FINAL TRANSCRIPT

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PRESENTATION

Operator

Ladies and gentlemen, thank you for standing by. Welcome to KKR's Third Quarter 2010 Earnings Conference Call. During today's presentation, all parties will be in a listen-only mode. Following management's prepared remarks, the conference will be open for questions. This conference call is being recorded.

I would now like to turn the conference over to Jon Levin, Treasurer and Head of Investor Relations for KKR. Jon, please go ahead.

Jon Levin - *KKR & Co. L.P. - Treasurer, Head of Investor Relations*

Thank you, Karen. Welcome, everyone, to our third quarter call. As usual, I'm joined on today's call by Scott Nuttall and Bill Janetschek.

We'd like to remind everyone that today's call contains forward-looking statements, which do not guarantee future events or performance. Please, refer to our SEC filings for cautionary factors related to these statements.

We'll also refer to non-GAAP measures on this call, which are reconciled to GAAP in our press release.

To begin today's call, I'll briefly highlight our results, cover our inaugural investment-grade debt offering, and wrap with an update on recent fundraising activity. Then, I'll turn it over to Bill to discuss the financials in a bit more detail and Scott to go over the business environment and an update on each of our segments.

This morning, we reported economic net income of $317 million for the quarter, which compares to pro form ENI of $823 million for the third quarter last year and $433 million for the second quarter of this year.

It's important to discuss the two comparisons separately. The year-over-year decline is primarily driven by a lower rate of appreciation of our private equity portfolio, but the sequential change is a function of mix. While the rate of appreciation of our private equity portfolio overall was higher in the third quarter than in the second quarter, the rate of increase on our balance sheet assets was lower. Importantly, though, this is the sixth consecutive quarter that our investments have appreciated in value.

In the quarter, our private equity funds appreciated by 6% compared to an 11% gain for the S&P 500, and on a year-to-date basis our funds are up 20% compared to only 4% for the S&P 500. So far this year, we've generated over $1.4 billion of ENI, roughly in line with last year.

On the bond offering, on September 29th, we issued $500 million of ten-year notes with a six and three-eighths coupon. We'll use the proceeds from this offering to continue investing in our business, seeding new strategies, investing in our funds and transactions, and supporting our Capital Markets franchise. As we have mentioned before, we like the dynamic of being a large investor in everything we do, and this offering will allow us to make sure that continues as we launch new businesses, products, and funds. $500 million represents a modest amount of leverage on our business given our significant fee-related earnings, carry generation, and $5 billion balance sheet. The notes are rated A and A- by Fitch and S&P. The ten-year term on the debt and the low after-tax cost of funding will allow us to maintain our long-term focus on the business.

Next, onto fundraising, during the third quarter our fee-paying AUM grew 2.5%, and since the end of the quarter, capital-raising activity has been significant. We held a first close on a China growth equity fund of over $700 million and expect to reach our hard cap of $1 billion on that fund. We also closed on an additional $500 million for our capital solutions effort in our Public Markets segment, and we raised a $1.1 billion separately managed account to buy a pipeline asset in partnership with the National Pension Service of Korea. This is in addition to the approximately $500 million we anticipate closing on in our infrastructure funds before year-end, $225 million of which came in during the third quarter. That would bring our total infrastructure-related capital raised so far to approximately $1.6 billion, up from zero at June 30th.

With that, I'll turn it over to Bill.

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

Thanks, Jon. Our assets under management were $55.5 billion at quarter-end, up $5.1 billion, or 10%, from the same time last year and up $1.1 billion, or 2%, from last quarter.

The sequential increase is largely a result of appreciation in our investments as well as new capital raised in our Public Markets segment. This was partially offset by significant realization activity in our private equity funds, primarily related to the sale of East Resources. Because this investment was in the 2006 Fund, which is still in the investment period and pays management fees based upon committed capital, there was no corresponding reduction to fee-paying AUM.

As Jon mentioned, our fee-paying AUM was up $1.1 billion, or 2.5% on a quarter-over-quarter basis. The sequential increase was driven by new capital raised, changes in foreign exchange on euro-denominated commitments, and NAV growth in certain vehicles in our Public Markets segment.

The recent fundraising activity Jon mentioned earlier will grow our fee-paying AUM base in future quarters.

Year-to-date, our fee-related earnings continue to outperform last year as a result of new capital raised and increased incentive and transaction fees due to an overall healthier environment. In the first nine months of the year, our fee-related earnings grew

40% from $160 million in 2009 to $223 million in 2010. Our economic net income for the same period was down less than 1%, which was due to a lower rate of appreciation of our principal investments.

Turning to our business segments, our Private Markets segment generated economic net income of $174 million in the quarter, which compares to $155 million last quarter and $304 million in the same quarter of last year. Both the sequential increase in ENI and the year-over-year decline in ENI were the result of changes in the amount of net carried interest recognized, which is largely driven by the rate of appreciation in our private equity funds. Our funds were up 6% this quarter versus 3.5% last quarter and 18.5% in the third quarter of 2009.

