



Rating
Hold

North America
 United States

Financial
 Brokers, Asset
 Managers & Exchanges

Company
KKR & Co.

Reuters: KKR.N
 Bloomberg: KKR US

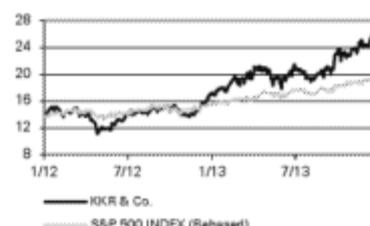
Brian Bedell

Research Analyst

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Price at 24 Jan 2014 (USD)	24.56
Price Target	25.00
52-week range	26.30 – 16.85

Price/price relative



Performance (%)	1m	3m	12m
Absolute	5.8	12.5	49.2
S&P 500 INDEX	0.0	4.7	22.3

Source: Deutsche Bank

Stock & option liquidity data

Market Cap (USD)	17,071.6–
Shares outstanding (m)	709.2–
Free float (%)	–
Volume (23 Jan 2014)	366,778–
Option volume (und. shrs., 1M avg.)	–

Source: Deutsche Bank

A battleground valuation stock; initiating at Hold on higher risk profile

Initiating coverage of KKR with a Hold rating and \$25 PT

We see KKR units trading in a range near current levels over the next 12 months for the following reasons: 1) market debate around the merits of KKR's differentiated balance sheet strategy should remain intense, but should the equity markets be choppier in 2014 vs. 2013 (as is the case so far), we think KKR units will struggle to advance as investors avoid stocks with more volatile & market-dependent earnings, and 2) KKR's distributable earnings (DE) profile through 2015 looks okay to us, and in fact could be less volatile than peers, but we also do not see a major growth catalyst in DE, thus investors may focus more on downside risks, & 3) KKR units look attractive on a sum-of-parts basis, but we see the heavier business mix toward principal income & capital markets as a weight on the P/E. Positively, KKR is executing well across each of its businesses, including generating strong organic growth, while using the balance sheet to both leverage its investing acumen and generating a higher recurring distributable earnings base (to be helped by KFN in '14).

Earnings outlook

We believe DE, from which cash distributions are paid to unit holders, is the most important earnings metric to value the Alts, rather than economic net income (ENI) that forms Consensus estimates. We forecast KKR's DE per unit to remain steady, from \$2.01 in 2013 to \$1.99 in 2014E and \$2.09 in 2015E. Drivers are: 1) steady growth in realizations & 2) good AuM organic growth.

Valuation & Risks

We think KKR units partially realize the benefit of the sum-of-parts debate and revalue up from 9.7x 2014E ENI to nearly 12x 2015E DE 12 months from now, narrowing its discount to the S&P 500 P/E from ~40% to ~20%. This drives a \$25 PT, near current levels, which implies a total return of 8% over the next 12 months, inclusive of a 6.5% forecast distribution yield for 2014. Downside risks for KKR are: 1) a slowdown in US/global economy, 2) a prolonged equity market correction, & 3) failure for investors to embrace the balance sheet strategy & award KKR a higher P/E from its current discount vs. peers, and 4) substantial negative marks on the balance sheet if values of its holdings drops sharply. Upside risks are 1) much stronger DE than expected if KKR leverages its investment ideas effectively in balance sheet investments and 2) investors awarding KKR a much higher PE if balance sheet risks are perceived as low.