KKR

Investor Day 2018

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Welcome and Introduction

Craig Larson

Head of Investor Relations, KKR

Welcome

Thank you everybody. Thank you for joining us at our 2018 Investor Day, and a special thank you to all of our out of town guests, in particular recognizing your Monday morning start.

So I'm Craig Larson. I am our Head of Investor Relations and to begin, as everybody knows, I have the pleasure of reviewing this first slide. So our presentations today will contain forward looking statements which do not guarantee future events or performance. Please refer to our SEC filings for cautionary factors and we also will be referring to non-GAAP measures over the course of the day that are reconciled to the most directly comparable GAAP figures that are in the materials in front of you and are also on our website.

So we are excited to be here. It has been fun preparing for this event because it has given us an opportunity to look back and reflect on the growth that we have seen across all of our segments while at the same time looking forward to how we think we are positioned across all of our respective businesses. And at the same time, it has been fun to be here again recognizing that we think we have an opportunity to introduce ourselves to an entire new audience. The timing of this event, of course, was really driven alongside of our decision to change our corporate structure.

We made that decision in early May and the decision itself became effective a little over a week ago on July 1st. Since May, we have had an opportunity to visit with roughly 100 institutions and the feedback that we have from those meetings really confirms what we felt for a long time that there is a large part of the investment universe that has just found it very difficult to buy our stock because of our structure. And that all changed a week ago. If you look at our trading profile of last week, again, interesting despite the July 4th holiday being in the middle of the week, we saw our three most active trading days in our history since we have been publicly listed since the beginning of 2010.

So for all of you who are newer to KKR, both in the room as well as on our webcast, again, welcome and thank you as well.

You see in front of you our agenda for the day. You see we will be hearing from a lot of our senior leaders across the firm and I think you will gain the sense of the broad enthusiasm that we have for our prospects again across all of our segments. Three final logistical notes. First, instead of having our speakers answer one or two questions at the end of their presentations, we ask that everybody hold their questions and at the end of the sessions, Henry Kravis, Joe Bae and Scott Nuttall are going to come back on stage. We will have a group Q&A session. Secondly, in terms of lunch, lunch is actually not being held in this room. It is being held one floor below us. So at the end of the Q&A session, we all can head down the stairs that are just at the exit of this room and we can all head to the Terrace Room downstairs. The tables that you will see once we enter the Terrace Room, there is not assigned seating and we are going to have a fireside chat with Henry and General David Petraeus. Then, finally, at the end of that session, please do not forget to take your gifts. We have a portable Sonos speaker for everybody as a thank you for joining us. Sonos is a US private equity portfolio company of ours and they actually filed for their initial public offering at the end of last week.

So with that, I am excited to invite to the stage Henry Kravis, our Co-Chairman and our Co-Chief Executive Officer.

Co-Chairman's Remarks

Henry Kravis

Co-Chairman and Co-CEO, KKR

Opening Remarks

Well thank you everyone for joining us today and particularly those that have come a long way to be here on a Monday morning. Thank you. We really appreciate that.

Jerry Kohlberg, George Roberts and I started KKR about 42 years ago now. We started with $120,000. Now the $20,000 is from George and me. The $100,000 was from Jerry. With a vision to create an investment firm and culture that rewarded collaboration and team work.

Now, since then, we have been more than fortunate than we could ever have imagined. We have turned the $120,000 into over $190 billion of assets under management and that is after giving back quite a bit of money during this 42-year period to our investors. We have grown the firm into a global diversified business across private markets, public markets and as you can see on the slide, that will break down what we have done, and we have also gone into a global capital markets business, which is very important, and you will understand that as we go through the morning. We have built our balance sheet, which supports all of our businesses and increased our permanent capital. The balance sheet, keep that in mind as you listen to every presentation because it plays a role throughout what we do at KKR. We have created significant value for the people that have invested with us. I firmly believe that today we are a stronger firm than we have ever been before, and I know George would say exactly the same thing to you.

What you are going to hear today is a lot about our strategy, our focus and how we are going to grow the firm. A consistent theme you are going to hear is focused on our growth opportunities and why we truly believe that we are positioned today to continue the trajectory that we have already started and put into place over the last five years. We have had meaningful growth across KKR and you can see this on a chart coming up. Since 2005, our assets under management have increased at an annual compounded annual growth rate of 19%. From $23 billion up to the $190 billion that I mentioned. Not only have our assets under management grown but it has become much more diversified than ever before. In fact, a lot of the growth has come through the innovation of new products and the diversification of our business, both product wise and geographically. In 2010, when we first listed our units on the New York Stock Exchange, we were primarily a private equity firm, which shows on this chart, with the leveraged credit business that was focused in the US. But if you look today, we have diversified into a number of businesses. In private markets today, we have private equity, we have real estate equity and debt, we have infrastructure, we have energy, we have growth strategies and we have core investing. In our public markets, we have hedge funds, leveraged credit, special situations and we are one of the largest players in private lending. Also over this timeframe, as Suzanne Donohoe is going to mention to you, we have expanded our investor base tremendously to a much more global and diversified group of investors. Looking specifically at the period since we listed in 2010, we have more than tripled our assets under management from $62 billion to the $190 billion and after-tax distributable earnings grew from $577 million to $1.5 billion. We have increased book value per share from approximately $8 to $14.50 currently while paying out almost $9 a share in distributions over this period of time in the form of dividends.

How Are We Different?

Now, we are often asked how we are different and what has been the key ingredient. Well, investment performance is clearly one of the critical pieces and we always say portfolio, portfolio, portfolio, which means focus on the portfolio and get the most out of it that you possibly can. You are going to hear from a number of presenters today across the different strategies and how they are focusing and how we are focusing as a business. Perhaps most critically, though, is this one slide that I just put up. To me, this slide says it all. We are one firm. We started that 42 years ago when we started this firm, and today it is as applicable as it has ever been before. Now what does it mean? Well, it means that every single person in KKR is paid on how well the firm does as a whole. We do not have silos. People do not have their own individual economics. We work in teams. We started it that way 42 years ago and it is still exactly the same, obviously much bigger, much broader and more diversified than ever before. We work around the world with everyone in the firm where they work together to help connect the dots, as we like to say, and make smart investment decisions and help make the firm a better place.

Now, this is very important and I hope you will keep it in mind. These values that we have up here very much is ingrained in our DNA at KKR. In fact, I am not going to go through each one of these points but I will just say to you that there is not a firm meeting that we have at KKR where George Roberts or I do not mention our culture or values to everyone in the firm. We repeat it and repeat it because this is what really drives our business. And it's this one firm culture, along with our values that allow us to achieve the growth opportunity that you are going to hear about in the presentations today.

With that, I am pleased to now introduce two of my partners, Joe Bae and Scott Nuttall. Last July, George and I appointed Joe and Scott as co-presidents and co-chief operating officers of KKR. This was an extremely important step for all of us at the firm. Now, while George and I continue to lead the firm as co-chairmen and co-COOs, Joe and Scott are jointly responsible for the day to day operations of the firm and work very closely with George and I. So rather than having 11 people that reported to us, we now have two people that report to us and the streamlining of this makes a huge difference at the organization. Both Joe and Scott have worked at the firm for over 20 years. In fact, they joined the firm within a few months of each other and they joined in our private equity business in 1996. They have adopted, which you will see on this chart, what they call a major/minor approach in terms of how they actually manage the business.

So as you can see on this page, Joe is primarily responsible for the private equity and real assets business, while Scott is responsible for our public markets, principle activities, capital markets and our distribution business. Their transition to these roles has really been seamless and effective. They both had worked in these areas before,in fact, started a lot of the business that we have at KKR today. So George and I could not be happier nor pleased with how well this transition is going, which is now one year in the making, and it is working very well. We are working extremely closely together.

With that, I am pleased to bring Joe and Scott up here to start taking you through our businesses. Thanks again for being here.

Positioned for Continued Growth

Joseph Bae

Co-President, KKR

Scott Nuttall

Co-President, KKR

Joseph Bae: Good morning everybody. My name is Joe Bae and I am here with Scott Nuttall, my Co-President of the firm. Thank you again for coming today for the 2018 Investor's Day. Before we get started on the presentations, we thought it might make sense just to give everyone in the room a couple of minutes on our own personal backgrounds.

So as Henry mentioned, Scott and I joined KKR back in 1996. We were the two analysts that year that KKR was hiring in our New York office. We were both 24 at that point in time. So we have spent the last 22 years working together here at KKR. For me, I started with my first ten years at the firm in our traditional US private equity business. So that was really '96 to 2005. And in '05, I was asked by Henry and George to move to Asia to start building out our business in that region really from the ground up and for the next decade that is really where I spent most of my time and attention, building out our Asia Business. Today, we have eight offices in Asia, around 150 executives and close to $18 billion of assets that we manage in the region. In 2015, I moved back to the US and was asked to take on the additional role of oversight for our global infrastructure business and our global energy businesses until the recent change Henry mentioned in July of last year where we were asked to be Co-Presidents of the firm.

Scott Nuttall: So as Joe said, we had the same start. We were the two analysts hired in New York in 1996 and we had our offices next to each other. So we actually grew up working on private equity deals together. I was a private equity investment executive for a number of years. Then about the same time Joe moved to Asia, I started to shift my attention to, really, three different areas. The first was building non-private equity investing businesses for the firm. The first and largest of which was in credit. The second major area of focus for me turned to distribution and how do we get more people to invest with us and alongside us and also how do we monetize our ideas to a greater extent. Working with a big team, we now have our client and partner group and our capital markets business as a result of those efforts. Then the third area of my focus was really permanent capital. How do we create more permanency to our capital base, extended duration of our capital base and ideally have capital for the firm to invest off its own balance sheet? So I have spent the last 10 to 15 years really focused on business building, distribution business building and strategy.

As Joe mentioned, we joined together at age 24, we have been close friends from the beginning, which I think is a really important element of this. It is a lot of fun to do this job with a great friend and Henry and George have been friends, mentors, partners for over 20 years. We are having great time working together and we have an extraordinary group of colleagues around the world, some of whom you are going to hear from today.

So, we are really excited to take you through our story. We have a lot of exciting aspects of what we are up to that we want to share with you. With that, let us kick it off.

Joseph Bae: Thanks, Scott. We have a lot of content to share with you over the next four hours. You will be hearing from all of the senior leaders of our firm and very exciting growth opportunities ahead of us but what we thought we would start with is really what we hoped you would take away today summarized in a couple of bullet points.

Positioned for Continued Growth

So, the four key takeaways. First is the alternative asset management industry itself is a very large and growing industry. Growing at double digit rates over the last ten years and projected to double in size by 2025. Within that very attractive industry dynamic, we are absolutely taking share, as Henry mentioned, both in terms of diversification of our product and geographic diversification. While the industry has many participants today, when you hear the story, I think hopefully you will walk away understanding we have a differentiated model that is different from our major peers in the public markets, our comps, as well as the private competitors in this space. We marry large scale third party capital with our own permanent capital on the balance sheet and what sits in between that is a large and effective capital markets business, which ultimately allows us to maximize the economic participation in all the activity we do at the firm and allows us to compound value and shareholder value sustainably.

Third, while we are a 42-year-old firm today, it is really our US private equity business that is 42 years old. We are the youngest 42-year-old firm you are ever going to meet. Most of our businesses have actually been launched in the last ten years. We will spend some time talking about that. Many of these businesses are at an inflection point where they are just starting to kick in significant contribution to earnings and carry. The opportunities are both global and scalable. Perhaps most importantly, our alignment of interest is absolute with all of you in this room. KKR and its executives own 40% of our public shares. We wake up every day thinking about shareholder value creation. We believe this recent change to C-Corp is an important milestone in unlocking that value for all of us in this room. As Henry mentioned, none of this would be possible, obviously, without investment performance and we are extremely proud of our 42-year track record in this regard.

The Alternative Asset Management Industry is Growing

So let me start a little bit with the industry. Again, our industry is a very attractive growth segment today. It has compounded at over 11% and again expected to grow to $21 trillion in AUM by 2025. What is driving this growth is a handful of strong tailwinds, secular growth trends. Our limited partners, which are typically large institutional investors and pension funds, are in search of yield and return today. If you talk to any CIO of a major pension plan in the US, they will tell you the alternative space, private equity in particular, has been their best performing asset class for probably the past five to ten years. So there is more allocation going to alternatives. We are seeing the emergence of new classes of investors around the world. In Asia, the Middle East in particular, the emergence of large sovereign wealth funds who have not been allocating to private equity and alternatives for the past 35 years, like many US pension funds have, but who are just starting to enter the market in the last five years. You are starting to see insurance companies and high net worth investors also start allocating meaningfully to private equity and alternatives.

Beyond the investor side and the capital side, you are also seeing an increased importance in terms of the role that we play in the markets. We have seen a retrenchment of banks, a pullback of risk taking, a shrinking of balance sheets across Wall Street. Governments around the world are stretched in terms of budgets. They do not have the capital or the money to invest in infrastructure and other asset classes that they desperately need. Finally, shareholder activism. We are seeing this as a unique opportunity where a firm like KKR can really lean into the complexity, work with activists and companies to provide solutions to the problems that they have.

This is what we are hearing consistently from our investors around the world. This is the most recent Preqin study of large pension funds and institutional investors, and there is absolutely an intent and a desire to increase allocations to the alternative space on a go-forward basis. Particularly in the areas that we are focused on today. Private equity, private credit, real estate and infrastructure. While this industry has very strong growth dynamics, I think what we are particularly proud of is that within this context we are taking share. Our AUM growth has been north of 20% over this time frame and we expect in the next five to ten years, as we continue to scale some of the new products and strategies globally, we will continue to grow faster than the overall industry.

Driven By Innovation and Diversification

As Henry mentioned back in 2007, so this is ten years ago, we were predominately a private equity firm. We had global reach in the US, Europe and Asia but that was really the extent of our PE franchise. We did not have any presence in real assets. So in real estate, energy and infrastructure, we had 0 AUM under management. In the public markets, we were effectively in the liquid credit space. Bank loans and high yield bonds. Capital markets was a nascent business, helping us to finance our own buy-out transactions but very limited in the scope of what they do. If you roll the clock forward to where we are today, a little over ten years later, you can see the dramatic diversification of our business. In private equity, we have not only continued to scale our traditional flagship products, but we have growth equity investing, we have core equity investing. In real assets, we are building large scale platforms now in infrastructure, in energy. In the public markets, again, we have expanded from two liquid credit strategies to a broad range of specialized credit strategies and today operate as one of the largest private credit providers in the US. Finally, capital markets, which Scott will spend a lot more time talking about, we have gone from financing our own portfolio companies to being a meaningful player of third party financing to the street, to mid-cap sponsors, also getting in the equity underwriting business in terms of IPOs and creating specialty finance platforms, like our platform in India.

Our goal is to be a top three player in every one of the strategies that we decide to enter. We are not going to be all things to everybody and we are not going to be great at everything, so our job is to really focus on those strategies, those product lines, those geographies where we can have a sustainable competitive advantage and get to a top three position.

Our Business Has Been Scaling

We have been scaling. So in our largest business, private equity, in 2010 when we went public we had $45 billion of AUM. Today that business is $81 billion, around 1.8x. In energy and infrastructure, again, we started from a very low base of $1 billion at the time we went public. Today, that is $15 billion of AUM. In real estate, we had 0 back in 2010. You are going to be hearing from my partner Ralph Rosenberg about the progress we have made in real estate and today we manage $6 billion. A similar trend in the public markets. In hedge funds, we had zero presence in 2010. Today we manage around $29 billion of AUM. Leveraged credit has nearly doubled from $13 billion to $25 billion and again, in private credit and alternative credit, we have made a dramatic jump in our market share, in our industry positioning from $2 billion to $34 billion in size.

KKR AUM Growth

Scott Nuttall: So, if you add up all this work on the diversification and the scaling front, this is what the AUM trajectory looks like. So, since we have been a public company, we have gone from about $60 billion to about $190 billion. If you look at the make-up, the majority of our capital that we are managing today is actually not in private equity. Our pure private equity is about 37% of our AUM and non-PE is now 63%. If you look at management fees, you will see a similar trajectory, a significant amount of growth over the course of the last several years and if you look at the split, it is about even now between private equity and non-private equity.

KKR Management Fee Growth

If you look at performance income, and this is really our carry plus our incentive fees, the definition we are using here, a couple of things on this topic. One, we do not think this is that well understood. The first obvious takeaway from the chart is that it is up and to the right. The second thing is what we are going to take you through in more detail later, is it is much more consistent than what the market thinks. The third thing that is really not that well understood, and we are going to spend some more time on with you today, is the right-hand side of this chart. If you look at our realized performance income, over 90% of it has been coming from private equity. Remember I just said that only 37% of our AUM is pure private equity. So we are under earning our carry potential as a firm meaningfully. The reason for that is a number of the businesses we have created are relatively young. So, there is dollars invested in the ground with a carry right and they are just starting to mature. So we expect that non-private equity component of performance income to scale considerably from here. We will take you through what we think that will look like over time. We also believe the private equity carry will grow at the same time. So a lot of upside further up and to the right on this chart.

KKR Book Value Per Share Growth

Book value is another metric we look at. I am going to break it into two periods of time. The first is 2010 through 2015. That is the period of time where we were paying out about 70% of our cash flow in our dividend. Over that period of time, you can see that we paid over $7 per share. We changed our distribution policy in the fourth quarter of 2015 to go to more of a fixed distribution so that we would compound our balance sheet. You can see the book value per share is just starting to compound in a very meaningful way and we think there is a lot of upside from here. So total distributions, as Henry said, nearly $9 per unit since our listing, broken into those two periods. We think this compounding of book value is a big opportunity for value creation on a go-forward basis.

Building Blocks for Future Growth

So, when we step back, we see an extraordinary amount of opportunity for growth. As Joe said, we are a 42-year-old firm, we are the youngest one you will ever meet because so much of what we have been doing has been created in the last two to ten years. We are in an industry that takes about ten years to start to achieve scale. So massive amount of opportunities.

There are really five building blocks for this growth opportunity. The first is continued performance of our flagship strategies, which have been performing great. We see continued opportunity for those to perform and grow. The second is growth and scaling of our newer strategies, both in terms of AUM and fee opportunity but also, as I said, as this latent carry opportunity already invested in the ground. The third is we are still building things. Many of our businesses have been started in the US and Europe and we are just now starting to think about bringing them to Asia. High priority for us, Asia real estate, Asia credit. There is a lot of businesses that we still see opportunities to create on a go-forward basis. Next is this concept of compounding, which is consistent throughout everything we are doing. It is both balance sheet and AUM. Finally, our model of AUM plus balance sheet plus capital markets allows us to capture more of everything that we are doing, and it is meaningfully more economics from every activity that we have. If you put all those together, there is a significant multiplier effect on all of our metrics.

In Order to Double Earnings and Book Value by Year 5

So we asked ourselves the question, we obviously doubled our AUM, our revenues, our profit, our book value now multiple times over and we thought we would spend a little bit of time on just a question, what do you need to believe to double our earnings and our book value per share again over the next five years?

So by way of background first, what did we do over the last ten years? Fee paying AUM grew from $40 billion to $133 billion. So, a 13% annual growth rate. Last ten years, if you look at management fees plus capital markets fees, they grew from less than $300 million to over $1.3 billion. So over $1 billion increase, a 16% annual growth rate. So that is just context as we sought to answer this question as to what do you need to believe to double again in five years.

The first answer to the question is if you believe just 8% fee paying AUM growth from here, you more than double. We think that is an incredibly conservative assumption, given what we have done historically and the fact that we have a number of young businesses that are now reaching real inflection points. It is also incredibly conservative by virtue of the fact that we already have $25 billion committed to us in AUM that is not yet in fee paying AUM. It will actually turn on the fees when it is invested but it is already contractually committed and there is an even more conservative capital markets growth consumption behind this. To be clear, we expect to do a lot better than this, but this is all you would have to believe.

From a return assumption standpoint, same thing, here is all you would have to believe, 17.5% gross returns before fees and carry for private equity and growth equity. 5% leveraged credit and 13-15% for a number of our other carry bearing strategies. Again, much less than we have been achieving historically.

So our goal is to exceed this level of performance, to be clear. We would be very disappointed if this is all we achieved. But if this is all we achieved, here is what the numbers look like.

KKR Looking Forward

So last 12 months, we have made $1.4 billion of distributable earnings. That is basically our pre-tax cash flow. If you use the numbers I just walked through in terms of the assumptions, in year five that becomes $3.2 billion, so more than a double. Part of the reason you got more than a double is carry kicking in from the dollars we have already invested across all these newer strategies. If you run that out to year 10, you get to five billion dollars. Book value per share, same assumptions running through, $14.56 as of Q1. In year five, it is $32. Back to this power of compounding. In year 10, it is $63. Again, our goal is to exceed this level of performance.

So Joe and I wanted to start with you with the high level and the punchline, which is what we just walked through. But now what we want to do is turn our attention to how we got here. So there is two more things we want to talk to you about in terms of main topics. The first is the foundation building we have been doing in the last ten years to get to this point and then the second is looking forward: what are we focused on in terms of how we build from here and achieve our potential?

The Last 10 Years – Building the Foundation

A Decade of Foundation Building

Joseph Bae: Thank you, Scott. As Scott mentioned, it is an important perspective, I think, to understand where the firm's focus was in the last ten years in building the tools, the capabilities and the strategy to position us today for future growth. The last ten years has been extraordinary busy and productive period of time for KKR. So we are going to walk you through a handful of the key priorities that we have been focused on in getting to this point.

The first is around globalization of our business and expanding the capabilities and the toolkit that we bring to the table every day.

The Last 10 Years – Global Expansion

Back in 2008, again a decade ago, we had ten offices, we were in six countries, primarily in the US and Europe, and 43% of our investment professionals were outside the US, 57% were in the US. One of the most important things we have done is we have made a big forward investment in the globalization of the platform. Today, we have 20 global offices, we are in 14 countries and the majority of our work force today resides outside of the United States. It may seem obvious to everyone today but if you do not have a global platform, a global perspective, it is impossible to think you are going to be a top quartile investor consistently. You need to understand the macro flows, not only capital but the economic activity around the world, the key demographic, technology shifts happening around the world. That perspective informs our investments in all the different strategies that we are making investments behind.

So this investment in the last decade of globalization, building out a substantial Asia footprint, European footprint has been absolutely critical.

We've Expanded the KKR Toolkit

I think the other thing that we have spent a lot of time thinking about this last decade is how do we create a competitive moat around our business? How do we create capabilities, how do we evolve as a firm and as a franchise in a way that it is harder for competitors to catch up with us? For KKR, I am not going to go through everything in a lot of detail but strategically what we have been trying to do is build unique capabilities, value added capabilities that not only make us better investors in everything we do but creates real differentiation in our approach to investing. So it is deep industry expertise. It is a capital markets capabilities, as Scott mentioned. It is building a dedicated global macro team inside of KKR led by Henry McVey. It is a dedicated operations team, over 50 executives that work full time on our portfolio companies around the world. It is expanding distribution and client relationships. You are going to hear from General Petraeus at lunch today, who is Chairman of the KKR Global Institute. It is having expertise around key geo-political risks, especially as we start investing in newer markets around the world. It is developing a real DNA inside the firm around public affairs and stakeholder management. These are reputational issues, it is environmental issues, social issues, the whole ESG complex that we are incredibly focused on at KKR. Importantly, within our firm, it is building internal capabilities in finance, in risk, compliance, HR, IT to help us scale faster and be better in everything that we are trying to do.

Growth & Diversification of AUM and Fee Revenue

The second key building block, as we have talked about already, is how we have diversified our business and how we are trying to scale these platforms. In 2007, 77% of our total AUM was in our traditional flagship private equity strategies and 23% was in the public markets. Today, less than half of our AUM is in private equity. There has been a significant growth in our public markets assets and we have a relatively young but rapidly growing real assets business in real estate, energy and infrastructure. That shift in diversification in our business is also reflected in the management fee and capital markets. Historically, 83% of that entire economic activity came from private equity and today, as you can see, we have a much more diversified fee stream at KKR, 35% being driven by private equity, 25% by our public market and credit businesses and incredibly, 33% by our capital markets business today.

Scaling Faster Than Peers

We are proud, not only with the diversification and the scaling, but I think it is important to note that we are scaling and growing our businesses faster than our peers. So what we have laid out here is our historical growth rates, both in AUM and I will talk about management fees in a second, compared to the five largest listed competitors we have. So that is Blackstone, Carlyle, Apollo, Ares and OakTree. Over the last year, we have organically grown our AUM by 28%. With the acquisition of Franklin Square, which is FS, we actually grew AUM by 38% this past year versus a peer average of 17%. On a three-year basis, we have grown twice as fast as our listed peers and again, on a five-year basis, meaningful out performance in terms of our ability to attract capital and scale these newer businesses. That has mirrored our growth in management fees at the firm. Again, meaningfully higher growth rates on a one, three year and five-year basis relative to our listed peers in the industry.