Fee-related earnings in the Private Markets segment were $43 million, up slightly from $42 million in the second quarter and down from $54 million the prior year. The year-over-year decline in fee-related earnings was driven primarily by lower monitoring and transaction fees. Monitoring fees were lower due to a termination payment made in the third quarter of last year, and transaction fees were lower due to a lower level of capital deployed. Investment activity is generally much stronger this year than last, but the timing in the closes can lead to volatility in transaction fees quarter to quarter. While we deployed on $350 million during the third quarter, we have now deployed $2.2 billion of equity in our Private Markets segment year to date and we have committed to transactions representing over $2 billion of additional equity capital that have closed or are expected to close in the fourth quarter.

As of September 30th, we are accruing carry in all of our funds except the European Fund II or in over $20 billion of the $26 billion in total invested capital in our active private equity funds.

Some of our funds are also in a cash-carry paying position, notably our first European and Asian Funds. In addition, we are close to being in a cash-carry paying position in the Millennium and Europe III Funds. The distinction between accruing carry and paying cash carry is an important one. Our private equity funds do not have a preferred return, which means we accrue carry from the moment a fund is marked above cost. However, we only begin to pay out accrued carry in cash upon a realization event once the fund is above cost and any netting holes have been filled.

In our Public Markets segment, we generated $13.9 million of economic net income during the quarter, which compares to $4.4 million in the same quarter last year and $12.2 million last quarter. The increase in both periods relates primarily to increased incentive fees earned from KFN. We saw growth in both AUM and fee-paying AUM, largely as a result of new capital raised on a net basis and appreciation in net asset value of our various vehicles.

Our Capital Markets and Principal Activities segment generated economic net income of $130 million during the quarter, which compares to $515 million in the same quarter last year and [$266 million] (corrected by company after the call) in the prior quarter. The decline in ENI was driven by a lower rate of appreciation of our balance sheet investments relative to the comparable periods. In the third quarter, our balance sheet assets were up less than our funds overall due to their weighting towards US investments, which saw lower appreciation than our portfolio as a whole.

The fee-related earnings generated by our Capital Markets business were above last quarter and significantly higher than last year. This was driven by 13 Capital Markets transactions executed globally that generated $19 million in fees for the quarter.

In terms of our balance sheet, our book value is $7.63 per unit as of the end of the quarter, which is up 3.5% from last quarter and up over 25% from the beginning of the year. It's worth noting that more of a quarter of our balance sheet investments are public securities.

We ended the quarter with approximately $1.1 billion in cash and drawn debt of $760 million. Subsequent to quarter-end, we repaid over $150 million of borrowing under our revolving credit facilities using a portion of the proceeds from our bond offerings.

Finally, we are making a third-quarter distribution of $0.15 per common unit. About half of the distribution this quarter is attributed to fee-related earnings while the other half is attributed to cash carry primarily related to the sale of East Resources, which we discussed last quarter. As a reminder, East was a 2006 Fund investment that did not net with the rest of the fund due to the structure we needed to use to make this particular investment. The 2006 Fund is above cost and accruing carry but is not currently paying cash carry as a result of fund netting. Thanks for joining the call, and I will now pass it over to Scott.

Scott Nuttall - *KKR & Co. L.P. - Member*

Thanks, Bill. Today, I'm going to comment on what we're seeing in the macroeconomic environment, cover key highlights across each of our businesses, and then conclude with a brief discussion of our economic model.

The macroeconomic environment has not changed much since we spoke last quarter. The overall economic recovery has been inconsistent from a regional perspective, and while Asian markets continue to gain momentum and European markets are generally experiencing a stable recovery, the pace of recovery in the US seems to have slowed.

Unemployment in the US remains stubbornly high, consumer confidence is stagnant, and policy and regulatory changes are still unclear, collectively leading to a generally cautious mood.

Despite all this, credit markets are strong. New deals have been getting done at over five times debt to EBITDA, and equity contributions have been declining and are back below 40%.

As a result of the strong credit markets, new issuance volume is booming, especially in high yield, where investors are increasing their risk appetites. Also, we've seen the return of dividend refinancings, typically an indicator of stronger markets.

On the more negative side, we continue to face an uncertain IPO market where pricing and post-IPO trading has left many planned IPOs on the shelf.

So overall, while things feel a lot better than they did a year ago, we still have a long way to go.

In our Private Markets business, we continue to be quite active. We invested $350 million during the quarter, and we have over $2 billion committed to deals that had not yet closed at quarter-end. About $1 billion of that's in private equity transactions, over $1 billion to infrastructure investments, and over $150 million is to oil and gas deals. Our pipeline continues to be quite diversified and strong by strategy, industry, and region.

As Jon mentioned, we have also had recent success in capital-raising in Private Markets. We raised over $1.3 billion for our infrastructure efforts in the quarter and expect nearly $275 million more to close shortly, and we held a first close for our China Growth Fund on more than $700 million. China Growth is a new strategy for us. It will enable us to take advantage of more of the opportunities we're seeing in China by giving us a pool of capital to deploy in smaller-cap companies there.

This quarter, I want to go into a bit more detail on the progress we're seeing in our private equity portfolio. So far this year, we've returned approximately $2.4 billion of capital to our limited partners, and we have returned $3.2 billion since the beginning of 2009.

The first step to returning capital is strong portfolio company performance. As mentioned, our portfolio is up 20% so far this year and up about 64% since our funds' valuation trough on March 31, 2009.

