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# EDITED TRANSCRIPT

KKR - Q2 2015 KKR & Co LP Earnings Call

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## PRESENTATION

**Operator**

Good day, ladies and gentlemen, and welcome to the KKR & Co. second-quarter financial results. (Operator Instructions) As a reminder, this call is being recorded.

Now I would like to welcome our host for today's conference, Mr. Craig Larson. Please go ahead.

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**Craig Larson** - *KKR & Co. L.P. - Head of Investor Relations*

Thank you, Carmen. Thank you, everybody. This is Craig Larson, Head of Investor Relations for KKR. Welcome to our second-quarter 2015 earnings call. As usual, I am joined by Bill Janetschek, our CFO, and Scott Nuttall, Head of Global 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. And please refer to our SEC filings for cautionary factors related to these statements.

This morning, we reported strong second-quarter results. Of note, we reported second-quarter economic net income of $840 million, equating to $0.88 of after-tax economic net income per unit. Both of these figures are up over 40% from last quarter, driven by strong investment performance.

Total distributable earnings were $491 million in the quarter, which translates into $0.57 of distributable earnings per unit, net of taxes. And in terms of the distribution, we have announced a distribution for the quarter of $0.42 per unit.



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Before we move on, I would like to bring your attention that this quarter, in addition to our press release, we have included a supplementary presentation for the first time, which is also posted on our website. We thought we would use these slides to highlight the key themes for the quarter as we reflect on our performance, and we will refer to the pages in this presentation over the course of the call.

If you could turn to page 2 for a moment of the presentation, this highlights the 4 main themes in our business that we'll expand on over the next 10 to 15 minutes: strong underlying investment performance, the continued scaling of our newer initiatives, how we are continuing to use our balance sheet to invest in our ideas and enhance our growth profile, and lastly, key initiatives we are focused on looking forward.

And with that, let me turn it over to Bill to discuss our financial performance in more depth.

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

Thanks, Craig. To set the stage for our results, let me touch on page 3 of the earnings supplement that Craig referenced earlier. As you can see on this page, we had strong investment performance this quarter across our carry paying funds in both private and public markets, helping our performance fees.

And the performance is broad-based. Our three key flagship PE funds were up between 9% and 15% in the quarter. We have also seen strong performance in our real asset strategies, which were up between 4% and 6%. And our alternative credit funds also had a good quarter, with special sits especially strong, returning 6% in Q2.

And that investment performance helped drive the results we announced this morning, most notably ENI, where we have announced record ENI on a total segment basis as well as within both private and public markets.

In private markets, we reported ENI of $666 million, which is up 17% from the first quarter and 77% on a year-over-year basis. This increase was primarily driven by the continued performance of our private equity portfolio which appreciated 7.4% in the second quarter and 11.8% year to date.

So far in 2015, through June 30, our portfolio has outpaced the S&P 500 by over 1,000 basis points. Our private market balance sheet assets were also marked up, contributing to material quarter-over-quarter and year-over-year increases in investment income.

In public markets, we reported $137 million of ENI. This is also up materially on a quarter-over-quarter and year-over-year basis, due mostly to strong performance fees and record quarterly investment income. Contributors to our performance this quarter include the performance of our carry funds, including our direct lending, mezzanine, and special sits strategies; $31 million in realized investment income driven by gains in both liquid credit and special sits; and we reported $59 million of net interest and dividends, which was up 14% from Q1.

Moving to capital markets, we reported second-quarter ENI of $37 million, up from the $28 million we reported in Q1, driven by higher transaction fees. Our capital markets footprint continues to expand globally for our own investments and third parties. For the quarter, about 40% of transaction fee activity stemmed from private equity portfolio companies.

Other KKR activity, like real estate and energy and infrastructure, accounted for 30%, while the remaining 30% represented third-party activity. Also, approximately 30% of the total transaction fees came from outside the US.

Turning to our balance sheet, our book value per unit was $12.77, also a record figure for us. Cash and investments on the balance sheet now total $11.8 billion and unrealized carry on the balance sheet is now $1.6 billion.

That is the highest it has ever been, which is up 15% from last quarter and 30% from June 30, 2014. All as a result of strong underlying performance seen within our funds.