Organic New Capital Raised Last Twelve Months – Diverse and Attractive

When we talk about diversification and scaling, this is one of the most exciting charts, I think, if you really understand the composition of where the capital is coming and where the firm is growing today. In the past 12 months alone, our firm has raised $41 billion organically in AUM. $4 billion, so just shy of 10% of that number, was raised in our flagship private equity strategies. In this case, our Asia private equity fund. $37 billion in the last 12 months has been raised around the newer strategies that we will be talking around today. Whether that is in the public markets, in credit and in some of the newer growth strategies on the private side around growth, around infrastructure, around energy and real estate. What is important is we are not chasing AUM for the sake of AUM. We are focused on those segments in our industry which we think are the most profitable dollars. 81% of all the capital that we have raised is performance fee or carry eligible and only 19% is not.

Current AUM Profile

So what that leads us to today, as KKR, is $190 billion of assets, very well diversified both geographically, by product line, in the private markets and public markets and again, we are focused on profitable dollars. 88% of our total AUM at the firm today is carry eligible, performance fee eligible. This is something we spent a lot of time focused on. We are just not trying to grow that AUM line, we are focused on making sure we raise dollars that have meaningful economic potential for us.

On a comparable metric, if you look at our peers, they are less than 50% carry eligible on average for their mix of business in terms of carry.

Went Public & Created Permanent Capital

Scott Nuttall: The third thing we did was to go public and create permanent capital. Now as a reminder, we came public in a non-conventional way. So we actually merged a then private KKR asset management business into a closed-end fund that we had created in Europe and then we moved the listing of that then combined company from the Euronext exchange to the New York Stock Exchange in 2010. So we never actually did a proper IPO. We never did an IPO roadshow. We have never actually raised a dollar of cash by issuing equity as a firm in our history.

Our Balance Sheet

So, what happened as part of that merger is it gave us a balance sheet back to the point at the beginning about having a desire to have permanent capital inside the firm. That balance sheet has now grown to about $16 billion of total assets and you can see the break down on the slide. This is very purposeful. We have a bit of a different business model than others. Our balance sheet is bigger than others in our space. If you look at the cash and investments part of the balance sheet, $12.4 billion, it is bigger than Apollo, Blackstone and Carlyle combined. We use the balance sheet in a number of different ways. We get asked a lot, 'well why do you have balance sheet? Why do you not just have a fee business and keep it really simple?' There are lots of reasons we have the balance sheet, but the most important reason is it allows us to grow our AUM fees and fee related earnings faster. This is not well understood. A lot of what we used the balance sheet for is to allow us to grow our AUM more rapidly. The metrics that Joe just took you through that we are the fastest grower in our space is as a result of the balance sheet helping to accelerate the growth of a number of our businesses.

The second reason we have a balance sheet is we really like our investments. All of us personally, historically would take our personal capital and invest in our own funds and investments and we did pretty well by doing that. So we all own 40% of the stock and we believe we are making very attractive investments around the world. Why would we not want to own more of those investments in that upside as well? It also allows us to support our capital markets business, which has grown rapidly and is highly lucrative for the firm.

The third reason we have a balance sheet is it allows us to invest for strategic growth. Marshall Wace, Franklin Square, our acquisition of Avoca, which was a European credit manager, would not have happened without our balance sheet. Lastly, it creates a direct alignment of interest with our limited partners. When you can walk into a meeting and talk to someone and say we are the largest investor in everything that we are doing, do you want to come along with us, you are talking to them as a partner as opposed to an agent. I think it is another reason we have been able to scale our AUM more rapidly than the rest of the space.

The balance sheet investments, as shown in the press release we issued, is on the left-hand side. This is about how it is broken down today and we are getting close to our targeted asset allocation. We have got nearly 40% in private equity and you can see the split amongst the rest. The performance based on this pure definition of balance sheet investments has been quite good. Since inception, over 14% meeting the MSCR world and our own custom benchmark. But to be clear, these reported balance sheet results only tell a small part of the story because these are just the pure balance sheet investments. It does not incorporate all the things we are doing with the balance sheet that allows us to generate fee and carry opportunity, which do not show up on this slide.

How We Use the Balance Sheet

So we use the balance sheet in a number of different ways. We invested in follow-on funds for our more mature businesses, we create first time funds and a number of different strategies. We will seed new strategies on the balance sheet. So real estate is a good example of this. We started that business by actually making investments on the balance sheet and then dropping those investments into a fund, significantly accelerating the path to AUM. We support our capital markets business. We will do strategic M&A, as I mentioned. Then periodically there is opportunistic investments that we find very attractive, WMI holdings is a good example of this. It is basically a tax advantaged SPAC in the public space that was a bit of an orphan and we decided to sponsor it and in the process of creating what we think will be a very attractive acquisition.

Buthis slide is not well understood on the screen. If you look at all of the businesses we have created where the balance sheet has been critical to their creation, it is $106 billion of $190 billion of our AUM. So it is about 56% of our AUM is businesses the balance sheet has been an important part of creating. The important thing from our standpoint is we see even more opportunity to have the balance sheet help us create new businesses and accelerate our growth.

So the balance sheet is an important part of our effort around permanent capital, but it is not the only effort. If you look at the breakdown of our AUM in 2010, you can see it was $62 billion. Virtually all of it was eight-plus year duration capital. So think of that as more private equity style funds committed capital locked up. Then we had a small public markets business for about 7%. In the last eight or so years, the 62 has gone to $190 billion and you can see we have still a significant part of our capital, 59%, over eight–plus-year duration, but there is two pieces of the chart that is growing quite rapidly. That 10% in permanent capital and the 12% in the strategic investor partnerships. The permanent capital, think about it as capital outside the firm that pays us a fee in carry forever and the strategic investor partnerships are very long dated relationships that we have created where we are able to recycle capital plus a percentage of the profits for a long period of time. These are partnerships that tend to have a 20 to 30-year duration. So we are focused on not only scaling the balance sheet with performance but also the permanent capital and recycling capital we have outside the firm. So we have even more visibility on our revenues than we even to do today and we have a lot today. On top of this, of course, the balance sheet will continue to grow.

Built a Unique Business Model

The fourth thing we did in this foundation building phase of the last decade is to build a unique business model. We really have three ways we monetize ideas. It is third-party capital plus balance sheet plus capital markets. The blue circles on the page, those are businesses we own 100% of. As Joe said, we want to be top three in every business we are in. We do not want to be all things to all people, but where we are, we want to be top three. Then the green circles on the page are relationships we have where we believe we can partner with others who are top three in what they do but we do not have to have it fully inside the firm. We are better off creating partnerships. The strategy is very straightforward. We want a scale where we can be differentiated, and we want to partner with others who are differentiated where we can help them or they can help us.

An important part of this business model is our capital markets business, which really sits in the middle of the firm and helps us access equity and debt capital for everything that we are doing and for third parties. You can see on this slide the growth of this business since 2008 has been significant and a big step up over the course of the last 15 months or so. This business has become much more diversified. We are doing a much better job using the model that we have built and that is part of the reason you have seen such growth. To be clear, we think we can grow this business from here. We do not think the last 15 months has been a fluke. We think we are on a new trajectory.

So if you put these four elements of foundation building together, you get the KKR that exists today. The numbers that have come out of that have been quite good. $47 billion to $190 billion of AUM, fees have grown, our number of limited partners has grown, and you will hear from Suzanne Donohoe later, we did not really have an organized sales force in 2007. We have made a lot of investment in distribution since, so that 920 number we think we can meaningfully grow from here and our headcount has grown around the world but our AUM and revenues and profits have grown at a much faster pace.

So we have made good progress. This slide is compelling. But from our seats, we are just getting started. So there is so many more things we can do now that the foundation is built and that is really our focus, which is looking forward to what can we do with this foundation.

Looking Forward

Joseph Bae: So in this last section, what we want to talk about a little bit is where is our focus now. We have all spent a tremendous amount of time and effort and capital building what is today KKR, the capabilities we have talked about, the strategies we have talked about but what is really going to drive value creation for all of us in this room?

Generate Investment Performance

The first and most obvious is to continue to generate superior investment performance in everything we do. That is how we get the top three, that is how we maintain our positioning with investors and we are very, very proud if the track record we have. In private equity alone, you will hear a lot from Johannes after our presentation, which will talk about our global private equity business, really our flagship franchise. Our long-term track records over 42 years are very strong. Nearly 26% gross returns and 19% net. On a comparable basis over this period of time, the S&P has compounded at 11.8% and the MSCI World at 9%. So on a net basis somewhere between 700 and 1,000 basis points long term outperformance of the public indices. Johannes will get into a lot more detail, we are not stock pickers, we are active managers of businesses. We are able to drive value creation in companies using multiple different levers, which allows us to generate this alpha to the public markets on a consistent basis.

Track Record of Outperformance – Private Equity

This again is our long-term private equity track record more by vintage. As you can see, meaningful outperformance over a long period of time to the public markets, we have been successful investors through different cycles, different macro environments and this has been consistent with our track record; again, these are gross returns in the top bar. 25.6% versus the long-term S&P returns. You see a similar track record; our credit business is obviously a lot younger and still scaling but the performance has been strong, consistently outperforming the public benchmarks.

In the last 12 months, while the markets have been strong globally, we are particularly pleased with the continued strength and momentum that we see in our flagship businesses and private equity in the US, Europe and Asia, our funds were up on average 24% in the last year. In real assets, again, strong performance across real estate, infrastructure and energy and in the credit space, again, particularly strong returns in the last 12 months.

Scale Our Businesses

Also I want to spend some time now talking about the implications of scaling our business and what that economic model looks like when you approach an inflection point. For us, what we have seen in our business is as we have organically scaled different strategies, you really get to a point of inflection around year ten where you have incurred a tremendous amount of the expense up front as you built the platforms, you have hired the people, you have opened the new offices, you have all the G&A costs loaded, that is in the first five years and then you start raising the funds, the AUM starts to scale. Your first fund, the successor fund and then the third fund. That takes ten years. What is exciting is the carry is lagged. You invest the capital, those investments season over three to five or seven years, then on the back end, you have a very meaningful economic opportunity in terms of the carry and the performance fees. So the margin, the economic contribution of these businesses really starts to kick in starting year ten and we will talk a little bit about that.

Our Global business, our US, European and Asian private equity businesses are really the three businesses that have been around for ten-plus years on the private side. US for 42 years, Europe for nearly 20 years and Asia just at that tipping point of north to ten years. Those businesses today, as Scott mentioned earlier, represent 91% of our total carry in the last 12 months, so the $1.3 billion of carry and incentive fees we generated this past year, over 90% have come out of those three flagship strategies. It is not because our other businesses are not performing well, they are. It is because the carry is lagged. You invest the capital, those investments season and then you generate the carry down the road. So that opportunity in the blue bar, the green bar, for real assets and public markets is meaningful.

You can see it on this chart in private markets. Our three flagship strategies are ten-plus years old but what we are building in real assets, infrastructure energy and real estate, what we are building in the growth equity space, what we are building in core, these are strategies that are one to five years old, so really just getting off the ground today. You see the same thing in our public markets. It is our leveraged credit strategy that has been around for 14 years today. Everything else we are building in direct lending and private credit, our expansion to Europe, special situations are still relatively young businesses for us that have meaningful contribution potential.

So this is a chart Scott put up earlier. This is a historical snapshot of our carry and incentive fee payments at the firm. Relatively stable and growing over time. When you factor in what I just mentioned about the latent potential of our carry-generating AUM that is already in the ground, we believe it is easily $2 billion or more on a run rate basis. So we expect a meaningful step up in that line item on our P&L.

So again, I am going to walk you through some examples of how the scaling, this inflection point, really work in our business as we think about scaling and diversifying our business model. We have seen it in credit, where we have gone from 0 to roughly $60 billion over 14 years; we have seen it in capital markets, which has been around for around 10 years now from a standing start to over a $400 million contributor to the fee line at the firm. We have seen it in Asia where we have gone from $4 billion of AUM back in 2007 to now $18 billion in private equity AUM in the region and we are seeing it again for the first time in real assets where our infrastructure business is finally starting to sale and get to that sweet spot at this inflection point where we have gone from 0 to $13 billion of AUM in the last decade.

These are the four businesses near that inflection point. As you saw on the prior slide, we probably have a dozen other strategies and businesses that are between one to five years old that have not even reached this level of scaling.

So let me walk you through a couple of specific examples. So Asia is a business I am very familiar with, obviously, given my experience at the firm. When we started the business in 2005, there were just two of us on the ground in Asia and we spent the next five years really incurring a tremendous amount of the cost to build the infrastructure. We hired really talented people in the region. We opened multiple offices up – we have eight today. We built a tremendous infrastructure to support our business in Asia, all before the AUM was starting to flow, before the deals were starting to happen, this was the forward investment we made in the region in the first five years. So you see the headcount numbers at the bottom of this page. What follows next is AUM. We raised our first fund in Asia in 2007, a $4 billion fund. Our successor fund was closed in 2013. That was a $6 billion fund. Our third fund that was raised last year was a $9.3 billion fund. So we have been able, with performance, to scale our AUM from 0 to $18 billion in a little over a decade.

The economics follow. These are management fees. As we scale the AUM naturally, the management fee income follows. As the deal activity increases, we are able to leverage this unique model with KCM and again drive more economics to the firm through the participation of our capital markets team.

Then finally, as these early investments that we have made in 2005 to 2007, 2010 start to mature and we start entering the window of monetization, this green bar really talks about the carry, the realized carry that we have generated out of Asia.

We have a lot more AUM in the ground today than we did five years ago or ten years ago. That green bar you should expect to continue to grow as we monetize the investments we have in the ground.

Infrastructure – Management Fee and Carry Profile

Infrastructure is a very similar trajectory. Again, when you think about the people side and the cost side of the business, you start with a relatively low base as you are starting these strategies. You are building the teams, hiring the people. Then you start raising the AUM.

Here again, we are in our third fund in infrastructure. Our first fund was actually $1 billion. Our second fund was $3 billion. We have just closed our third fund which is $7 billion in size. The AUM is ramping. The management fees are growing in line with that AUM. You can see the step function change as we bring on Infrastructure III this past year. We are just at this tipping point where we are starting to exit some of our early infrastructure investments and carry is just starting to kick into the strategy.

Infrastructure – Total Revenue Profile with Capital Markets

Infrastructure is one of the poster childs in our firm, of our model working right. It is a relatively young strategy where we have relatively low AUM today, but we have an ability to punch way above our weight in this business because of our capital markets team.

We can target larger deals where we can speak for the equity check. We can syndicate to our partners, to our LPs and drive meaningful capital markets revenues for the firm.

Credit – Revenue Profile

Finally, in the credit side, a similar trajectory. You look at the headcount growth followed by the AUM growth driving meaningful management fees both in terms of leveraged credit and then alternative credit. Then finally, you start getting to a point where carry is kicking in. So a relatively consistent track record of building these businesses.

I think the other way you could think about scaling other than the ten-year inflection point approach is when you think about the size of some of our businesses today relative to both market size and the leading competitors in that space. Again, our desire and our goal is to be a top three player in everything that we are doing.

Large Addressable End Markets across Businesses

We are operating fundamentally in end markets that are large and scalable. These are the relative market sizes. When you look at KKR's participation within this industry, we have a lot of room to grow. Even in our largest most mature segment in private equity, we are a sub 5% market share player globally in this space. In many of the newer strategies that we have been talking about, we are somewhere between 0% to 3% market share players in that industry.

Our Goal Is To Be a Top 3 Player in Every Business

If we look at this relative to our current size and the market leaders, again, meaningful opportunity in all of these businesses for us to grow through diversification of product, geographic diversification and successor funds. You see that in every single one of our businesses. There is a roadmap for our real asset strategy. There is a roadmap for our growth equity and our core investing businesses. There is a roadmap for our credit businesses in terms of product and diversification where we could meaningfully double the size of our businesses going forward.

Significant Scaling Opportunity

At a high level, whether it is real estate, infrastructure, credit, core equity investing or the hedge fund space, we are talking about growth opportunities that are two times to 40 times our growth over the next five to ten years if we are going to catch up and become a market leader in those areas.

For Example: Where Does Asia Go From Here?

Let me take Asia again as one example. When we started the business in 2005 and we raised our first fund in 2007, we were just a private equity firm in Asia at that point in time. What we have done is we have built around that platform to create more distribution, build investor relationships, establish a capital markets presence in the region and to a small scale enter the specialty finance space in India as a direct lender in that marketplace.

However, this first decade of work in Asia was in many ways the hardest thing to do. Trying to figure out how to operate across eight different markets in the region – how to do business in China versus India versus Japan – building those relationships with the entrepreneurs in each of these markets, with the CEOs and chairmen in all these markets. That all takes a tremendous amount of time. It does not happen overnight.

Japan is our busiest market in Asia today. While everyone reads the headlines and we are doing large deals in Japan, they forget about the fact that we did not make our first investment in Japan for the first seven years on the ground. Looked at thousands of opportunities but we did not get comfortable deploying capital until year seven when we found the right pitch and took a hard swing at that. In the last five years, Japan has been our most productive, most profitable market in the region. But, this just takes time.

Looking Forward

What is really exciting is when you put in that investment of people, time, relationships, you have a massive ability to outcompete and scale even faster going forward.

As Scott mentioned early on, we are going to leverage those same relationships with entrepreneurs to provide financing in terms of direct lending, specialty credit. There is an enormous real estate opportunity in Asia for us today.

A lot of the large families are heavy in real estate. A lot of the big corporates in Asia are heavy in real estate. Again, that is our wheelhouse. That is where we have strength and those corporate relationships and founder relationships.

We are very excited. This is where we think we are going to take the business in the next five years is to leverage our existing capabilities, our existing franchise, to build four or five new businesses in the region.

KKR's Balance Sheet – a Growth Enabler and Accelerator

Scott Nuttall: The third thing we need to do looking forward is use our balance sheet to drive growth. We talked a bit about how we use the balance sheet, but it is really essential at several stages of our business development. It helps us create and develop new businesses. You can see real estate, Marshall Wace, healthcare growth, etc., on the slide. This is not an exhaustive list. It has been a big part of allowing us to create a number of new businesses at the firm.

It also allows us to accelerate the growth of many businesses. You can see some of those listed. For example, the private credit BDC platform with the Franklin Square partnership – not possible without the balance sheet. That took us from number eight in private credit globally to number one or number two – a meaningful accelerator of that business amongst others. Then it supports our more mature businesses like private equity and our CLO franchise.

Example: Marshall Wace

A good example of how we have used the balance sheet to drive AUM and fee related earnings growth is Marshall Wace. Now, Marshall Wace does not show up in our investment table on our balance sheet. The returns from the Marshall Wace investment do not show up in the balance sheet returns. They show up in our AUM and our fee related earnings. We do not mark the Marshall Wace investment to market on the balance sheet because we are booking the fee related profits.

When we made this investment, we now own about 30% of Marshall Wace – one of the largest and fastest growing hedge fund players in the world. They had $22 billion of AUM. It was actually less than 20 billion when the deal was agreed. It has now grown to nearly $40 billion so a 76% increase. It has been a great contributor to our AUM growth and our fee related earnings growth. We believe they can double again from here.

Critically, we would not have been able to build a business like Marshall Wace inside KKR in this period of time. But, the balance sheet has allowed us to now get exposure to the largest part of the alternative asset management space and a significant growing player with a lot of upside.

When you find the right partner that is top three in what they do, and you participate with them – they are helping us; we are helping them – you see you can create real upside in terms of growth. This gives you a sense of how the hedge fund industry has been growing:

about 11% per year back to 2010. Marshall Wace growing at three times that growth rate. The balance sheet allows us to make investments like this to really scale AUM and fee profits.

Use Our Model to Increase Participation

The fourth thing we need to do going forward is use our model to drive participation. When we say participation, what we mean is we want to participate in more of the outcomes that we are creating as a firm.

I want to do a little example here with you. Let us say that we are all in a private equity firm together that we are all partners in this private equity firm. We find an investment that we like. It requires $1 billion of equity to buy this company. We look at the size of our fund. We cannot responsibly put $1 billion investment into a given fund, given we want to keep the fund diversified.

Let us say that we can take $500 million of that $1 billion and put it into our fund. We need to do something else with the other $500 million – find a partner somewhere else to fund that part of the equity. Let us say that investment pays $100 million of capital markets fees over its life. Let us say we make a good investment, 2.5 gross multiple of invested capital.

In a traditional fund-only model, the math is very straightforward. You probably have to call a competitor to syndicate the other $500 million of equity to them. You put $500 million into our fund. That $500 million turns into $1.25 billion, make 2.5 times our money. We have a $750 million profit. Twenty percent carry rate, we get $150 million of carry revenue. That is the revenue from that investment. It is pretty good.

Our model is a bit different. What we will do is we will take that same $500 million in this example and we will put it into the fund. We will generate that same $150 million of carry revenue from the fund part of the investment. But instead of calling a competitor and giving them our content for free, what we will do is we will use our model of balance sheet and capital markets and monetize the opportunity to a much greater extent.

Let us say that in our model, we take $100 million and we invest off the balance sheet because we like this opportunity. We think it has a lot of upside. That 100 turns into 250 so we have $150 million of capital gain from that balance sheet investment. Let us say that we then take the remaining $400 million. Instead of giving it away, we syndicate it through our capital markets and Client and Partner group. Those groups go off and find $400 million and we syndicate it with a 10% carry. That gives us $60 million of incremental carry revenue.

Let us say also through our capital markets teams, we have a 30% capture rate on that $100 million of capital markets fees that this investment generates over its life. That is $30 million. If you add it all up in our model, we generate $390 million of revenue relative to the $150 million in the fee-only approach, fund-only approach. You can see significant increase in revenues from the same investment with the same team members.

It is not just the incremental profits that we are generating under our model. There is a lot of other benefits to it that are strategic. It increases our opportunity set meaningfully. We can punch above our weight and speak for larger transactions and lock them down. We maintain ball control.

What that means is that we have a CEO and a management team with one partner, one boss instead of multiple different firms in the board room, really important. Because we are in the market every week with capital markets opportunities, we can enhance our capital markets execution. We are a more valuable partner for our LPs because they want to get this direct co-invest call. So, we are calling them all the time. There are not league tables for this kind of thing, but if there were, we would be number one in syndicating alternative assets directly to third parties. Our model allows us to significantly increase our participation in the economics from the transactions that we like. It allows us to do deals that otherwise we would not be able to do.

Example: Infrastructure in 2017

This is not just theory. This is happening inside our firm every week. You are going to hear later today from our partner Tara Davies who is going to take you through two examples of this from just in infrastructure, just in 2017, just in Europe. We are very active utilizing this model day in, day out.

Increase Duration of Our Capital

The fifth thing we need to do looking forward is utilize the power of compounding. Our balance sheet compounds with performance. We have permanent capital outside the firm that stays with us forever. We have core and strategic investor partnership capital that we recycle and with performance it grows. Then we have our more traditional locked up capital and then our leveraged credit and hedge fund capital that is subject to periodic redemption but we find with performance is very sticky.

We got the $190 billion third-party capital plus the balance sheet. Our goal is to grow all types of capital, but we have a dedicated effort around growing permanent capital and this recycling strategic partnership capital. You should see that increase as a proportion of a growing total.

Three Elements of Compounding Power

We are big believers of compounding at KKR. There are three elements of the power of compounding: the balance sheet compounds, permanent capital as a nice baseline and then recycling capital compounds with performance. As we have got growth on top of this compounding model and with the increased participation from using our model contributing, it allows us to compound our AUM, fees, carry and book value much more rapidly.

Compounding Example: Impact of Core Investment

Core is a great example of this. Core is basically a strategy, long-term investments, think 10, 15-year hold, more mid-teens returns, lower risk. Historically, we passed on these types of opportunities. We have now decided to pursue them. We now have a $9.5 billion business focused on that opportunity set. Joe showed you a slide. We think there is lots of growth opportunity in this business. $3.5 billion of the $9.5 billion is from our firm's balance sheet.

If you believe we invest that capital over the next four years, generate a 15% gross return, you can see the $3.5 billion with the book value gain that we will generate plus the retained fees and carry profit turns into $11.7 billion or about 3.3 times multiple of invested capital. That is the compounding part of just one thing we are doing with our balance sheet.

Looking Forward

As we do these five things – we generate performance, we scale and we have lots of opportunities for scaling, we use our balance sheet to drive growth, we use our model to drive participation in everything we are doing, and we compound – we will unlock our potential as a firm.

We are excited to be with you today because we think we are just starting to reveal the potential of this enterprise 42 years in. But we are just at the very early stages of it.

We Want to Leave You with Four Takeaways

Joe and I want to finish where we started. There are four big takeaways we want to leave you with today. We are taking share in a growing industry. Our model is different. We can create and compound value in a highly differentiated way. We have massive opportunities for growth everywhere we look. We are still creating new businesses. We are the biggest owners of the stock. We are committed to value creation. We believe as we do all this work to unlock the potential of our firm, the conversion to C-Corp will allow us to find shareholders who want to be part of what we are doing which will allow us to unlock the value in our stock.

KKR Looking Forward

As a reminder, if we meaningfully underperform our historical performance and our own expectations, these are the numbers that result. We have really been looking forward to today to be able to share our story with you. There is a palpable energy inside our firm about all the opportunities we have for growth everywhere we look. We are particularly enthusiastic about where we can take this enterprise based on the foundation we have built and all these great efforts we have ongoing. We keep our culture and we do everything we just walked through in these slides, which to be clear is happening everyday inside our firm. The opportunity is immense.

