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KKR - Q4 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 fourth quarter 2013 earnings conference call.

(Operator Instructions)

Please note today's conference is being recorded. I will now hand the call over to Craig Larson, head of Investor Relations for KKR. Craig, please go ahead.

Craig Larson *- KKR & Co LP - Head of IR*

Thank you Karen. Good morning and welcome to our fourth quarter 2013 earnings call. Thank you for joining us. As usual I'm joined by Bill Janetschek, our CFO; and Scott Nuttall, Global Head of Capital and Asset Management.

We would like to remind everyone that we will refer to non-GAAP measures on the call which are reconciled to GAAP figures in our press release. This call will also 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.

As well, we will be providing estimates on cash carry and its impact on future distributions on the call. These estimates are based on December 31 valuations and share counts prior to the KFN closing. And on the KFN transaction, please refer to the proxy statement and other SEC filings that KFN and KKR may make because they will contain important information about the transaction.

On to our results. This morning, we reported fourth quarter and full-year 2013 results. For the quarter, economic net income was $790 million, which equates to $1.08 of after-tax net income per unit, 29% higher than the $0.84 we reported for the third quarter of 2013 and over twice what we reported for the fourth quarter of 2012. Total distributable earnings were $510 million for the quarter and $1.5 billion for the year.

Before we move on, I'd like to highlight some new disclosures in our press release on pages 7 and 15. By way of backdrop, with over $7 billion of cash and investments on our balance sheet and our capital markets business in addition to our third-party business model -- third-party business, we have a differentiated business model.

Our objectives are to deliver excellent results on behalf of our LPs and at the same time generate significant cash flow from the ideas that we generate across all three of our segments. When we find something that we like, our goal is to capture as much value as possible for fund investors and shareholders.

We can achieve this goal through three main avenues, all of which contribute to our overall revenue. One investing third-party pools of capital like our funds and separately managed accounts. Two, investing our own balance sheet. And three, syndicating and underwriting in our capital markets business.

We don't manage our business focused on only one earnings stream. Rather we are focused on leveraging all of our people and infrastructure and minimizing costs to drive the highest amount of revenue for the firm whether that comes in the form of fees, carry or balance sheet income. We continue to work through our reporting to ensure we provide the most representative metrics to understand our profitability, particularly as we work towards the closing of the KFN transaction.

In advance though, to better help frame this, we've introduced a new page in our press release on page 7 that realigns the historical figures in our press release into two main buckets -- total segment revenues and total segment expenses -- and highlights our ROE on the bottom of the page. As well, we also realigned our total distributable earnings disclosure on page 15 and also disclosed specifically our payout ratio which for the fourth quarter and year 2013 was around 70%. We believe these changes provide even more clarity around how we measure our financial progress, and with that, I will turn it over to Bill.

Bill Janetschek - *KKR & Co LP - CFO*

Thanks Craig. Before I review our fourth quarter and full-year results, I want to highlight four aspects of our performance.

The first is fund raising and organic growth. Scott is going to walk through our inorganic activity later, but we raised over $21 billion of new capital organically in 2013, increasing our fee paying AUM by 27%.

And if you focus on our newer businesses excluding private equity, the growth is even higher, up 48% for the year. This scaling of our fee paying assets drove a 25% increase in both management fees and total fee revenue which exceeded $1 billion for all of 2013.

Second is cash carry. We reported $150 million of net cash carry for the quarter and over $400 million for the year, a 45% year-over-year increase in 2013. These figures exclude pending transactions like US Food and Oriental Brewery.

A year ago, 32% of the remaining fair value in our mature private equity funds was in position to pay cash carry. That figure has increased to over 90% today.

Third is performance. Our businesses had a strong fourth quarter, and the $790 million of ENI we reported in the fourth quarter is a record for us since we went public.

And finally our distribution. We announced the quarterly distribution per unit of $0.48, which is comprised of the traditional fee related earnings and cash carry components of $0.12 the $0.22 and includes $0.14 of realized balance sheet income, bringing our total distribution per unit for the year to $1.40, up 15% from the $1.22 distributed for 2012.

Now let me turn to the fourth quarter results. We ended the fourth quarter with assets under management at $94 billion, up 5% from last quarter and 25% on a year-over-year basis.

Our fee paying assets under management was $77 billion, also an increase of 5% from last quarter and 27% from last year. Here, the majority of our quarterly fee paying assets under management growth was due to the $3.5 billion of new capital we raised in our public market segment, which includes the final close of Special Sits, bringing that total fund size to $2 billion.

We also raised $1.5 billion in new capital and private markets, and the majority of this amount came from the $9 billion final close on NAXI and $1.5 billion final close in our real estate strategy. Fee related earnings were $120 million, up 13% from last quarter.

We saw a meaningful increase in fourth quarter incentive fees, largely from Prisma and Nephila, which offset lower monitoring and transaction fees. Total distributable earnings were $510 million for the quarter, more than double the $250 million we reported in the third quarter.

Turning to our segment results, in private markets, ENI was $369 million, up 50% from the third quarter. Our private equity portfolio appreciated about 8.5% in the quarter which compares favorably to the MSCI world which was up about 8%.

Touching a public markets, fourth quarter ENI in this segment was $73 million, more than 2.5 times the $28 million we reported last quarter. The quarter over quarter growth was driven primarily by higher incentive fees at both Prisma and Nephila that I mentioned earlier.

We also had $17 million of gross carry in the fourth quarter, primarily from mezz and Special Sits funds. We now have unrealized carry on our balance sheet from public markets in excess of $60 million.

Moving to capital markets principal activities, ENI was $348 million, up slightly from the third quarter ENI of $340 million as our balance sheet appreciated 7% in the fourth quarter. The increase in the carrying value of our balance sheet investments resulted in the December 31 book value of $10.83 per unit, which is up 10% from last year and includes a 55% increase in unrealized carry, bringing that total figure to about $1.2 billion.

