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Apollo Global Management's (APO) CEO Leon Black on Q3 2017 Results - Earnings Call Transcript

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Apollo Global Management, LLC (NYSE:APO)

Q3 2017 Results Earnings Conference Call

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Executives

Gary Stein - Head, Corporate Communications

Josh Harris - Co-Founder, Senior Managing Director

Martin Kelly - CFO

Analysts

Alexander Blostein - Goldman Sachs

Mike Carrier - Bank of America Merrill Lynch

Kaimon Chung - Evercore ISI

Bill Katz - Citigroup

Patrick Davitt - Autonomous Research

Chris Harris - Wells Fargo

Michael Cyprys - Morgan Stanley

Jordan Friedlander - Credit Suisse

Brian Bedell - Deutsche Bank

Ken Worthington - JP Morgan

Devin Ryan - JMP Securities

Robert Lee - KBW

Gerald O'Hara - Jefferies

Operator

Good morning, and welcome to Apollo Global Management's 2017 Third Quarter Earnings Conference Call. During today's presentation all callers will be placed in a listen-only mode and following management's prepared remarks the conference will be open for questions. This conference call is being recorded.

I will now turn the call over to you Gary Stein, Head of Corporate Communications. Please go ahead.

Gary Stein

Great. Thanks operator. Welcome to our third quarter 2017 earnings call, and thanks for joining us. With me today from Apollo are Josh Harris, Co-Founder and Senior Managing Director; and Martin Kelly, Chief Financial Officer. This call includes forward-looking statements and projections, including with respect to future distributions by the company. These statements do not guarantee future events or performance. Please refer to our most recent SEC filings for risk factors related to these statements. We'll be discussing certain non-GAAP measures on this call which management believes are relevant to assess the financial performance of the business.

These non-GAAP measures are reconciled to GAAP figures in our earnings presentation, which is available on the Apollo website. Earlier this morning, we reported non-GAAP economic net income or ENI of \$1.07 per share for the third quarter ended September 30, 2017 including \$0.40 per share of fee-related earnings or FRE. Apollo also reported distributable earnings to common and equivalent holders of \$0.42 per share driving a cash distribution of \$0.39 per Class A share. If you have any questions about the information provided within the earnings presentation or on this call, please feel free to follow up with me or Noah Gunn.

With that, I'd like to turn the call over to Josh Harris, Co-Founder and Senior Managing Director of Apollo Global Management.

Josh Harris

Thanks, Gary, and thank you all for your continued interest in Apollo. I would like to take this opportunity to walk through the two key drivers of our business that helped produce our strong third quarter results including continued asset growth and strong investment performance. I would also like to provide you with some context on our capital deployment and the expected timing of the commencement of the Fund IX's investment period. As usual Martin will conclude with some comments regarding Apollo's financials results before we take your questions.

Starting with asset growth, Apollo has now surpassed \$240 billion of total assets under management. Today the platform includes the largest alternative credit business and the largest dedicated private equity fund. We're driving our business forward through traditional fund raising efforts and strategic capital initiatives, which we believe provides us with a strong base of nearly \$100 billion of primarily capital to manage. The third quarter continued to reflect our strong momentum in one of the most significant asset growth periods in our history with growth inflows totaling \$56 billion over the last 12 months.

Third quarter inflows of \$8 billion included approximately \$6.5 billion from our credit business. Credit inflows were generated by diverse group of products concentrated around a \$2.4 billion increase in assets managed for Athene primarily driven by continued organic growth in their business, approximately \$2 billion from Drawdown funds, where we're raising larger amounts for every flagship successor fund in the market. For example total capital commitments for EPF III, the third vintage of our European Principal Finance Strategy rose to \$4.3 billion after the fund held an \$800 million close during the quarter.