We want you to now meet a number of other members of our team. We have an extraordinary group of 1,200 people around the world. You are going to meet several of them today. We would like to now go a level deeper and get into a number of different opportunities we see in all of our businesses. We are going to pass it off to our partner, Johannes Huth who is going to talk about global private equity. Thanks for the time.

Global Private Equity

Johannes Huth

Head of KKR EMEA

Opening Remarks

Good morning. Again, thank you everybody for being here. My name is Johannes Huth. I am responsible for our operations in Europe, Middle East and Africa. I joined KKR 20 years ago. I actually started my career in private equity in 1990 so almost 30 years in private equity and originally was a banker at Salomon Brothers.

KKR's Global Platform and the Current Environment

What I focus on today is obviously looking after our private equity business, the investments we are doing. However, I spend a lot of time trying to connect our different businesses. That is really core. Henry mentioned it when he started that we are working as a team. That means I spend time talking to our colleagues in China if they are potentially looking to sell a business that we have in Europe to a Chinese acquirer. I am talking to our colleagues in the United States if one of our businesses in Europe would like to expand there.

We have businesses that may not fit private equity but that are very interesting investment opportunities and passing those businesses to maybe our special sits investment fund. It is important. We may see a hotel business that has a significant operational aspect. It does not fit our real estate business. I want to make sure that we are effectively using this opportunity in our private equity business. Staying connected geographically and across our businesses and making sure that happens is something I spend a lot of time on.

KKR Private Equity: From US-Focused Start-Up to Global Franchise in 40+ Years

With that, let me talk a little bit about what we are doing in our private equity business. I will give you a quick sketch of what we have today. We have been in this business for a long time: 42 years. I may look like I have been in it for 42 years, but it has only been 30. We have deployed a lot of capital over the history in this business.

What is important here is that we have a distinctive strategy. We are sourcing on a global basis. We are looking at thousands of opportunities globally every year. Out of those last year, we ended up doing 22 transactions. It is a huge funnel. Utilizing what we have across the globe in achieving that is very important.

I will talk a lot more about the second point, how do we really generate value? We generate value by working with the businesses that we own, by trying to improve the operations of the companies that we own. That is where we create value. That is how we generate alpha. That is why, I think, private equity is such an attractive business because this is something that is sustainable that cannot get arbitraged away.

Then as I started and I said where do I spend a lot of my time, we really try to work as one team globally, one private equity team. We talk on a weekly basis with everybody globally to understand what they are seeing in their businesses, what trends could we observe maybe in Asia, or in the US or in Europe that are applicable globally.

We are the biggest investor in our funds. $2.2 billion of the money that sits in the KKR funds come from its employees. We basically put our money where our mouth is. All of that has resulted in some very, very good returns: 26% gross IRR across our history in terms of what we have been doing.

With that, let me talk a little bit about what we are seeing in the market, how we are seeing the business today and then I will come back and talk a bit more in detail about how we are actually generating value in the companies that we own.

The Macroeconomic Outlook Is Strong Globally

Just very quickly, despite trade war, despite other wars, we see in each of the regions that we are active in: Asia, Europe and the Americas, the macro outlook still quite strong. The reason that I mention it, it sets what we are seeing reflected in our global portfolio.

KKR's Industry Leading Global Private Equity Portfolio…

When you look at these slides – we have got a lot of logos on here – we are a market leader in our business and private equity in the US, in Europe and in Asia. None of our competitors is active in each three regions and is a leader in each three regions.

Our businesses, if you add them up, make over $170 billion of revenues. We have got almost 670,000 employees across the world spanning 19 industries and 20 countries. Every month, we look at that portfolio. We look at how that portfolio is doing. What we are seeing right now is what I said in the beginning, we are seeing a good macroeconomic environment reflected in the portfolio performance.

…Has Performed Very Strongly

Our portfolio has been doing well. We look at how it has been doing against budget. Almost 90% of our companies right now are making budget. We have a benign environment and that has resulted in some very, very good performance over the last few years.

The Current PE Environment

That is good but there is another side to that equation. Basically, high market prices and here, we really have two different stories from what we are seeing in Europe and the US and what we are seeing out in Asia and more in the emerging markets.

In Europe and the US, we have seen stock markets that have been running for a long time. We really think if anything, we are later in the cycle rather than early in the cycle. Acquisition multiples since 2007 have risen to really the highest that we have seen both in Europe and in the US. A little lower in the US than in Europe but about almost 11 times EV to EBITDA is what we are currently seeing in Europe.

Leverage multiples have gone up. There has been a lot of liquidity. That has been driving up some of these multiples. The environment is more challenging from what you need to do.

What have we been doing in response? We have really been trying to focus more on value transactions and complexity. Probably five years back, we would have looked more at growth businesses. We saw good opportunities there. But multiples today are so high that we have been trying to find value and we have been focusing on complexity in companies.

I will talk a little bit more about what we mean by complexity. It could be complexity in the acquisition process. A very difficult carve out where in the example of the margarine business we just bought from Unilever, we bought 60 different countries. We had to establish organizations in 60 different countries to buy that business. Or we may have complexity after we have purchased a business. Through that, we can find value and we can keep multiples at a reasonable level.

Still, when we look at acquisitions today in Europe and in the US and we look at the multiple that we are paying when we buy a company versus a multiple that we are projecting that we can get when we sell it, we are assuming either flat or decreasing multiples. That is just the environment that we are in today.

Now, that environment is a little different in Asia. In Asia, we have actually seen opportunities. Valuations have been more attractive. Just by the effect of market growth, there have been much more growth opportunities.

We actually last year had our most active year in the last 12 years in Asia. We put a lot of money to work, and that is really a reflection of the opportunities that we see there. Two different stories but in both of these markets, we are active and we are continuing to invest.

We Have Been Returning Capital While Unrealized Carry Has Increased

The other thing we have been doing is we have been trying to take advantage of what we have been seeing in the market. We have been trying to effectively use high multiples to sell, and to sell a lot more than we have been investing.

Here, as you can see, over the last three years, we have probably returned twice the amount of capital that we have put out. What is important though here and we have basically last year if you look at how much we have generated in terms of realized cash carry, $1.2 billion. It has been a very good market to realize capital.

What is more important though is that that has not meant that the carry that we have in the ground that effectively sits in the portfolio that has not yet been realized has decreased. That carry has also increased. We have continued to make good investments. The carry that is effectively available to be realized in the future has increased. We have returned more money, made good cash carry but also increased the amount of carry that is still available to be realized going forward.

Strong Global Historical Private Equity Performance…

You have seen different versions of this slide before, but I am just going to quickly again go through it. Performance has been very good. That is really the key of this slide. We have returned a lot of capital. We have invested a lot of capital.

…As well as Regionally in North America, Europe and Asia

It has not only been on a global basis. Here, I am trying to split it out and I like this slide a lot because it shows that in Europe, we made four times the MSCI. We have basically returned multiples of what you have been able to realize in the public markets across each one of our markets. That is why we have been able to grow our AUM because we have been continuing to deliver very, very good results across every region that we have been active in.

Performance of Flagship Funds Has Helped Drive Scaling

We have talked about scaling. The numbers in the top corner there are the gross and net returns that the fund has returned. In the North Americas XI fund for example, we have had a 26% gross and 21% net return. That performance has allowed us to significantly increase the amount of capital that we have been able to raise.

You can see there in Europe IV, we are saying we have a successor fund. We are currently 77% invested in our fourth European fund. Hopefully, we will see at least a similar gross there going forward. Good performance basically allows us to continue to what is already a scale business to grow that business.

As we said, we have got $70 billion in the ground in private equity, but we are continuing to be able to scale it by driving the scaling of our existing funds.

Growing Private Markets AUM

This shows the AUM over the period. The real point here for me is that the other private equity point is something that I am going to come back to just in a second. We have been able to add new businesses. We have been able to effectively expand what we are doing in private equity by adding further things. Let me go into detail on that.

We Are Well Positioned For Continued Growth

This is how we are growing the private equity business. I talked about one which is delivering good performance and because you have delivered good performance, you can raise bigger funds. We have done it North America. We have done it in Asia. We are going to do it in Europe.

Secondly, we are adding other businesses. Some of these are important. Our TMT growth business, we today have a fund that is $750 million in TMT growth. You may say that really does not move the needle very much. It is a relatively small fund. But first of all, it is the first time we have raised that fund. Secondly, there is a strategic idea behind this. We want to invest in growth to basically have a window of what is happening in the disruptive space and utilize that information to be better informed in our core business to see are there potential trends coming down the pipe that could adversely affect the business that we have invested in in our core business. Therefore, we should sell it sooner. Or are there opportunities that we may be able to leverage? Again, we are trying to leverage what we have across the firm to create better returns for everybody.

Healthcare growth is another good example. We have a very good franchise in private equity and healthcare in the United States. We are really the leader in that business. What we said is, there are other sectors in healthcare which are probably a little bit smaller and more growth driven but we have all the contacts that we have to pass on.

We created a separate fund for that, raised significant capital. We think we can basically repeat that model in other areas of the firm where either we have a leading franchise in a particular area where we can go into more of a growth aspect where we can find other opportunities to grow that business.

Something that we touched on only shortly is ESG. That has been something that has been very important in our investing. When we look at investing in companies, in our due diligence, we look at environmental, social and governance matter of every business that we buy. Once we own the business, we have a lot of standards that we implement. We try to make sure these businesses source responsibly. We try to make sure that these businesses from a green perspective are responsibly run. This is something that we have been doing for a long time in all of our companies.

We have had then some of our investors come to us who have seen this and said, 'Look, could you create a fund that just invests in those assets for us?' We have done that for a number of our investors.

We have taken that idea a step further and we have said, 'Let us raise a separate fund.' That is we call our impact fund for that and we are going to try to raise that fund in the next year or so. We have an idea here that we have used. It was attractive to some of our investors. Now, we are effectively creating AUM and fees for the firm out of that.

Lastly, in three, there are some additional opportunities – permanent capital vehicles. What is an important one is that last point. We have a lot of our investors who want to give us long-term capital. A key part of those arrangements is to have private equity part of it. We are able to raise money for the private equity business which is not reflected in one of our core funds but comes from outside of those core funds and pays us very good fees. It is AUM that does not come through one of our traditional funds but effectively expands again the amount of money that we can deploy.

Before I go into the sort of more how do we generate value section, I think to remember is our private equity business is a scale business. It is highly profitable. It generates a lot of cash. It has got significant growth left.

Decades of Experience and Decades Investing Together

I just thought we would spend some time on this because very often, what we hear is well, all you guys are doing is basically putting some leverage on. If I put some leverage onto the public market interest, I will make the same returns that you make in private equity. I think nothing could be further from the truth. We are doing something very different. It all starts with our team.

We have a great team across the world, over 200 people that are very active in private equity. Now, almost 60; it says 55 on there. We have hired some more people since of people that are operational executives. These are people that have been at a consultant firm or have been a CEO of the company that help us going into the businesses we own and helped us restructure those businesses.

In addition to these 215, we have our capital market team which work with us on the fundraise and the raising of debt and equity for each of the businesses we own. We have a group of 40 senior advisors around the world that have significant industry experience and expertise that advise us with that and we work with our public affairs team. We effectively scale other parts of KKR within what we are doing in our private equity area.

Unique Opportunities across Sectors and Sizes

What this allows us is to source opportunities. I talked about 22 deals in 2017 and probably over 4,000 opportunities that we looked at globally so a big funnel. A couple of points to make on here.

The average, over 55% of the transactions that we have done have been less than $1 billion. When you ask people what does KKR do, everybody will say, 'Well, you are doing the big $10 billion deals.' Actually, more than half of what we have been doing hasn't been there. We like that sector. It is very often less transparent than what you have in a very large company. They are mainly family businesses where we partner and work with family businesses. We are really focusing significantly on that.

Yes, there are some very big deals that we have done. However, the majority of what we have done have been deals that have been less than $1 billion.

We are sector agnostic. We have done deals in many different sectors. We have expertise in many different sectors through our teams. Most importantly, by having a global sourcing team that has been working together for a long time, over 40% of the deals that we have done have been proprietary. That means there has not been an auction. There has not been another competitor. We have been in a one-on-one dialogue with the family or the seller of that business. That is part of the reason that we have been realizing very good returns. We have avoided the competition.

Private Equity Model Evolution: 40+ Years of Experience

Just maybe to sort of take a step back and say how has our industry evolved. Probably when we started, well, when Henry and George started in 1976, you were able to buy assets at some attractive prices. There was not much competition. There was an arbitrage game there.

Then in the 1980s and 1990s, we were able to generate value by leveraging businesses significantly. Financial engineering effectively was a differentiator. That again got arbitraged away.

Probably in the 1990s, we started to become more active but really through active board membership. Again, that's something that the competition became harder. What we realized is that for us to create permanent value, to create alpha, we have to improve the businesses that we own.

To do that, we created that toolset that you see there on the right with all of the different teams that we have in our various businesses. KKR Capstone, I will come and talk more about in some detail and the various different aspects of our firm that help us to really improve companies fundamentally. I am going to go through a few examples to explain what does that actually mean. What do we mean by creating value and how do we do it?

KKR Capstone—Value Creation through Operational Improvements

KKR Capstone is 60 people, as I said, with significant operational background working together with the PE team. We have a couple of portfolio examples here as to what they have been doing.

Latitude was probably one of the largest deals that was done in Australia. It was a consumer finance business that we bought from GE Capital. When we came in there, we realized management was not that great. We changed the CEO, the CFO, the CIO, the head of HR, so a significant involvement in recruiting a new team.

Then we spent a lot of time looking at improving their product platforms. Through improving the product platforms in New Zealand and in Australia with Capstone, we were able to improve productivity of this business in terms of how they sold their credit products, their credit cards, their credit insurance businesses to the consumer by almost 30%. We achieved some significant overhead savings. The business has performed very well. A large number of KKR executives in the company involved in the outset helping recruit management and then involved in actually improving the business itself.

Hensoldt is another example. This is the electronic defense business that we bought from Airbus. It was a highly complex acquisition. We needed approval from the German government. It took us over a year to get all of the approvals to actually be able to buy the business. Again, it was a carve up. It was not even a business before. It was just some divisions.

By putting this together, getting it more focused, getting the Capstone team inside, we were able to identify €105 million of cost savings that we could realize in this business. That is over 20% of the company's cost base. We have already realized 50 of these cost savings and effectively created a lot of value by doing this.

The last example is Epicor, the transaction that we did here in the states. The reason that I picked it is that it was a company that we bought from another private equity firm, in this case, Apax. You may say, 'Well, if somebody else owned it, there is probably not much left to do.' That is really not very often the case. Very often, we find other people that we compete with do not have the same focus on operational value improvement.

We were able to go in there and in this case, again, we have hired a new C-suite here. But what we had identified was really not necessarily a cost-cutting approach. This was focusing on how can we drive the top line. We had a Capstone team in there focusing on CRM, focusing on pricing, effectively better running the funnel and trying to improve sales growth in this business. A team that was working very actively with the management of Epicor to try to aggressively drive growth in that business.

Three separate examples of focusing on cost, of focusing on growth where we are actively working with the companies to improve their operations and in that way generate alpha and generate return for our investors.

The reason that we are spending time on it is to really explain it is not all about picking stocks. It is really about working with the companies and improving their operations. It is through that that we generate value for our investors.

KKR's Value Creation Approach: Panasonic Healthcare

I have got one more example that I wanted to spend a bit of time on because this is an area where we see so much value. It sort of highlights a number of things that we do well.

In the late 1990s, early 2000s in Europe, what we saw is we saw an opportunity where there were some very large existing conglomerates like Siemens or Daimler in Germany, like Schneider in France. Where we could go to those conglomerates and say, 'Part of what you need to do is focus and sell us one of your businesses.' Then those businesses, we were able to improve significantly.

We have taken this playbook to Japan where you have significant conglomerates. Those conglomerates are under exactly the same pressures. They need to focus. We have been able to basically convince them to work with us to improve their portfolios. We have done that with Panasonic. I will spend a minute on that in a second but also we have done it also with Pioneer, we have done it with Nissan and we have done it with Hitachi. We think there will be significantly more opportunities. These are all scale opportunities where we can create significant value.

Firstly, when we bought this business, it was a complex carve out. Again, it was not that simple to buy this out of Panasonic in 2014. We then worked with our colleagues from KKR Capstone to improve the operations in this business. Focus on procurement, effectively focus where before that was all done at headquarters across all of Panasonic, they now could do this themselves. It turned out that they could do it a lot more efficiently than they had done it before.

About a year and a half into this acquisition, we identified an opportunity in Europe that Bayer AG, the large chemical company was selling. They were selling a diabetes care business which was going to fit extremely well with Panasonic Healthcare. The European team worked together with our Japanese team in trying to convince Bayer to sell this to us.

We were able to get the Japanese bank to finance that business with 100% debt in that acquisition. There was not a lot of competition here. It added significant value to Panasonic Healthcare through synergies.

In the beginning of 2017, we were able to sell a 22% stake to Mitsui. We returned 1.7 times our cost in cash and the business is currently marked at 4.3 times cost. It is an example of how we can create value across different geographies by using our active value creation approach.

KKR Well Positioned To Continue To Deliver Results in Private Equity

With that, I am going to finish up by just going through the key themes. We currently see the macro being pretty strong. We see that reflected in our portfolio on a global basis. Our portfolio is performing very, very well. That has resulted in some very good returns in our private equity business.

We have a strong global team that works on an integrated basis with significant experience. We have got $34 billion of dry powder in our private equity business so a lot of money that we can deploy. As I said before, we have got a business that is very profitable that is generating good cash and that has significant growth opportunities going forward.

With that, I am going to hand back to Craig. Thank you very much.

Craig Larson: Thanks, Johannes. Just first from a schedule standpoint so everybody knows, Pete Stavros is going to be up on stage here in a minute. We then have Ralph Rosenberg who is going to run through our real estate business. After that, we will take a 10- or 15-minute break.

Ahead of Pete's presentation, I wanted to provide a minute or two of context. It actually builds on one of the things that Johannes said a few minutes ago. I do think when many people think about private equity and really the industry as a whole, they can think that we buy companies, we put a lot of leverage on these businesses and we hope multiples go up.

Now, of course, that really would not be much of a business model. That brings us to Pete's presentation. Pete is the head of the industrials vertical within our US private equity business. He is also a member of the investment committee for our US private equity business. We really asked Pete to touch on three things. First, at a very granular level, how we look to affect operational change within the portfolio of companies that we invest in as a control investor.

The second thing is Pete has a couple of interesting examples in here how we can be the second or third sponsor, and again, recognizing the focus we have on operational improvement, how we are still able to see operational change in the framework of those companies.

Then thirdly, again, it is a very interesting piece as part of this, but how as part of all of this we actually can do some pretty neat things for the employees of those companies in which we invest. With that, I am pleased to turn things over to Pete.

Incentivizing Employees and Creating Value

Pete Stavros

Head of Industrials, KKR

Preamble

Good morning. As Craig mentioned, my name is Pete Stavros. I am a partner in the New York office and I run our industrials group. As an industrials investor, as you can imagine, I spend most of my time with manufacturing companies. Within a manufacturing company, the majority of the workforce are blue-collar workers who are paid an hourly wage. In fact, that is usually the vast majority of the employee base. Despite the fact that that group of employees is so large and so important, what we find time and time again is that the relationship between the blue-collar workers and the company that they work for is not a positive one. It oftentimes is outright contentious. Of course, that impacts performance. We have been spending the better part of the past decade trying to understand why that relationship is not working, what we can do to improve it and thereby improve the performance of our companies and drive some of the operational change that Johannes and Craig have talked about. Also, positively impact the lives of these employees. That is really what I would like to talk about for the next 25 minutes or so.

History of Hourly Employee Relations

This history of poor employee relations when it comes to blue-collar workers, this goes back generations. This is of course where the labor union movement started. This is actually a picture of my dad. He was a blue-collar worker. He worked for a construction company in Chicago and earned an hourly wage. I just remember at the dinner table countless conversations about conflict between the workers and their employer. As a kid growing up, I was able to see this through the eyes of an employee. Now as an adult, I get to see it through the eyes of the company. It has been kind of fascinating to see both sides of it.

Misaligned Incentives

There are a lot of reasons I am sure why this relationship does not work. But one of the really obvious ones that I have observed is the hourly wage itself creates a huge misalignment of incentives. You have got on the one hand the employer who cares about quality, cost, on-time delivery and the employee who just cares about hours because that is exclusively how they are paid.

If you look at the bottom line just as one example, think about a situation where the employer falls behind on a job. They have got upset customers. They are working overtime to try and catch up. It is very expensive, terrible thing for the company. It is actually a great thing for the employee. They get more hours and they get time and a half or double time for the overtime hours.

Current Engagement Model

If you are the employer and you have got the vast majority of your employee base as blue-collar workers with exactly the wrong incentives, how do you engage? How do you behave? What is very common is to just apply an extreme amount of oversight and monitoring of your employees.

As you can imagine, the employees often do not react well to this. They evade oversight where they can. Where they cannot, they meet the bare minimum of expectations. Over years, this really devolves into a situation where the company gives up on the people, the people give up on their jobs. They stop investing themselves in their work and worker morale is very poor.

KKR Industrials as Engagement Laboratory

Here is what we have been trying to do in industrials. We have been trying to use our portfolio as a bit of a laboratory to experiment with ways of changing this relationship. We are in a great position to do this because of course, we are constantly buying new companies. That moment of change in ownership is a golden opportunity because people are not only open to change, they are expecting change.

CHI Overhead Doors

What I would like to do now for about ten minutes is take you through a case study. This is one of these examples that Johannes and Craig both referred to. This had been owned by private equity three times prior to KKR, a lot of head-scratching when we bought the business. What could you possibly do with this? This had been owned by Smart Money for 20 years. One of the things that had not been addressed was engagement and using the whole workforce to drive the operations of the business.

CHI Employees

The company makes overhead garage doors like the one you see here in the picture. They are based in Arthur, Illinois. When we bought the business, the company had from top to bottom about 800 employees, each one represented here by a purple dot. Now, 600 of the 800 were hourly workers in the manufacturing plant. Another 54 were truck drivers paid by the mile so very similar to being paid by the hour. Then you have got the balance here of salaried office employees.

Now, of the total employee base, 18 had ownership in the business when we bought the company. Those are the green dots in the lower left corner. Those 18 people got a payout of $57 million when we bought the business and $30 million went to two people. This is really a microcosm of the industrial world in this country. The vast majority of employees barely getting by on an hourly wage. Then a small segment with ownership and as everyone in this room knows, capital is so much more productive than labor. That is the group getting ahead. The getting ahead is concentrated in the hands of a couple of people. This is kind of what we see in almost every situation.

Low Worker Morale – Safety Concerns

You see some of that and you wonder what employee morale might be like. Well, in the manufacturing world, one other thing to look at if you want to get a quick snapshot of how employees are being treated is look at safety. This is something we see time and again. The workers are usually not being taken care of at the most basic of levels. They are not even getting sent home safely at night.

This, what we are showing you here is the total recordable incident rate. It is an OSHA-mandated statistic which shows you for every 100 workers in the manufacturing plant, how many are getting injured on the job every year. Simple first aid does not count. These are typically trips to the hospital.

You can see when we bought the business, there were 14 out of every 100 workers with let us say hospital visits every year. As I mentioned, we had 600 in the plant. Six times 14 would be 84 hospital visits per year. Over the course of let us say a five-year hold period, that would be most of the workforce which is kind of a staggering failure on the part of the company.

First Ever Employee Survey – 2016

We did the first employee survey the company had ever seen shortly after we bought the business. Not surprisingly, the results were terrible. We had a 30% response rate and 90% of the results were well below benchmark. In our favorite question, most people who filled out the survey said it would have absolutely no impact. Unfortunately, the survey company got rid of that question, so we cannot track our performance against it.

Performance Reflected Low Employee Engagement

As is always the case, this lack of engagement will manifest itself in poor performance. The company had as an example quality challenges that matched their safety challenges. If you have a safety issue, you will always have a quality issue because it reflects a lack of process or a process that is out of control. That is what we had at CHI.

There was also no margin growth despite pretty robust volumes as the housing market was recovering. There was excess working capital in the business. This is a build-to-order model and they had still a ton of inventory in the business.

New Approach under KKR

We bought the company. We brought in new leadership, established a new set of priorities. We brought a real process orientation to the business. Then importantly, we rolled out this employee engagement model that we have been developing over the better part of the past decade.

Our Employee Engagement Model

This is constantly evolving. We are trying to improve it all the time,but as it stands today, there is three legs to the stool on our engagement model. The first one is investing in the workforce, making people feel cared for, showing you want to invest in their professional development. Making everyone in the business an owner, down to the janitor who sweeps the floors in the manufacturing plant. Then engaging with the community through the company. This kind of community service is all about building pride in the organization. I would like to just talk through each of these in the next few slides.

Engagement: Investing in the Workforce

First, investing in the workforce. Again, this is all about making people feel cared for. We typically would have training in everything from lean manufacturing through to sales force effectiveness.

In this case, the burning platform, as I showed you, was and remains safety of the employees. You can see in a short period of time, we have cut the injury rate in half. But you can also see it is still well above the benchmark. There are two things that we are doing right now that we think will take us below the benchmark and hopefully on a path to world-class safety.