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Turning to the distribution, we announced a distribution of $0.42. The largest component was $0.18 of realized cash carry, driven by the sale of Biomet to Zimmer; a secondary at Nielsen; a secondary at Pets at Home, a UK listed company; as well as a series of less visible monetizations in Asia, including Aricent, Bharti, Far East, MMI, and UEL.

From a realized carry perspective, we are off to a good start in Q3, given the recent announcements of the sale of Capital Safety to 3M as well as the sale of the majority stake in Alliant Insurance to Stone Point, both of which we expect to close in Q3. Coupled with the dividend recap at Academy, these will combine for roughly $0.12 of distribution per unit in Q3.

And when you look at the more recurring portion of our distribution, fee and yield earnings, together with cash carrying balance sheet gains, and assuming the transactions I just mentioned earlier are completed, we'll be at around $0.27 a unit for Q3 as we sit here today.

Finally, in terms of AUM and fee paying AUM as of June 30, our assets under management were $102 billion and fee paying assets under management were $84 billion. And again, keep in mind these figures do not reflect nearly $10 billion of committed capital that will be included in AUM once it's invested.

This shadow AUM is up over $4 billion from March 31. And also doesn't include the pro rata portion of AUM from our stakes in seed investments, which Scott will walk you through in more detail in a little while.

And with that, I will pass it over to Scott.

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

Thanks, Bill. As Craig and Bill walked you through, we had a very good quarter. I thought I would focus on the big takeaways for the quarter, share what we have been doing on the balance sheet, and spend a few minutes on areas of focus and what is next.

The first takeaway from the quarter is that we are generating strong investment performance. Bill ran you through the data on page 3. As you can see, performance in the quarter was not only strong, but also broad-based.

Let's turn to page 4 and dig into the details of our private equity funds. We have executed a number of strategic sales over the last couple years. In several of those transactions, we took back stock in the acquirer. Overall, those stocks have performed well.

In addition, we have taken a number of companies public. The result is that we have seen the value of the public securities in our private equity portfolio increase from $4.6 billion a year ago to $11.9 billion today.

And those stocks continue to perform. As you can see on the right-hand side of the page, Walgreens is up 14% over the last year and Haier, HCA, PRA, and GoDaddy are up between 40% and over 100% each. And the $11.9 billion of public securities does not include First Data, which filed its S1 earlier this week.

As a reminder, we have total exposure to First Data of approximately $4.5 billion, approximately $3.2 billion in our funds, and $1.3 billion of total exposure on our balance sheet. So PE performance for the quarter was strong. We have line of sight to liquidity in the portfolio, and the exit environment is good.

In our non-PE strategies, we are also seeing strong investment performance, good deployment, and strong asset flows. Which brings me to the second big takeaway from the quarter: our progress in business building.

We have discussed for several quarters the opportunity for us to scale the eight more recent platforms we've created over the last several years. On the back of strong investment performance, we are seeing that happen.



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If you look at page 5, you can see a couple examples of this. Our Direct Lending II fund is 2.9 times the size of the first fund. Our Infrastructure II fund, which had a final closing a couple weeks ago, is $3 billion or 2.9 times the size of Infra I.

Our special situations business continues to scale as well. Our first comingled fund was $2 billion. We have had two closes on the Special Sits II fund at $1.7 billion and we now manage over $6 billion in assets in this strategy.

In addition, we are making progress on an adjacent strategy, Direct Lending Europe. So we continue to see these newer businesses scale and have a larger impact on our P&L, as fees are increasing and carry is starting to be generated.

But if you look at just our stated AUM, the true impact of the scaling of these businesses is understated. Some of the funds we are raising are what we call shadow AUM, where the capital is committed, but we do not get paid fees until it is actually invested.

Many of our private credit mandates operate this way. We do not report shadow AUM in our AUM or fee paying AUM figures until it is invested. We do track it, however, as it gives us a good sense of embedded potential upside in our management fees and carry.

If you look at page 6, you can see that our shadow AUM grew from about $6 billion at March 31 to about $10 billion, a $4 billion increase just in the second quarter. So if you want to get a real picture of our capital raising in the quarter, you should look at the $3 billion we raised in AUM on page 13 of the press release and add the $4 billion of shadow AUM increase in the quarter. Combining the two, we had a very active fundraising quarter.