Finally, I want to give you a peek at the first quarter distribution based upon where we stand today. Since December 31, we had three monetization events that we estimate will contribute a total of about $0.10 to the first quarter distribution, $0.06 of cash carry and $0.04 of net realized balance sheet income. These events include secondaries at Kion and ProSieben and the IPO of Santander Consumer, or SCUSA.

In January, through the IPO, we sold over 80% of our interest in SCUSA at approximately 3 times cost and a gross IR in excess of 70%. We also recently announced the sale of Oriental Brewery, and we expect to receive proceeds from the sale in the second quarter.

In 200,9 we invested $360 million in OB, and assuming the sales closes we expect to receive about $1.9 billion, or over 5 times our money. We expect OB alone will contribute about $0.25 per unit to the second quarter distribution. And with that, I will pass it over to Scott.

Scott Nuttall - *KKR & Co LP - Global Head of Capital & Asset Management*

Thanks Bill. Looking back on our fourth quarter and full-year results, there's three areas I'd like to focus on with you. The first is investing across all phases: deployment, creating value, and exiting.

Second, fundraising, as Q4 capped a particular active year for us. And finally, our strategic initiatives, notably Nephila and Prisma as well as the pending of Avoca and KFN transactions. I will start with investing.

On the capital deployment front, we maintained our active investment pace in both private and public markets. In private markets, we invested over $2 billion of fund equity in the fourth quarter with about 85% of this coming from private equity investments in the US and Asia.

We also had several investments that have been announced but not yet closed for an additional $2.5 billion dollars of committed equity capital. Since the beginning of 2013, we invested or committed over $8 billion in private markets, more than $2.5 times the $3 billion we invested for all of 2012.

In public markets, if we look at the gross assets invested across all of our accounts in Special Sits, mezzanine and direct lending, we deployed $1.5 billion of capital in the quarter and over $4 billion in 2013, or 2.5 times the $1.7 billion invested in 2012. And more importantly, these strategies continue to perform.

To give you a sense, in 2013, our mezzanine and direct lending funds had 23% gross IRRs, and our Special Situations fund had a 40% gross IRR in its first year. Performance in private markets has also been strong as our private equity funds appreciated over 20% during the year.

Additionally, we have been active on the monetization front. Last year, we participated in 30 liquidity events, distributing over $9 billion of cash to our fund investors, including $3 billion in the fourth quarter alone.

The majority of the $3 billion came from the six secondaries we completed in the quarter, including Dollar General, Parkett, Prosieben and HCA, and were done at a blended multiple of 2.2 times our costs. This is the second year in a row we've realized over $9 billion, returning a total of $19 billion since the beginning of 2012.

We've also seen an increase in strategic exits. In December, we announced the sale of US Foods to Cisco, and more recently, we announced the sale of Oriental Brewery to AB InBev.

Strategic exits are highly efficient. As Bill mentioned, the sale of Oriental Brewery alone is expected to generate $0.25 of cash carry in the second quarter distribution. So it was a good year for both capital deployment and monetizations.

The second area that contributed to our results last year was fundraising. We raised $5 billion of fee paying capital organically in the fourth quarter across our private and public market businesses. Over 30% of this came from the final closes in our NAXI, real estate and Special Situations funds, which are now investing a total of $12 billion.

The other $3.5 billion of capital raised in Q4 came from a number of our accounts and strategies. Mainly Prisma, CLO's, public market separate accounts, and corporate capital trusts (our BDC), which is now managing over $2 billion.

Over the course of the year, we raised $21 billion of fee paying assets organically, with over half of the capital coming from our non-private equity products. And for the year, total fee paying AUM was up 27% and non-private equity fee paying AUM grew 48%.

Now let's turn to our strategic initiatives. 2013 was our first full year with Nephila and Prisma as part of the KKR franchise, and the year went better than we'd anticipated. For example, Nephila accounted for about 25% of our fourth quarter incentive fees, and Prisma raised over $1.5 billion of new capital in 2013, increasing fee paying assets under management to over $10 billion as of December 31.

Profits grew significantly, integration went smoothly, and the businesses contributed to the origination and investment capabilities of the firm as a whole. Next in line is Avoca, the European credit manager that we're in the process of acquiring. Avoca ended the year with $8.4 billion of assets under management, and we look forward to adding their capabilities to our European credit platform at an opportune time.

The last area we want to touch on is KFN. We announced the KFN transaction last December, and we are on track for a Q2 close. KFN brings us more permanent capital, more recurring balance sheet income, and more net cash flow to invest behind our ideas and continue to build our firm.

Over the last 12 months, we earned $3.4 billion in total revenue across our three main earnings streams: fees, carried interest, and balance sheet yield. We incurred $1.3 billion of operating expenses.

So net, we generated $2.1 billion of earnings on an average $7.4 billion of book value or a 27% return on average equity for the year. And all this is translated into 2013 total distributable earnings of $1.5 billion and an annual distribution per unit of $1.40, up 15% from the $1.22 we paid in 2012.

As Craig mentioned, our business model is different. We are marrying third-party capital with our balance sheet and capital markets capabilities to capture maximum economics from the opportunities we see and the returns we generate.

In short, we want to make more money for our investors and shareholders from everything we see and do. In 2013, we expanded our payout ratio, balance sheet, investment capabilities, and our participation in the economics we generate to the benefit of all of us as shareholders. And the great news is there's even more to do.

So thanks for joining our call. Operator, can you please open the line for any questions?

QUESTIONS AND ANSWERS

Operator

(Operator Instructions)

Our first question comes from Bill Katz from Citigroup.

Bill Katz - *Citigroup - Analyst*

Thanks very much. Maybe Scott, starting when you finished off, when you talked about the strategic initiatives.

Can you give us a sense of where you might be in terms of fully maximizing either Prisma or Nephila. This seems like there's a lot of momentum there. What percentage of your clients might be -- have access to that, and what might the pipelines be looking like?

