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KKR - Q1 2013 KKR & Co. L.P. Earnings Conference Call

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PRESENTATION

Operator

Ladies and gentlemen, thank you for standing by. Welcome to KKR's first quarter 2013 earnings conference call. During today's presentation all parties will be in a listen-only mode. Following Management's prepared remarks, the conference will be opened for questions and instructions will follow at that time.

I will now hand the call over to Craig Larson, Head of Investor Relations for KKR. Craig, please go ahead.

Craig Larson *- KKR & Co. L.P. - Head, IR*

Thanks Jeanine. Welcome to our first quarter 2013 earnings call. Thank you for joining us. As usual, this morning I'm joined by Bill Janetschek, our CFO and Scott Nuttall, Global Head of Capital and Asset Management.

We'd like to remind everyone that this call will contain forward-looking statements which do not guarantee future events or performance. Please refer to our SEC filings for cautionary factors related to these statements and we'll also refer to non-GAAP measures on the call which are reconciled to GAAP figures in our press release.

This morning we reported after tax economic net income per unit of $0.88 which compares to the $0.99 that we reported in the first quarter 2012. Total distributable earnings were $291 million for the quarter, up sharply from the $164 million reported for the first quarter last year. This increase was driven by the realized gains from our balance sheet which went from the $53 million we reported in the first quarter of 2012 to the $153 million that we reported this quarter.

Importantly, these realized balance sheet gains will now directly impact our first quarter distribution given the change we've announced to our distribution policy. Beginning with this quarter, in addition to the fee related earnings and realized cash carry that we've always distributed in the quarter in which they're earned we're changing our distribution policy to include 40% of the realized balance sheet income earned each quarter. This 40% is comprised of realized balance sheet gains, dividends, and interest income, less realized balance sheet losses and interest expense.

This realized balance sheet income component of our distribution will be paid out on a quarterly basis and replaces the annual additional distribution that we've historically announced in the fourth quarter of each year.

With this change in our policy we've announced a first quarter distribution of $0.27 per unit. This has the traditional fee related earnings and cash carry components which are $0.10 and $0.08, respectively, as well as $0.09 of realized balance sheet income.

And finally, before we move on I'd like to remind you of our second Investor Day to be held in New York on Thursday, May 23. We will issue a press release in the coming weeks with information on the live webcast but we'd like to invite you to attend in person. If you haven't already registered please follow up with either Sara or with me after the call. We all look forward to seeing you there.

And with that, I will now turn it over to Bill to walk you through the drivers of our performance and give you an update on netting and then Scott will discuss the environment and what we have been focused on across our different segments. Bill?

Bill Janetschek - *KKR & Co. L.P. - CFO*

Thanks Craig. We ended the first quarter with record assets under management of $78 billion, up 4% from last quarter and 26% from the same time last year. Distributions to our fund LPs in the quarter were more than offset by investment appreciation and new capital raised which is true for both our private and public market segments.

As of March 31, our fee paying assets under management were also the highest we've reported, totaling $62 billion and representing an increase of 3% and 32% from last quarter and last year. Keep in mind these numbers do not include approximately $9 billion of committed capital, over $5 billion from Asia II as of March 31, $1 billion from the Texas Teachers mandate that we have not yet allocated and about $3 billion of capital in other vehicles that will be included in AUM once it's invested.

Let me give you an update on Asia II. In April, the investment period for our first Asia fund closed and with that, our Asia II fund was activated. In our second quarter press release you will see for the first time Asia II listed on the investment summary table and this fund will officially be included in our AUM and fee paying AUM figures.

So what does this mean for our financials? Now that Asia II is turned on we are entitled to a management fee on the third party portion of that capital. Assuming that we reach a final close of $6 billion by the end of the second quarter, we would earn a fee of 150 basis points on the $5.75 billion of LP committed capital.

Additionally, when Asia II turned on, our first Asia fund switched from the investment period to the post-investment period and the management fee on Asia I is now based on invested, not committed capital. We have about $3 billion of remaining invested capital and we are now entitled to a fee of 75 basis points on that remaining capital. Simply said, the annual management fee associated with our Asian private equity funds will increase from about $58 million to $109 million starting April 1, increasing our second quarter management fees by about $13 million.

Turning to our segment results, in private markets, fee related earnings were $41 million compared to $32 million last quarter and $38 million for the first quarter of last year. We saw a small uptick in management fees compared to the fourth quarter due to the incremental NAXI capital that we closed on during the quarter.

The 5.9% write-up in our private equity portfolio combined with higher fee related earnings in the quarter translated into ENI of $267 million which is up 50% from last quarter. Our publics were up 15% in the first quarter which compares favorably to the 8% increase in the MSCI World while our private companies in our PE portfolio were up a little more than 3%.

Public markets had a particularly strong quarter. Fee related earnings were $37 million, up 26% from last quarter and almost 2.5 times the fee related earnings year over year. This quarter over quarter growth was driven by a 50% increase in incentive fees as well as higher management fees as we continue to grow our fee paying capital in this segment. First quarter ENI in this segment was $49 million and included about $12 million of accrued carry, up from $37 million and $24 million last quarter and last year.

Touching on capital markets and principal activities, fee related earnings were $10 million in the quarter, down from last quarter and last year. This decline was caused by lower transaction activity. However, we had strong first quarter ENI in this segment of $332 million driven by the appreciation of our balance sheet assets.