SCRF III, the third vintage of our Life Settlement Strategy rose to \$1.9 billion following a \$1 billion final close during the quarter and the fund has already been actively deploying capital recently completing a transaction which utilized more than \$1 billion of the fund's capital, driving the fund to be approximately two-thirds deployed. We also had approximately \$2 billion of inflows from a combination of CLOs, advisory assets, mid cap, hedge funds and other credit mandates during the quarter.

Lastly subsequent to quarter end, the fourth vintage of our structured credit recovery strategy SCRF IV, Structured Credit Recovery IV, had a strong first close of nearly \$1 billion. We expect this fund will be larger than its credit factor, which had totaled commitments of \$1.2 billion.

Turning to investment performance; the funds we manage delivered solid results across

each of our businesses during the quarter and served as a primary driver of our significant earnings and net receivable growth, that Martin will discuss further. On a gross basis, for the quarter Private Equity was up 7.3%, and was the largest contributor to our unrealized net carry income during the period. In addition credit was up 1.9% and Real Assets up 3.8%.

The 7.3% appreciation in the Private Equity funds we managed was driven by a continued strong performance among our funds' private portfolio company holdings. Importantly we are seeing continued positive momentum for funding, which appreciated 11.5% during the quarter and is up 25% year-to-date. At the end of the third quarter, Fund VIII had since inception growth and net IRRs of 29% and 19%, respectively. Fund VIII's net IRR has increased by 600 basis points in just the last 12 months and we expect additional value creation from this fund for two primary reasons.

First, with the average whole period of just under 2 years, the Fund VIII's investors, many of these companies are still in the early to middle stages of implementing their respective value optimization and strategic initiatives that were set forth for the original investment thesis. And second, since the average creation multiple of Fund VIII portfolio companies is nearly 5 multiple points below industry averages of approximately 10.5% enterprise value to EBITDA, there is a meaningful upside potential as these portfolio companies execute their business plan on are increasingly valued more in line with relevant market metrics.

In credit, despite a tight credit environment investment formats of the funds we managed continued to year-to-date upward trajectory during the quarter appreciated 1.9% on a gross basis and up 1.6% on a net basis. If we look at some of the cost drivers within our credit business, our Drawdown funds generated gross and net returns of 2.7% and 2.2%, respectively during the quarter, primarily driven by our European principal finance strategy. Within Real Assets our U.S. Real Estate Funds continue to perform well appreciating 3.8% during the quarter on a gross basis, with since inception net IRRs in the mid teens.

Touching on the capital deployment for a moment; we are maintaining our value oriented discipline across the platform. In Private Equity, although market valuations remain near on for highs we are continuing to utilize our differentiated sourcing capabilities to find what we believe are good investments at attractive prices and we have an active pipeline of potential opportunities. The pipeline includes respective investments in both the U.S. and Europe, reflecting a variety of transaction types such as corporate credit outs and opportunistic buy outs. These prospects also include picked private opportunities, to a de

novo component of our capital deployment strategy during the last 24 months.

And we seek to try to identify companies that have lagged in the public market for a variety of reasons. As we finish up committing the capital and funding, there is approximately \$1.5 billion remaining from new investments that we expect will be allocated to yields in the coming months, therefore our current expectation is that Fund IX will enter its investment period sometime during the first quarter of 2018.

When Fund IX enters its investment period and begins generating management fees, Fund VIII's fees will move into the post investment period. In addition on January 1, 2018 Fund VI, which is a 2006 vintage fund, will stop collecting management fees. It is worth reiterating that we expect the net effect of these movements will add approximately \$200 million or \$0.50 per share pretax of annualized accretion to our fee related earnings.

Accordingly this will allow us to deliver a net minimum cash distribution of \$1.30 per share on an annualized basis, a 30% increase from the prior level of \$1 per share we had been indicating previously. Importantly the \$1.30 per share reflects what we believe is a conservative baseline distribution equating to a 4% yield on our current share price and does not include any FRE upside or any incremental distributions from realized cash incentive fees which have averaged more than \$1.50 per share annually over the last five years.