Page 7 shows another element of AUM growth. In addition to the shadow AUM dynamic, we also own stakes in hedge funds that manage approximately $12 billion in AUM, where we get a portion of their profitability. The assets of those hedge funds do not show up in our AUM, but part of their profits flow through our income statement.

Page 7 shows what our AUM and fee paying AUM would look like if you include shadow AUM and our pro rata share of our hedge fund partners' AUM. As you can see, including those figures increases our AUM by 13% to $114 billion and our fee paying AUM by 14% to $96 billion. And all these numbers ignore our capital markets business and our $14 billion balance sheet, which don't contribute to AUM or fee paying AUM.

Speaking of our balance sheet, take a look at page 8. We want to provide you with more transparency regarding what we are doing with our balance sheet. Page 8 details some of the activity on the balance sheet year to date.

Since the beginning of the year, we have invested about $1.4 billion from the balance sheet and realized about $1.4 billion. As you can see, the largest realizations relate to Walgreens Boots Alliance and monetizing some of our on-balance sheet credit portfolio, including a number of positions acquired in the KFN acquisition.

On the right-hand side of the page, you can see how we are using the freed up balance sheet capital. We listed 3 of the larger uses of funds, including an additional $200 million investment we made in WMI Holdings, the former holding company for Washington Mutual. We made this investment opportunistically, as we think WMI is a great vehicle through which to facilitate acquisitions. WMI's stock is up 27% through June 30, so our investment is performing well so far.

We also invested $210 million from the balance sheet as of June 30 to seed our real estate credit business. We are seeding a portfolio and see an opportunity to create a substantial real estate credit business for the Firm by dropping the balance sheet seeded portfolio into a fund or other type of vehicle to attract third-party capital. This is very similar to how we started our real estate equity business.

Another first-half investment from the balance sheet is Acion Partners, an Asia-based hedge fund that we seeded, as we view Asia as an underpenetrated hedge fund market.

Hopefully, this walk-through gives you a sense of some of our recent activity and how we continue to use our balance sheet as a strategic weapon to start and scale newer businesses and make off-the-run investments we think are interesting.



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The bottom of page 8 lists the two largest PE portfolio company investments on the balance sheet. You can see that First Data and Walgreens are now valued at $1.3 billion and $600 million, respectively. So combined, these two assets account for 20% of our balance sheet investments. Over time, you should expect us to add additional large-scale holdings selectively.

So we had a good quarter. Our investment performance is strong and our businesses are scaling, perhaps even more than is apparent.

So what is next? Let me mention three items. I am on page 9 of the deck. First, we want to continue to take advantage of our strong investment performance for clients and the good fundraising environment to scale our newer initiatives even further. This includes the Fund II dynamic I mentioned and also finalizing fundraises for newer strategies, such as direct lending and newer hedge fund products.

The second is Americas private equity. As a reminder, our last Americas PE fundraise, our 11th, called NAXI, was approximately $9 billion. NAXI is now 60% committed, has strong performance as a top quartile-performing fund, and the fundraising environment and LP interest in investing in the Americas feel good to us.

Third, we continue to explore ways to do more in liquid alternatives. At a high level, we continue to see a significant amount of investor interest in alternatives. If you look at where alternatives are expected to grow over the next several years, liquid alternatives specifically are expected to be a fast-growing component.

While we have added liquid alternative capabilities in credit and hedge fund-of-funds, we are actively exploring strategic partnerships to allow us to bring more products globally to this fast-growing space to meet the needs of our investment clients and further grow our fee paying assets.

We are going to host an investor day in New York in the fall and we will get back to you with details. At the investor day, we will walk you through how we see the revenue growth opportunities globally for all of our businesses.

Hopefully, you found this new format helpful in understanding the main messages for the quarter. We feel like we are making real progress on a number of fronts. And thank you for listening.

Operator, please open the line for questions.

## QUESTIONS AND ANSWERS

**Operator**

Before we go into Q&A, Mr. Larson, would you like to add anything before we open the lines?

**Craig Larson** - *KKR & Co. L.P. - Head of Investor Relations*

Thanks, Carmen. I was just going to say, just looking at the queue, we actually have quite a few people lined up in the queue. So if you could please ask one question and then get back in the queue, if necessary, we would appreciate it.