Turning to our balance sheet, in the first quarter our balance sheet investments appreciated 7% and unrealized carry increased 25% to $935 million, continuing the strong balance sheet growth we saw in 2012. Our book value per unit of $9.89 though was relatively flat from last quarter since we paid our fourth quarter distribution of $0.70 per unit or about $500 million back in February.

And now, on to netting -- we told you on our call in February that the size of the netting hole in Europe II was about $500 million and as of March 31, the netting hole increased to $700 million due to a couple of write-downs in our European II portfolio. That said, with the sale of BMG in April, our European III fund will be paying out cash carry and in the second quarter we expect to distribute $0.02 per unit from this transaction.

Turning to the 06 fund, at the time of our last earnings call the size of the 06 fund domestic netting hole was about $275 million. The HCA secondary offering we completed in February combined with the Dollar General secondary offering that we executed in early April filled the netting hole based on March 31 valuations and produced $500 million of excess gain so we expect to pay out over $100 million of gross carry or about $0.09 a unit net of the carry pool from the 06 fund as part of our second quarter distribution.

In total, by filling the 06 fund netting hole we currently have about $30 billion or over 80% of our private equity remaining fair value in position to pay carry and benefit our distribution.

To give you a sense of our progress here we first talked about netting holes on our earnings call a year ago. At the time the netting hole in the 06 fund was $1.5 billion. In total, we had about $10 billion of private equity value in position to pay cash carry. Twelve months later we have filled the netting hole in the 06 fund in its entirety and again have $30 billion of private equity remaining value in position to pay cash carry, almost triple what it was a year ago. As of today, away from Europe II, annex, and China growth, all of our other private equity funds are now in position to pay cash carry.

I'd also like to touch on our distribution. As Craig mentioned, our first quarter distribution is $0.27 per unit. We will continue to pay out cash carry and fee related earnings quarterly as we have done historically and in the first quarter those two totaled $0.18 of the $0.27.

In addition, we are now including 40% of realized balance sheet income that we earn each quarter in our distribution policy. We decided to make this change this quarter and as a result, $0.09 of the $0.27 in our first quarter distribution will come from realized balance sheet income. We will continue to report the earning streams that make up our distribution so you can clearly see the breakdown of earnings that we generate from our overall enterprise and how it affects all of us as shareholders. We believe this new, simpler approach to our policy will help to directly align our quarterly distribution with balance sheet performance while still allowing us to retain significant capital to invest in our business.

One final piece of good news as we look towards the second quarter distribution, based on transaction activity to date in the second quarter we have already realized a good amount of cash carry through the Dollar General and BMG sales as well as the Pets at Home recap in Europe III. We also announced the sale of Intelligence which is in our Asia fund and is expected to close in the second quarter. From these transactions alone we expect to have approximately $0.18 of cash carry in the second quarter distribution which would be the highest quarterly cash carry figure we've had since being public.

With that, I'll now pass it over to Scott.

Scott Nuttall - *KKR & Co. L.P. - Global Head of Capital and Asset Management*

Thanks Bill. I want to give everybody a quick update on how we feel about our progress one quarter into the year.

The way that we look at it we have several jobs we need to do well to generate performance for our investors and shareholders. We need to be thoughtful around our deployment of capital. We have to generate strong investment returns including exits generating cash back to our fund LPs and carry. We need to scale our newer businesses and we have to put our balance sheet to work in high ROE opportunities.

Let me give you a quick update on each of these. This is a really interesting time in that we're finding good opportunities to both deploy capital and exit investments. On the deployment front in the first quarter we closed or announced six new private equity investments and a handful of follow-ons with total committed equity from KKR of about $2.3 billion. The transaction activity was global with deals in the U.S., Europe and Asia and we've also been busy in our originating credit businesses, in particular direct lending and special situations.

On the exit front, we had several monetizations. We had a secondary, Jazz Pharmaceuticals, at approximately four times our cost. We did secondaries at HCA, Nielsen and Dollar General at 3.2 times, 2.1 times, and 5.5 times our cost and we announced strategic sales of BMG in Europe for 1.8 times and Intelligence in Japan at 5.4 times our cost. Together, these exits helped contribute to the $4 billion in actual and expected distributions to our private equity investors so far this year and filled the netting hole for the 2006 fund. In addition, they generated $0.08 per unit of carry distribution in Q1 and are expected to generate $0.18 of carry so far for Q2.

Turning to performance, our private equity funds were up 19% over the last 12 months and our credit and hedge fund businesses had a strong start in 2013, continuing their top quartile performance. In addition, our balance sheet investments were up 7% in the first quarter.

Another focus has been building the businesses we've started. Here we continue to see progress. In private markets with the closing of the second Asian private equity fund, our fee paying assets in Asia private equity were more than double from $4 billion to nearly $9 billion. Our energy and infrastructure business now oversees $5 billion of assets, up from $2 billion two years ago and since launching a dedicated real estate platform, we've committed over $650 million of equity to ten transactions with a balance sheet representing about half the capital to date.

We've also seen real progress in public markets. Our credit fee paying assets have grown 35% year over year to $12 billion. Prisma's assets have grown from $7.8 billion when we announced our acquisition to nearly $9 billion and our total public markets fee paying assets have grown from $9 billion to $21 billion including Prisma over the last year with profits up materially.

Critically, our balance sheet investments continue to perform. The balance sheet is up 30% since the beginning of 2012. As you know, we use the balance sheet to seed new businesses, invest alongside our fund LPs in everything that we do, support our capital markets business and make acquisitions and strategic investments and the balance sheet is generating real cash flow with over $850 million of cash income and gains last year and $153 million in the first quarter of 2013.