I think these two will give you another sense for how this employee base feels they have been treated over time. The first one is, we are changing the staffing model. What the company had done was because the business is so seasonal, they would lay people off right before the holidays during the slow period and then rehire in the spring to save on labor costs. That was obviously a morale issue, but it was also a safety issue because the people that you let go off right before the holidays, they cannot afford to wait around until the spring. They would go off and do other things, which meant you had a portion of your workforce that was new every spring. Then they hit their first busy season in the summer and those were the ones who all got hurt. We are changing that. We are going to keep the labor force intact through the slow season. It is going to cost us a little bit of money on labor, but it is going to have a huge safety benefit and a huge morale boost.

The second thing is we are air-conditioning the facility. In the height of busy season in July and August, it gets to be 110 degrees in the plant. In the trailer that we are loading the doors into, it can get to be 125 plus in the trailer.

You have got people running around like mad to meet production requirements. All they have got are a couple of fans to try and cool them off and so they get hurt. They make mistakes. We think that is going to have another big morale boost and safety benefit. That is the first thing we do, invest in the people.

Engagement: Making Everyone an Owner

The second thing is as I mentioned make everyone an owner in the business. You go from a situation like this to one where everyone participates in the financial upside in the business. To give you a sense for how we do this, we do this with very large option plans so much larger than a typical private equity firm would do. It is important that we use options because we obviously only want our investors getting diluted to the extent there is real performance.

In terms of order of magnitude, what we are talking about, if you take one of our truck drivers at CHI, we gave them an opportunity to invest up to $5,000 in the deal right alongside KKR in the same terms. They could do zero and we would still give them free options. However, if they did the maximum of $5,000, we gave them free options that under our base case we think will be worth $200,000. This is really life-impacting amounts of money.

Now, we have learned that it is more complicated than just sprinkling ownership around the company and then flying back to New York and watching the results flow in. As Johannes mentioned, we are deeply, deeply involved in our companies from an operating perspective.

We also do a lot to try and have this ownership be real for folks and drive performance and make it more than just a feel-good story. Part of that is education. A lot of people have never owned equity before. These options are options in a levered capital structure. It is a complicated concept to explain.

We figured out how to do it over time. We have gotten better at it. Then what we do is share a lot of information about our business plans. It is quasi kind of open-book management. We share the business plan, where we are headed, how much money we make, where we expect margins to go and then we try and tie the high-level plan down to all the different functions of the business, so people know how they are contributing and how what they are doing every day creates value.

We do a lot to make the ownership feel real. We do some things that would sound silly to people in this room. We print physical stock certificates. We have found that the physical manifestation of ownership really makes this feel real and tangible to people. Even though the stock of CHI, it is a private company. It is not publicly traded. We actually opened Fidelity accounts for people so that as our valuation mark improves, they see value being created for themselves and their families.

Then the most impactful thing you can do which we try and do every chance we get is to pay an early dividend even if it is tiny because there is nothing quite like people receiving a check to understand that the ownership is real.

CHI's First Dividend in 2017

That is what we did at CHI. What we wanted to do was just play a 60-second video to bring you on to the shop floor in Arthur, Illinois and have you feel what the enthusiasm that starts to build pretty quickly. This is only a little over a year into the investment. We paid a very, very small dividend. It was only out of excess cash.

For the hourly workers, the range was $1,300 to $4,000 which may not seem like a lot. But you have got to keep in mind, we are the fourth private equity firm to show up. They have never seen anything like this. Also, we emphasized that if we kept performing, we could deliver many, many, many times this amount of money to people. Lastly, keep in mind, half of America has no savings or negative net worth. A lot of those people operate in manufacturing facilities.

As you watch the video, also just keep in the back of your mind what was when we showed up in terms of employee morale, safety, lack of investment in the facility, the staffing model. Now, everything is starting to turn around. If we can roll that quick video.

[VIDEO]

That is obviously what we are going for is to get people to think differently about the company and their role at the company.

Community Involvement Engenders Pride in the Company

Those are the first two legs of the stool. I mentioned investing in the people, making everyone an owner. The third part is this idea of getting the company involved in the community. This is one of these things a lot of companies do on a check-the-box basis, but what we found is if you do it in a meaningful way through the work of all the employees, it can really have an impact on how proud people feel to go to work every day.

What we do is we find a charity that has a need for the product that our company manufactures. It is tied in almost naturally with the mission of the company. Then we strike a formal partnership where we provide financial support, free product, free training, and then we get the employees involved in the charity.

In this case, Homes For Our Troops builds customized homes for wounded vets like the one you see here in the picture. We provide garage doors all over the country for wounded vets.

Then in the local community, we are sponsoring entire homes. When those homes are getting built, we basically rent buses and bus our employee base out to the home and help build it.

I have been at CHI shareholder meetings where sometimes you get a bigger reaction out of some people through this work we are doing in the community than you even do around the ownership stuff.

Employee Survey Update – 2017

One year later, we did our second employee survey. The results were dramatically better. We went from a 30% response rate to an 80% response rate with the results going from 90% below benchmark to 60% above benchmark. Still a long way to go but a huge improvement in just one year.

Engagement: Practical Example of Changed Behavior

One of the questions that our investors often ask us is can you give us an example of changed behavior. What does an engaged employee look like? Here is an example. This is Larry Beal. He is 60 years old. He has been with CHI for many years. Larry invested the maximum amount, the $5,000 I referred to earlier. He is looking at a very significant potential payout. Larry is very, very focused on helping the company get better.

I am going to give you one example. As I have mentioned, we spend a lot of time directly involved in our businesses. We do things like ride along with truck drivers making deliveries to really understand how value is being created and where additional opportunities might come from.

This is an actual route that Larry and I drove together. This is from Arthur, Illinois. This is his Central Wisconsin and Western Wisconsin routes. You can see he goes almost to Minneapolis all the way up almost to Duluth back to the center part of the state. Then we inexplicably sent him to Northern Michigan to deliver one garage door.

Larry says, 'Hey, Pete, before I was an owner, all I cared about was miles. It is $0.90 a mile. You could have me driving around in circles for all I care. But I really wanted to show you that this is what I am seeing out of our scheduling department and there is no way we are making money on this stuff because I know what you pay me to deliver a door. I know roughly what we are charging for a door.'

You go through the math, and of course, Larry is right. We are making no money. This was reasonably pervasive in the scheduling department. What was happening was we were overriding our own route scheduling system to accommodate small deliveries. Our heart was in the right place. We wanted to accommodate small customers and small orders, but it was costing us a lot of money. This is what happens when employees start to become engaged is it almost becomes an issue of prioritizing all these ideas.

CHI Operational Transformation: Results So Far

To touch on what both Johannes and Craig mentioned, here is an example. Again, we were the fourth private equity firm to show up. It is a building products company so people said margins were already very good at 21%. KKR must be crazy. Why would they be buying this?

You can see in under three years, we are pushing 30% in the EBITDA margin. We have taken almost all of the working capital out of the business. This started at 12% of revenue which in the industrials world is totally respectable, probably top quartile. By 2018, I think we will be negative on working capital.

Potential Macro Impact of this Engagement Model

In the time we have got left, what we wanted to do was to talk to you or maybe tell you about some of the conversations we have internally about what could this kind of engagement model mean for the industrial economy if this were to become more common. We discuss it on three dimensions: wealth and income inequality, productivity and technology disruption.

Just to touch on the last one which might be the least clear, the idea is that technology is great unless you are the blue-collar worker who is getting disrupted. If we can get our employees using their whole brains like Scott Nuttall likes to say and get them behaving like employee owners, they are less likely to get disrupted and more likely to survive alongside of technology. I will give an example of that.

Capital Safety

Starting with inequality, we all know there is a massive inequality problem in the country. Broad-based ownership could be a part of the solution. We wanted to illustrate what this can mean for people by touching on Capital Safety. This was a business we bought in 2012. They make fall protection equipment so like the safety harness and the cabling system you see this gentleman wearing on top of a wind tower. We owned the business for three and a half years and sold it to 3M.

Employee Ownership Prior to KKR

When we initially bought the business though, this was what the picture looked like so very similar to CHI – 1,250 employees, 35 people had ownership. The vast majority were hourly workers in the plants and the distribution centers making $14 to $18 an hour.

Those 35 people when we bought the business got a payout of $157 million and two people got $60 million of the $157 million. Again, a microcosm of the industrial economy more broadly.

Employee Ownership (Update)

We rolled out our engagement model, our broad-based ownership, our operational improvement program. It was a great investment for our investors. It was a fantastic outcome for the employees when we sold the business.

We went from only 35 people even participating in ownership to 204 making more than $100,000 and 44 making more than $1 million. If you are worried about the top two people in the lower left here, they actually made more money with us than they did in the prior deal. This can work. Everyone can participate in value creation.

Capital Safety Exit

We want to play one other video. This one is about 90 seconds long. This is some footage that was captured inside of our Red Wing, Minnesota plant. This is the moment that the employees find out what their equity is worth. This is the first time they hear that news, if you can play that video.

[VIDEO]

One of the unexpected benefits of this program was the impact it had on our senior leadership teams and how much easier it became to drive operational improvement and break down barriers to change. That gentleman, Kevin Coplan at the end who ran the US business for us, once we rolled out that program, it just kind of became all about how do we maximize the value of the equity and really deliver for our people.

Capital Safety Operational Transformation

Now, although it has nothing to do with inequality, we cannot pass up the opportunity to show you the results again just like CHI, fourth private equity firm to own Capital Safety. Margins were already really good in the mid 20s. These are EBITDA margins. You can see in three and a half years, we took them from the mid 20s to almost 40%. People would have said that was impossible.

Operational Transformations: A Broader Set of Results

Craig tells me there are some people here who are tough critics and we need to show a little bit more data. Just so you do not think we are cherry picking, this is the last five industrial deals we have done. You can see the margin improvement on the low end has been 600 basis points. On the high end, it has been over 1,000 basis points. Three of these businesses had been owned by private equity firms who prided themselves in operational change.

Gardner Denver: Engaged Employee-Owners Driving Productivity

Moving on to productivity, this is probably intuitive that engaged employee owners will be more productive employees. But, wanted to give you one example. I would love to talk about Gardner Denver because this was a public company in 2013. At the time, there were 6,000 employees and there were 86 people with ownership in the company: 86 out of 6,000.

We took the company private, rolled out this engagement model. We have now taken it and transformed the company during the years it was private. It is now public: 6,400 employees. Everyone is an owner in the company. The least amount of ownership anyone has is equivalent to about 70% of their annual compensation so totally changed culture.

The Gardner Denver Challenge

The CEO Vicente and I spent some time after the IPO thinking about how we could prove to Wall Street that as a result of this engagement model, we could in a differentiated way execute on an operational improvement agenda. We wanted to find something that we could really take a metric and move it in the right direction rapidly by working through all 6,400 engaged employee owners.

We picked net working capital for a bunch of reasons. One is that everyone touches working capital in some way between receivables, payables and inventory.

Two is these are reasonably easily understood concepts because everyone has got inventory at home in their pantry. They all have bills to pay so they all have payables. You can really explain this stuff to people even if they have not got formal training.

Lastly, there is a lot of room for improvement. Gardner Denver forever has had over 30% of revenue in working capital. When we started, it had almost 32%. If we drove the improvement we thought we could, it would free up hundreds of millions of dollars of cash to reinvest in the business.

Our Approach to Improving NWC at Gardner Denver

We really went after this starting about a year ago. We took a train-the-trainer approach which means you basically establish master trainers in your company. They go around the world training new trainers and then they train the rest of your employee base. With just a few steps, you can actually reach all 6,400 employees.

We did a lot of measurement and reporting so that people knew on inventory for example how we were doing by facility, by product line every week.

Then lots of ongoing communication, not just ongoing training but also celebrating success. We found this as a big way to drive engagement and to build on quick wins.

We had a film crew basically follow our management team around and capture these moments. We created little ceremonies out of them. We take the video, translate it into a bunch of languages and zap it around the world. We have found that creates positive followership.

Celebrating Examples of Improved Engagement

I will not play any of the videos in the interest of time, but we have got dozens of these. This example is of a woman named Holly in our Redditch, UK facility. After her training, she went out and resolved a bunch of five-year-old accounts receivable that aggregates to £1 million. Again, people would have said that just would not be possible. Of course, the message to all the employee base is just imagine if everyone would behave this way.

NWC Reduction at Gardner Denver: Early Results

We just started this but we have already taken 230 basis points out of working capital. Gardner Denver is public. We will be announcing second quarter results soon if you are interested. You can see how we are doing on this metric.

CHI Overhead Doors

Then finally, technology disruption. If we go back to Larry the truck driver at CHI, if all Larry is doing is picking up garage doors and dropping them off at customer sites, some day that will get disrupted by autonomous vehicles. But think of all the things a human being can do that a computer or a robot cannot do.

How an Engaged Truck Driver Creates Value at CHI

One is identifying improvement opportunities. Our truck drivers are now constantly coming up with ways to load and unload doors or improve our route efficiency – something a computer cannot as easily do if it takes creativity.

Second is another thing a computer cannot do is actually get out of the truck at every stop and physically unload the doors. We are the only company that does this because we have got this unique relationship with our drivers. It is a huge differentiator and a huge productivity benefit to our customers.

They can provide competitive intelligence to us. When they are dropping off doors, they are in the customers' warehouses. They can see our share of wallet, whether there has been competitive entry, etc.

They can also serve and do serve as a feedback loop on quality. When they are unloading the doors, they take note of dented panels, missing hardware, etc., report it back to the plant and so we can fix the problem before it spreads.

Lastly, another thing a computer cannot do is serve as another source of customer relationship. These guys are almost like second-line salespeople in the job that they do.

The point in all this is that even if we had autonomous vehicles, as engaged employee owners, they are delivering so much value. We would still have them sitting in the truck doing all of these things even if the truck was driving itself.

Work In Progress

As I mentioned at the outset, this is very much a work in progress. We have started in US industrials. We are working globally and across business lines to see where this could have other applicability. We are honored that Harvard and Rutgers have taken note of what we are doing and are starting to study what we are doing and are helping us isolate the performance improvement impact related directly to employee engagement.

With that, I hope we have done a decent job of proving to you that we are doing a whole lot more than just levering up companies and hoping multiples go up. Hopefully, I have given you some sense for just how deeply involved we get with our businesses once we buy them. As Henry likes to say, that is when the hard work really starts is after you make the acquisition. With that, I am going to hand it over to my partner, Ralph Rosenberg.

Real Estate

Ralph Rosenberg

Head of Global Real Estate, KKR

Opening Remarks

Thank you very much. I am very happy to be here. My name is Ralph Rosenberg and I run the global real estate business for KKR. I am going to basically illustrate in the context of the real estate business several of the things that Henry, Joe and Scott mentioned this morning.

We have an incredible brand, a robust balance sheet, a differentiated culture and a global presence. In 2011 when I joined KKR, we had zero fee paying AUM that was dedicated to commercial real estate. This is basically the story of the beginning of the scaling of a sector of the KKR franchise that runs fee paying real estate capital in an industry that Joe pointed out is an $800 billion industry that we have a very, very, very small fraction of the AUM currently under management. I am going to walk you through from where we have come to where we are, and where the future might lead us.

To give you two seconds of background, I have been in and around the real estate investing business both debt and equity since I graduated from college in 1986. I joined KKR in 2011. As you are going to see, we raised our first dollar of fee paying AUM in 2013.

KKR Global Real Estate – What We Do

As Joe mentioned, we are not just in the AUM aggregation business. We are in the AUM business where it is the high value AUM – high value with respect to earning fees, high value with respect to earning promote.

In both the debt and the equity space in commercial real estate, we are always migrating towards complexity, investing capital and originating credit in situations that are complicated. The story is differentiated, etc. Then we effectively work to create a very simple fact pattern with respect to that asset. Then we sell that fact pattern to the next buyer or in the context of debt, we get refinanced out.

In this world that we are living in where risk-free rates are very, very low globally, we are investing primarily in assets that can be created in a defensive context that can create a lot of cash flow which resonates very, very much with our investor base. Additionally, we are globally looking for market inefficiencies where we can use our balance sheet and use our AUM to basically do things that other people cannot do.

KKR Global Real Estate – Our History

This is a timeline effectively from when I joined the firm in 2011 to where we are today. As I mentioned, we started with the idea of high value add, high fee paying, high promote opportunities in the US equity business which was 2013 when we raised our first dollar of AUM. We migrated to taking advantage of a market opportunity in India. Then we migrated to the United States to effectively set up an integrated credit platform which I am going to tell you more about.

Then we launched a European equity business. We listed one of our credit businesses in the US in the New York Stock Exchange and created permanent capital that Scott referenced earlier. We took advantage of Dodd-Frank and risk retention. We raised the largest risk retention vehicle in the credit space in the real estate industry and now control about 40% of the market share there.

Then just last December, we raised our second successor US equity fund. As Joe said, that is like the beginning of this incredible journey that we can take to creating real scale in a business unit where we have planted a lot of seeds that are now just starting to grow.

Then lastly, as Joe mentioned, the opportunity in Asia is quite extraordinary. We have been investing off our balance sheet in Asia for many years, but we just recently hired a gentleman named John Pattar who starts next week who is one of the more formidable players in the real estate equity investing business in Asia. As you would expect, the playbook should be to raise dedicated fee paying AUM around his joining of the firm.

Importantly on the bottom of this page, you can see we started with a vision. We had five people when I joined back in 2011. Now, we have 63 people. We are in seven offices in five countries.

KKR Global Real Estate – Team Overview

This shows you the cities that we are in. We are obviously a global business. We also importantly have dedicated professionals who work with Suzanne in the client and partners group. We have dedicated professionals in the capital markets business. Just as we do in private equity, we have this adjacency where we can create opportunities to earn fees from a capital markets perspective in the real estate space just as we do in private equity. I am going to tell you a little more about that.

Lastly, you can see on the right-hand side of the page, we started with nothing in 2011 with respect to AUM. Now, we run in terms of actual fee paying AUM $4.7 billion, and the KKR balance sheet along with employees have invested $800 million in the businesses that I have currently pointed out to you guys.

Importantly, the difference between the $6 billion of AUM and the $4.7 billion that you are seeing in this chart is AUM that we have not yet drawn on that is only fee-paying when we draw on it. We have actually returned several hundreds of millions of AUM as we have harvested transactions throughout the world.

KKR Global Real Estate – Our History

Here is how we look from a geographic perspective. In North America, we have a traditional real estate private equity 11-year fund life business. We have a core plus platform that is actually a permanent capital vehicle that is only about $400 million right now. Then as I mentioned, we have two credit vehicles. One is this B-Piece Risk Retention vehicle which reacted to the Dodd-Frank legislation. Importantly, that is ten-year capital and we control 40% of the market share as I mentioned. Then lastly, KREF is our permanent capital vehicle that is listed in the New York Stock Exchange.

In Europe, we have a traditional private equity real estate fund called Real Estate Partners Europe. We have a direct investment off our balance sheet in an integrated asset manager in Germany that runs core real estate all the way through the risk spectrum to opportunistic real estate in the German market which is a very, very closed market that primarily attracts German domestic capital.

Then lastly as I mentioned, there is a huge opportunity in Asia. You should expect that we are going to leverage our balance sheet and our franchise to create permanent AUM in Asia. I also mentioned we have a credit business in India.

KKR Global Real Estate – Our Performance

As Joe mentioned, it is all about performance if you really want to scale. This slide really illustrates our performance to date across the strategies that report. Real Estate Partners America, close to a 20% gross IRR. As of the end of Q1, we have distributed back 85% of the invested capital. We are just getting to a point now where we can see visibility on hitting our pref and hitting a multiple of money that will allow us to really start booking both realized and unrealized promote as these investments continue to season.

In Real Estate Partners Europe, we are off to a great start, almost a 22% gross IRR. This is at a fund stage where we are not yet at a point where we even can book unrealized promote because we have not yet hit an inflection point to see visibility on the hurdle and the multiple of money.

Then you can see on the bottom of the page, on the credit side, we have had very, very strong returns as well. We pay out a fairly high current yield which is very attractive to investors in our public stock which is KREF and also was one of the differentiated aspects of the product in the BP space to attracting a lot of global capital to that product, primarily insurance companies.

Our successor fund in the US just got closed at the end of last year. It is a $2 billion fund. We are not yet in a position to report either IRRs or multiple of money because everything effectively is held at cost.

KKR Global Real Estate – Our History

When I mentioned the incredible opportunity available to KKR with respect to brand, balance sheet, global reach and culture, I was really referring to this particular slide. As Henry mentioned at the beginning of the day, our culture is incredibly differentiated relative to our competitors. That is absolutely true as it relates to the real estate space.

If you think about real estate private equity firms, the overwhelming majority of them are standalone investors who only operate in the real estate private equity world. Because we are adjacent to all these other parts of the firm, we can create incredible sourcing channels. We can create incredible access to information. We can create incredible access to capital markets information. We can create incredible synergies internally to creating operational improvements at the investment level in the real estate space.

We are really drawing day in and day out across the firm to really differentiate ourselves in the context of a real estate asset management universe that quite frankly is pretty crowded. As Joe mentioned, there is $800 billion of AUM that is managed in the real estate space globally. By definition, there are lots of people we compete with. It is all about how do we differentiate ourselves from our competitive set. In my opinion, it all comes back to this particular page.

KKR Global Real Estate Business – Evolution

As I mentioned, on the left-hand side of this page, for those of you who were here on investor day 2013, I had been here about a year and a quarter, we had no AUM. We were using our balance sheet – Scott referenced that – to do proof of concept investing. Now, you fast forward and we are really hitting on all cylinders across all product types in all regions other than Asia – but that is to come – and we have had incredible results from an investment return standpoint.

As you can see on the bottom of the page, you start to see the fruits of our labor. The balance sheet has invested about $800 million. The returns on that direct balance sheet investing are not shown on this page. When I mention we are up 20% in our US equity business, we are up 20% plus in our European business, that direct balance sheet allocation of those businesses does not show up on the bottom of this slide. But we did want to illustrate to you the power of this franchise with respect to starting to earn fees and recurring income for the P&L of KKR.

Management fees are kicking in. Capital markets fees are kicking in. As I mentioned, we are just starting to see the fruits of our labor with respect to promote.

Where Does Real Estate Go From Here?

Where do we go from here? In 2013, we started with a high-margin, high promote-paying vehicle in the United States. That is Real Estate Partners America I.

Today, in the equity space, we have Real Estate Partners America II, and we have Real Estate Partners Europe. There are incredible opportunities to create adjacent products that not only are complementary to successor funds like Joe mentioned but that allow us to go up the safety spectrum in the real estate world and then continue to capture fee paying AUM.

In the real estate world, the safest product is what is called the core investment product. Then we run the higher-margin, higher fee-paying, higher risk-taking funds and value and opportunistic. The spectrum between core and where we are today is incredible. Our ability to leverage what we have today and to move towards the core product and to raise additional AUM that is fee-paying and promote-paying is extraordinary.

I mentioned we have got the opportunity in the equity space to raise an Asia fund. In credit, we are continuing to leverage off our Real Estate Credit Opportunity Partners fund which is this B-Piece Risk Retention fund. We are currently in the process of a successor vehicle there. We continue to have very, very strong results in KREF which is our permanent capital vehicle. You would expect over time that we will continue to issue primary shares in KREF and continue to scale that permanent capital vehicle.

In the credit space in the bottom-right-hand side of this slide, you can see that there are also incredible opportunities for adjacencies to our existing credit products to increase AUM but to do so in a way where it is both fee-paying and promote-earning over time.

I would conclude in saying the following: that in my opinion, in an industry that has $800 billion of fee paying AUM that is being captured by GPs globally that KKR with our brand, our balance sheet, our global reach and our culture should be able to capture more than our fair share of that $805 billion of AUM.

Today and historically, we have effectively gotten to $6 billion. There is a huge opportunity for us going forward. I am going to pause there. I am going to offer everybody the opportunity to take a 15-minute break and then we are going to continue the program.

Credit And Markets

Todd Builione

President of KKR Credit and Markets, KKR

Agenda

Good morning. I am Todd Builione; I am President of our Credit & Markets business and over the next 20 minutes my plan is to cover four topics. I will start out by talking about how Credit & Markets has evolved over the last ten years. I will then spend some time on our business model and use a couple of case studies to highlight that business model. I will then talk through our partnership with Franklin Square, or FS Investments, which recently closed in April of this year. Then I am going to end by talking about the growth path ahead.

KKR Credit & Markets

Ten-plus years in the works

Our Credit & Markets business has really been ten-plus years in the works. Back in 2007 we had just $11 billion of assets under management across KKR Credit; today we have under $60 billion. Credit management fees were $53 million back in calendar year 2007; in the latest 12 months just under $250 million. Transaction fees were a mere $1 million back in 2007; it was the first year that we got our Capital Markets business up and running and we participated in one public equity deal. In calendar year 2007 we syndicated $4.7 billion of equity and we arranged $106 billion-plus of debt. That placed us number 11 in the sponsor loan league tables, surprisingly to us one spot behind Citigroup and two spots behind JP Morgan. You can see we monetized that transaction volume in the form of transaction fees: $434 million over the latest 12 months.