**Operator**

(Operator Instructions) Craig Siegenthaler.



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**Craig Siegenthaler** - *Credit Suisse - Analyst*

Asia Fund II had a very strong mark in the second quarter, but the Asian markets have been rolling over since May. I am wondering if you can talk about the potential for negative marks in 3Q and how the recent volatility has impacted your privates in Asia Fund II?

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

Craig, this is Bill. I will take this one. As it relates to the performance in Asia during the second quarter, you are right. It was pretty strong. And as you heard in my prepared remarks, we had several monetizations in some of those Asia positions.

Interestingly, when you take a look at our public holding in our China investments -- and I ran these numbers on Tuesday -- our portfolio was only down about 4%. And so when you look at where the marks were as of June 30 of those public companies and again, based upon the drop in the Asian market, again, we have solid companies in our portfolio. We believe in China. And again, it was only down about 4%.

Also want to point out, as I ran the numbers, if you take a look at where our publics were as of Tuesday -- I am talking about all the public positions that are embedded in that 32% that Scott mentioned, we were about 4%. So that would be positive 4%.

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**Operator**

Glenn Schorr, Evercore.

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**Glenn Schorr** - *Evercore ISI - Analyst*

I don't know if there is anything that is driving the specific shift into some of the structures and arrangements that you put under the shadow AUM, but I appreciate the slide and the disclosure.

I am curious: do they come at different fee structures, things like the sovereign wealth partnership, the expansion of the existing strategic partnerships? And does it change the way we think about the earning power of the dry powder in this expanded definition?

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

As it relates to the economics on most of those structures, take for example Special Sits and Special Sits II. Special Sits I was originally based upon committed capital. Special Sits II, it was a little more challenging environment to raise on the public market side committed funds. And so we went to a model where we were going to get paid on invested capital.

The good news is that really, when you look at Special Sits I to II, it is really only a timing issue, because the management fee that we are going to be able to get on Special Sits II is 1.75% on invested capital as opposed to 1.5% on the original Special Sits. But that is just one example.

As it relates to some of the more strategic partnerships, where we are raising large amounts of capital and we are going to be deploying that capital, those are very economic trades for us. So there might be slight fee concessions that we give up, but overall, it is a very profitable business for us.

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**Operator**

Chris Kotowski, Oppenheimer.

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**Chris Kotowski** - *Oppenheimer & Co. - Analyst*

Thanks for the slide deck. I was wondering, though, about out of NAXI. We saw the first market major harvest; looked like more than $800 million in realized proceeds out of NAXI.

And I was wondering, is that -- is this sooner than one would normally expect? Or do you think it is now at the point where you have a number of mature investments? Or was this kind of a one-off quarter for that?

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

Very specifically in NAXI, what has ended up happening in a couple of the investments that we have made is we've actually refinanced those companies and returned that capital to our investors. And all you are seeing is us putting money up, closing the investment, seeing early performance go the right way, doing a little refinance, and getting money back to our LPs sooner.

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**Chris Kotowski** - *Oppenheimer & Co. - Analyst*

Okay. So those were basically like dividend refinancings.

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

Yes.

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**Chris Kotowski** - *Oppenheimer & Co. - Analyst*

Okay. And then secondly, I had -- just if we look at your balance sheet, your investment in credit in terms of cost basis in the alternative credits, the last three quarters, it has gone from $3 billion to $2.8 billion. And then to $2.7 billion this quarter.

So it just seems like there is kind of a deliberate rundown in that and like you are not replacing what you are harvesting. Can you give us the thinking underlying that and whether we should see more of that?

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

I am happy to take that one. Look, if you look at slide 8 of the deck, you will see on the left-hand side, we call out that we have been selling down some of our on-balance sheet credit portfolio, CLOs, and otherwise. And frankly, what we have seen there is an opportunity to redeploy that capital at higher returns and opportunities like those we lay out on the right-hand side of the page.

So it has been somewhat deliberate because we have seen valuations in credit move up. And so we have seen the returns from this point forward go down and we saw opportunities to redeploy at a higher return level. And so hard to say where we are going to go from here, but it has been a deliberate move to bring down credit to redeploy into other areas.