The continued performance in the balance sheet has given us the comfort to make a quarterly distribution out of the net cash income that we generate so as Bill said, going forward we're going to be paying out 40% of all net investment income and realized gains off the balance sheet on a quarterly basis as earned. So now all of us as shareholders can calculate the distribution with more precision as under our policy it will be 100% of all after tax fee related earnings, 100% of all net cash carry and 40% of all net realized investment income and gains every quarter.

So we feel like we've had a good start to the year. Total distributable earnings were up 75% year over year in the first quarter. We filled the netting hole for the 2006 fund and we've tripled our cash carry paying private equity assets from this time last year. We already expect to generate $0.18 of cash carry for the Q2 distribution and retroactive to January 1 we're changing our distribution policy to make a quarterly distribution of 40% of our balance sheet income so everyone can participate in the balance sheet upside with more frequency and clarity.

Thanks for joining our call. We're happy to take your questions.

QUESTIONS AND ANSWERS

TRANSCRIPT

Editor

(Operator Instructions)

Operator

The first question is from Robert Lee of KBW. Please go ahead.

Robert Lee - *Keefe, Bruyette & Woods - Analyst*

Thanks for the update and I appreciate the change in the distribution policy. Just a quick question, first thing, simple one is can you just update us on where NAXI is? Is it still fundraising or was the last raise the last close or are you still kind of out there with that fund?

Scott Nuttall - *KKR & Co. L.P. - Global Head of Capital and Asset Management*

NAXI is still fundraising. We're at about $7.5 billion give or take as we sit here today and we expect to wrap up fundraising sometime in the second half but we're still in the market.

Robert Lee - *Keefe, Bruyette & Woods - Analyst*

Okay great and maybe just going down the fundraising path, I know you've got multiple irons in the fire but I guess the first thing is can you, your number one, with the good inflows in the quarter into the public markets, how much of that came from Prisma? How much has that added to the organic growth and then secondly, if you could maybe call out some of the strategies where you see where you're really focusing on in the markets right now and you think there is pretty good fundraising momentum aside from Asia and maybe update us on real estate progress.

Scott Nuttall - *KKR & Co. L.P. - Global Head of Capital and Asset Management*

Bill, you want to take this first one?

Bill Janetschek - *KKR & Co. L.P. - CFO*

You're referring to page 16. We raised about $1.5 billion in public market segment alone in this quarter and that is a combination of capital that we raised at KFN of about $500 million, about $400 million from Prisma. We also raised about $400 million from CCT which is that BDC that we launched about a year and a half ago, and about another $350 million in SMAs but as you point out, NAXI was still fundraising from now until the second half of 2013. We hope to hit our hard cap in Asia by June 30 of '13 and then on a public market side, we have plenty of venues on which we're trying to raise capital. We launched two mutual funds at the end of 2012 and we're continuing to raise a modest amount of capital in that strategy and as we mentioned on a prior call, it's early days on that and we're not expecting anything big from that but we hope that will ramp up over time.

We're also raising capital still for a special situations fund and is there anything else that we're, that we've got open funds on on public markets, Scott?

Scott Nuttall - *KKR & Co. L.P. - Global Head of Capital and Asset Management*

No, I'd say those are the big ones. We continue to raise capital around some of the liquid strategy and high yield end loans but I think Bill covered the big ones. I think on your question on real estate, Robert, we have been doing the deals that I mentioned off the KKR balance sheet and the KFN balance sheet basically in partnership. We will here be creating a real estate fund. It's not going to be our typical long fundraise. I think that we'll club together a group of investors, drop some of those investments down into the fund to seed with some of these investments that we've made with a portion of what we've deployed off the balance sheet but it's very early days on that. We'll give you an update in future quarters.

Robert Lee - *Keefe, Bruyette & Woods - Analyst*

Great, thanks for the update.

Operator

Thank you. The next question is from William Katz of Citigroup. Please go ahead.

William Katz - *Citigroup - Analyst*

If you look at the margin of the business, on the fee related margin, that improved pretty nicely sequentially. How much of that was just seasonal factors versus a more sustainable level?

Bill Janetschek - *KKR & Co. L.P. - CFO*

Bill, if you're referring to page six in fee related earnings you can see our margins are about 40% which is up a little and when you take a look at these three quarters just as a snapshot, none of these were what I would say quarters where we had significant activity like a quarter where we had the Samson transaction close in the fourth quarter of 2011 so I would say that this is more or less what we should expect more or less on quarter to quarter basis. To the extent that we have significant transaction activity in a particular quarter you will see those margins increase. However, in a quarter where we don't have any transaction activities, you might actually see margin decline.

Scott Nuttall - *KKR & Co. L.P. - Global Head of Capital and Asset Management*

I would say, Bill, the way I would look at is there tends to be a higher flow through margin on incentive fees and transaction fees. We had a decent incentive fee quarter so the margin is up a bit as a result of that so part of it I would say is due to that dynamic but I also say part of it, frankly, is that we're starting to get scale on some of the expenses that we put into the ground on these newer businesses and so I'd say some of it is sustainable and part of it is just due to the good incentive fee quarter.

