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CORPORATE PARTICIPANTS

Craig Larson *KKR & Co. L.P. - MD of IR and Head of IR*

Scott C. Nuttall *KKR & Co. L.P. - Co-President, Co-COO & Director*

William J. Janetschek *KKR & Co. L.P. - Member and CFO*

CONFERENCE CALL PARTICIPANTS

Alexander Blostein *Goldman Sachs Group Inc., Research Division - Lead Capital Markets Analyst*

Chris Kotowski

Craig William Siegenthaler *Credit Suisse AG, Research Division - Global Research Product Head for the Asset Management Industry*

Devin Patrick Ryan *JMP Securities LLC, Research Division - MD and Senior Research Analyst*

Gerald Edward O'Hara *Jefferies LLC, Research Division - Equity Analyst*

Kaimon Chung *Evercore ISI, Research Division - Senior MD, Senior Research Analyst and Fundamental Research Analyst*

Chris Harris *Wells Fargo Securities, LLC, Research Division - Associate Analyst*

M. Patrick Davitt *Autonomous Research LLP - Partner, United States Asset Managers*

Michael J. Cyprys *Morgan Stanley, Research Division - Executive Director and Senior Research Analyst*

Michael Roger Carrier *BofA Merrill Lynch, Research Division - Director*

Robert Andrew Lee *Keefe, Bruyette, & Woods, Inc., Research Division - MD and Analyst*

William R Katz *Citigroup Inc, Research Division - MD*

PRESENTATION

Operator

Ladies and gentlemen, thank you for standing by. Welcome to KKR's Second Quarter 2017 Earnings Conference Call. (Operator Instructions) As a reminder, this conference call is being recorded.

I would now like to turn the call over to your host for today, Mr. Craig Larson, Head of Investor Relations for KKR. Craig, please go ahead.

Craig Larson - *KKR & Co. L.P. - MD of IR and Head of IR*

Thanks, Nova. Welcome to our second quarter 2017 earnings call. Thanks for joining us. As usual, I'm joined by Bill Janetschek, our CFO, and Scott Nuttall, our newly appointed Co-President and Co-COO. We'd like to remind everyone that we'll refer to non-GAAP measures on the call which are reconciled to GAAP figures in our press release and the supplementary presentation, which are available on the Investor Center section of kkr.com. The call will also contain forward-looking statements which do not guarantee future events or performance, and please refer to our SEC filings for cautionary factors related to these statements.

And with that, I'm going to begin on Page 2 of the supplementary deck. This morning, we reported strong second quarter results with record after-tax economic net income and record book value per unit. Investment performance was strong and we've continued to have success from a fundraising perspective. In terms of our financial performance, we reported after-tax economic net income of $753 million for the quarter, which translates into $0.89 of after-tax ENI per adjusted unit, and over the trailing 12 months, we've generated over $2.2 billion of after-tax ENI.

After-tax distributable earnings were $322 million for the quarter and we've generated over $1.5 billion of after-tax DE on a trailing 12-month basis.

Also of note as you look at page 2 of the deck, our after-tax ENI and after-tax DE margins for the quarter and trailing 12 months are all attractive, ranging between 49% and 59%. Our fee related earnings have grown meaningfully on a year-over-year basis. Focusing on ENI, we've generated an LTM return on equity of 23%. We're reporting $13.50 of book value per adjusted unit and we've seen book value compound by 19% on a year-over-year basis. The firm continues to grow nicely with AUM and fee paying AUM up 13% and 19%, respectively, over the last 12 months.

One additional note, within our press release you'll notice we've added a new page, page 8, which shows the buildup of our after-tax distributable earnings in greater detail relative to what we've reported historically, further enhancing our overall disclosure. As a whole, it was an excellent quarter and I'm pleased to turn the call over to Bill to run through our performance in more detail.

William J. Janetschek - *KKR & Co. L.P. - Member and CFO*

Thanks, Craig. We had strong investment performance both on a quarterly and LTM basis across our carry paying funds. This performance, which Scott will discuss in more detail, contributed to the positive results we reported this morning.

Focusing on our total segment financials, Management, Monitoring and Transaction fees were $365 million in total, up 39% year-over-year. If you turn to slide 3 of the supplement, you can see the growth and diversification of our management fees. Year-over-year management fees are up 13% and the highest we've ever reported. One item of note is Asia III is contributing to management fees for the first time this quarter. The fund entered its investment period on March 31 and has total commitments of $9 billion. As a reminder, on a run rate basis, Asia III will add approximately $50 million to net annual management fees.

In terms of transaction fees, we reported $156 million of fees this quarter driven by our continued momentum within our Capital Markets segment. Page 4 of the supplement profiles the growth of the KCM segment. LTM revenues were up 65% compared to 2016 and year to date revenues of $215 million already exceed the $182 million we reported for all of 2016. On the bottom half of the page you will see that KCM has been active in all geographies, in debt and equity, and in financing and syndication for KKR-led and third party investments.

Turning to performance income, we reported $564 million, the highest in two years. Several exits drove $265 million of realized carry, up 28% compared to the last quarter, and the exits were well diversified between strategic and secondary activity. On a blended basis, the PE exits were done a 2.6x our cost. Strong marks across the portfolio also contributed favorably to total performance income as unrealized gains of $300 million were more than double last quarter. This is resulting in a 15% increase in unrealized carry on our balance sheet quarter-over-quarter.

Investment income came in at $336 million, up nicely quarter-over-quarter and year-over-year. Strong performance across our private market strategies drove more than $300 million in unrealized gains, the largest figure we've reported in over 5 years.