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**Operator**

Michael Kim, Sandler O'Neill.

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

Just to maybe follow-up on the discussion on shadow AUM. I know it is difficult to generalize, just given the different strategies and opportunities beneath the surface, if you will. But any thoughts or color on how you are thinking about the timeline or trajectory for potentially deploying those assets?

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

I guess what I would tell you is one of the biggest component of the shadow AUM is our private credit business. And that business, as we talked about on our last call, has really scaled from $3 billion to now well in excess of $15 billion in the last few years.

And if you think about the deployment in those strategies, if you look at our Direct Lending I or our Special Sits I funds, we've managed to get that money to work in a 2- to 3-year kind of time frame. These funds are going to be larger, would be our expectation. And obviously, Direct Lending II is much larger than Direct Lending I. But if you think in the 2- to 4-year time frame, that is probably a reasonable expectation.

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

And Michael, this is Bill. Just a little bit of a follow-up on shadow AUM. We have been talking about shadow AUM on the earnings call for probably the last couple of years and it has always been roughly at a range of in between, say, $4 billion, $5 billion, $6 billion.

We saw a significant increase this quarter and what we're end up doing is we are signing commitments, we are raising capital, but it is not just coming through our AUM or fee paying AUM because of the way we report it. But we wanted to make sure we drew it to your attention the significant capital raising that we have had over the last couple of quarters and I hope you find this information useful.

Another thing that I want you to just take a look at is if you looked at page 15, in that uncalled commitment column, a lot of the shadow AUM that we are talking about on the slide 6 is actually reflected on that table. So you could see Special Sits II, where we have got uncalled capital at the $1.6 billion. That is part of that shadow AUM.

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**Operator**

Bill Katz, Citi.

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**Bill Katz** - *Citigroup - Analyst*

Thanks for taking my questions. Appreciate the extra disclosure. It is very helpful. Just a big picture question, Scott. Maybe I read too much into this, but it sounds like as you monetize some of these bigger stakes on the balance sheet, you said you would be tactfully adding to it over time.

So I guess the question is, as you are scaling the business, whether it be what you have now or shadow AUM, and given what looks like a bit of a slowdown in dry powder deployment and a bunch of your peers saying, hey, the markets look pretty heavy here, whether it be equity fixed income, can you talk about the rationale of managing such a large balance sheet at this point in time? Is it as strategically compelling now as you scale the business?

And maybe the root question here, so Craig doesn't yell at me, is could you lower the size of the balance sheet and maybe pick up capital return in terms of repurchase on top of the distribution?

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

Great. Thanks for the question, Bill. I'd probably separate topics a little bit, if that is all right.

First, let's talk about deployment. If you look at actually the deployment that we have seen across the Firm over the course of this year, it has actually been pretty strong. Relative to the first half of last year, $4 billion in private markets; this year, $3.3 billion so far. That doesn't include some investments like WMI. So if you include those, it's actually closer to $4 billion. So we have seen private markets deployment kind of flat to off a little bit after a very active first half last year.

And if you look in public markets, you can actually see deployment has gone up. So for gross dollars invested of $1.8 billion first half last year, $2.3 billion first half this year, that is across Direct Lending, Mezzanine, and Special Situations.

So we continue to find interesting ways to deploy capital. We are being very prudent because valuations have moved up in most markets. But if you look in the markets like Asia, where we have been active in a number of different areas, we have been able to find some very interesting opportunities in Special Situations, Direct Lending. We are finding needs for capital and have been active there.

I would separate that discussion from the balance sheet question. As we've talked about the last several quarters, our model is a bit different. It is a model that we chose. And then we like having this marriage of third-party AUM with our own balance sheet and our capital markets business, because we think it allows us to really monetize our ideas to a much greater extent.

And I would actually take the results this quarter as a proof point as to what the model can generate when we see strong investment performance across all of our different businesses.

So if you look at what's happened, you can see we have had good investment performance that translated into good performance fees, carry, and balance sheet results. And the capital markets business intermediated a lot of that and was able to generate attractive risk-free economics, for the most part, for the Firm.

So we kind of view the quarter as saying here is what it looks like when the model is really working on a number of fronts. And we like having our balance sheet as our own largest investor.