On a year-to-date basis through August, over 80% of our private equity portfolio companies grew their revenues and EBITDA year over year, and in the first eight months of 2010 our portfolio companies' aggregate revenue is up 5% and aggregate EBITDA is up 11%.

We're also very focused on the capital structures of our portfolio companies, and we've refinanced almost $35 billion of debt since the beginning of 2009. While we continue to work hard to reduce refinancing risk across our portfolio, we're pleased that over 80% of the debt maturities in our portfolio companies are in 2014 and beyond.

Of course, operational performance and managing our debt maturities are only part of the story. Ultimately, we'll need the capital markets and M&A activity to help us achieve realizations. And while we've seen a pick-up in corporate M&A activity, which may lead to some exits for our investments, the IPO market remains subdued.

When the IPO market opens, we believe our companies' strong operating performance will drive realizations for our limited partners and drive carry generation for our firm.

Now moving to our Asset Management business, it was a strong quarter for below-investment-grade leveraged credit. Year to date, leveraged loans have returned 7% and high-yield bonds have returned 12%, which compares favorably to the equity markets.

In liquid credit, we have continued to be a top-quartile performer over the past year. Our strategies in this space include secured credit, which is up 12%; banks loans plus high-yield, up 15%; high-yield standalone, up 22%; and opportunistic credit, up 24%.

We still see select opportunities in liquid credit with floating-rate loans offering attractive cash yields plus inflation protection. And despite the recent strength in the market, high yield spreads remain above their historical averages. Having said that, we remain cautious and very selective in the more subordinated parts of the capital structure, given the uncertain economic environment.

In originated financing, distressed, and proprietary credit, we continue to see a lot of opportunity. Companies appreciate the return of relationship financing, and trust and speed of execution and command premium pricing. Our mezzanine and capital solutions efforts are well positioned in this type of environment and have been very busy. Year to date, we have invested or committed to invest approximately $1 billion of capital in originated credit and special situations, including over $650 million since June 30.

To augment our asset management platform, we recently announced that key members of the Goldman Sachs Principal Strategies team will be joining our firm in January. They'll be a fully integrated part of KKR and our Asset Management division, working alongside our existing credit team and building out a strategy focused on long/short public equities for our clients. We're extremely excited to pursue this new opportunity with such a high-caliber group.

We continue to raise capital in our Asset Management business. Most recently, we held an additional close for our mezzanine fund and raised new separate accounts for liquid credit focused on leveraged loans and high yield. We also added a new $500 million separate account in capital solutions, which includes special-situations strategies like distressed and rescue financing.

In our Capital Markets and Principal Activities segment we reported a strong quarter, particularly in North America. Our Capital Markets group participated in transactions involving several of our private equity portfolio companies, including First Data, NXP, Visant, Avago, and Inaer, among others. They were also involved in transactions for Harden Healthcare, a company we invested in through our Public Markets business.

Overall, we feel we had a good quarter and we're making progress across our segments.

At the end of our call last quarter, we discussed our strategy, which is founded in the simple observation that we can do more with the intellectual capital, insights, and relationships we have at KKR.

We explained that we are investing in our business in multiple ways to better monetize our content and that we are doing so in a one-firm model where we bring our best thinking and resources to bear in everything we do.

This quarter, we've continued to execute on this strategy and vision. We launched our China Growth Fund to allow our China team to invest in smaller companies they know and like.

We advanced our infrastructure business by completing a first close on our infrastructure fund and raising capital through an innovative relationship with an important partner and investor.

And we hired the Goldman Sachs Principal Strategies team to allow us to create a public equity long/short platform.

We feel that we're better leveraging our content, but there is much more to do to realize our full potential.

We think about our earnings and distribution in a similar fashion.

Our firm has a significant amount of earnings power -- $1.4 billion in the first nine months of this year alone.

year to date, we have accrued $385 million in net carried interest but only paid out $115 million in cash.

As our private equity funds continue to perform, we expect our cash carry to increase, which would lead to meaningful increases in our distribution.

In short, we believe we can monetize more of our investment content and more of our earnings power. And since all of us at KKR own 70% of the equity right alongside you, we're excited about this potential.

Thanks again for joining the call, and we're happy to take your questions.

QUESTIONS AND ANSWERS

Operator

Thank you.

(Operator Instructions)

We'll take our first question from Michael Kim with Sandler O'Neill.

Michael Kim - *Sandler O'Neill - Analyst*

Hey, guys. Good morning.

Jon Levin - *KKR & Co. L.P. - Treasurer, Head of Investor Relations*

Good morning, Michael.

Michael Kim - *Sandler O'Neill - Analyst*

First, if I could just follow up on the portfolio company marks this quarter, I know the marks are partly a function of public market comps. But, did you make any kind of changes in terms of your EBITDA assumptions more recently?

Jon Levin - *KKR & Co. L.P. - Treasurer, Head of Investor Relations*

No changes to the process this quarter, Michael. It's Jon speaking here. I think as a general matter, as we've talked about in the past, the mark-to-market process for the private companies, which represents about 75% of the portfolio, is a function of DCF analysis and comp analysis.

As a general matter, it's -- we could give a rule of kind of 50/50 to each weighting, although that can change depending on a specific company's circumstances. And we kept that methodology in place.