Scott Nuttall - *KKR & Co LP - Global Head of Capital & Asset Management*

Sure, thanks Bill. I'd say it's frankly still early innings on both.

Prisma closed in October year before last. Nephila was a bit over a year ago. As I said, the integration has gone really very well.

The fundraising teams have been working together. We're starting to see the pipelines continue to build in terms of jointly sourced opportunities. So I'd say it's still quite early days, and the good news is when you look at the backlog of potential fundraising opportunities and you look at the product development ideas, I think there's a lot of good things ahead.

Bill Katz - *Citigroup - Analyst*

That's helpful. You mentioned that -- curious what you meant by this undertone of the statement -- that the strategic exit quotes are quite efficient.

Is that in terms of MOIC, is that in terms of the realization potential? I'm trying to get a sense of what you meant by that.

Scott Nuttall - *KKR & Co LP - Global Head of Capital & Asset Management*

All I meant by that, Bill, is that with the strategic exit, you tend to get the proceeds in one closing. As opposed to an exit through the public markets where you do an IPO with some secondary or no secondary and a series of secondaries over time. It's more of a comment of how quickly the cash proceeds from the exit show up.

Bill Katz - *Citigroup - Analyst*

I see. And one final one for me. Thanks for taking all the questions. When you think about KFN, you may say to be determined, but as you had more time now to study the asset, any update or thoughts around synergies were incremental return potential against those assets?

Scott Nuttall - *KKR & Co LP - Global Head of Capital & Asset Management*

Not much we are able to share incremental to what we shared back in December, Bill, but suffice it to say, we already know the assets quite well because we built the portfolio and have been managing it since 2004. So we like what we are buying, and as you know, we see quite a few opportunities to redeploy that capital into higher returning strategies and ability to seed new businesses for the firm, and that remains the case.

Bill Katz - *Citigroup - Analyst*

Thank you for taking my questions.

Scott Nuttall - *KKR & Co LP - Global Head of Capital & Asset Management*

Thank you.

Operator

Our next question comes from the line of Chris Kotowski from Oppenheimer and Company.

Chris Kotowski - *Oppenheimer & Co. - Analyst*

Good morning. Couple of things. Just I wonder if you can update us on -- if I look at where you have the realizations, about $1.3 billion came out of E2, and $600 million out of Millennium, and $850 million out of the 2006 fund.

And I'm wondering if you look at the carry, is it kind of spread proportionally to that, or are there still netting hole effects in E2? Can you update us on the netting hole concept if it applies anymore?

Bill Janetschek - *KKR & Co LP - CFO*

Chris, this is Bill Janetschek. As it relates to netting holes during the fourth quarter, all the netting holes were filled. We've got right now, to go granular, a small netting hole in Millennium domestic, but when you look at the total funds that we're managing, right now in excess of 90% of the fair value of those PE portfolio assets are in position to pay cash carry any time we have a realization.

Chris Kotowski - *Oppenheimer & Co. - Analyst*

Okay. And if I think about it as of last quarter, your E2 was marked under 4% net IRR, and the 2006 fund more at a 8%. Just conceptually, the carry potential then out of the 2006 fund would be significantly bigger than out of E2, right?

Bill Janetschek - *KKR & Co LP - CFO*

Sure. Just based upon the size of the fund, but when you're talking about 2013 and on a mark to market basis, it really drives ENI. You mentioned earlier that overall, the fund performance was up about 20.5%. Europe actually fund performance was about 28%, so Europe actually outperformed in total, and we had a good amount of monetization, especially in E2 during 2013 which once we fill that hole, now we are in ability to payout hopefully a significant amount of future cash carry.

Chris Kotowski - *Oppenheimer & Co. - Analyst*

Okay, and secondly, just because it's an interesting case study, it looks like the position in First Data was marked up from about 70% to 81%. And they reported earnings, and EBITDA has been kind of flat. So is that -- as a case study for us, was that driven primarily just by market appreciation?

Scott Nuttall - *KKR & Co LP - Global Head of Capital & Asset Management*

Chris, it's Scott. I would say primarily the market comparable traded up, and as you know, that's about a 50% component of our valuation methodology. That's largely what drove it.

Chris Kotowski - *Oppenheimer & Co. - Analyst*

Okay. And then last question for me is if you look at the assets in the Special Situations vehicles, went up nicely from [2.6] to [3.5]. And I'm wondering is that driven by specific new funds and vehicles coming into existence, or is this kind of a regular add-on quarterly activity that one might expect? I guess what I'm getting at is this hopefully theoretically a recurring event or is this just the result of a fund launching?

Bill Janetschek - *KKR & Co LP - CFO*

Chris, it's Bill again. As I mentioned earlier, what I would say that co-mingled dedicated fund for special sits closed at $2 billion, but remember and we've actually said that's our first fund, but in essence we've actually been managing what I would call fund of ones for big institutional or wealth investors where they gave us committed capital and within a private equity like structure, so were entitled to management fees and carry. Those were pretty big checks.

So we actually have three mandates prior to actually going out and launching the dedicated Special Situations funds. So that's what represents that number right now. But keep in mind that we still have the ability to continue to raise capital as interest in special situation investments, and so we could raise another mandate with a big institution, which would then if it was like a private equity type fund where it would be committed capital would show up on the table next quarter.

Scott Nuttall - *KKR & Co LP - Global Head of Capital & Asset Management*

The biggest reason for the increase, Chris, is the capital rates for the special sits fund in the quarter ahead of the final close.

Chris Kotowski - *Oppenheimer & Co. - Analyst*

Okay great. Thank you that's it for me.

Craig Larson - *KKR & Co LP - Head of IR*

Chris, I will add one other thing as it relates to your point on the netting holes, and Bill had mentioned this. Year ago when you think of the 90% figure, that was roughly 32% a year ago, so the implications of that when you look at our financials in terms of total distributable earnings and

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realized cash carry specifically. This year when you look at that, we saw 45% increase in realized cash, carry and the netting hole certainly plays an important part in terms of the monetization, and ultimately they end up flowing through to the distribution.