Total revenue back in 2007 was $78 million. That was a mere 7% of the aggregate of KKR. The last 12 months just under $800 million or 25% of the aggregate of KKR. Back at the end of 2007 we had 62 employees. Today we have 293 employees, or roughly 23% of the total firm.

Since inception

Adam Smith is going to follow me and drill down on our Capital Markets business. So I thought I might take you through the 14-year journey that we have been on in our Credit business to get to the point where we are today. First, I will start with leveraged credit; when I say that you should think traded credit: the tradable markets.

The business started back in August 2004 as we raised $800 million for a credit-oriented permanent backed capital vehicle called KFN. We did three things really well since then that has resulted in the scaling of the business. The first is top-tier investment performance. As an example, if you look at our flagship opportunistic credit strategy, over the last ten years we have outperformed the benchmark by more than 460 basis points on an annualized basis and our performance ranks on a relative basis to our peers top percentile over a one, three, five and seven-year basis. Not top quartile, not top decile but top one-percentile.

Second, we have been able to rejuvenate our CLO business since the crisis. Over the last 12 months we raised $2.4 billion of new CLOs. And finally, we bought Avoca back in August 2014. With Avoca came $8.5 billion of assets but much more importantly, a top-tier European leveraged credit team that took our leveraged credit business from being a US-only business to now being a US and European developed markets business.

In alternative credit we did two things really well back in 2010 that sowed the seeds for the building of this business over the years. First, we raised our first dedicated comingled fund to private credit: Mezzanine Fund I. We put up good numbers and we learned some lessons over the years about how to manage private credit mandates. On the back of those lessons and that investment performance we have been able to raise three comingled funds since: Lending Partners I, Lending Partners II and then Private Opportunistic Credit II, which we closed at the end of last year at $2.3 billion of overall AUM.

Second, back in 2010, we were able to convince three clients of KKR to entrust us with their capital with a brand-new investment strategy for the firm: special situations, distressed, the event-oriented investing. We had really strong performance out of the gate. On the back of that performance we have been able to raise two comingled funds since: Special Sits I at $2 billion and Special Sits II at $3.2 billion.

You can see over the last five years we have had an awful lot of momentum across this business: 20% CAGRs on an AUM basis excluding FS Investments; 26% with FS Investments. On a management fee basis, also a 20% CAGR.

There is something that is missing from this slide, though. Of the $59 billion of AUM, $6 billion of it is in dry powder. Like Real Estate, our model in Credit is that we need to invest the capital in order to turn those management fees on. There is about $60 million of annual management fees embedded as we turn that $6 billion of dry powder into invested capital.

Our business model

Back in the summer of 2016 the leadership team spent the full day together in a room that we call the KKR incubator. It is a funny name; all it is is a room full of whiteboards. We spent that day in a whiteboarding session, a brainstorming session. We were not talking about all the momentum that we had in the business, not talking about all the success that we had had over the last ten years. In fact, I do not remember any mention of that. We spent all of our time in classic KKR form talking about what lessons we had learned, how we could get better, how we could take our business and punch through to the next level.

There were two good, maybe great, ideas that came out of that session. We looked, by the way, as background, at the private credit industry and realized that maybe was the best opportunity that we had right in front of us. Why? Because we saw that industry AUM for private credit had grown by $400 billion over the prior ten years. We felt like we had the capability to attack that market in a more aggressive way.

The two ideas that came out were, one, to develop a more compelling business model. First, we realized that although the 134 investment professionals that we have across Credit & Markets are focused on originating financing opportunities for their sponsor and corporate clients, we had not really done a great job at connecting the dots with the 262 investment professionals that sit across our Private Markets business. We felt, bluntly, that that was pretty silly. The last we checked, our senior private equity partners, people like Pete Stavros, get paid in part to have very strong relationships with corporate CEOs and CFOs. The stark reality is I think at least 90 out of 100 times when we ask the question, 'Do you want we, KKR, to buy control of your business,' the answer is no. However, the reality is within 90% of the no’s, there is a yes. The reality is many of those same CEOs and CFOs need our help, helping them finance acquisitions, growth opportunities and many other uses for debt financing. So we started by connecting the dots more specifically across the organization.

The second thing that we did was turn our originators from product peddlers to solution providers. Any of us that have tried to build relationships in any context over time know that if you are product peddling one product versus really being a solutions provider, you are going to have a much better time and you are going to build much stronger, stickier relationships by really putting yourself in a client's shoes. We realized that we needed to move our originators from that product-peddling position to a solution-providing business. We did that by merging our Credit and Capital Markets business, creating Credit & Markets, and making our originators understand and appreciate that they ought to be indifferent between providing financing solutions that were capitalized by our credit and investing pools of capital, which might be a highly-structured private credit solution, or those that could be capitalized by our debt capital markets capabilities that might be a plain vanilla syndicated loan opportunity that we could underwrite and distribute with our capital markets capabilities.

Case Studies – Leveraging our Business Model

There are a couple of case studies which hopefully will highlight this business model. I will talk through Sycamore's acquisition of Staples, which leveraged our entire solution base, both our credit and investing pools of capital, as well our capital markets distribution capabilities. I am then going to talk through Marlin Equity's acquisition of Virgin Pulse and Redbrick Health, which started with our Americas PE team.

Delivering a Financing Solution to Sycamore Partners

First, Staples. Back in June 2017 we got a call from Sycamore. Sycamore has been a longstanding client of KKR. They asked us for our help in helping them finance their take private of Staples. It was a highly complex transaction as their intention was to split Staples up into three entities. We were, within 2.5 weeks of getting that call, able to commit to a $500 million first lien term loan which formed the foundation for their capital structure.

How did we deliver this solution? We leveraged our full model: $150 million investment from our credit pools of capital, a $350 million commitment from our balance sheet and ultimate distribution via our capital markets capabilities to bring the $500 million together. What did it mean for the KKR shareholder? We turned on that $150 million of dry powder. So $3.8 million of management fees, $5.8 million carry potential and a $7.5 million capital market fee. To Scott's point earlier, around monetizing our opportunities, we created a $17 million revenue opportunity for a KKR shareholder.

Delivering a Financing Solution to Marlin Equity Partners

Next, in the first quarter of this year our Americas PE team was considering an investment in Virgin Pulse and Redbrick Health. We did not ultimately get there on the PE side but we, as an organization, running the firm as one firm, one team were able to pivot and create a financing opportunity out of it. We worked with Marlin, who had Virgin Pulse and Redbrick under LOI. We ultimately committed to a several-hundred million-dollar first lien term loan.

In this example we were able to capitalize that term loan 100% via our credit investing pools of capital. By doing that we turned on $8 million of management fees, $12.3 million of carry potential for a total revenue opportunity of $20 million-plus.

As I step back and think through these examples, it is clear to me that we are approaching this business in a way that only we, KKR, can. We have all 396 investment professionals focused. We have a scaled credit platform with $59 billion of credit capital. We have debt capital markets capabilities that we have honed over the last ten years. We have a $16 billion balance sheet which allows us to optimize those debt capital markets capabilities.

Before joining KKR, above five years ago, I spent 15 years at other firms. I can tell you first-hand that those other firms do not have all the tools in their toolkit that we have. They definitely do not bring them together in the way that we do at KKR.

Partnership with FS Investments

Overview

Let us go back into that incubator room, back into the summer of 2016. I mentioned we had two ideas. We talked through having a more compelling business model. The second idea was a pretty simple one to come up with, but a harder one to execute against. It was scale.

This is where our partnership with Franklin Square, or FS Investments, comes into play. Just a little bit of background because many of you might not know FS Investments. They are a Philadelphia-based firm; they manage \$25 billion of AUM. They are expert at delivering alternative investment product to the true retail client. By true retail, I mean \$25,000, \$30,000, \$35,000 average ticket size. FS served as investment advisor and Blackstone's GSO as sub-advisor to the FSIC BDC franchise. Think middle-market lending, private credit BDC franchise. On April 9th this year, FS ended that relationship with GSO and formally formed a partnership with KKR.

That franchise, as you can see, consists of \$13.2 billion of gross assets. We combine that with the franchise that we, KKR, built over the years through that same retail channel but with a different partner: \$4 billion of gross assets. For \$17.4 billion of aggregate AUM, 250,000 underlying retail clients. We make loans through this franchise through 150 sponsor relationships to 325 underlying borrowers.

Strategic rationale

My team, our team, is just as enthusiastic as I am about this partnership with FS because they see that the strategic value that it brings to our platform is great.

First, it delivers that scale word that we were after. It is scale in a space where scale really matters. Scale allows us to narrow the competitive universe in private credit. It is no secret that private credit has gotten competitive. The last I checked there were 75 or 100 different firms that are competing somehow in that space. By having scale, we narrow that competitive universe. We now compete with three, or four, or five firms that, like us, can routinely write \$300 million, \$400 million, \$500 million, maybe even \$1 billion-plus checks. Scale allows us to have ball control; Scott referenced it earlier. In every situation in which we lend we effort to be sole lender so that it is just us and the borrower at the table. That type of bilateral negotiation tends to result in, for example, a better covenant package and more downside protection.

Scale allows us to focus on a part of private credit where we want to be focused: the true upper end of the middle market. At the end of the day, this is a simple business. We are lending money, we are collecting a coupon and then we are getting paid back our principal. Common sense would therefore tell you that you would rather loan money to bigger companies because bigger companies tend to have better competitive dynamic, they tend to do better through downturns and they tend to attract better management teams.

Second, the FS partnership delivered \$13 billion-plus of incremental permanent capital to KKR. You have heard a few times from Joe, from Scott, from Henry, about the importance of permanent capital to our go-forward strategy. It took KKR Credit's permanent capital to 31% of overall AUM. If you include strategic client capital, it took the aggregate KKR's capital, permanent and strategic client capital, to 22% of AUM.

You are going to hear later on today from Suzanne Donohoe, who is going to talk about the rise of the individual investor in alternatives. This partnership gives us optionality to do things with a partner that is particular expert at bringing product, which we produce, manufacture and manage at KKR, to the retail client. We fully expect that we will be doing more with FS Investments over time.

Even if you wipe number one to number three off the slide, the economics of our partnership with FS are highly compelling to the KKR shareholder.

KKR Credit Snapshot – 31st March 2018

Where does this leave us? $59 billion of aggregate AUM in Credit: $25 billion in leveraged credit, $34 billion in alternative credit. We have investments in 750 underlying portfolio companies: about 500 in leveraged credit, 190 in private credit and 60 in special situations. We, importantly, have $2.7 billion of our own money invested alongside our client capital. $2.4 billion is from KKR's balance sheet; $300 million of it from employees.

Where Does Credit Go From Here?

As we think about where we can take KKR Credit from here, the first point, and it is an important point, is that we have expanded our investment capabilities over the years. Look back in 2007; it is only roughly ten years ago. Back then we were managing CLOs, loans and bonds, mandates and that permanent capital vehicle called KFN which I referenced earlier. Back in August 2014 we, with KKR shares, bought in that permanent capital vehicle in a highly strategic transaction for KKR, to increase the size of our balance sheet.

Today, look at everything else we are doing. As we think about the path forward, because of all the different investment capabilities that we have built within KKR Credit, we have many different ways to double AUM and double fees. There are really four priorities that we have, as we think forward, to get to that point.

The first will always be on every single page of priorities across KKR. We have to deliver top-tier investment performance. With top-tier investment performance everything gets a lot easier and everything gets a lot more fun. But as we think about businesses that we can scale from here, there is a handful of them where we just need to continue to run hard and capitalize on the momentum that we currently have.

I mentioned $2.4 billion CLOs raised over the last 12 months. This year we should probably get to something like $3 billion and we think over time we can take that number to $4–5 billion per year.

Our opportunistic credit strategy, I mentioned the top-percentile performance, but what I did not mention is maybe the most exciting piece of this, that it is only about $1.5 billion in size today. With that investment performance and with the competitors' sized funds, which are $10 billion-plus in size, we ought to be able to grow that business to $10 billion-plus over time.

BDCs, I mentioned our partnership with FS Investments. What I did not mention is that that partnership will add, over time, about $100 million of run rate annual management fee and performance fee income. That is just on the current-size business, but as you can imagine, we and our partners in Philadelphia have plans to grow the business, to grow the equity capital, to tap in to that individual investor community in a bigger way and to grow our BDC franchise.

On private opportunistic credit I mentioned we closed on the second fund, $2.3 billion at the end of last year. We are doing really differentiated investing within that strategy: asset-based investing, structured finance investing. That is a fund that over time should have fund sizes of $5 billion, or even $10 billion.

And then special situations, our distressed business, is about $8 billion. The last I checked, the leading competitors are $20 billion or even $25 billion. We have a lot of room to run there.

We, like other businesses, are going to look to build out geographically. In fact, we took ourselves back into that whiteboarding room the week before last to talk about Europe as a management team. We decided that we could take that Credit & Markets combined model that I described earlier, that has worked so well in the US and we could apply that equally to Europe. Over time we should be able to raise $5 billion-plus for European private credit.

And then Asia credit; the beauty there is it is a new business. We are sending someone who is a star in New York and his family to Asia to help us build out that business. It is technically new, but we are able to leverage the franchise and the platform that we have built in Asia across KKR. Eight offices, 125 investment professionals all of whom have relationships with CEOs and CFOs that can help us originate investments.

We will do all of this while always being creative, always being agile, always thinking around the corner, thinking about how markets are going to evolve and then leveraging all of the tools that we have in the KKR toolkit in order to go after those opportunities.

With that, I am going to hand it off to my partner Adam Smith, who is going to dive a little bit deeper on our capital markets business.

KKR Capital Markets

Adam Smith

Head of KKR Capital Markets

Agenda

Good morning. My name is Adam Smith; I joined KKR in 2007 and run our Capital Markets group globally. While many investment firms have capital markets teams that work to arrange financing for their transactions, we are fairly unique in terms of the breadth and scale of what we do and the fact that we have turned this into a full-scale business for the firm. I would like to spend a few minutes this morning providing you with an overview of our Capital Markets platform as a whole, reviewing our financial performance and spending a little time talking about what I think the key drivers of our success have been. We are going to ask Tara Davies, a partner in our London office, who is responsible for our Infrastructure business over there, to join me and share her experiences working with Capital Markets.

KKR Capital Markets Overview

If you think about our Capital Markets business, the first thing you will notice is it is a full-service platform that serves both KKR companies and independent clients. We operate globally with a team of more than 40 professionals who are experts in debt, equity and structured transactions. For me, the most important part is that it is an investor-facing, market-driven business, meaning that our individuals are not only responsible for structuring transactions but being able to place them in the markets themselves. For us, those markets are quite broad. They include not only the public markets, where many of the people in this room reside, but also the private markets, where we are able to place private securities with holders of long-dated assets.

The breadth and the frequency of our interactions in the market is driven by the size of our portfolio and our investment activities. The frequency with which we approach the markets gives us unique insights into current trends and developments. It allows us to innovate and share experiences from one transaction across the other.

Components of our Business

Organizationally, we have divided our business into two key components. The first is equity capital markets, which is involved in raising additional equity capital from co-investors to help facilitate transactions. We do this alongside our partners in CPG. That provides us with an important competitive advantage. We can speak quickly for transactions; we do not need to partner with others; we can retain control of our companies and we can avoid sharing proprietary ideas with competitors. Our equity capital markets team is also involved in the monetization of our investments when we exit them in the public markets, where the focus is going to be on valuation and aftermarket stock performance with the goal of driving a seamless transition of ownership of the companies from our private funds into the markets themselves.

Our debt capital markets team acts as an arranger and a capital provider to both KKR companies and independent clients across a broad range of transactions. As Todd just mentioned, importantly, by using a combined sourcing model, we are able to partner with our credit funds to deliver solutions that other folks are not able to do. We do this globally and we do this at scale. Our debt capital markets team, for instance, has arranged over $0.5 trillion in debt financing since we started that initiative, $100 billion of which was raised last year. Our equity capital markets team syndicated out $27 billion of co-invest since we began that initiative. It has managed over $109 billion of public equity offerings.

Opportunity to Generate Business over the Life of an Investment

When we think about the combined capabilities that this team brings in the context of the lifecycle of a portfolio company or investment, you can see the earnings potential. We can generate revenue by arranging debt financing when we acquire a company, or by syndicating the equity. We can participate in refinancings and repricings, amendments, extensions, modifications and debt capital structures. We can raise incremental capital to fund growth initiatives, or CAPEX, for acquisitions or even dividends. When we are looking to monetize the company, we can act as an underwriter in an IPO or a follow-on offering and we can provide staple financing in the case of a sale.

If you think about that in the context of a large portfolio and an investment complex with significant dry powder, you can really understand the financial returns that you can generate.

Financial Performance

When I first got to the firm we generated $1.3 million in our first year of operations as a capital markets business. Last year we were able to generate $440 million. While there has been a number of drivers of that growth I think one of the most significant has been the introduction of new business lines to our firm and the scaling of those new business lines.

New Business Lines have Helped Drive Growth and Diversification…

You can see, for instance, that whereas private equity generated almost 90% of our revenue in the first five years of our operation, today we have a much more diversified business mix with new business lines, such as our infrastructure activities or our third-party business, generating about half of our results.

Not only has this allowed us to grow our top line. It has given us a much more balanced and stable earnings stream and allowed us to win in many different ways. The same has been true of our geographic expansion.

…And So Has Global Expansion

We have seen steady growth in Asia and Europe provide additional top line revenue. It has given us a much more balanced mix of fees from the global markets themselves.

The Contribution of our Product Lines has Remained Balanced

While this has occurred our composition of earnings across the debt and equity markets has maintained relative stability and a healthy blend. We typically generate about 60% of our earnings from the debt markets and about 40% of our earnings from the equity markets.

The Firm's Investment Activities Provide us with a Strong Foundation

But I do not think you can really talk about our financial performance without touching on 2017 and asking the fundamental question: what was the driver of that significant growth last year? How sustainable is it really?

To me, while it is true that 2017 was a record year in terms of financial performance, I think what it really did was highlight the earnings potential of our platform and the model that we have. It shows you what you can achieve when you have a diversified business where you apply the right organizational structure and management approach and you have scale on your side.

In our case, we have many ways to win. We can generate revenue when we acquire companies. We can generate revenue when we own companies. We can generate revenue when we sell companies. We can do the same things with third parties. We do that globally and we do that across asset classes.

If you look at the scale of KKR, with 119 portfolio companies in private equity alone, $59 billion of dry powder that needs to be invested and a large third-party client base, you will see that there are a lot of places we can draw from. What that gives us is the flexibility in a strong baseline business to start with, and the capacity to achieve 2017-like results whenever there is economic activity. To me that is the lesson of 2017. That is actually what really excites me to be part of this business and part of this firm.

Transforming our Debt Capital Markets Business: 2015–2017

I would like to take one minute to transition to our debt capital markets effort. This is a business that we started to grow in 2015, recognizing what we believed to be a new market opportunity, as different market entrants were joining the financial markets and banks, in some cases, were retrenching.

The first thing we did is we decided we needed to scale our direct distribution to allow us to sole-distribute transactions and multiple transactions at that, into the broadly syndicated markets. We capitalized on what we saw as periods of bank retrenchment and regulatory pressure to gain market share. We essentially doubled down when others were not. In so doing that, we combined our product offering with our credit funds to create a strategic and competitive advantage to approaching clients. We used a high-volume KKR business and control over debt allocations in our portfolio companies to drive a deep dialogue with the markets and ensure that our transactions, when they are executed by us, would perform. We added additional capital from, internal or external sources, to our business in order to become more relevant to our clients.

All these factors combined to allow us to increase our transaction volumes and win more leadership mandates across our roster of clients, which ultimately generated higher levels of fees and more performance.

Growing Contribution From our Third-Party Business

The third-party business that we operate was a clear beneficiary of this. 2017, I think, proved the scalability that we had. That was built off the back of the debt capital markets initiative. In 2017, for instance, we had 25 sponsors across the world mandate KKR to lead their financings. Many of these folks mandated us on multiple occasions and gave us sole lead roles. In fact, what I find most impressive is that in 2017 in the United States we led more financings for other sponsors than we did for KKR. If that is not a validation of our capabilities and the strength of our franchise, I am not sure what is.

Approach Financings From a Differentiated Perspective

When people ask, 'What is the driver of your business in the third party? Why do people want to hire you?' I often point to the AM General case study. I think what drives us is a unique ability to approach financings and capital structures from the perspective of the owners and investors, to come up with solutions and to bring the full resources of our firm to bear in ways that others are not.

AM General is a leading manufacturer of military and commercial vehicles, probably the most famous of which is the Humvee. It is a nuanced credit story, though, given its significant government contracting nature and uncertainty and confusion over what the future will be for the Humvee.

We were initially invited to participate in this transaction as a passive syndicate member in a bank-led unitranche financing. That transaction went to market but failed, ultimately, to gain investor demand. When the bank-led financing failed we approached the company and said, 'Let us have a chance at leading this transaction.' We took over, converted the capital structure into a first lien, second lien structure and involved our credit investment team who looked at the first lien. They developed the thesis around the credit story and decided to go ahead and anchor that transaction. We were then able to take their learnings and their credit story, position the company for success in a marketing roadshow and take them to a place where they were able to get a transaction completed when others had failed.

Connect the Dots Across Transactions

The second reason, I think, that we often succeed is that we are able to connect the dots. By centralizing all of our activities, all of the functions that we have and all of the dialogues we have around capital structures inside a single team, we are therefore able to use our experiences across deals and markets to identify opportunities, create results and drive mandates.

As an example, in 2015 we acquired a company called Mills Fleet Farm. It was a regional retailer that we agreed to buy in the depths of the worst credit dislocation since the financial crisis. We went out to the market and we could not find a bank-led solution to finance the acquisition. Our team placed the capital structure directly in the market itself.

The understanding that we were able to get in the market from those interactions gave us the confidence to shortly thereafter underwrite an acquisition financing for another sponsor who, similarly, could not obtain bank financing. It also gave us the confidence to take one of our portfolio companies on the road and lead a dividend recap transaction when no one thought it could get done.

After we had successfully led the dividend recap transaction we approached all of our other sponsor clients and pitched them dividend recaps. One of those conversations turned from a dividend recap into an opportunity to arrange financing to allow one of the companies to grow through acquisitions. That company happened to be one of the largest franchisees of Pizza Huts and Wendy's. So we gained a tremendous understanding of the market for financing franchisees of restaurants.

We took that market intelligence, that understanding and went on the road. We pitched to two of the largest franchisees of Taco Bells similar refinancings. We successfully won mandates to take them into the broadly syndicated markets and arrange covenant-light financings for them. So if anyone asks you how is it that KKR overnight became a top-five market share in fast food franchisees and number three if you look at deal count, it is somewhere on this page.

Right now I would like to invite Tara Davies, who is a partner in our London office, involved in our Infrastructure business, to share her thoughts on experiences working with our team.

Infrastructure Case Studies

Tara Davies

Head of European Infrastructure, KKR

Profile

Good morning. My name is Tara Davies and I am Head of the European Infrastructure team. Just by way of background, I am a chartered accountant by trade. I started investing in infrastructure at Macquarie Group back in the late 1990s. In 2004 I moved to Europe and then continued to invest in the infrastructure space there. In 2016, I joined KKR. Some of my portfolio responsibilities include two renewable energy businesses. One is a global solar developer; the other is a partnership with Acciona in the onshore wind space. I also sit on the board of a telecommunications company, a towers and cables business in partnership with Telefónica, called Telxius. I also sit on the board of Calvin Capital.

Today I am just going to spend a couple of minutes talking to you about two case studies where the Infrastructure team has worked very closely with the Capital Markets team. The first one is Calvin Capital.

Calvin Capital Case Study

Calvin is a UK gas and electricity meter asset provider. What is interesting about that market in the UK is that the government has mandated that all homes must have a smart meter by 2020, providing a really exceptional growth opportunity. Just to put the UK market into context, that is a 50 million meter market and Calvin is one of the three largest meter asset providers.

The Calvin deal was a big deal. It was £1 billion transaction. We in the Infrastructure Fund had £250 million to invest. But it was a business that we were very well prepared for. We had met with the energy suppliers, we had very strong conviction on the thesis for this business.

We worked very closely with Adam and his team. His team raised competitively sourced debt on attractive terms and also syndicated the rest of the equity to our LPs. But what was even more powerful was we wanted to move quickly. The balance sheet backstopped our bid. We made a pre-emptive offer on this transaction. The balance sheet backstopped it, providing a syndication opportunity to our LPs and we managed to take this transaction out of the competitive process. We signed a sale and purchase agreement before the auction bid date. It was a super powerful point to use the Capital Markets team, coupled with the balance sheet, on this transaction for us.

Calvin is one of 12 investments that we have made in Infrastructure Two, one of our funds. Eight of those 12 investments, we have worked alongside Adam and his team on the equity syndication, providing co-investment opportunity for our LPs. For us, in a very growing franchise within KKR, this is the rule rather than the exception to the rule.

Q-Park Case Study

Our next case study is Q-Park. Q-Park is the number one parking operator in Western Europe. It is very much focused on off-street car parks and purpose-built car parks. It is a market we know very well, having invested in the space before, but what was very exciting about this particular business was that it was owned by a very fragmented shareholder base, and therefore was a very undermanaged business. When we saw this business, we knew there were lots of levers to pull in terms of value creation, from yield management to operational efficiencies to even some M&A opportunities.