Bringing it all together, on a total reportable segment basis, fee-related earnings came in at $214 million, our after-tax distributable earnings were $322 million with after-tax ENI of $753 million.

Moving to deployment, we invested $4.9 billion of capital this quarter. Public markets deployed $1.3 billion. This deployment came from investments made across our alternative credit vehicles, primarily within direct lending. As you will recall, we are entitled to economics on our alternative credit vehicles largely on invested, as opposed to committed, basis.

On the private market side, we invested $3.6 billion. The largest contributors were a Private Equity investment in a specialty travel company out of Europe IV and a core private equity investment in USI, a leading retail middle market insurance broker. This is an investment that we made through our core private equity partnership with Caisse which included funds from our balance sheet.

Moving to AUM and fee-paying AUM, AUM increased by $11 billion in the quarter driven by inflows in Asia III, healthcare growth, real estate and our alternative credit funds. We ended the second quarter with fee paying AUM of $113 billion which includes $8.5 billion of third party capital committed to Asia III.

On page 3 of the supplement you can see the increase in fee paying AUM has in turn resulted in management fee growth with fees growing at a 10% CAGR since 2010. Overall, our capital raising activity has resulted in approximately $43 billion of dry powder across the firm as of June 30, an increase from the prior quarter despite a robust level of deployment.

One other thing to note, on June 1 we completed the strategic transaction to combine PAAMCO and Prisma to create PAAMCO Prisma Holdings. The combined business is now one of the largest in the liquid alts industry with more than $30 billion of AUM. Our hedge fund business now includes 5 strategic partnerships with $77 billion of AUM, of which our pro rata share is about $24 billion. And with that, I'll turn it over to Scott.

Scott C. Nuttall - *KKR & Co. L.P. - Co-President, Co-COO & Director*

Thanks, Bill. And thank you, everyone, for joining our call today. Let me start off by saying that Joe and I are honored to join Henry and George as part of the leadership team to help lead KKR in its next stage of growth and development. Importantly, we take on this responsibility as long-time friends with a view that partnership is the key to KKR's success. These roles are a natural extension of what Joe and I have already been doing and our focus remains on making KKR an even more successful firm. So with that, let me turn to the results.

As Craig and Bill discussed, we had a very good quarter. And looking at the last 12 months, we're pleased with the fundamentals we are seeing across our firm and businesses. Our investment returns are strong. Our deployment pace is high and activity broad-based. We've monetized a number of investments. We've had good fundraising momentum and we've used our model to capture more of everything that we do.

So let me take each of these in turn. Let's start with performance. Take a look if you would at page 5 of the supplement. We've had strong investment performance across our asset classes. In private equity, our portfolio appreciated 12% year to date and 19% in the last 12 months. If you look more closely at our benchmark private equity funds, on a trailing 12-month basis, our North American, Asian and European PE funds, shown on the left side of the chart, are up 33%, 13% and 22%, respectively. In our non-PE strategies we're also seeing strong investment performance. Our real asset strategies are performing with a rebound in our Energy Income and Growth fund in particular.

We've also seen strong performance across our alternative credit strategies with our special situations, mezzanine and direct lending funds up 34%, 11% and 15%, respectively, on a trailing 12-month basis. Our balance sheet investments also had strong performance, appreciating 10% year-to-date and 18% in the last 12 months.

Now moving onto deployment, we had another active quarter. And over the last 12 months, we've deployed about $17 billion across businesses and geographies compared to $11 billion in 2016. Activity has been broad based by strategy with $12 billion coming from private markets and $5 billion from public markets. In terms of realizations, Bill already walked you through the details. We are continuing to see strong monetization activity.

Looking at the last 12 months, we returned over $13 billion to our private markets investors, driving $1.5 billion of after-tax distributable earnings. And on a blended basis, these exits were done at 2.4x our cost.

Let's turn to fundraising and business building. Page 6 highlights the growth in assets over the last 12 months. Fee paying AUM and AUM were up 19% and 13%, respectively, driven by $25 billion of organic capital raised. Private markets accounted for $15 billion of the capital raised driven by Americas XII and Asia III, a $9 billion fund raised in just 7 months.

The remaining $10 billion of new capital came from public markets, specifically in CLOs, private credit strategies and our strategic partnerships. Shifting to our model of AUM, capital markets and balance sheet, this was another quarter where the power of our model was evident. Our strong activity level in Capital Markets continued with almost $94 million in transaction fees in the quarter. And looking at the last 12 months, we've executed 162 transactions, generating about $300 million in fees.

This includes 84 third party transactions. Our third-party capabilities are directly synergistic with our credit investing business. We're able to deliver multiple solutions in a single conversation creating an underwriting opportunity for our Capital Markets business and a new investment opportunity for our Credit business.

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As we've mentioned before, Capital Markets and the balance sheet do not show up in our AUM, but they are powerful economic contributors for the firm and allow us to move quickly, speak for larger investments, and scale our third-party business while generating fee economics for the firm.

We believe capturing more of everything that we do through a model of third party AUM plus Capital Markets plus balance sheet allows us to increase alignment with our fund investors and drive a highly attractive ROE and a larger quantum of total cash flow.

The power of our model is evident in our results. Over the last 12 months, our book value is up 19% and we generated a 23% ROE on an after-tax ENI basis. To bring it all together, our core fundamentals are summarized on page 7. We're pleased with our progress this quarter and with $43 billion of record dry powder, multiple scaling businesses, and improved utilization of our model, we're looking forward to what's next. And with that, we're happy to take your questions.

QUESTIONS AND ANSWERS

Operator

(Operator Instructions) Alex Blostein, Goldman Sachs.