Chris Kotowski - *Oppenheimer & Co. - Analyst*

Great.

Operator

Our next question comes from Michael Carrier from Bank of America Merrill Lynch.

Michael Carrier - *BofA Merrill Lynch - Analyst*

Thanks guys. Just a question on fund raising. 2013 was a huge year kind of across the board.

When we start thinking, going forward whether it's 2014, 2015, just want to get a sense of what's in the pipeline, what are you guys working on, where can we see additional demand from clients and new money coming in? And this is a minor thing, but remind me -- I think in the table on page 13 when your new capital in terms of AUM can be less than fee AUM, I think that's the transfer of some of the money that was raised and now it's collecting fees, but want to make sure we're clear on that.

Scott Nuttall - *KKR & Co LP - Global Head of Capital & Asset Management*

Yes Michael, it's Scott. I will take the first question.

In terms of fundraising, there's no question we had the benefit last year of the closes of NAXI and Asia 2 and our real estate fund. That aided us getting to the $21 billion number for the year, so you get some larger episodic funds that were closing over the course of the year. But as we look ahead, we also have a lot of things in the market, and as you know, we have a significant amount of the offerings that are now continuously offered.

So if it does reflect on the fact that Q4 we had $3.5 billion of the $5 billion came from the public markets businesses, a lot of which was the more recurring components of the product set. But just to be specific with you, we are finishing fund raising for our energy income and growth fund, $1.4 billion closed. We expect that to wrap up that fund over the course of the next several months.

We are also in the process of raising a Europe 4 fund which is now launched. We expect that will continue into this year and likely into next year.

Other things that kind of are on deck, as you know, we've had a lot of fund of ones that are getting close to be fully invested. And so if you think about infrastructure 2, direct lending 2, we are looking at private credit. Our first mezzanine fund is nearly fully invested.

On the ongoing front, you have public and private market separate accounts, you've got high yield, you got loans, Prisma and Nephila, KES et cetera. There's a lot of different things that we have in the market right now and that will be in the market over the course of this year.

And then parenthetically, a couple of things. As you know, we've been focused on continuing to expand our individual investor franchise, and so we continue to see opportunities there across a number of our different products.

Last year that was about 23% of the capital we raised came from individual investors, which was up -- so it was basically $4.7 billion which was up $1.8 billion the prior-year, so up 160%. So we will continue to focus on bringing products to that channel.

And as you also know, a big part of the focus for the firm is expanding the number of investors that entrust us with their capital. Last year that number went up 23%, so we're now up to nearly 700 investors, up from 560 or so at the end of 2012. So hopefully that gives you some color, and I'll hand it over to Bill to handle the second question.

Bill Janetschek - *KKR & Co LP - CFO*

Just to answer the question. Generally speaking, you would expect fee paying AUM to actually be less than AUM when it actually is brought on board. Interestingly in this quarter, you saw the fee paying number actually go up.

In private markets, the anomaly is around our Annex fund. We didn't fully deploy all the capital. We gave the people the choice to take that Annex commitment and roll it into E3, and if so, it went from a non-fee paying entity into a fee paying entity, so you saw fee paying AUM go up.

On public markets, interestingly, we actually had an old hedge fund that was invested in credit. Most of its assets were in the CLO.

We decided to sell those CLOs off to a third-party investor. That was about $1 billion. When that happened, because that old investor was not being charged his CLO fee, we sold it off to a new investor, we turned on the CLO fee, and by doing that, our fee paying AUM went up by about $1 billion.

Michael Carrier - *BofA Merrill Lynch - Analyst*

Got it. And Bill, maybe one more -- a few things on the income statement, just any expenses this quarter that were seasonal. I know sometimes it's dead deal costs and stuff in the private markets, just wanted to figure that out.

And then I know it's impossible, but incentive fees, when we think about Prisma and Nephila going forward, would you characterize this as a great quarter? Something we could see in the seasonal fourth quarter or second quarter?

Just trying to get some sense. And in private markets, given the money that was raised, is this a good quarter in terms of all the fee AUM and the management fees in the run rate where we see any step functions in the first quarter?

Bill Janetschek - *KKR & Co LP - CFO*

Okay. As it relates to run rate fees, you could probably take notice that the basis points on management fees when you take the management fees over total fee paying AUM went down a little in the fourth quarter. The reason being is that a lot of that capital was raised at the end of the quarter.

And so obviously as of December 31, we're reporting the big fee paying AUM number, but we don't have the management fees to match up in this particular quarter. And so you will actually see somewhat of an uplift in that prospectively.

Your second question as it relates to incentive fees. On a public market side, just to give you a broad stroke as far as how those incentive fees come as far as a crystallizations, as it relates to Nephila, generally speaking Nephila is going to realize its incentive fee once a year.

And so you might see small amounts come through, through the first three quarters if there are redemptions, but you're not going to see any significant activity again. You only see that pop if performance is there in the fourth quarter.

Prisma is a little different. About half of the capital that they manage crystallizes vis-a-vis the incentive fee in June and the other half in December.

And so you're not going to see any real activity in the first quarter or third quarter, but with Prisma, you're going to see it in the second quarter and fourth quarter. And it relates to what we call KAM.

There are a couple of funds that actually do pay an incentive fee. One being the BDC called CCT, and for the most part, that has got an annual crystallization event, so you will see that in the fourth quarter. Long-winded answer, but for the most part, you're going to see, if performance is there, higher incentive fees in the fourth quarter and some incentive fees in June because of Prisma.

Michael Carrier - *BofA Merrill Lynch - Analyst*

Okay.

Bill Janetschek - *KKR & Co LP - CFO*

On the choppiness or lumpiness sometimes of expenses, you can see in private markets that the operating expenses were up quite considerably in the fourth quarter from the third quarter. We actually closed on a lot of investments, and we announced the closing of several investments in the first half of 2014, but we also looked at other investments which were unsuccessful.