For us, as a mere $3 billion infrastructure, this was a €3 billion. It was a huge deal relative to our fund. Typically we will invest about 10% of the equity from the fund per deal. Again, we therefore worked with the Capital Markets team; we raised $1.2 billion of debt and $1.5 billion of equity. That meant, given the size of the equity, we actually went beyond the LPs of the infrastructure fund to KKR's friends and family.

The interesting thing here was that, of the 18 co-investors on this transaction, 11 of the 18 became new LPs when we started to raise Infrastructure Fund III.

As an investing team, working with the Capital Markets team allows us to speak for the whole deal. We do not get bogged down in consortium arrangements and therefore always have control of our funding situation. It allows us to focus on the things that really matter, like due diligence, assessing the risk and developing our investment thesis. It also creates new follow-on opportunities as we develop our relationships with our LPs. They are underwriting the transaction along with us, and so they are understanding how we assess risk and how we underwrite these deals.

In terms of Calvin Capital, the revenue event for the Capital Markets team was $80 million. On the Q-Park transaction, the revenue event was $62 million.

KKR Capital Markets: Conclusions

Adam Smith

Head of KKR Capital Markets, KKR

Conclusions

I think that is a very good segue into our conclusions. The full-service nature of what we do can be a major competitive advantage for our firm and our investment teams. It is also an advantage for our third-party clients that we serve. We, as a firm, have experienced significant growth and diversification in all of our investment strategies. That has translated also into growth and diversification in our Capital Markets business, which as we talked about earlier, achieved very significant earnings of $440 million last year.

What we see today is a very strong baseline business across private equity, infrastructure and our third-party activities in Capital Markets, with a healthy balance of revenue generation across the debt and the equity markets. The transformation of our debt and capital markets platform to allow us to lead transactions and stand alone has been a major accelerator of what we have been accomplishing.

For me, when I look ahead and think about where we are going, I get particularly excited. I see a lot of runway in our debt capital markets and third-party activities. There is certainly room to grow. We also have new business opportunities that we expect to appear, like we saw with the infrastructure team, as the newer strategies that we have in our firm start to reach greater scale and greater maturity.

Finally, we are going to follow the geographic expansion of the firm as it builds out new business initiatives in Asia and elsewhere, or as we build new credit capabilities and raise new types of credit funds in our Credit business. That is what excites me to be part of KKR.

With that, we would like to turn it over to our partner Suzanne Donohoe, who heads our Client & Partner Group and would like to spend some time talking about our fundraising.

Client & Partner Group: Observations from the Marketplace

Suzanne Donohoe

Head of Client & Partner Group, KKR

Introductory Remarks

Good morning everybody. My name is Suzanne Donohoe and I have the pleasure of leading the Client & Partner Group here at KKR. I am a partner in the New York office and I have just begun my tenth year at the firm after spending close to 17 years at Goldman Sachs. It is nice to be back with you; I think there are quite a number of you that may have joined us in

2013. We have a very good next chapter to our story and even more importantly, lots of room to run.

What I thought I would do in our time together is really cover two broad areas. First of all, we are going to focus on some quick industry backdrop points, some of which will echo what you heard from Joe and from Scott this morning, but I think will really feed well into understanding the environment in which we are competing. Then I will turn to some KKR specifics.

We Are in a Vibrant Fundraising Environment

First of all, for those of you that have not been watching, we are operating in an ebullient fundraising environment. Normally I might hesitate to put a slide like this up in front of you. I do not know about you guys but any time I see something where the last bar on the page is surpassing the earliest bars on the chart, it makes me a little bit worried.

But the reality is what has driven this growth in fundraising in the alternative space is both an incredibly supportive macro backdrop but also, importantly, some very durable trends that we are going to talk through here in the next few minutes, which will help you understand why we think this is not a near-term trend but a longer-term trend supporting our industry.

Returns from Private Equity have been Strong

First of all, as we all know because you all serve many of the same clients that we serve, the client organizations, the institutional and high-net-worth pools of capital that are out there have a thirst for return. We are operating in the asset classes that have delivered that return for them most clearly over the last ten years.

What is happening as a result of that is investors are allocating increasing proportions of their asset allocation to the spaces in which we compete. They have to do that, as you know, because the state of the funding gaps that pervade these organizations is startling.

If you look at this number, you can see they are now facing in the aggregate close to $4 trillion of deficits globally. So people are having to get much more creative about their sources of return and thinking about how they arrange their assets in that quest to plug the gap. Old solutions are not working anymore. With 30-year treasury yields around 3% and a liability profile still close to 8%, there is a big problem to fix. So we find the clients that we serve are really looking in all sorts of places for sources of return that they believe can deliver for them for the future.

Sovereign Wealth Funds Continue to Grow

Importantly, not all the pools of capital are facing these trends. Some are newer and just beginning to allocate but operating in that same low-return environment. So if we focus on the sovereign space for a moment, where today, there are $7.5 trillion of investable assets, up almost $1 trillion from just one year earlier. And where over 25% of the pools in this space were just established within the last decade. This is a very large and growing pool of capital that in many cases is just beginning to allocate to alternatives.

Meaningful Opportunities for Growth

As you can see if you focus on the bottom part of the chart, you have several very established institutional pools of capital, names that are familiar to you all. You can see what they have done over time to take advantage of the illiquidity premium and the attractive returns offered in the space in which we compete.

Now focus on the top part of the chart and look at some of these pools of capital that in many cases are multiples bigger, where they are really just beginning this journey. This is one good example of a positive tailwind that we are benefiting from.

Overall High-Net-Worth Market is Large and Growing

A second is the high-net-worth market. Todd Builione mentioned a few minutes ago the focus on retail, but if I broaden the landscape for a minute and talk about it as the individual investor market, what we see here is a huge and growing pool of capital. In many cases, particularly in the high-net-worth space, there is a predisposition to think about locking up capital to take advantage of long-term returns to really, again, access that illiquidity premium.

When I look at this pool of capital, at $60 trillion growing faster than pension pools around the world, this is a very exciting space and one where we are really just scratching the surface.

Insurance Companies' Allocations to Alternatives are Scaling

Insurance companies as well are finding that increasing their exposure to alternatives is really one of the most important things they can be doing to plug their own funding gaps. which look not dissimilar, in some cases, from what we see in the pension space.

Today the global insurance market is something like $27 trillion. We surveyed a group of these insurers, particularly those that have been more forward-thinking, just recently, in a paper that we did together with our Insurance Group and our global Macro & Asset Allocation team. What we found is that they are moving apace. They are recognizing the return opportunities available in the alternatives space and readjusting their balance sheets in order to take advantage of this.

Alternative Asset Management Industry Continues to Grow

What does all of this add up to? Joe talked about it this morning. Today we are competing in a $10 trillion alternatives market that is set to double by 2025, growing historically at a rate over 12% compound annual growth rate.

When I step back and think about the competitive landscape and think about the many different industries in which we invest, very few of them have growth rates that look like this. This is really the landscape in which we are operating.

The Largest, Global Firms are Best Positioned

Importantly, it is also a highly fragmented market. This is also a point that we touched on this morning. This is just one small illustration of it. What we see is that even the big are not that big, at market shares of, call it, 2–6%, depending on which number you want to focus on, on this page, and then they are gaining share from others around them.

As I step back and think about that $10 trillion alternatives market and I think about us at $190 billion in capital and still one of the larger providers in our space, we have a ton of room to run.

Client & Partner Group: Our Client Effort

Client & Partner Group Today

Now I thought I would pivot to a bit more of a conversation about we have been doing at KKR. I will really try to touch quickly on four key areas: our team; our performance in generating growth in assets under management; the build-out of our franchise, probably most importantly and then, finally, what are a handful of the areas we are focusing on.

First of all, on our team we have about 80 people who wake up every day at KKR thinking about clients, thinking about how we raise capital, how do we ensure we are listening to our partners, understanding what they need, what we can do for them and how we can help them to access all the intellectual capital of KKR and to deliver return for them in the process.

That team is increasingly experienced and tenured at KKR. As you can see we have about half a dozen years of experience, on average, at the firm and somewhere between 15–20 years of experience at the senior levels of the team in the industry.

AUM Growth Across Asset Classes

Why does this matter? I think it matters because it is becoming a very important accelerant of growth for us. We just talked about the industry growing at 12% a year. We have been growing at almost 20% a year over similar time periods and importantly doing it across the board. So not just been gathering private equity capital where the firm clearly has our longest track records, but really helping to seed so many of those new businesses that we have touched on previously, and in the process diversifying the toolkit that we are able to offer to clients and really solidifying the depth of relationships that we have.

Gross New Capital Raised

What does that look like on a gross capital raised basis? Because what you just saw included the effect not only the new capital we brought in but also the impact of all those monetizations that have been going on over the past few years in very healthy capital markets.

This is the gross capital raised over the last several years. You will note that if you look over the last 3–4 years, we have raised about $100 billion over the last four years, or in excess of that and really look forward to continuing that pattern.

Investor Base Growth Across Platforms

How are we doing that? I think it is exciting to pivot from a conversation about asset growth to one about franchise growth. This really may be the page that I am most proud of as the leader of this team. When we look here what we are really doing is laying the foundation to support all the growth that we have been talking about all morning.

As I compare progress from 2011, we have grown the number of Private Equity investors more than double in just a short period of time. In Credit, we have grown the number of investors over nine times; in Real Assets somewhere between five and six times; and in growth equity we are really just getting started. So it is exciting to step back and think about when we go back with fund IIs and fund IIIs and fund IVs, that we start with a much more broadened investor base and really a variety of different organizations that know us from different vantage points.

One Team, One Dream

Another way that you can see the franchise impact of what we have been building is to take you back to Capital Markets for a moment. Adam did a great job of talking through the growth in the Capital Markets franchise. We are a very proud partner of the Capital Markets business in helping to drive that acceleration of growth.

You can see the CPG contribution to the equity syndications that have been done over the past few years. Importantly, as you evaluate the question of is 2017 a repeatable number, the reality is it is much more repeatable today because the breadth of the client franchise has extended by so much.

We are Reaching More Investors

So Tara's illustration, I did not even know this stat until she delivered it, but 11 of 18 of the co-investors in Q-Park coming into Infrastructure Three that had not been investors previously. That is a great illustration of the power of our model. So finding ways to both use the model to enhance the profitability for the firm, but more importantly to enhance the relationship with a client and in the process cement what they are doing with us, do more with them and make it a durable and lasting relationship.

Maybe stepping back, what does this mean when we look across? Obviously the page we were looking at a few minutes ago showed some examples of clients that invest with us in multiple franchises. Today, even by very conservative measures, we have over 900 clients of KKR and we have on average two mandates per client. These are both metrics that we track religiously, that we incentivize our team to focus on and that we plan to continue to develop over time.

I say these are conservative measures. It may help you to understand them a little bit more as you compare us to our peer set. First of all, the 920 gives no credit for any of the relationships that sit in any of our hedge fund stakes partnerships. So no Marshall Wace clients, no PAAMCO Prisma clients, no Nephila clients, no BlackGold clients are really being counted in this number unless they are also clients of KKR.

Secondly, in terms of the cross-sell count or the number of mandates per client, we only give ourselves credit for a cross-sell if a mandate is sold into a completely new platform of the firm. In other words, no counting re-ups in the math here. Even on the basis of this conservative approach, we have seen very significant improvement in the efficiency of what we are doing and as I said, in growing the depth of our franchise.

Client & Partner Group: Current Areas of Focus for CPG

Extend the Duration and Scale of our Capital Base

What I thought I would do in the last couple of minutes is just share with you three or four of the areas where we are spending a lot of time and a lot of focus right now. The first, again, will be a recurring theme from this morning; I guess we like to repeat ourselves a little bit. We are highly focused on extending the duration and the scale of the capital that we raise. We talked in earlier discussions today about permanent capital, but maybe just to spend another minute on the strategic investor partnerships with recycling that Scott alluded to this morning.

These are very, very long-duration, multi-asset-class partnerships where a client will award us a very significant mandate to begin. The typical size has been around $3 billion at a clip. And where we have an extended duration to manage those assets, we have a lot of discretion in how those assets are deployed, with a lot of input, of course, from the client. Then we have, typically, recycling rights of all of the capital and a very good portion of the profits.

The net impact of these types of partnerships is that, if they begin at $3 billion, they are typically 2.5–3 times that size by the time we reach the conclusion of the investment period of these mandates. Then we will end up with another, call it, 5–10 year harvesting period.

These are very significant mandates where is a great deal of customization with the client and I would say a great depth to the relationship, and certainly wonderful examples of an area where we are increasingly differentiating ourselves in the market.

Continue to Add New Clients and Cross-Sell

A second focus is, to me, a little bit like motherhood and apple pie. We plan to continue to grow the franchise, adding dozens and dozens of new clients a year. We have typically been adding about 100 a year, and to continue to cross-sell.

You can see this is another way to view the progress that has been made on these measures over the last several years. Importantly, though, you can also see how many of our clients are now entrusting us with multiple mandates. It is over a third of the total client count, which I think is impressive when you think about how many of these relationships are actually still quite new to us. If we are layering 100 or so a year on, we have probably 300 clients in this count that have really only joined the party in the last couple of years.

Importantly, as these mandates expand what we hope to do is achieve an even greater proportion of clients at the so-called platinum level, which we would identify as those who have given more than $500 million in capital to manage. Those clients typically have about 4.5 mandates with us, if you will, per client.

Drive Insurance Penetration

We plan to continue to drive those two franchise builders. We also will keep focusing on the insurance space. Today we have a dedicated team in this space that is small but very focused on differentiating ourselves through research, through building custom products that really address the specific needs of the insurance market, and we feel like that hard work is paying off. We are showing a 35% growth rate in this segment and today enjoy relationships with about 90 different insurers across a wider range of asset classes.

Keep Growing Individual Investor Business

And finally, we want to keep focusing on the individual investor market. When I think about that $60 trillion of AUM that I showed you just a few minutes ago and think about our share, at $27 billion, we have plenty of room to run and it is a space where our brand tends to resonate incredibly well. Where people are interested in how do they access the intellectual capital of KKR, and where we are really just getting started.

Where Does CPG Go From Here?

Medium-term objectives

So, what does all of this mean for CPG? I think it means we are up and to the right. Is that to the right, sort of to the right? When I look at our medium-term objectives that are here on this page that we have had out there for a little while, I am highly confident that we can achieve or surpass these objectives in the requisite time that we have laid out, and I am really excited about the chapters to come.

Active components

And really it is very basic from where I sit. I look at all the different components that we have working for us. Between the seasoning of our team, their tenure at the firm, the fact that we have been able to broaden the investor base as much as we have, deliver on the cross-selling promise, where I think we are really only in very early innings. We are benefitting from the fabulous performance that my partners are putting up across the board; really across pretty much every investment area at KKR, we have strong performance to sell. And then we have these macro tail winds, whether in sovereigns, in insurance, in high net worth, and I look at all of that and say, this is a great story yet to tell.

So I would like to thank you all for your time and I am going to hand it over to my partner, Bill Janetschek.

Financial Overview

William Janetschek

Chief Financial Officer, KKR

Introduction

Good morning, everyone. I am Bill Janetschek. I have been with the firm indirectly and directly for 33 years. I started my career at Deloitte and I was at Deloitte in the Tax Department for 13 years and 12 of those 13 years my only client was KKR. So one could argue that I was actually interviewing for a job at KKR for 12 years.

It finally took me 12 years, but 12 years later I actually got offered a position as a Tax Director at KKR, so I left Deloitte as a Tax Partner and came on to KKR, and was there about a year and then Henry and George asked me to be the CFO and that was in 1998, and so that is 20 years ago.

What I want to do today is cover three topics. Number one, I want to walk through briefly our business model. What I want to try to do is wrap everything up over what you have heard all morning and to reference some numbers.

Number two, I want to give you a little color around our C-Corp conversion; and lastly, I want to give you a little visibility into some numbers around our second quarter performance.

Business Model Review

Simple financial model

So when you think about our model it really is quite simple. We have three forms of revenue and two forms of expenses. We receive management, monitoring and transaction fees, and receive realized performance income and so that could be either carry or incentive fees from the third-party capital that we manage. And secondarily, we have realized investment income, and that is income off our balance sheet. And so that is investing side-by-side with the third-party capital that we manage. So again, pretty simple, only three revenue streams.

Operating expenses, categorized into really two major buckets. Our compensation, which includes equity-based compensation and occupancy and other operating expenses. When you think about our reporting historically and where we think we are going to be reporting prospectively, that compensation number, again, including equity-based comp has been roughly in the low 40%.

When you take a look at occupancy and other operating expenses that has varied anywhere in between 8–10%. So adding those two numbers together, on a pre-tax basis our margins have been roughly 50%.

We are going to be reporting not on ENI prospectively but on after-tax distributable earnings and that will be our new P&L metric prospectively.

Revenue Streams

Fee revenue

So let us briefly go through the revenue streams. Number one is our fee revenue. That is made up of really management fees and transaction fees. Management fees, fortunately a good majority of them come from long-dated locked up capital that we get to manage over a very long period of time. Approximately 80% of the capital that we manage is of that nature.

And you can see that to the extent that we are making investments both for the capital that we are investing for the third-party capital that we manage, as well as transaction activity for our capital markets business, that is going to drive the increased revenue.

The one thing that I want to point out is that we have got $59 billion of dry powder; so that is capital that is already contractual, but we have yet to actually invest. $25 billion of that capital is what we call shadow fee paying AUM; meaning we have that capital but we just have not invested that capital. That $25 billion is being invested at a run rate of roughly 100 basis points. So, assuming we do not raise any additional capital from here on forward, which is not going to be the case, we already have got $250 million of run rate revenue built into this system that actually has not come through our management fees.

One last point, and this is for our new investors, I just want to make sure that you understand that the majority of the management fees that we receive are based upon either committed or invested capital. So to the extent that there is mark to market in any particular quarter, that does not impact the management fees that we calculate. Quite honestly going into the beginning of the year I can probably project with 95% accuracy what the management fee is going to be at the end of the year.

Infrastructure

I want to spend a little time around infrastructure. When we actually raised our first infrastructure fund we actually gave away below market terms only for the fact it was a first-time fund and it was hard to raise that capital. So you could see that the first fund was $1 billion and the blended management fee and carry rate was 1%/10%.

Successful fund number one allowed us to raise $3 billion for fund two, but we still did not really see the solid performance as we were raising Infra II and so those terms were quite similar. But now, as we were raising capital for Infra 3 we had top quartile performance for Infra I and Infra 2, it was a lot easier to raise the capital and you could see that the blended management fee went from 1–1.2%, so a 20% increase. And, more importantly, the carry went from 10–16%.

We will be closing on roughly a $7 billion fund in Infrastructure III and that will take place in the back half of 2018. Now when that does happen you can see that Infra II, of the $3 billion, $2.9 billion is from third party capital at 100 basis points, that is $29 million. It is an infancy fund and so we have not sold any of those assets, infrastructure, those assets we hold for, you know, quite a long period of time. And so, when we go from the investment period to the post investment period, the rate is still at 1% so no change in fee. So 29 still is 29.

However, now we are layering on an additional $7 billion of capital at 120 basis points and you will actually see the management fees, in just the management fees from infrastructure go up by $80 million. And so, based upon the targeted final close, we will certainly see at least $20 million come through our P&L in the fourth quarter of 2018.

Impact of FS partnership

Todd briefly talked about Franklin Square. I just want to help everyone model some numbers. Even though the transaction did not close until April 9th, we signed the deal in the fourth quarter, we were actually a sub-advisor to Franklin Square in the first quarter of 2018 and received roughly $7 million of management fees. Transaction closed April 9th and when you run through the numbers for the second quarter we are adding an incremental $6 million of additional management fees from that JV.

Taking into account the management fees and the incentive fees that we could earn from having that JV with Franklin Square, Todd mentioned earlier we expect that to be at a run rate of roughly $100 million annually. And again, that is management fees and incentive fees.

Realized performance income

Realized performance income, there is going to be two things that are going to drive this number. Number one, and we talked about this all morning, as Fund I turns to Fund II turns to Fund III and we scale these businesses, we are certainly going to be managing a lot more third-party capital, and what drives performance income is clearly based upon investment performance. So to the extent that our investment performance is strong, we are entitled to a certain percentage of the profit that we manage for our third-party capital. And you can see that number go up.

Bottom left, this shows the performance fee eligible fee paying AUM from ’13 on an LTM basis growing to $98 billion. And, more importantly, you could see, this is realized performance income that we have received, grow from where it was in 2013 of roughly $750 million to right now at approximately $1.3 billion.

Now, keep in mind we are investing, we are growing those investments and we are harvesting and so the number to the left is what we are actually monetizing. While we are doing that we are also having the ability to invest new capital and on a mark-to-market basis grow the net accrued carry. And that number has grown pretty significantly over the last few years.

Realized gross performance income and dry powder growth

This is a very interesting slide and it brings back fond memories of having conversations with Henry once we went public, and he would call me and say, I do not understand the stock price. You take sum of the parts, you look at the balance sheet, you look at the fee related earnings, it looks like our carry is trading at zero, am I doing the Math right? And I would say yes, yes, we are doing the math right, Henry.

I do not know why, but what I have heard from our investors is that the carry that we have realized is episodic, meaning that it does not happen on a regular basis and so we are not getting the full credit that we should deserve. And Henry's point to me was always, well go and tell them that the value proposition at KKR really is not about the management fee, it is about the carry.

And I would say, Henry, Craig and I and Scott will try. And try as we did over the last eight years, but this is an interesting slide because if you take a look at, and this is on an LTM basis, first quarter of '18 it is $1.3 billion off of going back to when we first went public at $346 million. So the realized performance income has gone up by 4x. The dry powder that we are able to invest to create carry later on has gone up by 4x and along the way the monetization of the carry has gone up by 3x.

And if you take a look at this chart it looks like a pretty steady stream of revenue and up and to the right, and so, and Henry knows this number so I do not want to put him on the spot again but we have been public now for 35 quarters. We have reported carry in 34 of those 35 quarters and so you might say carry is episodic, but if it happens 35 out of 36 quarters I would actually challenge that.

Significant opportunity key for realized carried interest

As we are talking about carried interest, when you bifurcate where the carry is, this is a very interesting slide. This shows the $120 billion of AUM that we have in which we are entitled to realize carry. 25% of the AUM is driving and has driven 91% of the realized carry, and that is really from the three flagship funds that we have in private equity. It is the '06 Fund in NAXI for North America, Europe III and Asia II.

Interestingly, if you go down one box below we have got roughly $30 billion of AUM in funds that are above cost and have the ability to pay carry, but they are immature investments, meaning we have only held those assets anywhere between three and four years. And so, when you look out over the next few years you can see that that number is equal to the size of where right now most of the realized carry is being generated. And as we roll the clock forward, we have significant upside on realized carry from that category of funds.

The third box is those mandates where we are in the seasoning or working through our preferred returns. So these are very early stage funds and so we just started funding capital work in Asia III, we just started putting to work capital in Americas XII, and so the funds do not actually have any real performance to speak of. And as those continue to grow roughly $60 billion so 60/120, so 50% of the AUM that we are managing that have realized carry are really immature assets, which have the potential to grow significantly over time.

Balance sheet

Balance sheet, very quickly, to state the obvious, we capture 100% of the earnings off the balance sheet, there is no fee sharing. And what is going to drive the balance sheet results are performance. And so, to the extent that we continue to do a good job and grow our platforms and produce great returns, this will come through in our balance sheet.

And as you know, and Scott mentioned this earlier, from the capital allocation policy, in the fourth quarter of 2015 we changed our model where, instead of paying out the majority of our free cash flow, we established a fixed distribution and took the excess and used it in two ways.

One was to either use some of that capital to buy back shares, or number two was to take the excess, put it back on our balance sheet, invest side by side with our third-party investors and continue to compound that book value. And you can see the realized investment income over the last few years has been pretty solid.

Expenses

Spend a couple of minutes on expenses, compensation expense; you can see that when you take into account all of the three forms of revenue, so that is fee income and carry and balance sheet earnings and you take into account the compensation that we pay. I mentioned that we are targeting in the low 40s and you can see that in 2017 on an LTM basis that number is roughly about 40%.

Occupancy and others

Occupancy and others, we mentioned this earlier. What we did was, as we were growing these platforms we spent money to build the infrastructure, knowing full well that the revenue would show up later. And so, you could see that when we started a lot of these platforms in 2010 through 2012, we spent a good amount building up the infrastructure. And so, when you see the occupancy and other expenses, it is growing at an annual compounded rate of roughly 3%.

However, from 2013 through 2018, and this is just management fees, so it is not any of the other earnings of the firm, that has actually grown at 11%, so far greater than the expense that we had just to establish all these platforms. And on an annual run rate I would imagine that this number is going to blend anywhere in between that 8 – 9% venue annually.

C-Corp Impact and Business Update

C-Corp conversion – financial implications

Let us spend a couple of minutes on C-Corp. From a capital allocation policy what we decided to do, we are going to pay more in taxes and so we have established a dividend of 50 cents annually that we are going to be paying to our unit holders. No more PTPs, everyone is going to be an owner in a C-Corp, and so the dividend that is received by our individual investors is going to be a qualified dividend and they are only going to have to pay tax on the dividend that they received. We also announced that we were going to increase our share buyback to an authorized number of $500 million.

