

**FINANCE/PRIVATE EQUITY**

## KKR's co-CEOs want to reach \$1 trillion in assets by 2030. It will require the PE firm to operate very differently than its founders envisioned.

*By Sharon Tully*

**I**n November of 1996, Joe Bae had been working at buyout shop Kohlberg Kravis Roberts & Co. for six weeks as an analyst doing spade-work on deals when Scott Nuttall, another recruit, moved into the office next door. Both Bae and Nuttall, who had each worked at big Wall Street firms, soon relished the freewheeling small-group vibe over, as Bae puts it, “feeling like a cog in a large, sophisticated machine.” KKR had just two dozen employees and lacked even an HR department. Their bosses were already legends, courtesy of their epic purchase of RJR Nabisco. “Back then, Henry Kravis and George Roberts were the de facto investment committee,” says Bae. The process was that after studying the transactions, “you walk into Henry’s office, then you call George, and then you talk about the deal.” Recalls Nuttall, “We’d have lunch every day with Henry at the end of the table. He’d walk around handing out checks to the assistants when we sold a company, because everyone owned a piece of everything.”

“It was an apprenticeship culture,” adds Nuttall. “The place was so tiny that whichever one of us was less busy that week would get staffed on the deal. I was the mini-M&A department, trying to sell different pieces of Borden, such as Cracker Jack and Elmer’s Glue.”

Bae and Nuttall, both 24 and recently married, became inseparable. Each evening, they’d walk to the nearest McDonald’s for takeout and unpack their Big Macs in a conference room while watching the TV news. One summer, the two couples rented a weekend house in Woodstock, N.Y. Since the down-market place came sans trash pickup, they’d schlep the refuse to Manhattan on Sunday nights for disposal.

Today, Bae and Nuttall are still locking arms. Only now they have a slightly loftier perch: They are co-



PATRICK JAMES MILLER FOR FORTUNE

**Scott Nuttall (left) and Joe Bae met as 24-year-old analysts at KKR. Now they’re unleashing a revolutionary plan to grow the firm.**

CEOs of KKR, the world’s third-largest alternative asset manager that boasts the industry’s hottest stock and biggest ambitions. They’re perpetuating the “two-parent” household model that Kravis and Roberts followed for 45 years. During most of that span, their predecessors ran a narrowly focused private equity (PE) purveyor that famously leveraged up troubled enterprises, hammered costs, streamlined operations, and sold its targets in whole or parts a few years later, pocketing big fees and a fat slice of the profits on exit.

But Bae, 52, and Nuttall, 51, in the three years since they ascended, and beforehand as co-COOs, have radically reshaped the machine that Henry and George built. In the rearview mirror

are the slash-and-burn leveraged-buyout (LBO) days immortalized in the famous book *Barbarians at the Gate*. They’ve expanded KKR into every realm of the alts universe, from financing housing projects in Ireland to owning wireless networks in Chile and

cell phone towers across America. That type of work, though it greatly augments traditional PE, simply can't grow fast enough at highly profitable rates to get where they want to go.

Instead, the firm that's dreaming bigger than any outfit on Wall Street is embarking on a remarkable journey that few could have seen coming. Bucking the famously "capital-light" approach their industry was built on, they're aiming to fashion the next Berkshire Hathaway—in other words, channeling the cash flows from alternative money-spinning franchises to acquire a roster of strong, stable businesses they own outright for a long period of time.

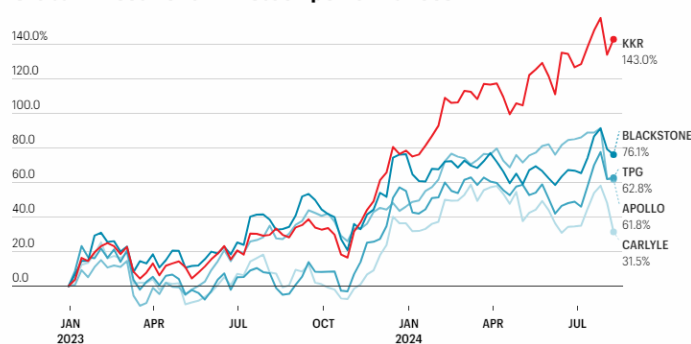
That unorthodox "ownership" approach, they claim, will drive the firm's valuation to levels never before witnessed in asset management. Another major leg of the strategy that's also Warren Buffett-like: KKR's 100% position in a giant insurer that's not only a big profitmaker in its own right, but provides multiple billions a year in premiums for KKR's fixed-income arm to manage.