Alexander Blostein - *Goldman Sachs Group Inc., Research Division - Lead Capital Markets Analyst*

Wanted to kick off with a question around Capital Markets. Obviously a very powerful growth driver for you over the last couple of quarters. Could you guys spend a minute on kind of what the next leg of growth here will be from? And I guess how are the economics shifting between you guys and just kind of the various members of the syndicate and how much that's been a helper in the recent growth?

Scott C. Nuttall - *KKR & Co. L.P. - Co-President, Co-COO & Director*

I'd say a few different things are going on. One is we've been doing a more effective job using the business model of Capital Markets and balance sheet across more parts of the firm. This year in particular, I'd focus you on infrastructure and Asia. Two areas of the firm where we're starting to do larger transactions where we've been able to underwrite both equity and debt and syndicate both of those and generate fee economics for the firm. So I'd say the first leg to the growth has been greater penetration of KKR's businesses and using the model with more frequency and effectiveness around the world. So that's part one.

Part two would be around our third-party business, in particular linked with our credit investing platform. So we spent a lot of time building out origination capabilities across areas like private credit in particular where we're doing transactions with other financial sponsors in underwriting debt deals for them to help fund their transactions, either new deals or refinancings of existing companies that they own. And so we've been making progress in terms of penetration there as well. That's sometimes on an underwritten basis and sometimes on a best efforts basis. So really what you see showing up in the numbers this year and the reason for the growth is kind of a combination of both greater penetration of KKR activity plus third-party activity. No real shift I would say in terms of how the syndicates are functioning, but I would point to the fact that we are doing far more lead left transactions this year than ever before and that's also part of the reason that you're seeing the growth in the fee line.

Alexander Blostein - *Goldman Sachs Group Inc., Research Division - Lead Capital Markets Analyst*

I guess technically just around the management fees, obviously very robust fundraising environment for you guys over the next couple, over the last couple quarters. I guess what else is on the come as we think about any larger funds coming in over the next 12 to 18 months and how we should think about the management fee trajectory from here?

Craig Larson - *KKR & Co. L.P. - MD of IR and Head of IR*

Why don't I start with where we are in the market currently and then as we think about it over time from a fundraising standpoint. First, in terms of episodic funds, that would include healthcare growth. Two real estate strategies, REPA II as well as Real Estate Credit Opportunities, Lending Partners III and Private Credit Opportunities II. And this is in addition to areas where we look to raise capital on a more continuous basis that includes our leveraged credit strategies both in the US and Europe. So that would include high yield and leveraged loan SMAs and CLOs. We actually expect to shortly close on a $700 million CLO actually. Our BDC as well as across our hedge fund partnerships which include Marshall Wace, PAAMCO Prisma and Nephila. And I think over time you'll see a third infrastructure fund, a second energy income and growth fund, and a fifth European private equity fund.

William J. Janetschek - *KKR & Co. L.P. - Member and CFO*

Alex, one other thing of note, Craig was mentioning what the possibilities are on capital that we could raise, but one thing to keep in mind is that as it relates to fee paying AUM, we've raised approximately $12 billion of AUM which hasn't gone online yet. So when you a take look at the dry powder that we've got which is shown on page 15, which is roughly about the $42 billion, we've got roughly $6 billion of AUM which we'll turn into fee paying AUM in private markets. And the same holds true on the public markets and that will obviously generate a healthy amount of management fees. And the blended rate on that is a little north of 1%.

Scott C. Nuttall - *KKR & Co. L.P. - Co-President, Co-COO & Director*

Yeah, I'd say look, the overall fundraising environment is excellent. The only thing I would add is we continue to see an overall trend towards strategic partnership type activity, larger mandates, multiple asset classes, long term. So there's more discussion along those lines happening in the market.

Operator

Patrick Davitt, Autonomous.

M. Patrick Davitt - *Autonomous Research LLP - Partner, United States Asset Managers*

Could you walk through the underlying kind of revenue and EBITDA growth of the private equity portfolio?

Scott C. Nuttall - *KKR & Co. L.P. - Co-President, Co-COO & Director*

Sure, Patrick. It's Scott. I'd say overall, continuation of the positive trends we discussed the last couple of quarters. So revenue growth 8%, 9% type level. EBITDA growth 10%, 11%. It's continuing to be quite strong, so just think generally speaking high single digits for both. And I'd say the only underlying trend I'd point you to is, Europe has been, just from an operating fundamentals standpoint, very, very strong. So, overall very happy with the portfolio company performance and particular strength in Europe.

M. Patrick Davitt - *Autonomous Research LLP - Partner, United States Asset Managers*

You guys have been one of the more active firms in China over the years and had some very successful investments. Are you seeing any shift in the opportunity and/or in ground? Particularly with in ground JVs given kind of the crackdown on the large conglomerates there and within more wealthy families?

Scott C. Nuttall - *KKR & Co. L.P. - Co-President, Co-COO & Director*

I'd say the big trend we've seen, Patrick, is the opportunity for us to start doing the larger transactions. There is a significant amount of competition at the lower end for kind of growth deals with relatively small equity checks. We're starting to move to larger sized opportunities in China. And that's where we're starting to spend our time with a much greater concerted focus on a go forward basis. The crackdown you mentioned is going to lead to some opportunities we think over time, but it's generally speaking on the larger end is where we're spending time today.

Operator

Chris Kotowski, Oppenheimer.