Bill Janetschek - *KKR & Co. L.P. - CFO*

Bill, just one other point, if you take a look on operating expenses you can see that they have been somewhat lumpy when again you're just looking at a snapshot of these three quarters. The fourth quarter of 2012 was higher than what you would think as a run rate number only for the fact that in that particular quarter we had a halfway decent amount of broken deal expenses. You can see that in the first quarter that number is about $44 million and I would expect that if you want to try to think about how to model this out it would be in that probably $40 million, $45 million range over the next few quarters barring any unforeseen write-offs in a couple of deals that we're chasing where we get close and rack up a halfway decent amount of broken deal expenses but don't actually close on it.

William Katz - *Citigroup - Analyst*

Second question is I think, I was writing down as quick as I could, about $400 million of net business from Prisma? Maybe just sort of stepping back, what is your sense for capacity and opportunity in that platform now that you've had it another quarter of integration?

Scott Nuttall - *KKR & Co. L.P. - Global Head of Capital and Asset Management*

I'd say, Bill, we feel very good about capacity both in the existing vehicles that they manage and also some new product ideas that we're working on and so I think there is a significant amount of running room there. There are some other competitors in the customized hedge fund solution space that manage significant capital, $20 billion plus and I think given our strategies, if we can keep our top quartile performance and they've done a great job both before the acquisition and since on the performance front but if we can sustain that, we think we have a significant opportunity to continue to scale the business.

William Katz - *Citigroup - Analyst*

And just one final one, just a clarification. Bill, you mentioned earlier that the delta between Asia I moving over to the monetization period and then Asia II kicking in is a plus $13 million in terms of management fee income? Did I hear that correct?

Bill Janetschek - *KKR & Co. L.P. - CFO*

Yes, so it's management fee income so about $13 million per quarter.

William Katz - *Citigroup - Analyst*

Per quarter, okay, perfect. Thanks for taking all my questions.

Operator

The next question is from Michael Carrier of Bank of America. Please go ahead.

Michael Carrier - *BofA Merrill Lynch - Analyst*

Just on the distribution, just wanted to get a sense in terms of your thought process on when you think about the payout, the fee related earnings makes sense, the cash carry makes sense. In terms of the 40% of the balance sheet, why the 40% and then going forward over time do you feel like those investments -- Scott, you mentioned in terms of making sure that you're investing for an attractive ROE, if that starts to slow, can that payout tick up? Just wanted to get your thought process around why the 40%?

Scott Nuttall - *KKR & Co. L.P. - Global Head of Capital and Asset Management*

I'd say we look at it obviously in the individual pieces of how we articulate the distribution policy but frankly, we also keep an eye on the overall payout ratio that is implied by the aggregation of how we payout our earnings so when you really add it up it's 100% of fees and carry and 40% of the balance sheet gains and that equates to approaching 70% of all of the cash earnings of the fund and so another way to look at it is we're kind of almost at a 70% payout ratio given the mix of our earnings as it has been historically anyway and so that is something we kept an eye on.

I'd say the other thing that we looked at is the uses of capital that we retain because obviously that implies that we're retaining 60% of the income and profits and we feel really good still today about how we're deploying that capital and the ROE that we're generating on it. As you know, we've been seeding new businesses and investing behind everything we're doing but with Prisma, with Nephila, we're starting to use the balance sheet for more strategic activity as well and so what I would say is that's the number that we feel good about right now. We think 70% is a very high payout ratio, frankly, which is about where this ends up and I think you'd expect us to stick with this for the time being. If the analysis changes of course we can change it but this is the distribution policy that I think you should think about at least for the near to intermediate term.

Bill Janetschek - *KKR & Co. L.P. - CFO*

Just keep in mind, when you think about the return on our balance sheet, for 2012 that was 24% for the year. The balance sheet is up now another 7% and that is just earnings off the balance sheet. That really doesn't take into account as we're launching new platforms and raising third party capital the benefit that we get from additional fee related earnings in the overall business as well so again to Scott's point, to the extent that we feel comfortable in using that capital to deploy in strategies where we think we're going to get a high return on investment we're going to continue to do that.

Michael Carrier - *BofA Merrill Lynch - Analyst*

Okay, makes sense. And then maybe just on the public market side, I guess two questions there. The incentive fees, obviously stronger this quarter, just wanted to get a sense of there has been a lot of changes whether it's with Prisma, the stake in Nephila, some of the products that you've launched, what should we think about in terms of driving that line? And then same thing on the carrier, the incentive fees and then the carried interest, when we think about the AUM that is in that segment, what portion, should we be thinking about more in line with the PE business versus something that won't have the same upside on the fees?

Scott Nuttall - *KKR & Co. L.P. - Global Head of Capital and Asset Management*

I guess a fairly simple way of breaking it down in terms of what goes where, more the hedge fund type economics plus KKR's financial incentive fee tends to flow through the incentive fee line so when you think about what's in there, it's Prisma, it's the equity long/short vehicles, it's the KKR financial incentive fee and other hedge fund type products which tend to be more high watermark than claw-back type in nature, will go into the incentive fee side and then the carry calculation that you see in the segment reporting kind of further down the schedule there, that tends to be more the fund products so think of the Mezzanine fund, Special Situations funds that have more typical private equity fund format so those would be more the locked up pools of capital that would fall into that part of the income statement.

Bill Janetschek - *KKR & Co. L.P. - CFO*

And to help you with the numbers that Scott just walked you through, if you take a look on page 17 you can see public markets. That lists out the committed funds that we've got which have more what I'll say are traditional private equity-like model where we're entitled to a profit participation and again you'll see that flow through in that line item in the public market segment and up on top again with the incentive fees. That is going to be KFN. It's going to be KES. It's going to be Prisma and it's going to be Nephila.