And during the third quarter and fourth quarter, the dead deal expense that we actually recorded in the fourth quarter was abnormally high. You wouldn't see that number being the run rate number in the first quarter.

Michael Carrier - *BofA Merrill Lynch - Analyst*

Okay. Thanks for the color.

Bill Janetschek - *KKR & Co LP - CFO*

You bet.

Operator

Our next question comes from Michael Kim from Sandler O'Neill.

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

First, I know you talked about some of the near-term realization events to come, but just curious to get your take on how you see the trajectory of distributable earnings playing out beyond that just given what seemed to be some building tailwinds for realizations around embedded gains, the level of AUM and cash carry as well as maturity and liquidity of the underlying portfolio holdings.

Scott Nuttall - *KKR & Co LP - Global Head of Capital & Asset Management*

Thanks Michael, it's Scott. I will take a crack.

It's hard to give you too much guidance on the trajectory of total distributable earnings overall, but maybe a couple things to think about. If you look at the portfolio, well step back.

We've announced a few transactions that have not yet closed. And so Bill mentioned some of those on the call, but SCUSA, Kion, Oriental Brewery a big one, and so there's some very specific math associated with those exits that we think our closings in Q1 and Q2 that will contribute to total distributable earnings in particular in cash carry and also in terms of balance sheet realized gains.

And then you look at the portfolio in terms of the potential for monetizations after that. And if you look at the actual unrealized value in our private equity portfolio, which give or take $39 billion, if you look through that, we have about 33% of the portfolio including the Alliance Boots stake that is in public securities, and the other two thirds is in private securities.

On the public side, as you know, we have several investments that we have just been continuing to sell down in the public markets, and so there's opportunities to monetize those positions on a continuous basis. Then you look at some of the private market investments that we have that are still private.

And as I mentioned in the prepared remarks, we are seeing a pickup in strategic exit activity, and we said that over the course of the last one to two years, and it continues to build. So there's always the potential to have exits on that front as well.

And then lastly, what I would say is if you look more broadly at the firm in terms of the trajectory of total cash flow growth, we have a number of businesses that you know that we seeded over the course of the last three or four years, probably 8 to 10 first-time funds since 2010. And what we are encouraged by is the strong investment performance that we've seen in those first-time funds and the potential now to get the fund 2, fund 3, which means we will be able to generate more revenues without meaningfully more expense associated.

And the balance sheet happily is invested alongside all those strategies. So as we start to have those portfolios mature, we will see more cash flow coming off the balance sheet as well.

So hopefully that gives you a little bit of color. But we continue to see quite a bit of upside in the portfolios that we manage and our balance sheet as well.

Bill Janetschek - *KKR & Co LP - CFO*

This is Bill. One other thing to add. For the most part, Scott is focused on the private market side and where we might see realizations, but don't forget that on the public market side, we've got now over $5 billion in committed capital which right now --

And remember, we only started investing in these committed structures a couple years ago, but I mentioned earlier that we've got now $60 million of embedded unrealized gain. As those strategies continue to mature, we're expecting to see realize cash carry coming from the public market side to help bolster the cash carry distribution that we anticipate making in 2014.

Scott Nuttall - *KKR & Co LP - Global Head of Capital & Asset Management*

Maybe just one addition for you Michael is if you step back, pro forma for the closing of the Avoca transaction, we have about $85 billion of fee paying AUM. That's now about evenly split between private equity and non-private equity. So to Bill's point about scaling the non-private equity businesses and their ability to generate more cash flow, we're starting to see that scaling happen.

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

Great. That's helpful. And then second, assuming more LPs increasingly gravitate towards more flexible multi-strategy solutions, just wondering how much of a competitive advantage do you think the bigger, more diversified franchises maintain? And then related to that, do you feel like firms need fund of fund capabilities just to provide a more comprehensive and liquid solution across asset classes?

Scott Nuttall - *KKR & Co LP - Global Head of Capital & Asset Management*

Well, on the first part of your question, I think there's clearly an advantage to being able to talk to a chief investment officer, a broad investment staff about their broader investment portfolio goals and what they're trying to accomplish. It's clearly helped us win a number of mandates, and as you know, we track our cross sell statistics. We continue to see more and more investors investing with us across asset classes.

Several have started with us in non-private equity that are now investing in our private equity funds. So I do think there is a clear advantage of being able to talk to them and give them asset allocation thoughts and advice across a number of asset classes, and we talked in the past as you know about how much interest we're seeing in alternatives. So it's hard to quantify what that advantage means, but clearly from our standpoint, part of the reason we're able to raise the $21 billion we raised last year organically was because of that ability to speak across asset classes.

In terms of the question on fund of funds, as you know, we've been very happy with the addition of Prisma to the KKR family. It has allowed us to broaden the dialogue even further to more liquid alternatives, and the hedge fund market is a meaningful part of the liquid alternatives opportunities set in the big and growing market. I don't know that I'd characterize it as a have to have for people, but it's certainly been quite helpful for us to be able to give even broader advice across an important and growing asset class to the people that trust us with capital or the prospects that are thinking about it.

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

Got it. Okay. And just maybe one final one for Bill.

Just on the equity based comp. Can you just talk about sort of the drivers behind the step up in those charges in 2013 versus 2012 and then any color on how we should be thinking about that line going forward as it relates to vesting schedules and further issuances?

Bill Janetschek - *KKR & Co LP - CFO*

Sure. Historically we've always reported the non-cash comp, but it was actually a footnote on page 7 now.

It is shown in the total economics of the firm. And so when you think about where we've been as public company in 2009 at 2010, we didn't issue any stock on the public plan. All issuances were from KKR Holdings which was non-dilutive to the public entity.

In order to compensate people, the bulk with cash and stock, that stock is now being issued by the public company, and so to give you a rough percentage, the total number of shares that were issued as part of 2012 comp which was reported in March of 2013 was a little under 2%. We've gone through the conversation process in December, and those awards will be granted in the first quarter of 2014. And so you won't see that in this coming 10K, but you will see it in the first quarter Q.