Chris Kotowski

I'm looking at page 12 where you give the balance sheet detail and there are a couple of new big investments that appear in the significant investments section. I wonder if you can just flush them out a little bit. One is USI and I'm curious on that one whether that's a -- I know that's with Caisse but is that also in funds or just on the balance sheet? And is it a strategic investment or is it just an investment investment? And then also, PortAventura, which I thought was owned in one of your funds, is now on the balance sheet. How did that come about?

Scott C. Nuttall - *KKR & Co. L.P. - Co-President, Co-COO & Director*

I'd say first on USI, it is I guess an investment investment would be the way to think about it. We have made a decision to invest some of the balance sheet capital into some longer hold opportunities. It's often referred in the market as core investing. And USI is the first of those investments that we're making. You're right, we did do that transaction in partnership with Caisse. And so that shows up for the first time this quarter on our significant investments table. You should expect that to be a long-term hold. In terms of how we will be accounting for that on a go forward basis, it's going to be equity method so we will be taking our share of the net income of USI to the earnings of the company that shows up on the balance sheet. So that will remain on the table I would guess for some period of time. And we're going to be just more broadly speaking about that strategy, we're going to be allocating balance sheet capital to that. We're not raising a fund per se, but we are going to have a couple of separate accounts alongside the balance sheet, so it will be this investment activity plus fee and carry coming from those separate accounts.

On PortAventura, very perceptive you're right, we did make a balance sheet investment in PortAventura, an asset we know and like. And alongside a partner and some of our existing limited partners who rolled into the transaction as well. So that is another large investment that showed up this quarter.

William J. Janetschek - *KKR & Co. L.P. - Member and CFO*

Chris, this is Bill. Just a little color on both. As it relates to USI and Caisse, we invested $500 million on the balance sheet, they also invested $500 million. And in that vehicle we are going to be receiving a fee and a carry. No different than a regular fund. But you could look at it really as a fund of one. As it relates to PortAventura, although that investment was executed by EIII, we offered the opportunity for our LPs that wanted to roll into the new investment. We also raised some outside capital along with the capital that we put in. And for that outside capital, we are receiving regular PE terms with the management fee and a 20% carry. So good economics on both transactions away from the balance sheet.

Chris Kotowski

Just as a follow-up, the -- you said you are going to carry USI as equity method. Is that going to show up in fee income or in which segment? Will it be in the principal investments? Where will we see it on the P&L?

William J. Janetschek - *KKR & Co. L.P. - Member and CFO*

Chris, that's a good question. It will probably show up on its own line item, but it will show up in investment income.

Operator

Chris Harris, Wells Fargo.

Chris Harris - *Wells Fargo Securities, LLC, Research Division - Associate Analyst*

Are you seeing a lot of competition out there right now for deals? It just seems like the pace of investing is still quite strong and it seems to fly in the face a little bit of what I would imagine to be a pretty competitive environment for transactions. So maybe you can talk a little bit about that.

Scott C. Nuttall - *KKR & Co. L.P. - Co-President, Co-COO & Director*

Hey, Chris, it's Scott. Look, there is definitely competition for transactions. Valuations generally speaking are pretty high. I'd say that if you look at where we're investing capital, it's really in a few places. One is kind of portfolio company add-ons where we're acting more like a strategic buyer. So a good example of that is earlier this week the Internet Brands acquisition of WebMD was really done through an existing company that we own. So where we have an angle like that, we find we are able to be competitive by acting like a strategic with synergies. The other thing, in terms of a recent theme you've seen in terms of where we're deploying capital is kind of more late cycle sectors. Health and wellness as an example. Both transactions we announced earlier this week kind of fit within that definition. So we're spending time on themes like that. Our healthcare team is particularly busy right now on the private equity front.

If you look more broadly at deployment for the firm, infrastructure continues to be incredibly active, US and Europe. So that is an area where, while there is competition, we are finding some very interesting opportunities with the contracted cash flow dynamic. And our credit areas continue to be deploying a lot of capital into the bank dislocation theme. So we are deploying capital. But if you really step back from the private equity business and look at it holistically, I wouldn't overreact to the announcements we've been making more recently. We've been selling on a global basis more than we have been buying, in particular in the US and Europe. Asia has been closer to a net deployer, but we see different opportunities there. The only other things I'd mention is we do have a view that now is a good time to be raising capital. We have record dry powder as we mentioned; a lot of cash on the balance sheet and it is a global market. So we are deploying a lot of capital in places around the world where the valuation dynamics are a bit different than what we're seeing here in the US.

Craig Larson - *KKR & Co. L.P. - MD of IR and Head of IR*

Chris, it's Craig. The one thing I'd add on that is that when people often look at our deployment and ask me about it, there's an assumption or a belief that it is, as Scott alluded to, its US private equity. And it's interesting A) when you think first recognizing that we are global firm, in the first half when you look at private equity, 75% of that was actually invested outside the US in Asia and Europe. And within private markets, private equity is 60% of that total. So when actually look at those statistics and think of US Private Equity and what percentage that's been in the first half, it's been about 15% of total private equity, of Private Markets capital deployment.

Operator

Craig Siegenthaler, Credit Suisse.

Craig William Siegenthaler - *Credit Suisse AG, Research Division - Global Research Product Head for the Asset Management Industry*

Scott, congrats on your promote. Just starting with the drop in oil prices, that didn't have the same impact on KKR's returns or the ENI results that we're expecting at some of your peers. I'm just wondering, how did you weather this latest volatility in the energy prices better than your competitors?