And part of the reason we want to give you this disclosure is we want you to see what we are doing with the balance sheet. We continue to use it to seed new businesses, scale businesses that we are in, and we see it as really an opportunity to help create new product, to drive more opportunities for our investment clients, and drive more fee paying AUM.

So we view it as kind of a virtuous cycle. So our view is that we want to continue to have a large balance sheet because we are believers in ourselves and our ability to generate investment performance. And we want all of us as shareholders to participate in that upside to a greater extent.

If you then go into another implicit question that you asked, which is dividend policy buyback. As we've discussed, we have chosen thus far to have all of us as shareholders participate in our performance through a large payout. So we have been paying out 75% to 80% of our cash flow.

We will continue to assess whether that is the right way for all of us to participate. Obviously, the topic of buyback has come up in prior quarters. Thus far, the view has been let's pay it out in dividend as opposed to doing a buyback, but we will continue to assess it.

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**Operator**

Brian Bedell, Deutsche Bank.

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**Brian Bedell** - *Deutsche Bank - Analyst*

Maybe just to focus a little bit on, maybe Scott, you were talking about the Americas private equity as sort of a what's next idea. If you could talk a little bit about -- two-parted question, I guess.

The deployment outlook in the Americas, given what we've seen in high valuations; where you are finding opportunities. And then thinking about the fundraising outlook beyond what you are already in the market for and the potential to raise a NAXI 12 sometime in the next, I don't know, 12 to 18 months or so. Thanks.

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

Happy to take it, Brian. A couple things. One, let's start with deployment. As I mentioned, the NAXI fund is about 60% invested and committed, if you include transactions we have announced, but that haven't yet closed. And so we continue to find interesting opportunities.

Valuations in the US are pretty high, but we have managed to find some opportunities a bit off the run that we find interesting. Two recent ones we announced were PURE, which is a high net worth life insurance provider, and CHI, which is a garage door manufacturer.

So these are not opportunities that you necessarily are going to read about in the paper, but in most of those situations, we will deploy $300 million or so of equity, which has kind of been in our sweet spot the last several years. So we are finding some interesting opportunities for deployment, and as we talked about, we are taking advantage of the equity capital markets to facilitate exits as well.

In terms of fundraising, all I can tell you is that we would expect to be in market soon to launch the successor to the NAXI fund. And as I mentioned, we are pleased the performance has been top quartile. So we are finding good ways to get capital to work. We are pleased with the early results and we will be in market soon.

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**Operator**

Ann Dai, KBW.

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**Ann Dai** - *Keefe, Bruyette & Woods, Inc. - Analyst*

Thanks for taking my question. There has been some discussion by some of your peers about creating pools of capital that invest for 10 years longer than the average PE fund. So I was just wondering what your thoughts are on that and is that something KKR would be interested in doing?

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

Thanks, Ann. We have looked at it. I think the thesis is that there is some investments that you may want to hold for a very long period of time, where the returns may be a bit below traditional private equity fund targets.

And it is something that we will continue to look at. If it does become a part of the business, I would expect it would be a relatively small part. But it is something that we are assessing and exploring with a partner or two.

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**Operator**

Patrick Davitt, Autonomous Research.

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**Patrick Davitt** - *Autonomous Research LLP - Analyst*

I think Alex at a conference last quarter mentioned that NAXI's EBITDA growth had been tracking 20%-plus year over year, which is clearly better than market and seems pretty outsized even relative to funds of similar vintage.

Is there any one or two positions driving that? Is there an industry concentration that is maybe driving that? I mean, it is pretty incredible.

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

I think what I would like to do is probably aggregate a little bit for you, maybe talk more about that portfolio more broadly.

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**Patrick Davitt** - *Autonomous Research LLP - Analyst*

Okay.

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

So our overall private equity portfolio, we track this quarterly, has continued to perform quite well. If you look globally, last 12 months, we have had about 8% revenue growth and about 13% EBITDA growth. And that is on the global portfolio.

Within that, you'd see North America and Asia growing faster than the 13% and Europe growing more slowly, but we have been quite pleased with the private equity portfolio performance.

The Americas private equity portfolio has been performing very well. I would tell you that within the NAXI portfolio, it has been pretty broad-based. It is not just one or two companies or one or two industries.