Bae and Nuttall unveiled their daring predictions at KKR's investor day in April. The plan calls for raising assets under management (AUM) in five years by at least two-thirds to over \$1 trillion, and posting an almost fivefold gain in earnings per share from \$3.42 to \$15.00 in 10 years or less. The co-CEOs say that the pieces are in place for KKR to double its market cap in a first phase to over \$200 billion, followed by a further doubling to \$400 billion. Although they don't give a timeline, the earnings target and the kind of returns they're now seeing, by Fortune's estimate, suggest a path to \$200 billion by 2030. The \$400 billion goal is almost four times KKR's current valuation of \$111 billion, and nearly two and a half times the cap of today's leader Blackstone (at \$167 billion). We're talking uncharted territory. If Bae and Nuttall hit the mark, KKR would be worth one-third more than Bank of America's value today, and almost 70% that of JPMorgan.

To be sure, their strategy entails huge risks, including the threat that a pending recession could delay or hammer the capital gains from sales of portfolio PE companies that are still a KKR staple; the risk that its leaders don't prove nearly as good at picking winners as the Oracle of Omaha (a pretty high bar); and that huge expansion will undermine its famously cooperative culture. But skeptical investors seem to be gaining confidence. The evidence? Over the past five years KKR provided annual shareholder returns of 36.5%, beating Apollo (32.7%), Blackstone (29.0%), and Carlyle (18.2%), as well as TPG (25.2%, from January of 2022). In the past 12 months, KKR's stock has doubled.

Notes Ted Pick, CEO of Morgan Stanley and longtime friend and observer of both generations of co-CEOs: "In some ways the job's an even steeper climb for Joe and Scott as heads of a publicly traded company that's no longer the old buyout shop but a \$100 billion market cap enterprise working towards \$1 trillion in assets. The paradox or solution is that they're keeping the

Global investment firm stock performances



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ethos and trust of a partnership yet running a global financial services firm."

### What KKR's leaders learned from the firm's founders

Seated side by side in a 79th-floor conference room at their Hudson Yards headquarters on this June afternoon, the co-CEOs are smoothly describing their plans. Framing the twosome are floor-to-ceiling windows offering panoramic views encompassing the Freedom Tower and the Statue of Liberty. They're both attired in what's practically the KKR uniform: blue suits and open-collared white shirts.

"Philosophically, the firm's culture is to under-promise and over-deliver," says Bae. "We wouldn't put out those long-term targets if we didn't have a hell of a lot of confidence we could get there and exceed them over time."

Nuttall and Bae each grew up in hardworking, first-generation middle-class families, and were born abroad. A New Zealander, Nuttall's father met Scott's mom as a high school exchange student in a Pennsylvania farming town. They wed in his dad's picturesque homeland after he returned to finish college, and welcomed Scott as an infant Kiwi. The Nuttalls settled in the Chicago suburbs, where Scott's dad worked at a real estate finance boutique, arranging sale-leasebacks for such clients as Walmart. His mother earned a degree in computer science and enjoyed a long career at Bell Labs. "The deal excitement was part of the household," he recalls. His early affection for finance guided him to the Wharton School, where he graduated in 1994.

Bae's parents were child refugees who fled during the Korean War from North Korea to South Korea, where his father was a chemistry professor. After the family moved Stateside, eventually making their home in New Jersey, his dad worked his way up from lab assistant to specialist in developing automotive plastics for large chemical companies. His mother became an ordained Presbyterian minister who counseled victims of domestic abuse. "You heard no deal talk in my household," Bae declares. The music of Chopin and Mendelssohn filled the Bae residence: Young Joe was a piano prodigy who practiced long hours after school on the family's baby grand.



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**The first generation: Henry Kravis (left) and George Roberts at KKR's offices in 2013. "Henry and George modeled how a really good partnership can work for 50 years," says co-CEO Joe Bae.**

Bae had spent two years at Goldman Sachs and was unpacking his dorm room at Harvard Business School in September 1996 when a headhunter called to say that Kravis wanted to interview him in New York. Bae drove the next day to KKR's Manhattan offices, and flew that night to meet with Roberts in Palo Alto.

Bae was two weeks away from starting classes. Kravis went into a comedy routine about needing Bae at KKR ASAP, even if it meant sacrificing his deposit at Harvard. "Joe said he needed a couple of days to get his money back from the registrar, and I said, 'You'd better get here right away!'" recalls Kravis. Bae relates that his future boss was jesting.

The cofounders turned their teasing technique on Nuttall as well: "Henry and George have a funny sense of humor, at least with me," Nuttall says. "And they tortured me [by saying], 'Before we make a final decision we ask everyone this math question'—something silly like, 'What is 323 to the 98th power? We just would like to see if you know that answer.' And then they'd just sit there and stare at you for a long time. I'm a 23- or 24-year-old kid, and they're just cracking themselves up."