William J. Janetschek - *KKR & Co. L.P. - Member and CFO*

Craig, this is Bill. We probably brought this up on a call in prior quarters, but when we do our valuations for energy and when you think about energy, about 50% of what we hold is in oil and about 50% is in gas. When you look out over the forward curve and you go three years out, the drop in futures prices from an oil standpoint was less than 2%. As a matter of fact, on gas it was actually up a little. So when you run a DCF model you're not going to see much of an impact. Now clearly if you look at spot, you saw a 10% drop. Also, we've been investing quite strategically in our oil and gas properties over the last couple of years and we're happy to report that performance has actually been quite robust. That's why if you take a look at the Energy Income Growth Fund it is now actually above cost.

Scott C. Nuttall - *KKR & Co. L.P. - Co-President, Co-COO & Director*

I'd say the only other thing I'd add on, Craig, is if you look at energy exposure we have as a firm, there's absolutely -- the hedge dynamic which Bill mentioned and the forward curve dynamic, but maybe even a bigger impact, is we only have about 3% exposure to energy in private equity and a bit less than 3% in credit. So we're underweight energy and then the energy stuff that we do have has been well hedged.

Craig William Siegenthaler - *Credit Suisse AG, Research Division - Global Research Product Head for the Asset Management Industry*

Just a quick follow-up on fundraising. It looks like we should probably expect a pretty big deceleration in the second half of this year really driven by the private market side. There are a few kind of public market funds, like some of your direct originations, which you expect to raise, but is this sort of in line with your thoughts? And is there any sort of fund that we could be missing?

Scott C. Nuttall - *KKR & Co. L.P. - Co-President, Co-COO & Director*

I don't think there's a fund you're missing. I think you're right in terms of the general trend that with the Americas XII and Asia III private equity funds closing at those sizes, we don't have anything that big that's going to be closing in the second half. I think if you aggregate everything we've got that we're working on, that we still think it will add up to a very attractive number in the second half if you aggregate all the smaller funds that Craig listed off. But I think you're right as a general theme that you'd see less raised in the second half than the first. The only thing I'd say is I wouldn't overreact to what closes in any one quarter or half. As you know, with the shadow AUM we have and the capital that's going to be kind of turned on as its invested, there's a lot of opportunity to grow management fees even with what we have in terms of latent capital already raised. And then the final thing I'd say as I mentioned before, these strategic partnerships, if one of those gets done, that can move the needle as well.

Operator

Gerald O'Hara, Jefferies.

Gerald Edward O'Hara - *Jefferies LLC, Research Division - Equity Analyst*

You obviously have a sizeable amount of capital here with Asia III and you talked a little bit about writing larger equity checks in China. But are there perhaps some other themes you might be able to elaborate on as to how you might be looking to deploy some of that capital over the next 12 to 18 months?

Scott C. Nuttall - *KKR & Co. L.P. - Co-President, Co-COO & Director*

Sure, happy to take a shot. We remain busy I'd say across Asia. Japan, India, we announced a transaction in Korea this morning, Australia we've been busy. Those are just a few of the areas that I'd mention. We have quite an attractive pipeline of new deals. In terms of themes, de-conglomeratization would be a big one. We're finding in particular in Japan larger corporates looking to sell non-core subs. We've now done several of those transactions in Japan. I think you'll continue to see more corporate carveouts as a theme across the region.

Another theme I'd point you to is kind of in the more emerging parts of Asia, in particular we're investing behind food safety, environmental safety, rising middle class, health and wellness, kind of more the growth of the consumer type trends and the growth of these economies. So we see opportunities on a broad based fashion across the region and it's actually in multiple countries. So we're quite optimistic about our ability to deploy the $9 billion plus fund and generate attractive returns.

William J. Janetschek - *KKR & Co. L.P. - Member and CFO*

Jerry, just one other thing to add. Scott mentioned pipeline. As we sit here today with deals that have been signed and closed or deals which have been signed but have yet to be closed, but if you take a look at what we've got right now today in the queue, and I'm just talking about the private market side, we're looking to deploy $4 billion over the next two quarters. And when you break that down, that's coming from PE across all three regions. And embedded in that $4 billion is about $900 million in infrastructure alone. So as we sit here today, the pipeline looks pretty robust. We can't guarantee that all those transactions will close, but right now we're pretty happy with the pipeline today.

Gerald Edward O'Hara - *Jefferies LLC, Research Division - Equity Analyst*

Maybe one just follow-up for you Bill with respect to pipeline as well. In the past you've sort of mentioned or called out some pending closures that could generate future distributable earnings. I'm not sure if that's something you guys are prepared to comment on or could give a little bit of color for us?

William J. Janetschek - *KKR & Co. L.P. - Member and CFO*

Always ready for the question. As relates to monetizations, and again, where we are today on either transactions that have closed during the first 4 weeks of this quarter, or what's signed and to be closed, the cash earnings for the firm is going to be a little in excess of $200 million.

Operator

Michael Carrier, BofA Merrill Lynch.

Michael Roger Carrier - *BofA Merrill Lynch, Research Division - Director*

First one, I guess, Scott, probably for you but just given the management announcements, just wanted to get your thoughts on when the firm and the Board is thinking about kind of succession and long term planning, besides those promotions, like what else is the firm focused on? Or what other steps are being taken for the long term to make sure the firm continues on the growth path and even accelerates over time?