So, you're going to see directional correlation to the equity markets quarter-to-quarter, but it won't be perfect. And certainly, if you look at the year-to-date performance of 20% for the portfolio versus 4% for the equity markets, that's got to be a function not just of equity markets but also of driving the EBITDA performance at the companies.

Michael Kim - *Sandler O'Neill - Analyst*

Okay. That's helpful. And then, I'd be curious to get your thoughts on kind of the fundraising environment. It seems like institutional demand for alpha is starting to pick up and your pool of potential investors seems to be broadening out. But, at the same time, maybe some of these investors are still dealing with kind of liquidity constraints. So, how do you think those trends kind of affect the fund-raising environment going forward?

Scott Nuttall - *KKR & Co. L.P. - Member*

Hey, Michael, it's Scott. Yes. I think what we're seeing is a much improved fund-raising environment, especially relative to a year ago. There are still some institutional investors that are cautious. But on the whole, I think your characterization is accurate. We're seeing people looking for alpha, trying to figure out how to drive returns, and that's leading to a highly productive set of conversations across a number of different products and geographies for us.

As we noted in the comments, we've seen quite a bit of success recently with the China Growth Fund, our infrastructure fund, the infrastructure separate account, and some more capital solutions dollars, so it's pretty broad-based, and the investor universe is across US, Europe, Middle East, and Asia. So, we're seeing interest from around the around the world and across our product set. So, we're much more upbeat on the fundraising environment than we would have been 12 months ago.

Michael Kim - *Sandler O'Neill - Analyst*

Any update on kind of the new North American fund and how you're thinking about that going forward?

Scott Nuttall - *KKR & Co. L.P. - Member*

No real update. I think it's similar to what we said last quarter. It's we expect to start the process sometime over the next couple of quarters, and we're not quite there yet but we're preparing to get started.

Jon Levin - *KKR & Co. L.P. - Treasurer, Head of Investor Relations*

Yes, Michael, I think the important -- just to add one point to what Scott said there, Michael, it's important to keep looking at that dry powder we have in the North America fund where we still have almost $9 billion -- $5 billion, sorry, to invest.

Michael Kim - *Sandler O'Neill - Analyst*

Yes. Okay. Just finally, can you maybe talk a little bit more about what you're seeing in terms of deal flow? The markets have stabilized to some extent. To your point earlier, financing seems to be available and you've certainly got ample dry powder to put to work. But, at the same time, maybe seller expectations are starting to get a bit more, lofty, as well. So, do you think that could potentially be a reason why we haven't seen deal flow pick up more meaningfully?

Jon Levin - *KKR & Co. L.P. - Treasurer, Head of Investor Relations*

Look. I think we've been pretty active, Michael. I'd say the way we think about private equity is it's about patience and investing and tenacity and ownership.

And what you really need is you need industry expertise and special relationships so you can drive proprietary deal flow, and you need an ability to dictate outcomes and change businesses so you're not just along for the ride.

And so, we've got teams all around the world that have the industry expertise, that have those relationships, and then we have our operating teams that can drive change in companies. So, we've been active globally.

In particular, if you look at the dollars that we've invested this year in private equity, it's been largely in Europe and Asia. But, we've also been very active in the US. There have been some situations that we were very interested in, but the valuations got away from us.

But if you look at where we put dollars to work this year, it's been pretty broad-based. We've invested in a couple deals in India, a large cement company called Dalmia, a fast-growing retailer called Cafe Coffee Day. We've done some proprietary deals in China. The deal we did in the US was an energy deal, which was proprietary (Hilcorp). We bought a company called Pets at Home, which is a retail company in Europe. And we've done two deals in the Nordics very recently.

So we feel like we've been active. The pipeline's full. I think we attribute that to companies and boards having a better line of sight as to what's going to happen with their profitability going forward and, frankly, the fact of the financing markets being open and allowing us to get some of these transactions done.

So it's all about patience, but you've got to know what you're going to do with the asset post-purchase. And if we don't have a strong perspective on that, we're not going to move forward. But I'd say, overall, we're very excited about the pipeline we've got in front of us and also the investments that we've made.

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

Hey, Michael, this is Bill. Keep in mind that, to date, we've invested $2.2 billion in private equity as of September 30. And, as Scott mentioned earlier in the call, we're going to close on, or have closed on, approximately $2 billion in the fourth quarter. So that'll bring the number up above $4 billion.

Michael Kim - *Sandler O'Neill - Analyst*

Yes, that's helpful. Okay, thanks for taking my questions.

Operator

(Operator Instructions)

Our next question comes from Bill Katz with Citi.

Bill Katz - *Citigroup - Analyst*

Okay, thank you. Good morning, everybody.

Scott Nuttall - *KKR & Co. L.P. - Member*

Good morning, Bill.

Bill Katz - *Citigroup - Analyst*

Wondering a little bit about the economics of the business a little bit, maybe on the incremental capital -- any changes in any of the structure between the GP and the LP, fee rates, hurdle rates, et cetera?

Scott Nuttall - *KKR & Co. L.P. - Member*

Hey, Bill, it's Scott. Look, I think this really varies product to product. There hasn't been a lot of material changes but on the capital that we've raised recently.