Taxes

Spend a minute or two on taxes. The transaction itself was tax-free. So our unit holders had a PTP unit, on July 1st that converted into a C-Corp unit and that was a tax-free transaction for our unit holders. However, because of the conversion from us being a partnership to a C-Corp, we actually received a $2 billion benefit, meaning we have the ability to step up the assets that we have in our enterprise by roughly $2 billion.

Roughly speaking, 50% is going to be allocated to goodwill and that is going to be amortized over a 15-year period. The other billion dollars is going to be allocated to the accrued carry that we have on our balance sheet as of June 30th, and to the balance sheet assets that we have. So we are stepping those assets up as we are monetizing those investments. The tax leakage is not going to be that severe, certainly over the next few years. So the way to think about it is we were a PTP on June 29th and when you look historically over the last seven or eight years, our effective tax rate was roughly 7%. It will be 7% starting on June 30th because again as we are monetizing some of that accrued carry, and we are selling those balance sheet assets, there is not going to be any tax leakage.

And the way to think about it is, our tax rate will go from 7% to roughly 20% over the next five years. We will receive some of the benefit from that goodwill, which will be amortized over a 15-year period. But over a longer period of time our run rate tax percentage is going to be that 22%.

One other housekeeping item around taxes: when we talked on the first quarter earnings call, we had several positions on our balance sheet that were marked down to next to nil. A lot of these were assets that we had in either energy or credit. On a mark-to-market basis those losses already ran through our P&L when we reported ENI. On a mark-to-market basis, which is how we value our book value, it was already embedded in our book value, and most importantly, to the extent that we monetize any of these assets is really going to be no impact on cash flow.

The subtlety here is that, as a PTP, our income flowed up to our unit holders. When you think about our unit holder base, if you are an individual in high estate tax, your tax rate would be 37%. Once we go C-Corp if we actually monetized those assets the corporation was going to receive only a 22% benefit. And so, we thought it was prudent to take a look at all those assets that had actually gone down and got a value, that we did not think had any real true opportunity for any recovery and decided to sell those assets to give that benefit to our unit holders pre C-Corp conversion and receive that 37% benefit.

From April to June and in April we actually had targeted that that number would be roughly $650 million, we went through asset by asset and took a look at every single asset and, happy to say that we did a little more work and monetized some of those assets that were written down and embedded in book value. And I want to make sure everyone understands that, and that number has actually grown from $650 to $725 million.

Simplified reporting

Simplified reporting. No more ENI. So when we reported in our first quarter we actually had two P&Ls. We had an ENI P&L and then we had a total distributable earnings, which is the real cash earnings, which is really how we run the business. So we are stepping away and not actually going to report ENI prospectively.

That being said, we are still going through our valuation process every single quarter and we will mark to market our carry as well as our balance sheet and embed those marks in our book value, so we will report true intrinsic book value every single quarter. But again, the metric that we are going to report on is after-tax distributable earnings. The one subtlety is that we are going to embed stock-based compensation in that calculation. Stock-based comp was in ENI. When we removed ENI, we thought it was prudent to actually burden our cash earnings by that stock-based comp.

We are going to simplify our story around fee related earnings and we will go through that momentarily. The one good thing for our new investors is that prospectively they are only going to see one compensation line. For old investors we were good about giving out granularity and so, believe it or not, we actually reported fee income and cash comp against that fee income. We reported performance income and performance expense against that earnings and then we had our balance sheet and we had stock-based comp.

And so, we are probably one of the only industries, and I am talking about the alternative asset managers, that actually report three compensation loads in their P&L. And so, we are going to combine those all into one and, as I mentioned earlier, that number is going to be targeted to roughly 40%.

One small item as it relates to interest expense; prior to the conversion we were re-looking at how we report, we actually showed interest expense as a reduction of our balance sheet earnings, so above the line in a revenue column we had realized and unrealized income, as well as interest and dividends minus interest expense. We are actually going to take that interest expense and move it down and just report it where we have the other expenses of the firm, mainly compensation, occupancy and G&A.

And one last thing, and you can see this in the appendix in the deck in front of you, is that we are giving you actually greater transparency around carry and incentive fee eligible AUM. What we had done historically in order to guide you as to the carry opportunity, we had one page in our press release that laid out all of the funds, all of the dry powder, the remaining costs and the remaining value. That number totaled when you added it all up, roughly $120 billion. We, at the time, as of March 31st, had AUM of $176 and we never actually built a bridge between that $120 reported and the $176.

When you peel the onion back, embedded in that $176 is roughly about $35 billion of capital that we are managing, we are entitled to an incentive fee. And we thought that was important to show both our old investors and our new investors. So $120 of the AUM we have is carry eligible, roughly $35–36 is incentive and the remainder is capital that we manage where we are just receiving a management fee and no performance income.

But when you add the carry and the incentive fee, that number totals roughly about 90% of the AUM that we have, we were receiving some sort of promote on. So we thought that was important new information.

Simplified reporting – four key metrics

We are going to keep it simple, so simplified reporting, we talked about this last quarter and we are going to talk about this every single quarter. It is important as far as the assets that we manage and obviously the assets that we manage are going to drive those management fees and so those are the first two metrics that we are going to report on.

Book value per adjusted share, again, this book value is burdened with the mark to market, and so this will be every single quarter on a mark-to-market basis what the true book value is of our balance sheet.

And lastly, no more ENI; after-tax distributable earnings burdened with that stock-based comp that I mentioned earlier.

Segment focus – fee related earnings

Real quickly I am going to go through this, but there is a numeric example in the appendix and so it is probably best for you to actually take a look at that to work through the numbers. But quite simply what we are doing is trying to keep fee related earnings simple. We have three revenue streams, that is a total. There are certain expenses that we are going to burden those revenue amounts by, one of which would be excluding non-interest operating expenses, to come up with a total margin.

That margin is going to be applied to our fee income and that is going to produce our fee related earnings. Again, if you want to take a look at an example you can look at it in your leisure, we have included that in the Appendix and so you can use that as a reference when you are modeling out what the second quarter fee related earnings number is going to be.

Q2 '18 Realized Carried Interest and Investment Income Update

As it relates to 2018 second quarter results, what we have historically done is certainly on the quarterly call we would give you a little indication as to what we knew as of that moment in time, and we said that in order to help you model your numbers on a quarterly basis, we were going to try to be more transparent and talk about the realizations that we have had in our fund, which would produce realized carry, or monetizations off our balance sheet, which would obviously produce realized investment income.

So right now as we have run through the numbers for the second quarter, the gross realized carry interest, so that is not burdened by any sort of compensation, this is the gross number, we are going to report roughly $350 million of gross realized carry. And when we look at our balance sheet, this is not burdened by any interest expense, again this is a gross number, the realized investment income off our balance sheet from a lot of secondaries and strategic sales as well as interest income and dividend income, interest income coming from our CLOs, is about $150 million, so $500 million in total.

Q1'18 after-tax distributable earnings

And before I go, just one housekeeping item. We reported after-tax distributable earnings, excluding equity-based comp, in our first quarter results. That number was 37 cents. We have gone back and we have actually put on our website and filed an 8-K on Friday and recast all our numbers to the new reporting and we have recast first quarter of '18, all of '17 and all of '16.

So I just want to make sure that you are mindful of the fact that when we report the first quarter numbers again it is going to be burdened by equity based comp and so it is not 37, it is 29, and obviously you are going to have to do the same thing in order to reflect what the second quarter TDE number is going to be, again with that stock based comp.

And so with that I look forward over the next several weeks and several months to sitting down with Craig and meeting with a lot of you as we try to get everyone to understand the KKR story, and with that I will pass it over to Craig Larson.

Frequently Asked Questions

Craig Larson

Head of Investor Relations, KKR

Introduction

Thanks, Bill. So before Henry has some closing remarks, I thought it would make sense for me to review four frequently asked questions that, from an investor relations standpoint, we hear from investors. I am going to spend a little more time on some of the things that we thought about in terms of our decision to convert to a C-Corp, how we think our shares should be valued, what the impacts of a rising rate environment is on us in a particular focus on our private equity business. And then finally what happens to KKR in a market downturn. We have some interesting case studies, again, how the business has performed when we have seen some volatility.

C-Corp Conversion – Shareholder Expansion

So first, a little more granularity on our decision in the conversion, and the decision itself is actually one that was pretty simple, and it is stated here in the first bullet point. In that we think over the long term the opportunity for us to create equity value through shareholder expansion and ultimately multiple expansion is greater than the taxes that we are going to pay as a corporation. And I think the alignment around this decision is something that should be pretty well understood by everybody in the room given the significant employee ownership that we have.

Now to be clear, this was not a decision that we made thinking that we would see a one-time pop in our stock price. And I actually think that it is going to take a period of several quarters before we are going to really see the transition in our shareholder base. This decision was one that was really made with a focus on the long term and what we think really positions the company for a success over a long time frame.

Historically, what did the investor relations team hear?

Now, how did we think about this decision? Because in many ways the only thing you know with certainty in a conversion is that you are going to pay more taxes. So the first thing we did, we actually spoke with a lot of people in this room. And so I am going to review a couple of the comments that we heard actually from three people, all of whom are actually in this room. This exercise is actually somewhat cathartic for Bill and me, as an aside, and Scott. But historically what did we hear as people talked about the valuation profile of the alternatives?

I would say that 40 – 50% of the investors will not engage on the alts. It is tough to say this is entirely due to structure and K-1s, but I will bring out my comp sheet and begin talking about how attractive valuations are and they will stop me outright and say they are not interested in the alts and we will move on. This happens all the time.

If you do not convert, what you are betting on is there are enough niche and momentum-oriented hedge funds out there that no one has ever heard of that will drive your equity value because it is not going to come from US mutual fund complexes. And we have a couple of statistics on this point in a second.

And finally, I just do not think it will realize fair value relative to your fundamentals without becoming a mainstream equity security. So these comments again are pretty representative of the feedback that we heard. And first, thank you everybody for your candor as we talked about this as it really did have an impact on us in a number of different ways.

Ownership profile as PTP

So, after hearing this anecdotal feedback we began to peel the onion back and again looked at some of the more fundamental statistics to look at our ownership profile and look at that relative to a broad group of financials. So here you see the ownership that you have in KKR over time and the level of mutual fund we have, ownership that we have, relative to a broad group of financials. And you see that pretty consistently that number has been at a big discount.

At the same point in time you actually have significant over-ownership from the hedge fund community. And while I love the enthusiasm of the hedge fund community, there is an aspect of this that does come with some risk. In my experience a number of folks in that category can have a shorter investment horizon, and when volatility enters the market they all can go risk off, all go risk off together and there is not a natural buyer on the other side of that trade.

So I think when you look at the volatility historically in our units, and I think it is also true as it relates to our peer group, this is something that has contributed to the volatility you see in our share price.

Again, I think as people broadly understand, as a publicly traded partnership we have been irrelevant essentially to the suite of passive strategies. And this, again, was another statistic that we looked at and found concerning. In that if you looked at the mutual fund ownership that we did have, how many fund complexes did you have to look at in order to get half of that ownership profile? Well, the answer is you could count them on one hand.

So we looked at this composition of our shareholder base, and it actually felt pretty fragile to us in all candor, and we feel very differently about where we are now and the opportunity we have to really expand our shareholder base. So how do we think about that opportunity? Well, we think of it in three buckets. The first really are our existing shareholders. Again, one of the things that we heard very consistently was that as a PTP we actually were relevant to only a fraction of the institutional AUM within those respective complexes. One of the comments that we heard that had a pretty big impact on us came from a top-20 shareholder and the feedback that we heard was that as a PTP we were only relevant to 10% of the AUM within that mutual fund complex. That changed as of a week ago.

We think we have a lot of white space as we think about new prospective investors. If you look at the largest twenty mutual fund complexes in the US, only three of those own one million shares of Blackstone together with KKR. Again, we just think there is a lot of white space.

And then finally as it relates to passive strategies, ETFs, indices, smart beta, of course these strategies represent a pretty significant part of the equity markets already, and again that is a growing percentage.

Distributable earnings versus ENI

And one other point as it relates to the decision to focus on distributable earnings versus ENI, again as you have heard a couple of times, perhaps most importantly DE really is more reflective of how we run the firm. But at the same point in time I think there is another subtle advantage that will be very helpful for us in the long term, because I think it is going to allow there to be a greater focus on our business and where we could be in three to five years on a DE framework as opposed to an ENI framework.

If somebody is trying to think through an earnings path for us and where we could be in that three- to five-year period, if someone is focused on ENI in many ways they are going to be making a market call and however with a distributable earnings focus I think it is much easier to understand and embrace an earnings growth path for us, focused on DE, reflecting a lot of what you have heard today from a management fee standpoint as well as a realized carry standpoint.

Valuation Framework

So on to the second topic and how we think our shares should be valued, again a very frequently asked question.

Well, we are advocates of the sum of the parts-based approach and I think one of the key reasons for that actually relates to our balance sheet. Not only the size and the significance of our balance sheet, but perhaps as importantly it really relates to the nature of the underlying investments.

So our private equity investments we are likely going to hold for four to five years and our core equity investments we are likely going to hold for even a longer period of time. So we think that mark to book value on a quarterly basis, as Bill said, is a much more relevant statistic in thinking of the value of our balance sheet in that book value, instead of looking at the balance sheet on a multiple of earnings. So let us talk about each of these three pieces individually.

Fee related earnings

First, on fee related earnings, we do agree that FRE should be valued on an after-tax basis but at a multiple that reflects the growth and margin profile as it relates to the nature of the underlying earnings.

You have heard a lot already about we have long term committed AUM that leads to recurring and predictable management fees. You have, in the course of our firm, increasing diversification of investors, of funds, of strategies, of geographies with a lot of identifiable growth avenues. And again, importantly we think that we are going to eliminate the PTP discount that you have seen in us recognizing the change in our structure.

So you see in the lower left-hand part of our page our FRE trajectory 2016/17/18, these are the last 12 months ended March 31st. From '16 to '17, you see a low double-digit growth in our FRE that was with an 8% growth in management fees. And from '17 to '18 you see a 21% growth in our FRE with a 17% increase in our management fees.

So we do believe that FRE deserves a valuation that is at a premium to the S&P 500 and if you look broadly across financials, and certainly there are a number of examples of financials given the nature of their earnings, with a high recurring piece, again with upside and growth opportunities, where you have those P/E multiples that are premium to the S&P.

And in addition to that you have two C-Corps with companies that are focused on the alternative opportunity if you will in terms of Partners Group and Hamilton Lane, and both of those companies actually trade at a pretty tight band as it relates to a multiple of 2019 earnings.

So we think, again, that multiple-based approach is something that makes sense, but it should be at a multiple that is reflective of the quality of those underlying earnings.

So the second piece gets back to the balance sheet, again at a very high level. We think that that marked book value is going to be a critical piece of this framework. Now, again, as a lot of people who have looked at us know, you will see that sum of the parts framework, and I would say traditionally you will see a discount placed on our balance sheet for conservatism.

I do think that we are in a very different position today relative to when we first became a public company and I think that argument for conservatism made a lot more intuitive sense to me again when we first became public in 2010. At that point in time private equity was really a pretty new asset class through the broad public markets and we had a pretty chunky holding when you look at the balance sheet position. We had almost 50% of our investments in top five names.

Again, we feel very differently about how the balance sheet is positioned today. You have seen a significant change and diversification of the balance sheet, both in terms of the asset allocation as well as the significance of those top five holdings. And a lot of those underlying attributes of the balance sheet itself again are very attractive. So there is no management fee burden as it relates to the balance sheet investment portfolio.

And when you look at those underlying investments and think about it, it is actually interesting because a lot of our partners are paying us a fee, or a fee and a carry, in order to have the opportunity to invest alongside us across the vast majority of those underlying strategies.

And the balance sheet itself is one that is quite liquid. As of March, we had over $2.5 billion in cash. Now I do think that we intuitively are likely to always think of the balance sheet as much more of a strategic asset, but at least as we think about that valuation it does not seem to be too much of a stretch to us to think that, from a book based value standpoint we should be at least one times book, at least one times book placed on the value of the balance sheet.

Realized performance income

And then finally let us talk about carry, one of the points that Bill talked about. First, I do think and agree that when you look at our realized performance income it has been more consistent than one might think. This earning stream for us, again it is tough to really understand and predict realized carry on any forward 90-day basis. But if you look at our realized carry on a rolling 12-month basis, you see again a chart that shows nice growth.

Of course you see that again if you look at it over a rolling 24-month basis. And I do think importantly the peak to trough statistics again might be lower than one might expect in terms of the nature of this underlying earnings stream for us.

So how do we think it should be valued, but actually before we even get to that point, and this underlines one of the points again you have heard pretty consistently from us. When you think of the carry that we have generated, what you are really seeing is the performance of the private equity business and we again, as Bill went through with some granularity a few minutes ago, we have a lot of our newer funds, newer strategies that are seasoning and over time are going to have an opportunity to contribute to that overall realized carry profile for us.

And as we look at that run rate figure, this is a slide actually from Joe's, again that number is at a significant premium relative to what we have reported on a trailing 12-month basis.

Discounted cash flow analysis

So it does strike us that a discounted cash flow analysis makes sense as you think about valuing our realized performance fees. Again, there are going to be a series of assumptions as you walk through this in terms of investment returns and underlying growth but again that framework is one that we think makes sense.

And importantly in that, again when you look at valuation approaches today in this framework, you do see this DCF based approach across a number of analyses. I think many times when you see that, that analysis is focused only on invested capital and dry powder that we have as of March 31st. So implicit in that assumption is almost a fact that it is a question whether we are going to be able to continue to grow and continue to raise capital, and again that feels punitive to us.

So when you put the three pieces together as we look at this overall framework this framework suggests a value of at least $40 per share and importantly, if we do our job, this number should continue to go up because we are going to be continuing to be focused on growing our FRE. We are going to continue to be focused on compounding our book value.

And again, if we do our job and are successful raising capital the opportunities for us to earn carry across our strategies is also going to grow.

What Impact Would Rising Rates Have on KKR?

So let us talk about rising rates. And I think the question or the belief that many people have is that a rising rate environment is actually going to have a negative impact, and this is the concern, on private equity returns. And I think that one of the things that is interesting about this concern is it is again very much opposed relative to the internal points of view that we have where there is lots of belief in our ability to generate attractive returns irrespective of the interest rate environment.

Historical perspective

So the first thing we did in trying to think through this question was we actually looked at our history. So the two charts on this page look at the, and I am glad I can see the small print from here, it looks at the 110 North American investments we have made in our private equity business since 1984. And what the graph on the left does, is it says, okay, let us look on the one hand at the returns that we have generated and let us bucket those relative to what the 10-year treasury was at the date of that investment.

And so two things I think are interesting in this, one, it is actually not the case that we have earned outsize returns in low rate treasury environments. In fact, the data would suggest we have earned the most attractive returns in our US private equity business when interest rates have been modestly higher relative to where they are today.

And I think the important point also in this is that again we have managed to earn attractive returns over a wide variety of interest rate environments.

And what the graph on the right shows is it kind of takes this data and looks at it a little differently and it buckets our investments, not in terms of where the treasury was at the time of the investment, but how treasury has moved over the life of the investment. And again I think you have a similar result here where it shows our ability that we have been successful in generating attractive returns across a wide array of interest rate environments.

And I think one of the things that actually is so that is the historical perspective as it relates to this question. We have also thought it would be helpful to try and frame this in the framework of an LBO analysis. So if you spend a minute with me and think through again a simplified LBO model. If we were to make an investment, 9x purchase price, put six turns of leverage on it, have an average cost of debt of 6.5% in that investment, have 7% annual EBITDA growth and in five years we exit that business for one multiple turn less than we paid for it, and if you hit calc on this LBO model, it would generate a 22% IRR.

Now, if we keep all of these assumptions the same but instead of that 6.5% interest rate we increase the interest rate to 8.5%, keep all of the other assumptions the same, you see that the IRR is 20.5%. So in this specific example is an increase in interest rates, is it helpful to your IRR? The answer is no, it is not helpful. You see the IRR goes down.

However, is that move enough to turn a good deal into a bad deal? The answer to that again is no. And the other point is that if you think of when a transaction is being put together, there is obviously a positive relationship between your cost of financing and your purchase price. So if your purchase price goes from 9x to 8.8x, again you have offset the increase, or the impact from that rising rate. That change from that 6.5% to 8.5%.

So the underlying model itself again is not as sensitive to your going-in interest rate as I think people fear. Now what this model actually is pretty sensitive to is that EBITDA growth rate assumption. So a lot of what you heard today in Johannes's piece and Pete's piece, again about our focus on operational change and increasing EBITDA, that again is the piece of the puzzle that this math actually is quite sensitive to.

And if we are in a rising rate environment, and that is because there is economic growth, again I think that could actually end up being a very positive thing for us as it relates to private equity returns.

What Happens to KKR in a Market Downturn?

And then finally what happens to KKR in a market down turn? I think again for those people who think of us only as a leveraged play on equities and do not really think of the underlying fundamentals of the business, there are some charts in here that I think will be interesting to people.

In our experience

So first and foremost, in our experience we believe volatility can be good for our business. So having long term locked up capital, not subject to redemption, being able to time your entry, being able to time your exit, is a huge strategic advantage for us. We have the ability to be patient.

And at the same point in time our model has withstood periods of historical stress. So before we get to those case studies, just a reminder in terms of the capital base we have. Over 80% of that capital locked up for eight plus years at inception. Again, growing diversification by strategy, by geography.

And the bottom part of this chart is also important. We have $59 billion of dry powder at the end of March, that is up over 40% from the year prior period, up over 70% relative to two years ago.

And again to be clear, when volatility enters the market, having $59 billion of capital to invest that cannot be taken away from you, and valuations that are cheaper, that is a good thing.

KKR during the financial crisis

So how have we performed during period of stress? Let us go back to the financial crisis. You see here two charts, the assets under management on the left-hand side and management fees. You did see volatility of course in terms of the AUM line. I think the interesting thing is actually on the right-hand side when you look at management fees.

So you look at management fees at KKR, you saw them increase sequentially over each of those four years. And I do not think there are many asset management businesses globally that saw their management fees increase at a 24% compounded annual growth rate during the financial crisis.

And the dynamic you saw here was we turned on a handful of our benchmark private equity funds. We turned on our 2006 Fund, we turned on our Europe III Fund, we turned on our first Asia fund and those were all funds where we received management fees based on committed capital, where again the management fees we receive are not impacted by mark-to-market movements. So pretty powerful in terms of the underlying performance from a management fee standpoint.

KKR during periods of volatility

Now, let us look at us during a period of volatility. We picked the third quarter of 2011, as a lot of people in this room I am sure will remember, lots of volatility, concerns around the US debt ceiling and European financial companies. And the underlying performance of what we experienced is on the right-hand side. Our AUM was down modestly, recognizing the mark-to -market impact. Our fee paying AUM was actually flat and our management fees actually increased by $8 million.

But the other important point in here again gets back to the point of how we are not forced sellers and we have the ability to time our exits and how this is an important real strategic advantage for us.

So to try and highlight this point we have this slide, I know it is somewhat busy. But this slide says okay, let us look at our ten largest private equity investments in the third quarter of 2011 and let us see what happened and how they performed?

So the first bar you see under each of the ten logos is where those investments were marked as of the second quarter, the middle bar as of the third quarter and then that last bar is the final monetization we had in those investments, or for those that we haven't sold it is the current mark.

So if you look at HCA, again a company that is probably well known to many people in this room, it is the fourth bar from the left. You see at the end of the second quarter it was marked at 3.7x our cost, a very successful investment. Like many stocks in that volatile period it was marked down, it went from 3.7x our cost to 2.7x, but we were not forced to sell that investment. We were not, we have capital not subject to redemption and instead we were able to wait until we feel it is an appropriate time to exit that investment. And you see ultimately that final investment was sold north of 7x costs.

So there is wonderful flexibility across our business model. When you look across these ten investments, eight of the ten you see that final bar being higher than the second or third quarter marks. And in many cases it is significantly higher, so again we thought that would give a little bit of a sense of the stability that we have and some of the advantages we have.

And so, with that I am actually very pleased to bring up to the stage Henry Kravis, who is going to offer some final remarks.

Closing Remarks

Henry Kravis

Co-Chairman, Co-CEO, KKR

Closing Remarks

Great, thanks very much. Before I get started I have to say I learned something today, and this was really important to me, and that is that Bill Janetschek, our CFO, actually listens to me. So Bill, thanks for raising that.

I want to just thank everyone for being with us today. We have given you a lot of information. We tried to take you through what we feel are the important points to KKR. So I am going to focus on three things that are the, as I wrap up: the significant growth opportunity that we see ahead of us, our differentiated business model and the two things that are vital to our success, which I talked about earlier, which is our culture and our values.

Positioned for Continued Growth

Now, first, a consistent theme that we have heard across the presentations this morning is our focus on growth. Clearly, the company is not going to perform well if we do not focus and innovate constantly, and there is a huge focus throughout the organization on this growth initiative.