Operator

The next question is from Michael Kim of Sandler O'Neill. Please go ahead.

Michael Kim - *Sandler O'Neill & Partners - Analyst*

First just to follow up on the shift in distributions, in the past you've talked a fair amount about the returns that you've been able to generate off the balance sheet and retaining capital to continue to build out the footprint and I understand you're still retaining 60% of the related income to earmark for those initiatives but does it also suggest maybe that you feel like you've got more of the pieces in place as it relates to kind of the broad evolution of the franchise, if you will?

Scott Nuttall - *KKR & Co. L.P. - Global Head of Capital and Asset Management*

I would say there is certainly some truth to that. I think we've clearly built out the platform materially over the course of the last two to three years and so some of it is a reflection of that but I'd say also it's 40% because we still see a lot of opportunities for growth and so we're trying to find the right balance but I think the other thing to think about is some of the legacy investments off the balance sheet, the private equity investments that were part of the legacy KPE balance sheet are becoming more liquid and so it's a combination of all of that that had us settle into this as a distribution policy. I'd say we are starting to get some scale on the newer businesses but one thing that we see as a big opportunity is that we manage today about $30 billion of non-private equity assets which gives us a pretty small market share, frankly, in those markets given how big they are but we see a significant amount of growth opportunity against that $30 billion but a lot of that $30 billion is in the U.S. so if you look at the firm's global footprint we see opportunities to scale the non-private equity businesses as we scale the private equity on a global basis.

I'd say it's a balanced perspective. We started to get good traction on these newer businesses and have a lot of runway.

Bill Janetschek - *KKR & Co. L.P. - CFO*

And Michael, when you think about where we were a year ago, our cash balance was down compared to where it is today and we also had a lot harder commitment in funds where we had the legacy KPE LP commitment and so if I go back probably a year ago, the hard commitments as well as the soft commitments we made to energy and real estate were probably $1.6 billion, $1.7 billion. That number has actually now come down to a little under $1 billion so if you were to turn to page three, you'd still say that we've still got what I'll say are hard commitments of about $650 million plus we've also got very hard indications of interest in our real estate and energy platform of about another $200 million so that's where I'm getting the $1 billion.

That being said, our cash balance is up and so we're at a point right now where we feel comfortable as we look out over the next year going with a 40% distribution on realized investment income off the balance sheet.

Michael Kim - *Sandler O'Neill & Partners - Analyst*

Okay that's helpful and then second, as you continue to build out your investment capabilities across the new strategies and geographies, is there an opportunity to maybe offer LP as sort of a multi asset class fund that maybe has a broader mandate? Do you feel like there is demand for that type of strategy that is more flexible and might offer more of a shorter timeline relative to sort of a traditional PE fund?

Scott Nuttall - *KKR & Co. L.P. - Global Head of Capital and Asset Management*

I think there are a lot of interesting opportunities like that, Michael, that come out from having all of these capabilities under one roof and we have done this with some institutional investors where we'll create multi product relationships where we do a lot of different things in one wrapper but I do think there is an ability to create over time kind of a KKR multi-strat capability and series of products for different investor types so that's one of the ideas that we're working on from a new products standpoint and are talking selectively to some of our limited partners about doing things like that with us.

Operator

The next question is from Howard Chen of Credit Suisse. Please go ahead.

Howard Chen - *Credit Suisse - Analyst*

Scott, you gave some really helpful updates on fundraising, deployment and harvesting and I was hoping you could discuss a bit more on what you're seeing across core portfolio company fundamentals and maybe some of the other real time data that you all look at in shaping an outlook?

Craig Larson - *KKR & Co. L.P. - Head, IR*

Hey Howard, it's Craig. Why don't I take a crack at that? When we look at the growth in the portfolio and we do this really on an NAV weighted basis and the data when we begin to look at it is about a month lagged so it's February 2013 versus November 2012 and we haven't really seen a change in that LTM EBITDA growth profile so when we look at EBITDA growth in North America and Europe, across the portfolios it has remained in the mid to high single digits. It is meaningfully higher than that across Asia which frankly you'd expect given the more growth oriented nature of these investments and also frankly the strong performance we've seen in our highest NAV businesses there. When you blend all of that together we haven't seen really any change in the overall growth profile within the portfolio companies.

Scott Nuttall - *KKR & Co. L.P. - Global Head of Capital and Asset Management*

The only thing I would add, Howard, I would say the U.S., I agree with Craig's characterization. There hasn't been a real change. It is kind of more of the same globally. U.S., the recovery continues to be pretty uneven. There are some sectors where we're seeing recovery like autos, housing, energy, manufacturing but it's a slow growth overall. Europe, the economies obviously are struggling. Asia has got better growth. It's still a bit uneven but overall, the economic backdrop for our companies is pretty much what we've articulated the last couple of quarters and yet we're really pleased that the portfolios themselves, of the companies themselves, have been able to keep growing revenue and have good flow through down to the bottom line so more of the same but hopefully that color is a little helpful.

Howard Chen - *Credit Suisse - Analyst*

That's really helpful. Thanks Craig and thanks Scott. And my follow up, the harvesting activity has been fairly balanced between equity offerings, strategic sales and other forms of monetization like dividend recaps. Do you have any point of view on how you see that balance of realizations evolving or changing?