The China Growth Fund that I referenced, it's a traditional private equity fund structure for us. So the economics are generally consistent with our traditional PE funds, so not much of a change there.

On infrastructure, that's -- it's a bit of a different economic model. So the capital that we closed on and hope to close on shortly, that's more like a 1% management fee and a 10% carry. And so -- and that does have a hurdle, as distinct from our private equity funds, which generally do not.

Also, we've raised this $1.1 billion in this transaction with the National Pension Service of Korea. That's a bit of a one-off, the modest management fee in a carry structure more similar to our infrastructure fund.

As we look to the Public Markets business, we haven't seen a lot of change in the terms relative to prior quarters, so not a lot of change. There's always a discussion about terms. But we found that when we walk people through the value proposition, we've been able to keep terms pretty consistent with what we talked about with you in the past.

Bill Katz - *Citigroup - Analyst*

Great. Could you specify what the hurdle is on the infrastructure fund?

Scott Nuttall - *KKR & Co. L.P. - Member*

8%.

Bill Katz - *Citigroup - Analyst*

Okay, terrific. Second question is, and this might be a little premature, but I have to ask it anyway. In terms of the group you're brining on, can you talk a little bit about the timeline you would think before you could actually start to potentially raise some capital for that group? And then, more broadly, just talk about -- you mentioned before (inaudible) that you want to use your capital for. Can you sort of prioritize maybe one, two, three how you're sort of thinking about the use of the incremental leverage?

Scott Nuttall - *KKR & Co. L.P. - Member*

Sure. On the first part of your question, Bill, are you talking about the Goldman team?

Bill Katz - *Citigroup - Analyst*

Yes, I am.

Scott Nuttall - *KKR & Co. L.P. - Member*

Okay, great. Look, I think for the Goldman Sachs Principal Strategies team, they're not going to start until January at the firm, so it'll take a while. And once they do start, we'll need to set up operations and IT, et cetera.

I think it's important to understand that this is going to be a third-party business, not a prop business. And so while we may seed the group with some capital off the balance sheet, and it'll be a reasonable modest amount of capital, the anticipation is that we will, once we're ready, go out and talk to third-party investors about investing in the platform. So I would guess it would be sometime next year, but probably the latter part of next year, before we start that process. And, Jon, do you want to talk about the balance sheet?

Jon Levin - *KKR & Co. L.P. - Treasurer, Head of Investor Relations*

Sure, just in terms of the bonds that we issued during the quarter, Bill, I think it's really just a capital-efficient way of allowing us to continue the strategy of investing in the business.

You're looking at ten-year paper at about a 4% after-tax cost of funding that allows us to pursue the organic growth strategy we have of seeding new strategies, investing capital behind the capital markets business, and continuing to be a meaningful investor in everything we do. And we think that this was an attractive way to finance that organic growth.

Bill Katz - *Citigroup - Analyst*

I mean, just one last question; just given the robustness of the business as it sounds like both in terms of results in this conversation, there's been some upward pressure on comp in some of the other ancillary businesses within asset management based on some of the third-party commentary of some of the other managers. So I'm curious if you could talk a little bit about maybe the underlying profit margins of the business. Are you seeing any kind of pressure to raise compensation or other type of investment spending?

Scott Nuttall - *KKR & Co. L.P. - Member*

Hey, Bill, it's Scott. No, there's no material change in how we think about compensation or the pressures we're feeling. We've got a lot of great people, and they're compensated kind of in accordance with market-plus. And we also, obviously, have a lot of folks who are owners in the company. Everybody in the firm owns stock. So, if anything, we feel, now that we have a lot of stock ownership, we feel a little bit more freedom because we have one more tool to use to compensate people on a go-forward basis. But there's no material change.

Jon Levin - *KKR & Co. L.P. - Treasurer, Head of Investor Relations*

Yes, Bill, I'll just add to what Scott said. It's Jon here. I mean, if you look at the fee-related earnings margin, which is really the one that would capture the comp. It's hovered around that kind of high 30s, low 40s percent range over the last several quarters.

Where you've seen upside or downside to that has been on some of the in the particular quarters where you may have a higher amount of transaction fees or capital markets business, which has a high flow-through relative to it versus adverse quarters where you have less of those fees and you see that hit the margin. But we haven't seen that much of a change to that as we've expanded the business.

Bill Katz - *Citigroup - Analyst*

Okay, terrific. Thanks for taking all my questions.

Scott Nuttall - *KKR & Co. L.P. - Member*

Thanks, Bill.

Operator

Next we'll hear from Patrick Davitt with Bank of America Merrill Lynch.

Patrick Davitt - *Bank of America Merrill Lynch - Analyst*

Good morning, guys.

Scott Nuttall - *KKR & Co. L.P. - Member*

Good morning.

Patrick Davitt - *Bank of America Merrill Lynch - Analyst*

Well could you give us a little bit more detail as to what about the principal portfolio in terms of differences versus the overall portfolio drove such kind of a disconnect between the performance?

Jon Levin - *KKR & Co. L.P. - Treasurer, Head of Investor Relations*

Sure, Patrick. It's Jon. I think the first thing I would just say is on a year-to-date basis, because we do expect both the (inaudible) assets and the private equity portfolio to be generally correlated. I mean on a year-to-date basis, they're both up around 20%.