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**Operator**

Michael Cyprys. Morgan Stanley.

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**Michael Cyprys** - *Morgan Stanley - Analyst*

Thanks for taking the question, and thanks for the enhanced disclosure in the slide deck. That is helpful. Just around that, on the balance sheet, you mentioned, I think it was on slide 8, that you monetized about $1.4 billion in the first half off the balance sheet and also invested about $1.4 billion.

Just curious: how much of that came through in the second quarter alone? And then as we think about reflecting this in our model, this enhanced disclosure, is this something we can expect to see a similar level of disclosure going forward?

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

I will take that one. As it relates to the $1.4 billion, approximately half of that came through the first quarter and the other half came through in the second quarter.

And as far as disclosure is concerned, I would say that because we have gotten a lot of emails from a few of the analysts that cover us and they found this quite helpful from a transparency point of view -- and you just mentioned it as well -- I would say that we are going to continue to report this on a quarterly basis.



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**Michael Cyprys** - *Morgan Stanley - Analyst*

Okay. That's great. And just -- I want just to make sure I understand. So the $1.4 billion on the monetization and the investment side, they were each roughly half/half first quarter, second quarter?

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

Yes. That is -- it was pretty close. It is not going to be exact, but it is very close to being in the neighborhood of 50/50 on both sides.

**Michael Cyprys** - *Morgan Stanley - Analyst*

Got it. And then any sense just on the deployment outlook off the balance sheet -- $1.4 billion in first half? How are you thinking about things going into the second half of the year?

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

Hard to be too specific, because it is going to be based on the opportunities as we see them. We continue to see opportunities in real estate credit, so I would expect that number will continue to go up.

As I mentioned, we are continuing to explore strategic partnerships and liquid alternatives, so you may see us do some more there. But it is hard to be too precise, because it is based on the opportunities that are coming our way and how the markets evolve.

**Operator**

Michael Carrier, Bank of America.

**Michael Carrier** - *BofA Merrill Lynch - Analyst*

Just had question on -- I guess the revenues and the expenses kind of on the core, like the fee earnings. Just on the management fees, it seemed like it ticked up. I just wanted to find out if there were any catch-up fees this quarter. And then in the outlook, if we should be expecting anything differently.

And then just on the monitoring fees, Bill, I think you mentioned -- you gave a range, because the first quarter was extremely strong. So just any update on that. And I know it is volatile, so whatever you can give us.

And then on the expenses, both like the core comp and the non-comp expenses, both were either well managed or came in lower than expected. So just wanted to see if there were anything unusual in the expense lines in terms of a run rate going forward.

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

Sure. And although you were told to ask one question, I think there were three questions.

**Michael Carrier** - *BofA Merrill Lynch - Analyst*

Sorry about that.



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

Give you a pass. When you talk about management fees, let's talk about private markets. You could see that there's a slight uptick. A little of that is a catch-up with regard to the E4 fund closing and Infra II. But that is modest.

When you look at public markets, you could see a slight increase. That is just assets coming online and it is like Direct Lending II and Special Sits II. So not being where you would see a reversal of that number in the subsequent quarter.

As it relates to monitoring fees, we had said last quarter that the average run rate on monitoring fees should be approximately $20 million a quarter. You can see that the number in the first quarter was quite large. We talked about a monitoring termination payment from the Boots Walgreens transaction.

In the second quarter, we also had two monitoring termination payments, one of which was of size. And that was the Biomet/Zimmer transaction. And so you would see those happen episodically, but again, back to your earlier question, the run rate number for modeling purposes should be about $20 million.

As it relates to expenses, you could see that the expenses in private markets were -- and we are talking about operating expenses -- were down from $42 million. That really was driven by smaller dead deal expenses in private markets.

But overall, you could see that the expense from the first quarter -- and I am talking about total reportable segments -- went down from $60 million to $51 million. I would say that this is probably a light quarter from an expense point of view and you should think that that number is going to be anywhere in between, say, $55 million and $65 million on a quarterly basis.

**Operator**

Devin Ryan, JMP Securities.