Scott C. Nuttall - *KKR & Co. L.P. - Co-President, Co-COO & Director*

Good question, Michael. Look, I'd say the focus is on our people. We don't make anything, it's all about making sure we've got the right people in the right seats aligned toward the right opportunities in the market. And so where we spend a significant amount of our time is making sure that we have teams that are aligned against the opportunities we have to scale the firm. And as we've talked about over the last few years, as you know, we have begun a number of businesses at KKR, probably in the last 5 or 6 years, where we see a significant amount of opportunity for growth from here. Both on an organic basis in the US and then kind of an expansion basis around the world. And potentially in some instances, strategically as well in terms of things that we can do in the market. So our focus as a firm is making sure that our people are able to use the model that we've built, that we are working as one firm on a global basis and ideas and relationships travel and that everybody is getting the help that they need to accomplish their objectives and really scale what we've started. If you look at any of the end markets that we're aligned against now, whether it's real estate or credit or infrastructure, we see opportunities to significantly grow these businesses, multiples of their current size. And that's really our focus. And the way we do that is by generating investment performance and doing a great job for the people we work for including ourselves and you. And if we do that, then those businesses will scale in time.

Michael Roger Carrier *- BofA Merrill Lynch, Research Division - Director*

Just as a follow-up, two areas that you guys probably have more history versus some of your peers is both on the Asia side and in infrastructure. It seems like there's more interest in terms of launching new products in those markets, maybe on the institutional side, allocation of more capital to both of those areas. So just wanted to get your perspective, given your history, it seems like that's going to be more of a tailwind for you, but you could face more competition. So just how you're thinking about both of those opportunities over the next few years.

Craig Larson *- KKR & Co. L.P. - MD of IR and Head of IR*

Why don't I do infrastructure first. Look, we think we are in the early innings of opportunity within infrastructure. There is an estimated $1 trillion to $2 trillion of investment required globally over the next decade to accommodate growth and repair infrastructure, so the capital needs are enormous. And as Scott had said a moment ago, in terms of KKR, we look at it as it remains a big opportunity for us. We established our dedicated infra team separate from PE in 2008, so you're right, for the better part of the last decade it's been a standalone effort for us. And as of June 30, with our two funds and SMAs, we have over $5.5 billion of AUM. And Infra has also been a significant contributor to our syndicated capital figures in Capital Markets, in particular given the size of recent transactions. We talked about Calvin Capital last quarter and we have some pending investments like Telxius and Q-Park.

The first fund was a $1 billion fund, it's full invested, performing quite well. We are investing the Infra II fund, younger fund. Investments again are performing. Second fund was three times the size of the first and not only did the fund triple in size, but the economics did improve from Fund I to Fund II as the carry rate increased. And as you heard from Calvin Capital last quarter, again, activity level there is really high. So when we look at infrastructure and think about something like Infra III, Infra II at this point is about 70% committed or invested. So I think over time you'll see us in the market with Infra III. We haven't talked about the potential size, but I know the team feels comfortable that they could certainly manage a larger fund given the opportunity set as well as the breadth of the team. And Mike, on Asia, look, I think the power you see and the result you saw through Asia III really speaks volumes. We raised the largest fund in the industry in a 7-month timeframe. We have the slide in our quarterly deck that shows the performance we've had across the Asia platform and I think the returns that we deliver on behalf of our LPs have been just exceptional. So the opportunity set is one, as we talk about the geographies and the opportunities, Pan Asia, they're all different. The local team that we have and the presence that we have and the longevity that we have in the region and in these local geographies, I think, are all differentiators for us.

Scott C. Nuttall *- KKR & Co. L.P. - Co-President, Co-COO & Director*

This is partly where the discussions we've had in the past, Mike, on distribution come in. I mean we're building relationships around the world with limited partner across different asset classes and see a significant amount of growth in both of these areas and frankly others. But if you think about the size of the infrastructure opportunity that is measured in the trillions, think about the size of the Asian markets and the pace at which they are growing and the fact that we've already gone from a $4 billion fund I going to $6 billion fund II to a $9 billion fund III, we're going to be doing multiple asset classes in Asia. Real estate credit, you'll see us expand into Asia as well, with products over time. So we see a significant amount of growth opportunity. Yes, there's always competition in what we do, but the size of the opportunity is so massive relative to the pools of capital formed around it, that we're quite optimistic.

Operator

Bill Katz, CitiGroup.

William R Katz - *Citigroup Inc, Research Division - MD*

This is Jack Keeler filling in for Bill. First question, I want to circle back to something I think Chris asked earlier and then dive into holding and core private equity. Can you first kind of talk about the opportunity you see in separate accounts for core private equity? And then second, just as a devil's advocate question, why not raise a core private equity fund? Some of your peers have done that. What leads you to focus just on separately managed accounts?

Scott C. Nuttall - *KKR & Co. L.P. - Co-President, Co-COO & Director*

I'd say in terms of the separate accounts, we'll have more to share with you over the next couple of quarters. But the way I would think about it is, you can basically think of it as just a synthetic fund in terms of what it means economically for the firm. The partnerships we're talking about creating will pay us fee and carry economics that will be similar to what you'd see in a fund format. So I wouldn't get too hung up in the semantics. What we decided to do was to do it in this basis where it's just a couple of partners and a significant amount of our own capital. As we look at the ability to drive value over the long term, we think having a lot of our money invested alongside a couple of close partners is the right approach for us for now and we'll see how it evolves in time. But I think economically for the firm, it's kind of a push relative to raising a fund.

William R Katz - *Citigroup Inc, Research Division - MD*

As a follow-up, I saw in the press release that the change in carry pool allocation has shifted to 43% from 40%, but it seems like there's some netting against previous management fee refunds. So Bill, I guess if you could maybe walk though some of the moving mechanics there and whether that should have an impact going forward on the P&L?