What happened last quarter is that the private equity funds were up about 3%, and the balance sheet was up about 6%. In this quarter, we saw the reverse of that, where the balance sheet was up about 3% and the funds were up 6%.

The biggest driver of that is just the weighting of the assets and really, specifically, around the euro-denominated investments, which are more weighted in our funds than they are on the balance sheet, which saw a higher uptick not only because of currency, but also just because of how that particular portfolio performed this quarter.

So over a longer term, given the mix of the portfolio in the balance sheet, we'll see a correlation. But it can break down to some extent on a quarter-to-quarter basis. And, given our P&L reflects 100% of the income off the balance sheet versus the portfolio where we're picking up 20% through the carry, you can see that impact come through in terms of the P&L.

Patrick Davitt - *Bank of America Merrill Lynch - Analyst*

Okay, that's helpful. Why in the management fee refund in private markets? Why was there not a larger refund this quarter with Euro III moving over the costs like you saw with Asia in 2006 earlier in the year?

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

Hey, Patrick. This is Bill Janetschek. That's a good question. What happens is we have a management fee refund where we actually have to return approximately 20% of all management fees collected for the EIII Fund. So what happens is the EIII Fund went from being flat to actually accruing carry. And the management fee refund is only going to be capped to the amount of carry that would be recognized.

Patrick Davitt - *Bank of America Merrill Lynch - Analyst*

Okay.

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

There is still additional management fee refunds that will come through the system as we continue to write up the portfolio, but for right now in this particular quarter, it's limited to that number.

Patrick Davitt - *Bank of America Merrill Lynch - Analyst*

Okay, that's helpful. And then you mentioned the dividend recap opportunity. As you look at your portfolio now, do you have an idea of the size of that opportunity to -- for your portfolio at this time?

Scott Nuttall - *KKR & Co. L.P. - Member*

Hey, Patrick. It's Scott - (inaudible - multiple speakers)

Patrick Davitt - *Bank of America Merrill Lynch - Analyst*

...relative to maybe...

Scott Nuttall - *KKR & Co. L.P. - Member*

Go ahead.

Patrick Davitt - *Bank of America Merrill Lynch - Analyst*

Go ahead.

Scott Nuttall - *KKR & Co. L.P. - Member*

No, I was going to say we don't -- we've had some of our companies pursue dividend recaps of some size, but we don't have a specific number to share with you today. We'll look to be opportunistic where it makes sense, where the company's ready, but I think it's going to be a limited number of cases.

Patrick Davitt - *Bank of America Merrill Lynch - Analyst*

Okay, okay. Thanks a lot.

Scott Nuttall - *KKR & Co. L.P. - Member*

Sure.

Operator

Next we'll hear from Oppenheimer & Co.'s Chris Kotowski.

Chris Kotowski - *Oppenheimer & Co. - Analyst*

Good morning. I wonder -- a couple of questions on the use -- sources and uses of capital on your own balance sheet. First of all, I guess just looking at page 21, we see that the amount of general partner commitment to the infrastructure fund is 22%. I -- , right? And for the other funds, it was typically 3% to 4%. Was it, I guess, a conscious strategy to put that much in? Or are you just expecting more of a raise before the final close?

Scott Nuttall - *KKR & Co. L.P. - Member*

Yes, I -- hey, Chris, it's Scott Nuttall. We're -- it's more of the latter. We're expecting that percentage to go down hopefully as we continue the capital-raising process. So we're just seeing the initial GP number relative to the relatively small dollars that came in first.

Jon Levin - *KKR & Co. L.P. - Treasurer, Head of Investor Relations*

Hey, Chris, just to add to that, even just on the comment Scott made on the call where we talked about having reasonable -- looking to getting to $500 on infrastructure, that 22 would go down to 10, just based on that comment that Scott made on the prepared remarks.

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

This is no different than the strategy we deployed when we actually committed capital to the mezzanine fund when we first launched that.

Chris Kotowski - *Oppenheimer & Co. - Analyst*

Okay. And then the China Growth Fund, that -- I guess is that a fourth quarter event? Or because -- and can you say how much you've committed to that?

Jon Levin - *KKR & Co. L.P. - Treasurer, Head of Investor Relations*

Sure. In terms of the funds raised, the $700 million that we talked about in the prepared remarks has already closed. The $1 billion we expect to get to, which is the hard cap on this fund, is something that we would expect to happen in short order. So that is a fourth quarter event. In terms of the firm's commitment to that strategy, it'll be meaningful, which will include both the balance sheet and as individuals.

Chris Kotowski - *Oppenheimer & Co. - Analyst*

Okay. And then were there in this quarter -- I mean, I guess a major realization was East Resources. Did that generate any cash for -- any meaningful amount of cash for the firm's own reinvestment in other funds? Or is it primarily coming out -- are these investments primarily coming out of balance sheet cash thus far?

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

Well you have to break East into, really, two components.

During the quarter, we sold the investment and the realized carry to the company was approximately $100 million. And that number is reflected on page 22 as distributable cash carry.

In addition, we're also an investor as an LP. And that transaction, again, closed in the third quarter and that amounted to roughly an incremental $75 million of cash for the balance sheet.

