1948 when it was transferred to his sons. Now, that's what I call a long time horizon and patient money! In light of the Market Crash and onset of the Depression, one might argue that investing in the complex was hardly prudent. But given his long time horizon and a net worth that was in excess of $400 million, I would call it a courageous but reasonable undertaking.

Without access to a vast array of private Rockefeller financial records, it is impossible to calculate a return on the project and compare it to other investments. But, we do know the following: it generated operating profits for many years, the family generated some liquidity by taking out a $1.3 billion mortgage in 1985, a majority interest in the Center was sold to Mitsubishi for $1.4 billion in 1989, and David Rockefeller is said to have realized about $170 million in the 2000 sale to Tishman Speyer. Along the way, family associates John Harr and Peter Johnson called the Center "by far the largest single repository of family wealth and the salvation of the Rockefeller family fortune." Today, the family's net worth is estimated at $11 billion.

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As to active engagement, Junior was intimately involved in every aspect of the planning and development of the complex, and Nelson was active in the early efforts to lease space and later assumed the roles of President and Chairman. Perhaps more important than the details of managing the project, Junior set a tone of quality, investment in distinctive features, and ethical behavior. And, as was discussed earlier, the project from the outset included a significant international component.

The Broader Community

Rockefeller Center completely changed a somewhat rundown and seedy section of New York thereby creating a venue that now attracts almost 500,000 people per day. It supported a number of artists who created preeminent works, and the Music Hall has entertained some 300 million people. The Center has served as a model for other mixed use complexes around the world and generated a number of architectural innovations that we now take for granted. Finally, by virtue of ticket fees paid by visitors, sales taxes on the goods and services they buy, income taxes paid by those working at the Center, the profitability of the complex itself, and so on, Rockefeller Center remains a powerful economic engine for the City of New York. All of these benefits are somewhat difficult to quantify, so let's end with a few more concrete facts:

- The project directly employed between 40,000 and 75,000 workers at various times during the Depression and perhaps as many as 150,000 including those employed by suppliers
- A large number of vendors (steel, limestone, windows, electrical and plumbing fixture manufacturers, transportation companies, etc.) would not have survived the Depression without the business generated by this project
- The lease payment to Columbia represented 25% of its operating budget in the early years and the ultimate sale of the land doubled the size of its endowment
- Four of the Center's buildings currently rank in the top ten in New York City with respect to real estate taxes paid totaling some $150 million in 2017.

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Conclusion

Several years ago, I read Richard Norton Smith's biography of Nelson Rockefeller which is titled On His Own Terms. Inasmuch as Nelson was active in the management of Rockefeller Center for many years, the book contains an abbreviated account of its development. I was awed and captivated by the vision, courage, patience, and taste of his father, John D. Rockefeller, Jr, in both his charitable endeavors and in the development of Rockefeller Center. Instantly motivated to do more research, I have since read several times the two books mentioned at the outset and chatted with people who have been associated with the family and Rockefeller Center. Frankly, my admiration for both Mr. Rockefeller and the Center have only grown with my knowledge of some of the nitty gritty details of its history.

My greatest epiphany occurred when I began to think about the project in terms of my career as an investor, and compared Rockefeller Center's long term success and broad impact to the investment world's current myopic focus on measuring results narrowly and over very short time horizons.

There currently seems to be a tug of war between two opposing views of capitalism. On the one hand, there is the Milton Friedman position that it is all about profits, and as just mentioned, that has certainly been the modus operandi in the investment world. As just one example of this point of view, I found an article titled "Why Enlightened Capitalists Never Seem to Win-the conflict between enlightened capitalists and the reality of our capitalist system." At the other extreme, there is now a significant and growing movement toward what is known as ESG investing. ESG stands for environmental, social, and governance which are considered the three central factors in measuring the sustainability and ethical impact of an investment or company. In many ways, the ESG movement is just a contemporary version of enlightened capitalism.

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So, the fundamental question is this: how do we collectively define return? Is it a precise mathematical computation that must be maximized irrespective of other considerations? Or, is there room for a broader construct that takes into account potentially hard to measure benefits to the world at large, even at the expense of some diminution in the actual reported number? My crystal ball is too cloudy to predict how this debate will turn out and whether corporate mores will change. But, Rockefeller Center is clearly one example in which an enlightened capitalist did win, as did a huge number of other beneficiaries. It may well be that this is a unique example that could only occur in another era and is not repeatable. I hope not. But regardless, I consider it the Pinnacle of Capitalism.

ATLANTA

400 Galleria Parkway, Suite 1400
Atlanta, GA 30339
Phone: 770.226.5333

GREENSBORO

701 Green Valley Road, Suite 300
Greensboro, NC 27408
Phone: 336.217.0151

MEMPHIS

6075 Poplar Avenue, Suite 900
Memphis, TN 38119
Phone: 901.761.7979

NASHVILLE

3102 West End Avenue, Suite 600
Nashville, TN 37203
Phone: 615.386.7302