Scott Nuttall - *KKR & Co. L.P. - Global Head of Capital and Asset Management*

Very hard to predict. I would say we're pleased that there has been more strategic exit activity recently which is something we've talked about in the last couple of calls. It's hard to predict how many of those are actually going to get done so we were pleased that a couple did get done and it's been global so that makes us feel good but I would expect that we are going to continue to see a mix of the three with frankly more on the public exit side and strategic exit and then selectively some dividend recaps from time to time.

Bill Janetschek - *KKR & Co. L.P. - CFO*

And just to give you a little color on our public positions in private equity portfolio, right now that stands at about 25% so if you take a look at the $36 billion of fair value we have in the private equity portfolio, about 25% of that is public so we still have that as an exit opportunity.

Operator

The next question is from Patrick Davitt of Autonomous Research. Please go ahead.

Patrick Davitt - *Autonomous Research - Analyst*

I want to focus on the energy and infrastructure. It looks like you've kind of characterized all of those strategies as various commencement date and end date so should we assume that those are just kind of always in fundraising mode and is there an opportunity to maybe raise a larger, more traditional type fund with a solid commencement date and end date in those strategies?

Scott Nuttall - *KKR & Co. L.P. - Global Head of Capital and Asset Management*

Just to be clear, what falls in the energy and infrastructure portion of page 17 there where we list the funds, that is the non-private equity assets in energy and infra but just to be clear, there is additional energy activity happening up in the private equity section but it's a good question. What you'll see there is a mix of funds and separate account activity and so on the funds side, you can see what is listed there, the Natural Resources fund and the Infrastructure fund. Those are going to be more traditional, kind of locked up capital, multiple investors in those vehicles and then also frankly in the same vein, we talked about the Energy Income and Growth fund that we're in the market with now. That would also kind of ultimately when raised show up in this section and be more traditional fund format.

To your question on the continuous fundraising, the answer is yes. We see such a large opportunity to deploy capital in the energy space and frankly a pretty interesting supply/demand dynamic that we will I would guess continue to be raising separate accounts for different elements of our energy strategy which is kind of aggregated as you see it there under this global energy opportunities heading and then there is co-investments as well so I think you'll continue to see activity in both funds, separate accounts and co-invest.

Patrick Davitt - *Autonomous Research - Analyst*

Okay, that's helpful. And just a follow up on your comments on the distribution in the second quarter, I wanted to confirm that that $0.18 number does not include the associated balance sheet gain.

Scott Nuttall - *KKR & Co. L.P. - Global Head of Capital and Asset Management*

Correct. That is just cash carry.

Patrick Davitt - *Autonomous Research - Analyst*

Just cash carry. Okay great, thanks guys.

Operator

The next question is from Matt Kelley of Morgan Stanley. Please go ahead.

Matt Kelley - *Morgan Stanley - Analyst*

Just one more question on the distribution policy from me. When you guys think about this, over time as the balance sheet gets deployed potentially in more kind of fee earning assets or some of the hedge fund businesses that you've been more active in, I wanted to get a sense for what you guys think and what your unit holders are asking you when you come up with this new distribution policy. The migration would seem naturally to be more towards a higher payout ratio than what you're talking about now over time, just from the natural migration of that business. Am I thinking about that right and is that what your shareholders are asking you for over time as well?

Scott Nuttall - *KKR & Co. L.P. - Global Head of Capital and Asset Management*

I'd say the way that we think about it, Matt, is that we would expect the balance sheet which as you know, what largely a private equity heavy balance sheet just given the legacy of the KPE platform, was to invest in our private equity funds and deals. I'd say that the balance sheet over time will begin to look more like the makeup of the firm's assets under management which are more diversified, as you know, across credit, hedge funds, real estate, etcetera, over time and so I'd say we're going to see a migration from what was a 90% plus private equity balance sheet to something less.

As part of that migration, if you think about it, just about everything that we do except private equity has either a current yield associated with it or liquidity and so one of the things that we're doing with this policy is as the current yield or investment income and dividends off the balance sheet increases, as we redeploy that capital into these other strategies we're going to be paying out 40% of that as well through the distribution so it'll be not just gains but it will also be that investment income and dividend component will also get paid out.

I think what you're hearing from us today is that we're repositioning that distribution so everybody can participate in that on a quarterly basis and then we'll share with you how much is coming from realized gains versus kind of more predictable ongoing investment income as that capital gets redeployed.

I think as we talk to our shareholders, what they're focused on is making sure that we have good uses for the capital and making sure that we are deploying that properly and that's why we emphasize so much the return on equity that we're getting for the overall firm and the return that we're generating off the balance sheet itself and keep in mind we continue to own nearly two-thirds of the stock as folks here at KKR so we're very focused on that as well as shareholders and frankly, we remain the largest shareholders in the Company so trust me, it gets a lot of focus internally here too.

Matt Kelley - *Morgan Stanley - Analyst*

Thanks Scott, that's helpful. And then second from me is I was hoping you could give us an update on LPs and your cross-sell because there has been a lot of change and additions, moving parts to the business as you indicated so I'm just wondering if you can tell us kind of how many LPs you have now, how many of them own multiple products and if there is any sort of subset that can't own multiple products just based on what they can kind of invest in?

Scott Nuttall - *KKR & Co. L.P. - Global Head of Capital and Asset Management*

Sure, I'd say roughly we have 580 or so LPs. It's somewhere between 575 and 600 today. We have, the cross-sell, it's about an average of 1.7 products per LP and there is a little pressure on that number, frankly, because if you add the number of LPs in one product it obviously pushes down the cross-sell metric but it's about 1.7 so we've seen the number of LPs continue to increase. We've seen that cross sell metric continue to increase and that has been on a global basis across all the different regions we cover and so we've been pleased that we continue to make progress there.