William J. Janetschek - *KKR & Co. L.P. - Member and CFO*

Sure, you did read the footnote correctly. The punchline is it's really about geography. The net impact is a push. So if you actually take a look at what the performance compensation was for all of 2016, that number was 43%. What we had done when we started reporting publicly is we used to actually have a separate line item called management fee refund. As well as then a 40% comp load. Those two numbers together equated to roughly 43%. It was confusing to explain to investors, and so we are just simplifying the process to exclude the management fee refund on newer funds and just go with the 43%. But again, the bottom line is there is no additional economics being paid to the KKR executives.

Operator

Mike Cyprys, Morgan Stanley.

Michael J. Cyprys - *Morgan Stanley, Research Division - Executive Director and Senior Research Analyst*

Just curious if you could elaborate a bit more on the longer duration fund strategy. It sounds like maybe bringing that out in a fund format, but just broadly speaking, how are you thinking about the strategy there? And how many sorts of these investments do you think you can do over time?

Scott C. Nuttall - *KKR & Co. L.P. - Co-President, Co-COO & Director*

Good question, Mike. I'd say in terms of how we're thinking about it, the second part of the question in terms of how many investments, I'd probably say something in the 8 to 12 type investments range over the next 5 years or so is a decent way to think about it. It's hard to predict precisely how many and when they will happen. But we are out looking for these opportunities and I'd say they largely fall in the bucket of opportunities where the return parameters are a bit lower than what you'd normally see in a traditional private equity context. It is broader than private equity. It could be infrastructure, it could be real estate as examples, could be credit. But these would be investments that we see as opportunities to hold for a very long period of time with attractive compounding characteristics. More recurring revenue in nature, not commodity exposed, just far more predictable in their general makeup.

Michael J. Cyprys - *Morgan Stanley, Research Division - Executive Director and Senior Research Analyst*

How do you think about the balance sheet component for this sort of business as you're building it out over the next couple of years? Would you expect the balance sheet to continue to take stakes in all of these particular companies? How do you see that playing out? Because it seems to be moving in a little bit of a different direction than what we had heard on prior calls where you're going to be funding it more in some of your larger private equity funds. Is this kind of in that same vein or is this just more stakes in big companies here?

Scott C. Nuttall - *KKR & Co. L.P. - Co-President, Co-COO & Director*

I would say think of it as a subset. What we've shared in the past is that we kind of think about having a balance sheet asset allocation of 40% to 50% in private equity. You will continue to see a lot of activity with us just investing in our private equity funds. That's how we're going to get a significant amount of that exposure. So no change in strategy. What we're also going to be doing though is to make up that equity exposure over time, is when we see these core type opportunities, we'll also be investing in those alongside a couple partners. So I would just think of it as there is going to be the traditional private equity funds and then some core investments as well alongside these separate accounts that I mentioned. So no real difference, just maybe slight characteristic difference within the private equity bucket between shorter term holds and longer term holds.

Operator

Devin Ryan, JMP Securities.

Devin Patrick Ryan - *JMP Securities LLC, Research Division - MD and Senior Research Analyst*

Just a couple quick ones here. So I guess first, there's been couple of M&A transactions of smaller managers with maybe nichier strategies recently. You guys have obviously done some deals in the past. And it seems scale, diversification of products becoming more of an advantage which obviously you guys have. Just curious what you're seeing out there currently. Thoughts around anything that would either add scale with maybe some expense dripping or incremental strategies that you could get into either through acquiring and also just with the contemplation that the stock price has had a nice move here, so how that may be influences the appetite at all there.

Scott C. Nuttall - *KKR & Co. L.P. - Co-President, Co-COO & Director*

I'd say in terms of the strategic acquisition potential, I think for the most part we're focused on growing organically. We've got the teams in place, we have the model built. As you can tell over the quarter, like this one and Q1, when the model is working it's incredibly powerful. So we don't feel a need to go do any strategic acquisitions to add capabilities. We do look from time to time around some of the newer businesses as to whether there's an add-on that will bring us something that we think we could build ourselves but it would take longer than we'd like. But there is nothing I'd point you to that's imminent. So I'd say for the most part you should expect us to do things organically and then if there's anything strategic, it would be more of the exception.

Devin Patrick Ryan - *JMP Securities LLC, Research Division - MD and Senior Research Analyst*

Appreciate all the detail on the infrastructure opportunity and clearly that's been a place that you guys have had a good presence and some of your peers are following. One area that is not as big for you, the insurance space seems to be an area that firms are going after in different ways and there's a lot of maybe complementary opportunities just with the types of products and strategies that some of the alternative firms have that can really relate with that relationship. So I'm curious, like is this an area that you guys are looking at doing more, if there's a strategy to go after that? Or just not, given all the other opportunities right now to raise and deploy capital is just not a big priority?

Scott C. Nuttall - *KKR & Co. L.P. - Co-President, Co-COO & Director*

Look, we spent a lot of time investing in the insurance space and the USI transaction is an insurance brokerage business as an example. I'd say in terms of capital formation, the couple of things I'd point you to. One, we are spending far more time talking to insurance companies and reinsurance companies about investing with us. So we've actually hired some people that are dedicated to spending time in that space and we're starting to see inflows into areas like credit as an example as a result of those investments that we made on the distribution side. In terms of the broader opportunity set to create affiliated companies, we do like the idea of creating permanent capital vehicles that invest with us. We've done that recently with our REIT, KREF, which just went public. We have a BDC that we've talked about that's in the process of listing. And obviously with KFN and KPE, a lot of our legacy is around creating entities that can invest in our products. So we like creative permanent capital ideas. We'll continue to look at it including in the insurance space and we'll keep you posted.

Operator

Robert Lee, KBW.