Chris Kotowski - *Oppenheimer & Co. - Analyst*

Okay. And then I guess I'm just thinking on your comments in general about the high yield market is open, the IPO market is not... I mean, it all just, to the extent that you -- to generate realized gains, it sounds like the logical thing to do would be to step up some dividends, especially from the companies that are financially capable of doing that. Is that a strategy? Or is the world just still too frail that one really can't do that in any significant way?

Scott Nuttall - *KKR & Co. L.P. - Member*

Hey, Chris, it's Scott. I'd say a couple things. One, the IPO market has been pretty choppy. It looks better in the last few weeks, frankly. There seems to be a much better tone to it. So we're hopeful that that continues.

In companies where the capital structure allows it and we think the financial results make it a responsible thing to consider, we will look at paying dividends. There's not many companies, frankly, where we think that's going to move the needle dramatically, but it is something that we consider from time to time.

Chris Kotowski - *Oppenheimer & Co. - Analyst*

Okay. And then, lastly, I guess, just you still have about $2 billion or half of the Asian Fund is un-deployed, yet you raised the China Growth Fund. I was just curious; why not deploy all that capital first and then another general Asia fund? Or why have these in parallel?

Scott Nuttall - *KKR & Co. L.P. - Member*

Sure. Hey, Chris, it's Scott again. The reason for that is the funds have different mandates. So the Asian Fund is meant to invest in larger opportunities across Asia and, in particular, is focused on opportunities where the equity investment is $75 million or greater.

The China Growth Fund is very specific to China and faster-growing companies where the equity check is smaller than that appropriate for the Asian Fund. So think of it as a specific strategy for China to invest in smaller, fast-growing companies. So it's got a different mandate than what was initially agreed for the Asian Fund on a traditional private equity basis.

Chris Kotowski - *Oppenheimer & Co. - Analyst*

Okay, great. That's all for me. Thanks.

Scott Nuttall - *KKR & Co. L.P. - Member*

Thank you.

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

Thanks, Chris.

Operator

Our next question comes from Robert Lee with KBW Securities.

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

Thanks. Good morning, guys.

Scott Nuttall - *KKR & Co. L.P. - Member*

Good morning, Robert.

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

Real quickly, I'm just curious. I mean, I know you've put a lot of effort in expanding your shareholder base, your investor base, excuse me. But I'm just curious on these recent fundraisings. Has it -- are you actually starting to see the broadening of the investor base? Is there any kind of color you can give us about what proportion you're seeing coming from new investors as well as maybe US versus non-US?

Scott Nuttall - *KKR & Co. L.P. - Member*

Sure. Hey, Robert, it's Scott. I'd say that we're actually pleased as we look at the makeup of the investor base of these newer products and recent fund closings, what it signals in terms of the impact that our client partner group's having.

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The majority of the capital we've raised, if you look across mezzanine, infrastructure, et cetera, has actually been new investors for the firm -- there've been people that have not really invested with us before and we've only really gotten to know in the last year or two. So we're pleased with that.

In terms of where the capital is coming from, it's pretty broad-based. It's US, Europe, Asia, Middle East, institutional investors, some sovereign wealth funds, some insurance companies. So it's a pretty broad-based group and a global group.

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

All right, great. And then, also, I'm just curious, Scott. I think you were the one that mentioned in Public Markets in addition to the $500 million earmarked for capital solutions, or closed for capital solutions, I think you talked about seeing success with additional separate accounts and leveraged loans and elsewhere. Any kind of color you could provide on kind of what size maybe, kind of the pipeline of closings you have out there or RFP activity, however you want to define it?

Scott Nuttall - *KKR & Co. L.P. - Member*

Sure. Well if you look at actually the press release on page 20, Robert, you'll see that we've laid out some of the dollars in terms of what was raised in the quarter, which was about $420 million. A lot of that was in our liquid credit products that were high yield and leveraged loans.

It's hard to be too specific about the pipeline. But we do see a significant amount of opportunity to continue to scale that business. A number of our track records are coming up on a three-year anniversary, which are top quartile.

So our intention is to continue to scale the capital that we have in our liquid credit products. And as we look at kind of the RFP activity and we look at the conversations we're having around the world, we think we're at the front end of hopefully being able to scale that business meaningfully.

Jon Levin - *KKR & Co. L.P. - Treasurer, Head of Investor Relations*

And, Robert, it's Jon. Just to clarify on that, one thing to what Scott said, the liquid loan and -- the liquid leveraged loan and high yield strategies and mezzanine capital Scott described we raised during the quarter, which makes up that $400 million, but the $500 million we discussed was additional money that was raised subsequent to the end of the quarter.

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

Right. Okay, and I'm curious about the $1.1 billion, that separate account. I guess it's for a specific infrastructure investment. I don't know if there's any -- I guess, related to infrastructure, that's obviously separate from the infrastructure fund. I mean, in addition to the incremental closing you expect this quarter, is there an open target you have for the infrastructure fund? Is it the $500 million? Is it $1 billion? And any color you can provide around that kind of one-off separate account and investment, I guess that would be helpful.

Scott Nuttall - *KKR & Co. L.P. - Member*

Sure. I'll take them in turn. In terms of the infrastructure fund itself, we haven't put out a specific target. So far, we closed on the $225 million, and then the $275 million that we anticipate closing shortly we hope will get us to this $500 million. But we will continue that capital-raising process, but we do not have a target.