We expect that number to be roughly about the same. What that means as far as a comp charge is obviously the awards are long in nature.

They're anywhere between three and five years. And as you take that, vest that over a certain period of time, you're going to continue to see that comp charge come through again as a non-cash comp item. Keep in mind that is not going to impact our distribution.

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

Okay. Thanks for taking my questions.

Bill Janetschek - *KKR & Co LP - CFO*

Thanks Michael.

Operator

Our next question comes from Brian Bedell of Deutsche Bank.

Brian Bedell - *Deutsche Bank - Analyst*

Hi, good morning. Thanks for taking my questions. If we can just drill down on the credit market strategy in Europe in particular. I know Avoca is closing soon, and maybe you could talk about the game plan for the fund raising and investing with Avoca in the context of Europe along with high yield and leverage loan strategies and also direct lending.

Scott Nuttall - *KKR & Co LP - Global Head of Capital & Asset Management*

Hello Brian, it's Scott. Happy to take that. In terms of a rough outline, Avoca is $8.4 billion or so of credit assets in Europe.

Prior to closing the Avoca transaction, we're managing $3 billion or so of credit assets already at KKR. So pro forma, we will probably be somewhere between $11 billion and $12 billion in terms of assets under management focused on European credit.

And we continue to see a very exciting opportunity over the course of the next several years. We've increased our headcount pro forma for the Avoca deal from 11 to the better part of 80 people focused on the opportunity set in addition to leveraging our private markets colleagues. So we're excited about the opportunity.

From a fund-raising standpoint, I think it's on several different fronts. One, you have the legacy Avoca businesses around European leverage loans and CLO format and separate account format potentially, commingled fund format, so we will continue to see growth in those businesses.

Avoca also has a Europe focused credit long short hedge fund where that will also be a focus for fundraising on a go forward basis, and we see opportunities to scale what they're doing before making them part of the KKR infrastructure. But another exciting opportunity that we see is to marry the more liquid Avoca capabilities with our illiquid capabilities in Europe. And our team in Europe today is focused on special sits and mezzanine and starting to focus on direct lending, and really by adding Avoca to the platform in Europe, we are able to have a footprint that looks like our footprint in the US where we have liquid and illiquid teams sitting side-by-side and teams working on both.

And so Avoca today at their database is tracking 1300 European credits, and we're already starting to capture some synergy and idea sharing and approaching companies together that may be in need of help. So a liquid opportunity company that gets into a little bit of trouble can turn into an illiquid special situation investment opportunity, and we're able to now create that bridge were we couldn't before.

What that means from fund-raising standpoint implications is that there's an opportunity for us to raise private credit funds focused on Europe, special sits, mezzanine, direct lending, and we're seeing potential opportunities across all those funds. And parenthetically, I would say institutional investors are quite interested in the opportunity set as they see how much incremental return we are able to get to do private lending in Europe as the banks are pulling back. So the Avoca transaction for us is highly strategic and gives us a bigger footprint and more capabilities at a time where we think there is going to be a very interesting period for investment the next several years there.

Brian Bedell - *Deutsche Bank - Analyst*

But fair to say it's early innings, and the long-term opportunity over the next 2 to 3 years is stronger than it is here in the US on that front?

Scott Nuttall - *KKR & Co LP - Global Head of Capital & Asset Management*

Yes, I would agree with that. I think it is relatively early innings, and we haven't even closed the Avoca deal yet, so very early innings.

But if you look even at the deployment we have, the gross deployment we had in our originated credit strategies last year was $4.2 billion, up 2.5 times from the prior year. And that is frankly without Europe yet firing on all cylinders, I think Avoca will take those numbers up meaningfully, so we're excited about it.

Brian Bedell - *Deutsche Bank - Analyst*

Great. And a comment on the emerging markets given the recent selloff I think in the third quarter.

You were talking about accelerating the pace there looking for IRRs over 20%; I guess how do you feel about that now? Just providing even the market providing a better opportunity.

Scott Nuttall - *KKR & Co LP - Global Head of Capital & Asset Management*

I would say two comments on that. First as it pertains to Asia. We are seeing more opportunities, good buying opportunities for private equity and special sits as a result of the valuation pulled back, and some of the deals we've been doing in Asia have really been as a result of this meaningful downdraft.

We mentioned the Haier investment we've made in China as an example -- as a good example of that. The volatility creates opportunities for us, which is great.

The other thing I would point to is markets like Brazil and South America. We've had an office in Sao Paulo for over a year, and we've been waiting for volatility to make valuations more attractive, and so I think it will be a net positive for us if this volatility continues; there will be some interesting things to do. So we do view it as a net positive for our business.

Brian Bedell - *Deutsche Bank - Analyst*

Great, thanks, that's the very helpful. Thanks for taking my questions.

Operator

Our next question comes from Matt Kelley for Morgan Stanley.

Matt Kelley - *Morgan Stanley - Analyst*

Good morning guys, thanks for taking my questions. First, I wanted to come back to the monetization realization front. The commentary I'm hearing from you guys seems to support this with the strategic commentary made, but with the markets kind of weak this quarter but the exit markets seemingly still open -- and granted it's very early in the year -- just curious from your perspective and the strategic talk you're hearing, how is your kind of inclination towards selling in this market changed thus far this year, and how has the strategic talk changed thus far this year?

Scott Nuttall - *KKR & Co LP - Global Head of Capital & Asset Management*

Hello Matt, it's Scott. I would tell you it's been a very short period of time, so I think it is far too early to be able tell you if there is any long-term implications from the recent market volatility. But I do think that while some investors are very anxious about what happened in January, we step back and say -- okay, since the beginning of last year, the total return in the S&P has been 26%.