Today, Bae is a self-declared "foodie" who delights in the elevation of Korean cuisine to fine dining—he loves the 10-course tasting menu at Manhattan's Atomix, and relishes red Burgundy.

Nuttall married his high school sweetheart, Amie; Bae met his wife, Janice Y.K. Lee, in his first year at Harvard. She's the Hong Kong-born novelist who penned bestsellers *The Piano Teacher* and *The Expatriates*, the latter adapted as the hit series *Expats*. Joe and Janice have four kids; Scott and Amie share five. The families frequently unite for vacations. Bae recalls a trip to Israel and Jordan just before COVID: "We did all the great sights with 13 of us traveling in a little bus."

The Bae and Nuttall personal and professional kinship echoes that of their mentors. Kravis and Roberts

are first cousins who grew up together. When they were children, the Kravis family would drive from Tulsa to visit the Roberts clan in Houston on holidays, and vice versa. "We're told that our parents took us on our first trip together, to Marblehead, Mass., when we were 2 years old," Roberts told Fortune. "According to their account, we as toddlers visited the battleship Missouri that hosted the World War II surrender ceremony for Japan."

In the early 1970s, Kravis and Roberts worked at Bear Stearns, where they detested the system that paid employees on the profits they generated individually. "It was 'eat what you kill,'" says Kravis. "Everyone was running around saying, 'That's my deal, that's my idea.' It's a mindset that killed teamwork." Convinced that a culture fostering trust and cooperation would prove far more profitable in the long run, they, alongside Jerome Kohlberg—who departed in 1987—famously launched KKR on \$120,000 in capital.

Kravis and Roberts huddle with Bae and Nuttall every other Monday afternoon at 4 p.m. ET for what's known as the G-4 meeting, and are present at the private equity investment committee conclaves, chaired by Bae and Nuttall, where the firm makes the final decisions on whether to make or reject transactions under consideration.

Kravis is renowned as a dealmaker-statesman, and Roberts as a granular investor famed for his deep understanding of businesses. In these settings, their divergent approaches are clearly evident, according to KKR employees who attend. Quips Alison Mass, chairman of investment banking at Goldman Sachs: "Ask anyone who takes a deal to the investment committee if George is retired!" Roberts tends to press the deal teams on financial details; Kravis focuses more on the big picture, posing such queries as "Where's the romance?" Both want KKR to think big, aim at candidates offering huge possibilities, and fire from a classic list of questions: "What can this become? Why should we own this business versus a competitor buying it? What are the angles we can use to make it better?"

One wrinkle with the handoff: In early August, Kravis and Roberts got a blast of negative headlines when the pension fund for a local of the steamfitters' union sued KKR for illegally granting the pair a "windfall" of \$650 million when they passed the reins to Bae and Nuttall in 2021. The action alleges that KKR deployed a complex transaction that handed the cofounders a tax benefit that should have gone to the company. Plaintiffs have brought similar suits against Apollo, Carlyle, and GoDaddy, and in the latter two cases, judges have allowed the actions to proceed. (KKR has said the deal offered substantial benefits to shareholders and that it expects to move to dismiss the suit.)

For Mass of Goldman Sachs, who's presented potential transactions to Nuttall, he's anything but a Wall Street pirate for whom price is all. In assessing acquisition candidates, his priority is finding a like-minded team, say colleagues and M&A bankers. "Scott has always been focused on preserving KKR's culture," notes

Mass. “For instance, when KKR was beginning to build their real estate business 15 years ago, we discussed many platforms for KKR to consider. He passed on all of them, not because the price wasn’t right but because he didn’t want to risk compromising KKR’s culture. That was his number one focus; [so instead] he chose to grow organically.”

### **How Nuttall and Bae made their mark on KKR**

These co-CEOs and fast friends rose to the top exhibiting extremely divergent strengths—and the threads of KKR’s current strategy started to emerge years ago as they were working their way up the ranks.

Kravis and Roberts recall that when Bae and Nuttall worked side by side as junior analysts, both were constantly bubbling with ideas. “A common trait was that they weren’t afraid to throw up ideas, and never feared whether we’d say yes or no, like a lot of their peers,” says Kravis.

For Bae, it was the coup of fashioning an entirely new business from scratch in Asia that propelled him toward the summit. In 2005, Kravis took Bae on a three-week tour of the region to decide if KKR should launch an Asia-Pacific arm. Kravis found the opportunity irresistible; Bae relocated to Hong Kong as KKR’s only employee in Asia. “I was living in my wife’s family’s house for the first six months under crowded conditions, which made it even harder,” he remembers.