**Devin Ryan** - *JMP Securities - Analyst*

Most questions have been asked here, but maybe just one on the energy exposures across the platform. Didn't really touch on that. I know it was a better story this quarter. But we have seen a slight reversal in commodities thus far in the third quarter.

So just trying to get a sense -- I mean, if we don't see a recovery in commodity prices from here, do you see any impact on related exposures or have to take any additional marks? Or do we get to maybe a point where hedges roll off and so there could be some more pain? Just trying to get some sense here.

**Craig Larson** - *KKR & Co. L.P. - Head of Investor Relations*

Yes, let me -- a few thoughts on that. First -- and it is a good question. One of the things that is important to remember is that as the energy investments largely are valued, we'll run long live-lived discounted cash flow analyses.

So when you look at the movements in commodity prices, both in terms of oil and natural gas -- and along with that, by the way, is that -- and you referenced this -- is that the majority of our near-term production is hedged. So the result of that is that the shape of the curve and prices 4 to 5 years out are important to consider. That is true both when prices are higher as well as lower.

So when you look at the movements that you referenced in terms of crude and natural gas, you have seen some low-teens to mid-teens movement downwards in spot crude. But when you look 4 to 5 years out, that you have seen movements a lot less than that.



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And from the standpoint of our overall holdings, we are pretty equally split between natural gas and crude. And natural gas prices actually haven't seen that same type of volatility -- at this point.

Now, one of the things that does lead into that's also just worth mentioning is from a deployment standpoint, one of the nuances is that if you look at the second quarter, at least, we actually were not terribly active in deploying -- or were not active, even, in terms of deploying capital in Q2 in our energy strategies. I think, as we have seen commodity prices moved down even since June 30, we actually think that could help opportunities in the back half of the year.

So we are pretty constructive on what that opportunity is and what those opportunities could be for us. Although, at the margin, we are probably seeing more opportunities at the asset level versus the corporate level.

And one other point as we think about this vertical actually would relate to infrastructure. Because infrastructure actually is an area where we have been very active. So even within the last couple of -- last two weeks, we have announced another couple of investments within our Infra II funds. Those naturally have not closed. But at this point, even with those four investments, Infra II is over 25% committed, which is certainly a healthy figure, recognizing that we only held a final close in Infra II earlier in the month.

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**Operator**

Patrick Davitt, Autonomous.

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**Patrick Davitt** - *Autonomous Research LLP - Analyst*

Thanks for the follow-up. You mentioned the third-party minority stakes in hedge funds. Could you walk through all of the hedge funds that are in that bucket and how they are performing?

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

Sure, Patrick. So a couple things. Stepping back, as a reminder, let's just talk about the hedge fund business broadly for a moment. So we've really got three or four different components.

So we have the KKR Prisma platform, where we manage about $11 billion of solutions in fund-to-funds mandates. We are creating new product off that platform, more direct investment product. So we will give you updates on that as those efforts build over time.

We mentioned the seed investment that we made in Asia, the Acion partners investment that I mentioned in the prepared remarks. And on the stakes side, today, we really have two. We have got Nephila, which manages about $10 billion, and then we have Black Gold, which manages approximately $2 billion.

So $12 billion in aggregate and we own approximately 25% of each. And so if you take the 25% of the $12 billion that is how you get the $2.9 billion on slide 7 as part of that bridge.

We have taken a different approach to stakes than others, which is that we are approaching it much more as a strategic matter. So this is investments that we are making off our balance sheet. And we believe that we have an ability to work with our partners to create new product and deliver solutions to clients that otherwise we cannot deliver with just the products that we manage on a 100% owned basis. Both Nephila and Black Gold, financially, for the Firm, have performed in line with or in excess of original expectations.

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**Patrick Davitt** - *Autonomous Research LLP - Analyst*

And was there another negative mark in the LP investment you have in Black Gold -- the $100 million?

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

It was flat to the second quarter.

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**Operator**

I would like to turn the call back to Mr. Larson for any final remarks.

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**Craig Larson** - *KKR & Co. L.P. - Head of Investor Relations*

Just thank you, everybody, for your time. Thank you, Carmen. If there are any follow-up questions, please feel free to follow up with me directly.

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**Operator**

Ladies and gentlemen, thank you for participating in today's conference. This concludes the program and you may all disconnect. Have a wonderful day, everyone.

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