So yes, January wasn't a lot of fun, but overall it's actually been a pretty good run. Maybe multiples got a bit ahead of themselves. And we're starting to see a little bit of a pullback, but the long and the short of it is we have not seen any immediate impact on the monetization environment or kind of things that we've got going on inside the portfolio.

So nothing that I'd point you to there in terms of any increased anxiety; we will see how it plays out through the year. But the bigger opportunity for us frankly as CEOs gain confidence around the economy, what they're seeing, and they start to be more aggressive with their own capital structures and what they want to do on the acquisition front. We still think through the noise it's going be a good time for strategic exits relative to the last five years.

Matt Kelley - *Morgan Stanley - Analyst*

Great. And then one more for you guys on Prisma and Nephila, and sorry for coming back to this again, but anything you can give us -- and maybe we have to wait for the 10K -- but on AUM for either the strategies percent above high water mark or how they performed or anything like that, that you can kind of help us quantify? I know you gave the Nephila disclosure for the quarter, but in terms of sizing how big the assets are, that sort of thing would be helpful.

Scott Nuttall - *KKR & Co LP - Global Head of Capital & Asset Management*

Scott, again Matt. On Prisma in terms of what we can share, AUM finished the year over $10 billion. Nephila finished the year a bit over $10 billion. So good growth in both.

Both had very strong incentive fee quarters and years, and so overall frankly both are well ahead of our expectations in terms of first year financial results. So the performance has been strong.

Virtually all the assets across the strategies are above the high water marks. Off to a great start.

Matt Kelley - *Morgan Stanley - Analyst*

Okay, great. And last one for me, in terms of your platform build out, obviously 2013 was a very impressive year from that standpoint. You built a lot of strategies, but I'd be curious -- you said you had about 700 LPs now. Are there any cross-selling metrics you can share and how that changed year-over-year, and as you think about that going forward, what do you feel like are the most obvious pieces that you could add still to your platform that you don't have?

Scott Nuttall - *KKR & Co LP - Global Head of Capital & Asset Management*

Let me take cross sell first. We ended the year with 693 clients. What that does is we don't look through the platforms, so when we sell through a bank platform and they have high net worth investors, that does not include the numbers, so think of this as institutions in direct high net worth nearly 700. We are now averaging 1.6 products per clients.

And if you think about it, you have a tension in that number, so it's been kind of 1.6, 1.7, 1.6. When you add an investor, you tend to add them with one product.

And so despite the downward pressure as a result of increasing the number of clients by 23%, we ended the year at about 1.6 products per client. To give you a sense, our largest 35 clients average about 3.5 products. We think there's meaningful upside opportunity because we have a lot of clients in one product and several in two or three or more, and so we see a lot of upside to that cross sell number.

And in terms of the platform build out question, I'd say it's a few different things. One, we've got the opportunity for geographic expansion across a number of the businesses that we built. As you know, a lot of the businesses we started, we started in North America, and we are now moving those to Europe, Asia, South America.

So there's an opportunity from a geographic build out standpoint, and we think that's meaningful. And we talked about South America and looking at credit opportunities in Asia, we talked about European credit as some examples, but the same thing is true across real estate, energy, hedge funds. So we see meaningful opportunity to expand both in the US and outside the US.

In addition, the platform build out frankly would be most driven economically by going from fund 1 to fund 2, 3, and 4. And starting to generate not only fees but carry as those portfolios start to perform. And in the more public side businesses, those incentive fees begin to get earned.

So in terms of do we see another big leg to the stool, there's nothing that we've got in our sights, but if you look at what we have today, private equity, energy, real estate, credit, hedge funds, capital markets, there is a lot to do across all those different asset classes. And just as a reminder, private equity is a trillion dollar industry. If you add up everything else that we're looking at, it's probably $5 trillion or $6 trillion, and our market share although AUM is up to $40 billion or $45 billion, pro forma, our market share is quite small relative to the opportunity set, so we have a lot of runway.

Craig Larson - *KKR & Co LP - Head of IR*

The other thing I would add on that which is interesting -- when you look at the specific stats on some of the fundraisers, so it again shows the strength we're having in terms of bringing new LPs, looking at by number LPs in Asia 2, roughly 45% of those were new investors to us. When we look at NAXI, again similar by number of LPs; that number again is about 40% by number. And by some of our newer funds like special sits, by number of LP that number is over half, so in terms of growing and focusing on the LP base, we feel we've made quite a bit of progress this year.

Matt Kelley - *Morgan Stanley - Analyst*

Thanks very much, guys.

Bill Janetschek - *KKR & Co LP - CFO*

Thank you.

Operator

Our next question comes from Chris Harris from Wells Fargo Securities.

Chris Harris - *Wells Fargo Securities, LLC - Analyst*

Hi guys. Subquestion on deals and kind of deal pace. You guys are starting to accelerate things a little bit here, and I'm just kind of curious to get your thoughts.

As you guys look at the deals you are doing today and maybe compare that to deals you did in the 2005 to 2007 timeframe, what would you guys say would be the main differences between those two periods of time? And I think what would maybe be helpful is if you could perhaps frame it out from a valuation perspective or if there is any other differences in the way transactions are structured, that would be great.

Scott Nuttall - *KKR & Co LP - Global Head of Capital & Asset Management*

Sure Chris, it's Scott. I would say today's deals versus 2005 to 2007, the first thing that comes to mind in terms of big difference is it's much more of a global opportunity set. So we went to Asia and started to build the business there in 2006, and if you look -- so in that period of time, there really was not much of anything in terms of deal opportunity in Asia because we're just starting to build the business, but if you actually look at -- as an example I mentioned $2.5 billion of deals we've announced but not yet closed, over $1 billion of the $2.5 billion is in Asia.

You would also see much more opportunity in Europe; of the $2.5 billion, $800 million of it is in Europe. So there's a meaningful amount of the answer that's frankly related to the globality of the opportunity set now and the types of transactions we're seeing relative to where we were in the period of time you referenced, so that's number one.