Guided by the founders, Bae took an original route in assembling a team. “I talked to Henry and George every night at 10 or 11 p.m. Hong Kong time,” recalls Bae. “They were so relationship-driven and focused. So they wanted people who were super-networked in these markets—local but had great reputations, great Rolodexes. Who could get to the right families, the right people, versus some financial wizard.” During his decade in Hong Kong, Bae mounted what one colleague calls “a dogged, blood sweat and tears offensive” that put all the pieces in place to make KKR the largest, most diverse alt firm in the Asia-Pacific. Today, the firm’s AUM in the region stands at almost \$70 billion, over three times the figure in 2018.

Interestingly, what most impressed Kravis and Roberts about Nuttall was how he performed when deals he’d advocated went bad. His biggest rescue operation was First Data, originally a misbegotten transaction that once stood as a symbol of private equity gone wrong. Nuttall took the lead when KKR teamed with coinvestors to acquire the payments giant for \$27 billion just as the market peaked in 2007. The LBO saddled First Data with a gigantic debt load just before the global financial crisis, and the slowdown in the shift from cash to credit cards, pounded its cash flow. A parade of four CEOs all failed to steer First Data back on a profitable course till Nuttall found JPMorgan executive Frank Bisignano, whom he persuaded to take the job. “Scott and Henry put in more of KKR’s money to save First Data. No other company with \$24.5 billion in debt and 10 times leverage ever survived, let alone made inves-

tors a big profit,” recalls Bisignano. Nuttall helped Bisignano negotiate First Data’s sale to Fiserv in 2019 at a big premium, and KKR eventually tripled its original investment.

But the pair had more in mind than just performing rescue operations.

### **The plan to grow KKR exponentially—and how the team was inspired by Warren Buffett**

They were learning from Berkshire Hathaway. “When Scott and I joined KKR, Berkshire’s market cap was \$40 billion,” says Bae. “Now it’s \$875 billion.” Adds Nuttall, “Buffett’s at 12 and a half, 13% [yearly gains] for 27 or 28 years, that’s how you get that,” noting the success of such long-term Buffett holdings as American Express and BNSF. “One of the things we learned: invest in great businesses; let them continue to compound so they pay you cash flow; and allocate that cash back [to] new investments. That’s one of those insights [from] looking at what Buffett’s done.”

For years, KKR would pass on buying just the kind of companies Buffett prizes, those in stable industries that consistently generate strong cash flows. The reason? They didn’t promise the 20%-plus returns of the fixer-uppers targeted by PE funds.

It was Nuttall who almost two decades ago put the scaffolding in place that enabled KKR to become not just an asset manager, but a major owner of businesses. “Scott was always bugging us with new ideas,” recalls Roberts. “Some we didn’t try, some we tried that didn’t work.” But, he adds, a bunch of Nuttall’s visionary plays proved big winners. The one that set the foundation for today’s KKR: In 2006, Nuttall structured a freestanding new company called KPE that raised \$5 billion in an IPO held on the Euronext exchange in Amsterdam. KPE used the cash to take big stakes alongside the regular KKR funds in companies including Dollar General, HCA, and Alliance Boots.

Then the financial crisis struck, and KPE’s shares tanked. But Nuttall saw an opportunity for KKR to exploit the meltdown, transform its model, and, over time, rescue the KPE shareholders as well. In October of 2009, he orchestrated a “reverse merger” where the partnership combined with KPE to form today’s KKR. The KPE shareholders got 30% of the combined entity’s stock, and the KKR partners received 70%. The deal made KKR the second of today’s alt giants to become a publicly traded enterprise, after Blackstone.

The genius of that gambit: Instead of just earning fees and capital gains on the holdings in its funds, KKR itself, the previous private partnership, now owned 100% of sundry companies, the ones inherited from KPE. And it had effectively purchased most of KPE when those companies were selling at around 20% of the prices KPE bought in at. Over the next several years, KKR unloaded that fully owned portfolio, mostly at multiples of what it had effectively paid. “We paid between \$500 million and \$1 billion for our controlling stake in KPE, and sold the companies for roughly \$15 billion,” exclaims Roberts.

Everyone knows that Buffett loves insurance, and in 2020 KKR decided it did, too, plowing some of the KPE winnings into a majority position in insurer Global Atlantic, then purchasing the balance in January of this year, for a total of \$7.4 billion (Apollo made a similar move with insurer Athene). Already, Global Atlantic accounts for around one-fifth of KKR's overall operating profit.