Having said that, we've got a lot of opportunity for growth. I think we had talked about kind of when we started this journey in terms of building out our distribution capability, getting from kind of the 250, 300 investors we had not that long ago to 1,000 plus and we're working our way toward that. I don't think we have many LPs that can only invest in one product. I'd say some kind of by virtue of their mandate are focused on just a handful of things that we do but one of the things we also look at, if you look at our top clients in terms of the ones that have the most capital with us, the biggest investors that we have, they tend to be in between three and four products or more and so when you segment it by size of relationship you can see those cross-sell statistics move up materially so we know what's in the realm of the possible. We have some that are in five plus different things that we do and so I think we can continue to make progress at that end and see the overall average blend up as well.

Matt Kelley - *Morgan Stanley - Analyst*

And then one last one from me, is there any color you can give us on the early returns that you are going to be able to market for your real estate fund? I don't know if you can talk about that or not but just any sort of incremental data or directionally on how the real estate investments have done thus far?

Scott Nuttall - *KKR & Co. L.P. - Global Head of Capital and Asset Management*

Hard to give you any return numbers, Matt, but I would tell you that thus far we have been really pleased with the investments we've been able to make both in terms of different types of investment, different types of opportunistic and value add real estate and so far we're quite pleased with the results.

Bill Janetschek - *KKR & Co. L.P. - CFO*

And Matt, keep in mind that Scott referred to the over $600 million of commitments that we made through the real estate platform, half of which is coming from the balance sheet. Of that we've only invested approximately about $150 million and it's really early days. The first investment we made was only probably six months ago.

Craig Larson - *KKR & Co. L.P. - Head, IR*

And one final thing on that, Matt, Ralph Rosenberg, who runs that business for us is one of the folks who is going to be, is on the schedule for Investor Day so certainly in terms of trying to get a sense of the types of investments that the team has made and how that has been integrated across the whole franchise, I think there is actually going to be a lot of color and perspective that will be helpful on May 23.

Operator

The next question is from Chris Kotowski of Oppenheimer. Please go ahead.

Chris Kotowski - *Oppenheimer & Co. - Analyst*

I'm looking at page 17, the schedule of investments and as you noted, it was a productive quarter in terms of realizations but I'm trying to figure out how that translates into the carry and specifically what I'm looking at is the Millennium fund where last quarter you had $7.9 billion of realized value in that fund and that went up to $9.15 billion so you had an increase or realizations of over $1.2 billion and if you take 20% of that you would have thought it would generate somewhere around $250 million of carry and instead there was $88 million so what am I missing? Is there an offset or a markdown against that?

Bill Janetschek - *KKR & Co. L.P. - CFO*

Sure Chris, the offset is cost. The realized takes into account the cost plus the profit on an exit of a particular investment and so you can't just take the realized at 20%. You'd actually have to have the information and you don't on this table but you could actually figure it out of the difference between what the sales proceeds were minus the cost and that gain at 20% pre-the 40% carry pool, would actually flow through the ENI.

Chris Kotowski - *Oppenheimer & Co. - Analyst*

Okay, but you're already over, you've returned more than 100% of cost. Is it still on an investment by investment basis or is it against the whole fund?

Bill Janetschek - *KKR & Co. L.P. - CFO*

Sorry Chris, I wasn't as clear as I could have been. It is investment by investment. We don't have a European-type fund where you have to return all costs and then anything beyond that is gain and we share in the profit participation. It's on an investment by investment basis.

Chris Kotowski - *Oppenheimer & Co. - Analyst*

And then as a follow up, as I said, there were $1.2 billion of realizations there and only about $400 million in the 06 fund. Does that mean that the funds do not sell the investments on a ratable basis always or how does that work?

Scott Nuttall - *KKR & Co. L.P. - Global Head of Capital and Asset Management*

Actually, if they were in the same investments they would sell on a ratable basis but Millennium and 06 are largely invested in different companies and so there will be some carryover investments like HCA so that's probably what you're seeing there is the HCA would be a good portion of the 06 number and part of the Millennium number but there were several other exits in the Millennium Fund like Nielsen and Sealy and Jazz that are just in Millennium and not in 06.

Bill Janetschek - *KKR & Co. L.P. - CFO*

And the other point on that, Chris, if you think of, if you were thinking of Dollar General, that was a transaction that did price in March but it actually closed in April so when Bill ran through the carry numbers that will be in the second quarter, that actually would have included Dollar General again in the second quarter as opposed to the first.

Chris Kotowski - *Oppenheimer & Co. - Analyst*

And then just a general, I guess I'm curious about both Asia and Asia II. I'm curious, roughly how much of that portfolio is invested in Japan if you can disclose that and does the existing portfolio get a lift from what is happening there now and does it make you more likely or less likely to invest a greater portion of Asia II in Japan?

Bill Janetschek - *KKR & Co. L.P. - CFO*

Chris, we generally don't comment on portfolio by portfolio Company data in a particular fund but being that you are directly asking in the Asia fund do we have any investments in Japan? At the time we only had one and as Scott mentioned, we signed an agreement to sell that portfolio company at roughly 5.5 times our money and we expect that to close over the next couple of weeks. Once that sale takes place we will then currently not have any investments in Japan although we see a lot of opportunities in Japan and we've got a dedicated team looking at investments daily.