Number two, the types of transactions are different. Obviously in Asia, we're not doing a lot of buyouts; we're doing some.

But a significant amount of the opportunity set there is more growth equity, is providing companies with capital, giving them operational and capital markets expertise. And that's something we see as an interesting way to invest in that part of the world and frankly the best way to invest in that part of the world, so you would see transaction structures a bit different.

The third thing I would point you to is some math related things. There's less leverage than you would have seen during the peak times; you would've seen leverage creep back up from the peak parts the low parts of the cycle. But we've got less leverage now than in the deals that were done in that period of time.

There's more of an operational focus.

We continue to build our KKR capstone efforts globally, so bringing more operational intensity to the businesses that we're investing in. There's more macro analysis.

We just made an investment, our first investment in Serbia. Our macro team, KKR Global Institute was highly involved to make sure we understood that market. That is a new way we look at transactions, and we're investing in different parts of the world with that focus.

So there's a lot of differences from where we were, and depending on the part of the 2005 to 2007 period you're talking about, it's size. Size of the transactions are smaller than some of the deals that were done back then, multiples probably on average are lower.

And the other thing I would say is we're doing more control deals, not from the standpoint of control the company, but from the standpoint of when we speak for equity transaction, we're speaking for all of it. And we're syndicating out the excess to limited partners and others. So that's another thing that has changed; as opposed to club deals, we're controlling more of them ourselves.

And finally -- sorry, there's a long list, and a lot has changed. By building these other parts of the firm, we have actually in creating a culture where everybody can help each other and everybody gets paid off one P&L, you've got more people and KKR sourcing for different parts of KKR.

So if we're talking to a company on the credit side, there is nothing to do there but a buyout opportunity, we've got credit teams sourcing for private equity teams and vice versa, and so there's more ideas coming into the place just by virtue of having more people out talking to companies around the world. I will stop at that.

Chris Harris - *Wells Fargo Securities, LLC - Analyst*

Thanks for that Scott. It sounds like you may have been asked that question once or two before.

Real quick numbers question for Bill, I know we're running long. But Bill, when I look at your results just holistically, this year was a record year in many respects, yet the taxes you guys paid from a GAAP perspective are the lowest they've been since the IPO. I'm sure there's a good explanation for that, but can you maybe help us understand the puts and takes along with that?

Bill Janetschek - *KKR & Co LP - CFO*

Sure, and to say it's complicated would be an understatement, so let me stop there. But remember, when we originally did the transaction with backend merger of KPE, approximately 30% of the assets on our balance sheet were actually held through the corporate blocker.

As we've monetized those investments, we've moved away from putting those assets back on what I would say the management company side and being subject to tax and taking those proceeds and actually investing them on the flow-through side of our public structure. So over time, the amount of tax that we've actually paid all things being equal has gone down considerably since we've gone public.

In addition, as we're making new investments and investment overseas like in Nephila, we structure that so that income is actually going directly to our unit holders, not actually going through a corporate blocker, and so by doing that, obviously we're minimizing tax. But there are other reductions as far as the typical fee related earnings as we've made investments in Prisma and Nephila. We get to amortize intangibles for taxes, and so that number is actually coming down.

There's a lot of to's and fro's on trying to figure out exactly what the run rate tax number is going to be, but I assure you that when you take a look at 2012, 2013, the number has actually come down. I would say that it would probably, if I look at 2014, be somewhere in the range of 2012, 2013.

But take into account another big driver of that is going to be what our fee income is. So a long-winded answer on that, and I don't know if that was clarifying point as you were hoping to receive, but the short answer is the taxes are actually lower for a couple of good reasons.

Chris Harris - *Wells Fargo Securities, LLC - Analyst*

Helpful. Thank you.

Operator

Our next question comes from Patrick Davitt from Autonomous.

Patrick Davitt - *Autonomous Research - Analyst*

Hi guys, good morning. Another question on Avoca. How should we think about that coming in relative to the current weighted average fee rate in public markets? Margin, is the margin similar to what's already happening in public markets, and thirdly, how much LP overlap is there between Avoca and your current business?

Scott Nuttall - *KKR & Co LP - Global Head of Capital & Asset Management*

Hey Patrick, it's Scott. So let me take maybe in reverse order.

LP overlap -- virtually none. So think of it as very similar to Prisma. In terms of most of it's net add in terms of the LP base of the firm, hopefully some cross-selling opportunity there for us.

If you look at the average fee rate for Avoca given its focus predominantly on liquid credit CLO's, some hedge fund assets, their fee rate on a blended basis has been increasing over the course of last couple of years, but relative to our embedded fee rate, it's going to be lower on average because CLO's tend to be a 50 basis point kind of business. And in terms of margins, it's going to be reasonably consistent with the business we have today.

Patrick Davitt - *Autonomous Research - Analyst*

How many LPs do they have?

Scott Nuttall - *KKR & Co LP - Global Head of Capital & Asset Management*

It depends on how you count it in terms of whether you look through the CLO's give or take, but call it between 50 and 100.

Patrick Davitt - *Autonomous Research - Analyst*

Okay. And on the distribution guidance, you gave nice detail on the Oriental Brewery detail. Could you give us similar detail on the US Food sale, and if you're not comfortable doing that, is it of a similar magnitude or can we expect it to be a similar magnitude?

Bill Janetschek - *KKR & Co LP - CFO*

Patrick, I'd much rather not comment on that as it relates to the distribution because remember that transaction is going to be part cash and part stock, and we are going to see owners of Sysco. And so I'm not going to try to predict the timing of that.

Patrick Davitt - *Autonomous Research - Analyst*

Okay. Thanks a lot.

Operator

That concludes our question session for today. I would like to turn the conference back over to management for any concluding remarks.

Craig Larson - *KKR & Co LP - Head of IR*

Thanks Karen, and thank you everyone on the line for your interest. Naturally please follow up with me or with Sara should you have any follow-up questions. Thanks again.

Operator

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

Editor

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