To reach their giant goals, Bae and Nuttall are banking on three growth engines: asset management, insurance via Global Atlantic, and the "ownership strategy." On the asset management side, over the past two decades, KKR has made massive moves into three booming areas of alternatives: real estate, infrastructure, and credit. The firm is now a major force in everything from data centers to student housing to LBO loans for midsize companies. Though old-line PE is still growing briskly, it's these newer franchises, plus the Global Atlantic

acquisition, that have turbocharged KKR's growth in assets from \$218 billion in 2019 to over \$600 billion today. The ever-creative Nuttall has also launched new ventures that build on KKR's strengths by offering services to outside firms, including competitors. A prime example: a capital markets group that if independent would rank among America's top 20 investment banks, and last year generated nearly \$600 million in fees, the vast preponderance of it profit.

The pair believe that the asset management and insurance pieces are already in place to propel KKR to clinching the first half of its goal: doubling its market cap to \$200 billion-plus in the years ahead. Bae says that all of these businesses are just starting to hit "escape velocity," all at the same time.

But in the years that follow, they're counting on the Buffett playbook to provide stage two of the blastoff. In the past several years, KKR has raised around \$30 billion in what's called the "core" private equity fund—under a new profit center dubbed Strategic Holdings—that purchases these Berkshire-style steady growers, and aims to hold them for two decades or longer. KKR provided 30% of the funding, and hence holds a like share of each company on its balance sheet. Over time, the firm plans to increase its stake in many of these holdings by providing equity infusions for acquisitions and new growth projects.

Today, the core fund owns 19 companies, a roster that encompasses such highly reliable profit-spinners as America's biggest online seller of contact lenses, 1-800 Contacts; and London-based ERM, the world's largest player in sustainability consulting.

Pete Stavros, co-head of global private equity, notes that the same dealmakers who identify candidates for the regular PE deals find the super-dependable performers for "core." Hence, KKR garners significant savings versus the expense of paying a separate core team.

In the deck for its April investor day, KKR forecasts that the fund holdings will be paying KKR over \$1 billion in annual dividends by 2030, and garner a valuation of \$28.6 billion. That's a staggering \$20 billion

addition from its estimated cap of \$8.6 billion today.

KKR stands alone among the big alts players in breaking decisively from the industry's long-standing religion, the capital-light mantra. But it's courting big risks by taking that revolutionary stance. KKR is transforming the former highly profitable model where it kept a lean balance sheet, banked fees and carry, and returned almost all profits to shareholders. That template generates extremely high returns on equity, and the asset management business will continue to do that. Under the new Buffett-like approach, it's constantly accumulating new billions in assets for everything from adding companies to its "owner" portfolio, to raising fresh capital for expanding Global Atlantic. KKR has built a mountain-and-rising \$23 billion in shareholder equity that far exceeds that of its rivals Apollo (\$12.6 billion) and much larger Blackstone (\$17.7 billion).

As the capital load expands, KKR will reach its goals only by generating mid-double-digit returns on each new dollar it invests. And that's a new and daunting challenge. Will Bae and Nuttall really succeed in choosing winners on the scale of Warren Buffett, the genius whose record has never been equaled? So far, the "owner" approach is still too new and undersized to show decisive signs that it will prove the powerhouse the copilots are promising.

As for their partnership, it might not be conventional, but they have some pretty solid role models.

"Henry and George modeled how a really good partnership can work for 50 years," says Bae. "They had a relationship coming up much like George's and mine," says Kravis. "When we named them copresidents in 2017, they came to us and said, 'Whatever we're paid, we want you to pay us absolutely equally.' That was another thing that showed they wanted to help each other and not compete." Kravis adds that the tendency to battle each other for power is the undoing of most co-CEO experiments. Adds Pick of Morgan Stanley: "Many of us would question if their arrangement is doable, except that they've been together from the earliest days, with Joe playing the role in extension of products and Scott in innovation. They can speak from the same hymnbook on what KKR should look like in 10 years."

According to an insider, Bae and Nuttall honor an informal code that prevents bottlenecks and clashes. If either one strongly favors a project and the other is moderately negative or neutral, the proposal goes forward. But if one is passionately pro and his fellow captain adamantly con, they agree to scrap the proposed program.

Most of all, Bae and Nuttall are joining hands on a journey into territory where no other asset manager has ventured before. More than three decades ago, Kravis and Roberts put private equity on the map as rebels laying siege to an American institution. In their way, the warriors they mentored are swashbuckling adventurers as well. Their audacious foray that Bae pledges "will get us to the promised land" isn't another instance of barbarians laying siege, but still a Wall Street spectacle for the ages.