And in terms of the $1.1 billion partnership with National Pension Service of Korea to invest in the Colonial pipeline, that is a specific transaction, it's a close partner of the firm, and it's something that we've been working on with them for a while. I'm not sure we're going to have too many transactions like that, Robert, but it was a situation where we knew the asset well and we had a partner that we wanted to work with. So I don't think you should be thinking about a lot of those in the future. But they'll happen from time to time.

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

Okay, and thanks for indulging my questions. One last one: just with the team from Goldman that's coming on board, I'm understanding that you've got to kind of build an infrastructure around it. Just in the near term, how should we be thinking about how we may see some lift in expenses just as you kind of have to build out a platform, take these guys and gals on board, and pay them something until the assets start coming in the door. I mean, anything meaningful or anything we should be thinking about?

Scott Nuttall - *KKR & Co. L.P. - Member*

Well, I think your characterization's appropriate. We'll have probably a modest lift in our expenses in the near term before the revenues show up. I'd expect hopefully the capital we use to seed the strategy will generate a positive return, which will help offset that. But it really won't have a meaningful impact one way or another until we scale third-party capital.

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

All right, great. Thanks for taking my questions, guys.

Scott Nuttall - *KKR & Co. L.P. - Member*

Thank you.

Jon Levin - *KKR & Co. L.P. - Treasurer, Head of Investor Relations*

Thanks, Robert.

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

Thanks, Robert.

Operator

We'll now take our final question from Marc Irizarry with Goldman Sachs.

Marc Irizarry - *Goldman Sachs - Analyst*

Oh, great. Thanks. Marc Irizarry. Scott, can you just talk about the private equity fund, the next vintage of PE fund for you guys? It looks like you're 70% of the way through the '06 Fund. What's sort of next on the horizon for the next big fund? And what do you think the size of that fund can be and the terms in that fund?

Scott Nuttall - *KKR & Co. L.P. - Member*

Hey, Marc. Thanks for the question. I think in terms of the next private equity fund that we anticipate, as we talked about, it will be a North American fund. I think that's probably something that we start capital-raising in earnest sometime early next year.

In terms of the size, it's really hard to say. We'll have to see what the market feels like. And in terms of the terms, again, we'll have to defer a bit until we get into the conversations with some of our investors to be able to give you a better sense for that.

One thing I'll tell you is that as we've talked about is investing a lot of time and effort in the spending time both with our existing investors to make sure they understand what's happening within our portfolio as we prepare for this next capital raise and also spending a lot of time introducing ourselves to new investors.

We've talked about that in the context of some of the newer products, but it's also been the case around private equity and then investing a lot of time and effort in doing that.

So we'll let you know as we kind of get closer to the launch and through the launch how it feels. But that'll probably be sometime early next year.

Marc Irizarry - *Goldman Sachs - Analyst*

And what's historically been the re-up rate for your LPs?

Scott Nuttall - *KKR & Co. L.P. - Member*

It's been very high, kind of 80%, 90% plus.

Marc Irizarry - *Goldman Sachs - Analyst*

Okay, great. And then have you rethought at all the appropriate level of co-investments in your -- throughout your funds? I guess the -- some banks are going to be a little bit more limited going forward in terms of what sort of the co-invest can look like for their own investments. How do you think about the appropriate level of your own capital invested in your funds?

Jon Levin - *KKR & Co. L.P. - Treasurer, Head of Investor Relations*

Hey, Marc, it's Jon. I think what we've done historically has been a meaningful investor in everything that we do. And for newer strategies where we really want to show that we are investing our own capital alongside investors, we've tended to deal with a bit higher, especially up front like you saw with mezzanine and infrastructure, expecting to end in the high single-digit range for some of those strategies and, furthermore, establish businesses.

I don't see us changing materially from the 2% to 5% range when you combine what the balance sheet will do and what people will do as individuals.

Marc Irizarry - *Goldman Sachs - Analyst*

Okay, and I know there's still a good amount of infrastructure probably in terms of third-party capital raising still to come. What do you think for the group you lifted in, what sort of capital-raising expectations do you have for that, maybe for that segment overall in terms of long/short equity?

Scott Nuttall - *KKR & Co. L.P. - Member*

Hey, Marc, it's Scott. It's really too early to say. I think what we'll do is we'll get the team here, get them settled, and get them integrated with the firm and then go from there.

I think our goal would be to start relatively small and then build over time to some scale. But we haven't put any numbers to that yet.

Marc Irizarry - *Goldman Sachs - Analyst*

Okay, great. Thanks.

Scott Nuttall - *KKR & Co. L.P. - Member*

Thank you.

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

Thanks, Marc.

Operator

And that does conclude our question-and-answer session today. I'd now like to turn the conference back over to Mr. Levin. Please go ahead, sir.

Jon Levin - *KKR & Co. L.P. - Treasurer, Head of Investor Relations*

Great. Thanks, Karen. Thanks, everyone, for joining the call today, thanks for your questions, and we'll look forward to talking to everyone soon.

Operator

Once again, that does conclude our conference for today. Thank you, again, for your participation.

Editor

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