Operator

The next question is from Marc Irizarry of Goldman Sachs. Please go ahead.

Marc Irizarry - *Goldman Sachs - Analyst*

Scott, I was wondering if you could just give us an update on your strategy and high net worth in retail and specifically, can you talk about the fees that we should sort of think about when you're innovating in those areas and also the amount of KKR capital that you sort of intend on a fund by fund basis to commit there?

Scott Nuttall - *KKR & Co. L.P. - Global Head of Capital and Asset Management*

High net worth in retail, there are a variety of different things that we're doing. I'd say our strategy has a few different elements to it. One is that we are building relationships with different platforms so we will work with different groups that have high net worth franchises and we'll create product with them and then market to their high net worth investors and so a lot of what we're doing is through those platform relationships.

The other thing that we've done is we've built a direct high net worth team at KKR and so we are calling actively on high net worth individuals and family offices and that has actually worked quite nicely in that we have found we can build relationships with those individuals that will bring us deal flow so there is a nice synergy back into the deal side of what we're doing at the firm but that's the second element of the strategy.

A third element is that, we have talked a little bit about this corporate capital trust, the CCT business development company that we've created in partnership with CNL. We are marketing that to individuals through the independent broker dealer channel and so that vehicle is now over $1 billion of fee paying assets.

And then on top of those we have created and launched two vehicles -- one is a high yield mutual fund and one is basically what they call an interval fund. It's more of a closed end fund that invests in the liquid portion of our special situations business and then in addition to that, we've filed for two new vehicles. One is for a Prisma multi manager product that could be sold to retail investors and another is a closed end fund that would invest across things we're doing in our credit platform.

So there are a variety of different distribution relationships and products that we're creating for individuals and as I said in the last call, it's relatively early days across a lot of this. We are still learning in these channels, whether it's the registered investment advisor channel or the IBD channel or high net worth where we have a little bit more experience. Just to dimensionalize it for you, last year we raised about 15% of our capital from these different individual investors across these different relationships and channels and so I think that number can continue to move up over time as we create new product and build more relationships.

In terms of fees, it really varies. Some of these will be 1.5 and 20 type products. For example, if we're marketing any of our private equity funds through a platform at a big bank we'll tend to get full economics on that and that will range all the way down to our high yield mutual fund which will be much more market based, call it 50, 60, 70-type basis point product with no carry attached so it really runs the gamut.

In terms of KKR capital, to your last question, I'd say that varies as well. The private equity fund type structures tend to be our traditional 3% to 5%, KKR capital alongside, but what we have done in some of these retail products is we've actually seeded the investments off the balance sheet so we put, when we launched the two products on the Schwab platform last year we put about $125 million of total capital off the firm's balance sheet into those to get them started and that number can come down over time as third party capital is raised.

So long answer to a short question but there is a lot of activity and I'd say we're still in the early days of continuing to build out the effort.

Marc Irizarry - *Goldman Sachs - Analyst*

And then just one quick one, Bill, for you. In the public markets segment, the AUM growth, if you look sequentially at that versus the management fee growth outstripped the AUM growth and the fee paying AUM growth by a big margin. What is that related to? Is it mix of funds or is there something that we're missing there?

Bill Janetschek - *KKR & Co. L.P. - CFO*

No, you're not missing anything and it's a good point and it has everything to do with the mix of capital that was raised. As I mentioned earlier in the $1.5 billion was $500 million of capital raised from KFN which actually paid a 1.75% fee so when you have something like that come in, you're going to see the overall percentage go up.

Operator

The next question is from Aaron Teitelbaum of Surveyor Capital. Please go ahead.

Aaron Teitelbaum - *Surveyor Capital - Analyst*

I just had a quick question. In the past, this is in regards to the new distribution policy and it's probably directed at Bill but I believe in the past you've paid tax distributions off your balance sheet and I'm just trying to understand a little bit better the implications of balance sheet gains, how it flows through your structure, whether it goes through the corporate blocker, purely from a modeling standpoint.

Bill Janetschek - *KKR & Co. L.P. - CFO*

Sure, Aaron. From a modeling perspective, really nothing has changed. We have earnings off our balance sheet and what we had done historically and with too much precision was just call that a tax distribution and we would only be paying that out once a year. Now because we have and we feel better about liquidity, instead of just trying to be granular and looking at this as a tax distribution only, we've come up with the formula internally here and are comfortable with 40%, where we are comfortable paying out 40% of all realized investment income. That is realized capital gains offset against realized capital losses, interest income against interest expense and dividend income and so we feel comfortable in paying that out.

Now, from the structure itself, our unit holders will still have a pass through income and depending on the type of investor, some investors might actually have a tax liability but the one thing that we came across as we talked to several investors, there are a lot of investors that are foreign and their tax situation is different than in the U.S. We have tax exempts, etcetera, and so what we really wanted to do is get away from a focus of calling this a tax distribution which it really isn't and more in line of just paying out a certain percentage of realized income off the balance sheet.

Aaron Teitelbaum - *Surveyor Capital - Analyst*

Got it. Thanks guys, appreciate the color and congrats again.

Operator

I am showing no further questions in the queue and would like to turn the conference back for any further remarks.

Craig Larson - *KKR & Co. L.P. - Head, IR*

Jeanine, thank you and thank everybody on the phone and we look forward to seeing everybody again on May 23. Take care.

Operator

Ladies and gentlemen, thank you for participating in today's program. This does conclude the conference and you may all disconnect. Everyone have a good day.

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