Robert Andrew Lee - *Keefe, Bruyette, & Woods, Inc., Research Division - MD and Analyst*

Just couple of quick questions. Just kind of curious, obviously you've raised a lot of capital in PE as have many of your peers who are in the process of it. One of the things given all the concerns about the ability to deploy, and I know you addressed a bunch of that, but if we get into an environment let's say where the wind blows to use a reinsurance phrase, maybe asset values start to come down, historically your PE hasn't really been as much of a distressed or opportunistic strategy. Is that evolving or changing if you look out ahead in terms of deploying dry powder, and if a more difficult environment was to come about?

Scott C. Nuttall - *KKR & Co. L.P. - Co-President, Co-COO & Director*

I'd point you to couple of things. One, if valuations come down, it's great to have $43 billion to put to work. So just from a straight private equity standpoint alone we think that will yield more opportunities for us. And part of the reason that we're pleased to be raising the capital we have been is that we're kind of getting ready if there were valuation dislocation. So that would be net good news from a deployment standpoint. We also have a distressed business at KKR that stands somewhere between $8 billion and $9 billion and our special situations area that works very closely with our private equity teams. So we have those capabilities in-house as well and if those opportunities turn into more distressed format or we can take control of a company through the debt, then we're quite equipped to do that and own several companies that we've taken control of through the debt. The other thing I would say is that we are making toehold investments in our private equity funds. So from time to time you'll see that we show up as an owner of some public securities on the equity side also as a way to get exposure to companies that over time could become private equity opportunities on a more traditional basis. So I think the way we think about it is if valuations go down, we have lots of ways to monetize that kind of environment and we're ready with the dry powder we have.

William J. Janetschek - *KKR & Co. L.P. - Member and CFO*

Rob, this is Bill. Remember, we've been investing in private equity for over 40 years. And when you look back historically, with market dislocation, at those times when we make purchases in a disruptive environment, is where we generate the highest returns.

Robert Andrew Lee - *Keefe, Bruyette, & Woods, Inc., Research Division - MD and Analyst*

Maybe one last question, just on thinking about capital management and the distribution. I know you've -- I believe you've kind of set the dividend level at roughly a level where you feel like it will take care of any tax liability for unit holders. But is there -- could you envision is you have a year or so where it feels like the tax liability would be higher that you would pay kind of a year-end popup or something to cover it? Or should we just think that you pretty much set it at a level you think is appropriate and that's that?

William J. Janetschek - *KKR & Co. L.P. - Member and CFO*

Rob, this is Bill. Right now we've set the distribution at a number to really take care of two things. One, we're comfortable in the $0.17, because if you take a look at fee income and cash expenses and then include on that the yielding assets of our balance sheet, that really covers that distribution. And so from a capital management point of view we're comfortable with that. In addition, you do point out that that distribution should cover that tax liability. Based on the numbers that we've run for 2017, we think that the distribution will certainly cover any tax liability. If there was ever an anomaly where that number would spike up, it would be something that we would look at, but I don't know if we would actually change that distribution to react to that accordingly.

Operator

(Operator Instructions). Chris Kotowski, Oppenheimer.

Chris Kotowski

Just a follow-up on the balance sheet. Two things. One is that last quarter there were two investments listed there, an oilfield service investment and a natural gas midstream investment, both around $160 million. They're not there now. Is that just because they dropped out of the top 5? Or is it that you divested them? And then secondly, you made the investment in WMIH quite some time ago, now two years. It's my understanding that's just kind of a shell company. Is there a time limit on when and how you can deploy that money, that shell?

William J. Janetschek - *KKR & Co. L.P. - Member and CFO*

Chris, this is Bill. With regard to the first question, those investments are still held by us and actually were up a little this quarter. But you are right, we are disclosing top 5, so because of PortAventura and USI which was brought up earlier, they dropped off the list. As it related to WMIH, that is its own public company and we don't really delve into the particulars around a particular portfolio company. So that's really not for us to answer.

Operator

Glenn Schorr, Evercore ISI.

Kaimon Chung - *Evercore ISI, Research Division - Senior MD, Senior Research Analyst and Fundamental Research Analyst*

This is Kaimon Chung, in for Glenn Schorr. I just had a question related to the leadership team. I just want to get some color on the departure of your head of Americas private equity. Maybe some comments on Alex's contribution to the company and maybe your plans for filling that spot?

Scott C. Nuttall - *KKR & Co. L.P. - Co-President, Co-COO & Director*

Thanks for the question. Look, I'd say on an overarching basis, Alex ran our Americas private equity business and that business is performing great. Just to give you one data point, the NAXI Fund has been up 33% in the last 12 months, so he's been a fantastic partner and leader and friend to a bunch of us in the firm for a very long time. Having said that, we do run KKR as one firm where everybody helps each other. And so we've got institutionalized processes, sourcing, value creation, overall portfolio monitoring. And as Bill mentioned, we've been in that business for 41 years. So we've got a really deep bench. 70 dedicated people give or take with 1,100 of us alongside and behind them. So the place is about more than any one person regardless of who that person is. And so we've got a lot of great people around that business, a number of partners, leading industry teams. And Henry, George and Joe have been on that investment committee. And Henry and George have been on that investment committee for 41 years and they're not going anywhere. So Alex has done a great job, but we'll keep on plugging.

Operator

Thank you. I'm showing no further questions in the queue at this time. I would like to turn the call back to Craig Larson for closing remarks.

Craig Larson - *KKR & Co. L.P. - MD of IR and Head of IR*

Nova, thanks for your help and thank you, everybody, for joining our call. We look forward to speaking with everybody next quarter.

Operator

Ladies and gentlemen, thank you for participating in today's conference. This does conclude the call. You may now disconnect. Everyone, have a wonderful day.

Editor

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