We have had meaningful growth across the firm, and we have invested extensively in our businesses to expand into new platforms. That will continue. We are going to build out what we have and we will continue innovating. In fact, that is the one thing that is great about our firm is that everyone and anyone at the firm can come up with an idea and we are going to test it. We will see if it makes sense for a future growth platform for the firm.

And as you can see on this slide, when we first listed on the New York Stock Exchange we were very much a private equity-centric firm; now you have seen that before. Since then our private equity business has grown and it has grown fine from $45 billion to $70 billion. But where you are seeing a significant scaling in our business is really in the newer businesses from $17 to $120 billion.

We have grown and we have diversified into a number of new businesses since 2010 and our non-private equity business has increased more than sevenfold. And that has been done by a combination of new businesses and new geographies as we have expanded globally.

Although we have expanded and we have diversified significantly, today we still only have in our view one business that is really at scale and that is our legacy private equity business that we have been in since 1976. All of our other businesses are young. We tried to show you all of that. We tried to show you how much potential there is in each of these businesses and the opportunity to be multiples of their current size.

Our share in markets such as infrastructure and real estate is quite low, quite frankly, relative to a number of our competitors and certainly low relative to where we are in our private equity. So we see a significant amount of opportunity for growth across the firm.

Scott and Joe showed you what all of this growth can potentially mean in terms of our earning power over the next five and ten years. And we believe strongly that we really are at an inflection point at the firm. George and I often talk about, where do we feel we are? How do we feel about the firm? What do we feel about the future? What do we feel about all of our people that we have, which is the main asset that this firm has?

And I have to say standing up here, I feel as strongly about KKR today as I have ever felt. The people are the best people that we have had collectively, and I think we are as well positioned today for the future as we have ever been.

Differentiated business model

Now secondly, our model of third-party assets under management, plus the balance sheet, plus our capital markets is a true differentiator for us. Now for some of you in the room, I have heard this question at the break, you know, not fully understanding the difference between what our balance sheet does and what our assets under management does.

Assets under management are basically third-party assets that we collect, people give us those assets to invest, and as you saw the large propensity of those assets are eight plus years in length as far as the duration that we have.

The balance sheet is the shareholders. That is permanent capital. That is about $16 billion of assets today. And we use that balance sheet to help fund our new businesses, as you have seen in infrastructure. You saw it in real estate, you have seen it in some of our other products. And we use the balance sheet to basically be one of the largest investors in all of our own funds that we have.

In addition, we use the balance sheet to grow our business by possibly making acquisitions or investments like Marshall Wace and we use it as a way to attract and retain people that we have at the firm. So it is a real differentiator for us, the balance sheet, and when you combine that together with our assets under management, which are third party assets for the most part, we happen to be the largest investor in almost all of our product categories, which comes from the balance sheet, and then our capital markets business. We feel that we are in a very strong position to take advantage of almost any situation and be a real solutions provider.

Our model certainly gives us a competitive advantage and the ability to earn greater economics relative to the fund only approach. And you heard Scott and Joe take you through that and explain how that works and why it is a real multiplier of what we could do if we had funds only and did not have the capability of our capital markets.

It allows us to create new businesses quickly, using the balance sheet capital, like we did in order to start several of our businesses. And it certainly gives us an opportunity on our core investing where we are putting up large dollars from the balance sheet alongside several other large core investors that just multiply the capability that the balance sheet has.

And it allows us to scale those businesses rapidly by using the balance sheet and syndication capabilities to win attractive investment opportunities and act like a much larger player in the marketplace than otherwise we would be able to do. Example – and you saw when Tara talked about that – was our Q-Park investment and how that enabled us to get that transaction done and earn significantly larger economics off that one transaction alone.

The balance sheet and the combination of the model we have allows us to supply co-invest opportunities to many people; many of you in this room, and others, to our limited partners, helping expand our limited partner base and increasing our exposure to the different teams within KKR. It allows us to make General Partner commitments to our funds, which align our interest with our LPs. There is no better alignment than our putting up as much money and as much capital as we do in each of the investments that we are in.

Then, it allows us to do all this while creating high-margin fee revenues for the firm, which are increasingly global and driven by us and by the third parties. Now, remember, capital markets and the balance sheet do not show up in assets under management. They do, however, allow us to scale all of our businesses more rapidly while generating significant economics for the firm.

Our People and our Culture

Finally, the key to achieving our potential is really our people and our culture. This is what makes KKR so special. That is why I mentioned that when I was up here to kick off the program, and that is why I want to mention it again.

We are a solution provider

First, and most importantly, we are one firm. We work together. We collaborate. We relentlessly try to do what we can to create the right solution for a company. Think of us as a solution provider. We have come so far from where we used to walk into a company when all we had was Private Equity and, basically, a second sentence that we would make would be, 'Is your company for sale?' Once that was over, we had nothing more to talk about if he said no and we would walk out.

Today, we can invest anywhere in the capital structure, whether it be through the debt stack from bank loans all the way through special situations. We can invest in equity – majority or minority equity. But, we are one firm and we work closely together to create this right solution. That is really important.

Attracting and retaining the right people with the right culture

Second: we care deeply about our people. We want to attract diverse professionals who are team-oriented, innovative, entrepreneurial self-starters. We spend a lot of time on our interview process. People sometimes wonder if it is not too onerous, too lengthy. We do not think so because we do not lose the people we want to keep for the most part.

The one thing that I am most proud of about when it comes to our people is we have been able to take from every single competitor we have out there – and we have taken some senior people – we have never lost one senior person to a competitor in 42 years. Now, one of the reasons for that is, I think, is that you rarely hear anybody at KKR use the words 'me' or 'I'. Nobody is raising their hands to say, 'That is my idea. That is my deal.' It is a team effort.

This is by design. Having the right people with the right culture and values is critical for us when we think about the integrated business model that we have at the firm. Today, you have met just a small part of the 1,200 employees that we have at the firm. I have got to tell you, I am really proud of the team that we have: the people that have chosen to work with us and to be part of this very special place.

Our Goal in 2018: Generate Attractive Risk-Adjusted Returns for our Fund Investors

Our goal is to generate attractive risk-adjusted returns for our fund investors and to use our business model to maximize the economics from these returns. I hope you have seen that today. I hope that came through, loud and clear, clearly to you.

To do this, we know we all need to work together. We need to think creatively and collaborate together so our 'One Firm' culture with no silos certainly facilitates what we are able to do at the firm.

We Have to be a Responsible Investor

Finally, we have to be a responsible investor. We have been this way for many, many years. We do not make a big deal out of it. We are not out there crowing and writing a lot of op-eds and so forth, but we do. We have been doing this because it is critical for us and it should be critical for every one of you in this room.

Creating value for our employees

When I look across our portfolio companies, just a few things jump out at me. Number one, and not in any particular order, we have hired 62,500 veterans and their spouses that come out of the military, cannot get jobs; many of them. We put them in our portfolio companies.

We prioritized and supported our employees' health, wellness and safety. We have created programs to ensure best practices when it comes to ethical supply chain management. I do not know if any of that came through to you in some of the things that Pete Stavros talked about, but it is embedded not only in our industrial sector. It is embedded in every single company that we have in our portfolio. This is a high priority for us.

58 KKR investments to date have had a partnership with the Environmental Defense Fund. That has helped us optimize each of those companies' environmental footprints. Now, you heard from Pete earlier about that. We are proud of the employee engagement that we have. Being able to say that every single person at CHI or at any of our other companies in our industrials sector and many of our other companies in other sectors are owners, not just

employees: that makes a huge difference. We want to do that. We are going to continue doing that by making everyone an owner, by granting them the opportunity to participate in the equity returns directly alongside us.

It is a model of alignment that we know works. We have done it for years. That is how we started the Private Equity industry, which we did not know was going to be an industry back in the 1960s, and then started KKR in 1976. We know it works. Thousands of employees have benefited from this ownership model, and we are going to continue that.

Proactive Focus on ESG Issues

Since 2008, when we began proactively focusing on ESG issues across the investment lifecycle of our various companies, we have seen a significant increase in global challenges facing our companies and the communities in which they operate. Our approach and commitment to responsible investment has also become a sourcing and deal-making advantage for KKR.

Unilever

Let me give you an example. Last year, we were in a very competitive bidding process to acquire the spreads business – that is margarine – of Unilever. Now, as many of you probably know, Unilever is in an enviable position, as a company, that has really been an industry leader when it comes to sustainability and being a force for good in the business world. When they decided to sell the business, they were not just looking for somebody with capital, but rather they wanted a buyer who would continue their commitment to ethical sourcing practices.

We happened to be just that group. We were able to do that by working toward and ensuring them that we are going to continue working toward the goal of sourcing 100% of sustainable palm oil by 2019. That is just around the corner. It was one of the reasons our team was selected to lead the division on its journey as a standalone company.

It is not just in our companies, we are doing the same thing at KKR itself with all of our employees in our communities and we are making a huge impact. At KKR, we believe we can make a difference by integrating our performance-focused investing philosophy with our ESG initiatives. It is our responsibility not only to serve our investors through strong investment returns, but also to support them by investing in their communities and the companies in which we invest. This is critical for us.

KKR: Connecting the Dots and Using the Whole Brain of the Firm

Let me just say, in closing, I am proud to stand up here. I am proud to have been a co-leader of this great firm along with my partner George Roberts and the many wonderful employees that we have at KKR. KKR is not about one person, but about an entire team. It only works if we continue to connect the dots, as Scott likes to say, and use the whole brain of the firm.

Well positioned for success

But we believe we are as well positioned today to connect the dots. We are doing it. It is working. You are seeing the growth out of that. We are so convinced that by doing so, we can continue to grow the firm. We are using our model well. We are scaling the new businesses. We are raising a lot of capital, much of it on a permanent or very long-term basis.

This is what many institutions want today. They do not want to just be number 64 in a fund. What they really want is to build a closer relationship on a longer-term basis, recycle the capital, and that is exactly what we can do for them. That is why we are seeing a big growth in these longer-term, separate-managed accounts that are coming our way.

Key Takeaways

And so we will continue to do all of the things I just summarized for you, and along with that: performance, execution within the growth avenues which are open to us for a third-party business now and the power of compounding. Think balance sheet, again. Think the fact that it has a fixed dividend, and that money that we are not paying out can be used to reinvest. We will have more capital to turn into more value for all of us in this room and others that are listening to us on the webcast.

Our objective is simple. We want to be the most profitable, valuable company in the industry by leveraging our unique business model and culture to deliver superior returns for all of you and for our limited partners who provide enormous amount of capital to us and have put a lot of trust into all of us at KKR. I just want to thank you all, once again.

You spent almost four hours with us so far. We are not through yet. We are going to get to Q&A. But I want to thank you. I want to thank you for at least having some trust in us and being willing to listen to our story. Those of you that have been with us either recently or for a longer time, thank you for the trust and confidence you have shown us. We are not going to let you down.

With that, let me ask my Co-Presidents, Scott and Joe, to come up along with Craig Larson, and we will answer your questions.

Q&A

Michael Cyprys (Morgan Stanley): Great, thank you. Just a question on investment returns. I think on one of the slides, you showed about 24% gross returns that you have generated historically in Private Markets, Private Equity. Just curious what level you think is sustainable, going forward?

Could you also tie in what has to be done differently today, relative to the past, in order to hit that level of return?

Joseph Bae: Sure. Our long-term, 42-year track record is around 26% gross. At different points in the cycle, obviously, those returns have been higher and lower. That is the average over the last four decades of our experience. I think what we are constantly trying to do in Private Equity is understand where the markets in both different industries and different companies are headed over the next five to seven to ten years in their evolution. That is really what we do.

What you have heard from Johannes and Pete today is our focus is not just around the capital structures and what the markets are doing, but what we, as a new owner of a business, can do to drive value creation. What are the levers? Is it operational improvement? Is it a consolidation play? Is it a big carve-out opportunity? We are underwriting in each of these investments in Private Equity, a specific set of value creation initiatives that we think we can control.

If we can consistently do that, we believe our returns in Private Equity will stay high. The slide that Scott put up which showed 17.5% gross; that is not where we are underwriting returns, just to be clear. All the deals we are doing, we are underwriting returns higher than that. Our expectation is our returns are going to continue to be very strong. I would say a 20-plus per cent on a gross basis, depending on the risk we are taking.

Again, a lot of these are risk-adjusted, right? We do not look at one base case. We are looking at a spectrum of probability-weighted outcomes, depending on the business and the industry it is in. But, our expectation is in our traditional Private Equity businesses, we are going to continue to maintain those types of return expectations.

Henry Kravis: Let me just add one thing to what Joe said, and that is that we are buying complexity – and we mentioned that somewhere along the way – whereas markets really like simplicity. What we like to do is to buy a company that is complicated, where value has not been really defined yet in the company.

Our job really begins the day we buy a company. I have a saying that is sort of inculcated in the DNA of KKR and that is, 'Do not congratulate us when we buy a company. Any fool can make an investment.' That is easy. Just spend enough money and you will own a company, or you make an investment. The hard part is what do you do with the business once we buy or make that investment.

If you combine complexity, the ability to really redefine the business, as you have seen some examples that we have gone through with you today, and the ability to bring on KKR Capstone, which is an approximately 60-person-strong operating group plus the teams themselves that do the deal and continue to stay with the company, there is an enormous amount of value that we can wring out. If you can buy complexity, you can also buy companies oftentimes more cheaply than if you are just going to buy simplicity because you end up paying top dollar for simplicity.

John Miller (Ariel Investments): First, Henry, on behalf of Ariel Investments and our clients, I want to thank you for creating such significant shareholder value since the time we first initiated our position back in 2011.

My question pertains to the traditional asset management space. You have made several successful partnerships in the hedge fund area over the last couple of years. What are the two or three reasons you would not want to try to duplicate that success with partnerships in the traditional asset management space?

Scott Nuttall: Thanks for the question. You are right, we have been able to create several strategic partnerships and hedge funds that have worked quite well and we have been able to grow a lot faster than the industry, as a whole. Just to give you a sense, we met with over 250 different hedge funds before we found the right partners in Marshall Wace.

I think the question, as it pertains to traditional asset management, is an interesting one. The short answer is we see less day-to-day connectivity with our business in traditional asset management than we do in the hedge fund space.

If you think about when we talk to clients – we talk to CIOs about alternatives – they will be thinking about hedge funds as it relates to alternatives. It is typically a different part of their group that will look at investing in the more traditional long-only public equities or fixed income parts of the market. There is less connectivity that we have seen. There has been less strategic rationale as a result, in terms of when we look at how can we help one of those businesses grow and how can they help us. In fact, to our prior point, we do not want to be all things to all people.

We are not in the traditional space. We think we are best to stick to alternatives, which is what we know. That is why we have not focused on traditional asset managers as partners thus far. I think that will continue to be the case, unless something changes.

Craig Larson: John, thank you, of course, for your kind words at the beginning.

William Katz (Citi): Thanks very much for taking the questions, and I appreciate the comprehensive presentation today. A two-part question. In terms of the dual class structure with the C-Corp as you are today, what is your thinking behind that, particularly that the employees own 40% of the business and whether or not, by moving to a single class, you might expand the opportunity for index inclusion is sort of question number one.

Unrelated question number two: when you put up your long-term distributable earnings target over the next five or 10 years, what is the underlying margin assumption that you are using against that? Thank you.

Scott Nuttall: On to the second one, first. The underlying margin assumption is consistent with what we have been achieving thus far. We have a margin of approximately 50%, give or take. There is no big presumed improvement just to get to those numbers, Bill, as we have talked about and we think is the case, as we scale.

We think we can get positive operating leverage in the business. It is basically where we have been, and we are not giving ourselves real credit for much operating leverage and margin improvement.

Sort of to answer the first question, look, I think we do have a dual class structure. It has been the case since inception for us. We get this question normally as it pertains to a couple of indices: the Russell and the S&P. Over the course of our considering whether to convert to a C-Corp, they both actually changed their rules around the inclusion.

This happened very recently, just last summer. We will see how this evolves. Obviously, we just converted to a C-Corp last Monday. If there is something sensible to do down the road that allows us to create more shareholder value, we will, of course, consider it.

To your point, we own 40%. However, we are taking this a step at a time. Right now, we are not planning to make any changes to our voting structure. Probably three years ago, however, we did not expect to be a C-Corp either, so let us see how this evolves.

Speaker: Thanks for the very detailed presentation. I have a question, as a longer-term shareholder. I do not disagree with you that the value of the KKR shares is north of $40. What I am surprised is why, as a management, you have not bought more shares back when you see so much upside. Why not do more share buyback of your own stock when you see so much upside?

Scott Nuttall: We have actually been reasonably active buying back stock. I think the last public numbers we gave out is we bought back over $600 million worth of stock at a blended price of between $15 and $16 a share. If you look across the alternative asset management space, I think we have been, by far, the most active repurchaser of our own stock. We have been watching the float, wanting to make sure that we do not impact the float to too great a degree because we want to make sure that there is meaningful liquidity in the stock. We are trying to get the balance as right as we can.

What we have said publicly is that we are committed to making sure we do not have dilution to our shareholder base as it relates to compensation of our employees. We have been delivering on that commitment, which you should expect us to continue to deliver on. But you know, let us see how things play out from here.

Obviously, the stock has made a bit of a move, but we think it is just the beginning. There has been quite a bit of volume in our stock even in the last week. We will watch it as it continues to play out. However, as we said on the slide, we own 40%. We are committed to doing what it takes to have the ultimate and appropriate fair value appropriately reflected in the stock price.

Craig Siegenthaler (Credit Suisse): Thank you. How has the size of your private credit origination team changed over the last six to twelve months, given all the new AUM coming on board this quarter? Because you are growing many multiples of size. You have a bigger mouth to feed.

Also, are you worried about increasing your volume dramatically, given where we could be in the cycle right now?

Scott Nuttall: Great question. The answer to the origination question is pretty straightforward. We went from about $12 billion to $26 billion in AUM in kind of direct lending private credit. Our origination team has grown in line with the growth in the AUM. It has kind of more than doubled over the period of time you referenced. We are continuing to bring on more people to help us make sure that we originate attractive opportunities in that space. As we have invested in the origination team, the flow has gone up quite significantly.

Your question about where we are in this cycle is a great one. We spend a lot of time thinking about that. Really, where we are focused – and Todd Builione referenced this – is going to larger companies that have more stability. We are trying to be very thoughtful about the cycle in that way is get ahead of it.

What we have seen is a lot of competition come into private credit, but it is in the smaller end: $30 million to $50 million EBITDA type companies. There are very few players at the $100 million to $200 million EBITDA range. We have gone up in size. More stability in the company is more protection in the documents.

We think that is the right way to protect ourselves against the cycle. The originations have gone up a lot, but so has our turndown rate. We are being highly selective in focusing on companies we want to be lending to through a downturn.

Robert Lee (KBW): Thank you, and thanks for the thorough day today. Question on the Capital Markets business. Clearly, it generates more dollars per investment idea through that and helps the business, overall. But one of the criticisms or feedback you get from some investors is that maybe it adds to the risk profile of the balance sheet or of the company. It may be better if you help us understand why that is or is not the case and how you think of that risk profile of the Capital Markets business?

Scott Nuttall: Sure. I think, look, to be really clear, our Capital Markets business is a moving business, not a storage business. The way that we use the balance sheet to support the Capital Markets business is not with an eye to having any hold.

Typically, what is happening is – take an example, even the Infrastructure examples we talked about, that Tara went through – we will actually be off risk and syndicate our exposure by the time the transaction actually closes. We are not actually funding those investments.

If you imagine what happens in the context of a transaction like this, whether we are underwriting debt or equity, we have a lot of inbound calls that are coming in, including from others that we maybe beat to buy the asset. And they are looking to partner with us.

So we have got a full syndication process that is running. We are out talking to 200 to 300-plus different potential investors alongside us on the equity side. If, for whatever reason, we decide we want to go call one of those people back that had the interest in investing alongside us, we can do that too.

It is one of these businesses where there is the theoretical risk you could potentially fund, but in actual fact, we actually have not. We have been doing it for a very long time. It has been the case both in the equity side and the debt part of our business.

It facilitates a placement of the equity and the debt. We have been able to create a nice recurring aspect to this business. You can see all the different ways that we are participating and everything that we do, but we view it as a very capital-light approach to the business, and that is how we will continue to run it.

Michael Carrier (Bank of America/Merrill Lynch): Just a question with the C-Corp conversion, and let us say longer term, if you deal with the dual share class or the voting percentage, just how are you thinking about incentives for both management, the employees, the percentage that is equity-based versus maybe carry, other forms of compensation to just better align or more align to the shareholders?

Joseph Bae: Listen, I think in terms of the motivation, the retention and our ability to both attract and retain great talent – which is the most important thing we have to do – we want as much flexibility, in terms of how to incentivize our people over time. Stock is a meaningful piece of that. Again, as Scott mentioned, we are committed to make sure share creep does not happen in a meaningful way, in terms of share buybacks and other ways, as we issue more stock to employees. But, just like Pete's example in Industrials, it is critically important for us and our employees at KKR to all feel like true owners of this business whether you are a partner at the firm, a junior executive at the firm or an administrative assistant at the firm. We want everyone to be an owner – 'One team, one dream' – and really foster that 'One Firm' culture.

So I think stock is going to continue to be a meaningful piece of compensation for the foreseeable future. But, we obviously have cash and carry as well, which are both big drivers of comp.

Henry Kravis: Let me just add one thing to that, so you understand the philosophy at the firm. When we went public in 2010, at that point, before we went public, George and I owned 100% of the firm. When we went public, we made a decision that we wanted every single person at KKR to be an owner. It did not matter whether they were an executive or somebody working in our mailroom or an executive assistant or somebody working in the kitchen. It did not really matter. We wanted every single person. So we gave away 60% of the firm to the employees.

Now, we exchanged some of that for some carried interest where we also thought it was really important, as we build the firm, that everybody continued to act and think like an owner and be part of the growth there. It has paid off exactly as we had suspected it would. By being an owner, by being a shareholder in the company, you just think differently. And you also think much more with a long-term focus.

Alexander Blostein (Goldman Sachs): Thanks. Maybe I'll squeeze in two quick ones. First, the follow-up on the margin discussion. You guys obviously outlined the opportunity to scale a lot of the businesses and kind of alluded to the fact that there is probably some upside if things continue to progress as you envision. What happens in the downturn? Can you spend a minute just talking through your ability to defend the pretax margin in case realizations dry up?

The second question, just a little more strategic. Could you spend a minute on what you guys are doing in the Insurance space as some of your peers obviously made a pretty big push into that industry?

Joseph Bae: Sure. I think we have built some conservatism, obviously, in terms of the guidance and the forecasts laid out today. As Bill mentioned in his presentation, we have a tremendous amount of visibility, in terms of our management fee line. Right?

Those are long-term contracted management fee based on committed capital. Whether the market is up 20% or down 20%, that management fee line is pretty locked in on an upward trajectory, based on the funds we have raised already and the capital committed to us.

I think where you could see volatility, obviously, in terms of the P&L is around transactional activity. There will be periods of time where there is fewer investments made and fewer exits made, depending on market conditions. Those are very short term. They will bounce back. It will revert back to the mean over time. So we are less worried about that.

Really, we have the benefit of patient capital where we can time our exit and time our entry and exits into investments. That creates us the opportunity to generate alpha in our business. So we are not worried about near-term volatility.

On the expense side, as I walked through in a couple of my slides, we have made a massive investment in the last decade in building out some of these platforms and capabilities. As these businesses approach scale – this ten-year inflection point we talked about – the expense growth really flattens out quite dramatically. If you can continue to scale AUM, that is really where you are going to see the operating leverage in the businesses that we have and the potential for margin expansion.

Scott Nuttall: I think with respect to the second question, the way we like to think about ourselves is that hopefully, we have the wisdom of a 42-year-old firm, but we have the runway and energy of an 18-year-old. You think about the weighted average life of our businesses, it is probably 17 to 18 years. We have a 42-year-old business and a bunch of businesses that are two to ten years old.

If you look at our Client franchise – and Suzanne walked through – we really started creating it in 2009. We still have a fraction of the number of investors of others that do what we do. Massive opportunity to expand the Client franchise alongside the investing businesses. Insurance is just one example of an area where we are just beginning to scratch the surface.

We have three or so people that wake up every day to focus on the insurance space, globally. That is it. Probably three years ago, we had one. Just with that little investment thus far from the last 15 months, we have gone from $12 billion to over $21 billion of assets in insurance and so, we are just getting started.

The answer to your question on insurance is very straightforward. We will continue to invest. We are building relationships. It takes a couple of years when you bring in a new relationship manager or product-focused person to really scale AUM. We are just at the very early stages, but we see that space as having material upside.

But, I would say the same thing is true about high net worth. The same thing is true about retail, broadly. The same thing is true about sovereign wealth funds. The same thing is true about virtually every institutional shareholder or investor we talk to around the world.

We have a lot of new and developing relationships that are just now starting to turn into AUM, so back to that point about having the upside of an 18-year-old. We see significant opportunity in virtually everything that we are doing both investing and on the client side.

Craig Larson: Everybody, again, thank you. I know by the raise of hands of the last go-around, there are additional questions. Please feel free to follow up with us directly. Again, we can all head down here and head to lunch one floor below. Thank you again, everybody.