And it is worth noting that there is one-third more private equity fund capital invested today versus the average level during those same five years. As Fund VIII which is a 2013 vintage heads into its fifth year in 2018, assuming markets remain accommodated to portfolio exits, we believe the fund's maturity profile will provide the opportunity for private equity realizations over the next multi-year period.

Before handing the call over to Martin, I would like to mention one last item. As we started to discuss one of our permanent capital vehicles, we have been helping to build out in Europe is currently named AGER. By year end AGER will complete a rebranding and will be named Athora [ph] going forward. Athora is a strategic platform established to acquire or reinsure blocks of insurance business in German and boarder European life insurance markets. But we believe there is a need for capital, as Apollo, our minority investors n Athora and long-term strategic partners.

The affiliate of Apollo, AAME is acting as an advisor with respect to Athora's investment

portfolio which currently stands at approximately \$8 billion. The team at Athora is continuing to evaluate investment opportunities for its business which is well capitalized with \$2.5 billion of equity and we remain optimistic about the vehicle's growth potential over time.

Now I would like to turn the call over to Martin to walkthrough our financial results in more detail. Thanks, Martin.

Martin Kelly

Thanks Josh and good morning again everyone. Overall our strong third quarter results contributed to Apollo's significant earnings growth so far in 2017. Year-to-date total economic net income of \$947 million or \$2.35 per share is more than 70% greater than total ENI for the comparable period last year. This is primarily driven by improving carry income resulting from strong investment performance across all of our business segments so far in 2017.

Private Equity funds have appreciated 18%, while Real Assets funds have appreciated 14% and Credit funds have appreciated 6%. In addition our fee related earnings continue to grow and we believe this will continue in 2018, as Josh mentioned.

Our solid balance sheet is also delivering meaningful contributions as strategic investments like Athene continue to creating value. It's clear that the breadth and scale of our platform is expanding, total assets under management are up 28% year-over-year to \$242 billion, which equates to a six-fold increase or a 21% compound annual growth rate over the past 10 years.

Focusing on the financial performance in the third quarter, we generated total ENI of \$432 million or \$1.07 per share. Pretax our economic income was \$458 million or \$1.14 per share, driven by the following key components. FRE of \$162 million which contributed \$0.40 per share, total net carry of \$209 million which contributed \$0.52 per share, and total other income predominantly investment income of \$117 million which contributed \$0.29 per share. FRE rose quarter-over-quarter due to higher management fees and one-time proceeds of [\$90 million] from the buyout of an office lease while expenses remained well controlled.

Our Credit segment drove the quarter-over-quarter leasing management fees as fee generating AUM grew 5% sequentially from strong inflows. Some of the inflows pertains to

follow-on closes in active funds which resulted in approximately \$12 million of one-time catch up management fees during the quarter. While the catch-up management fees in Q3 will not return recur, we believe other fee related revenue will provide an offset in the near term. Thus far in Q4 we have earned approximately \$30 million in fee related revenue in connection with capital deployment activity.

In terms of performance fee and balance sheet related income we earned \$326 million of net carry and investment income during the quarter driven by two primary factors; positive investment performance across all of our businesses with a particularly robust contribution from Private Equity, and appreciation in the fair value of Athene. In Private Equity the vast majority of the carry income earned in the quarter was derived by the strong appreciation in Fund VIII which Josh described. The appreciation was broad based with more than three quarters of the FRE or so portfolio companies in Fund VIII generating positive marks. In terms of sector strength we saw the greatest contributions from investments in the consumer services, business services 2... and manufacturing and industrial sectors.

Turning to Athene, the fair value of our investment increased by approximately 10% during the third quarter, resulting in \$73 million of gains within other income; as well as \$14 million of net carry interest income from AAA and related accounts, driving an aggregate contribution to third quarter ENI of approximately \$0.22 per share.

Looking at our balance sheet at the end of the third quarter we had nearly \$6 per share of value which is up meaningfully from just a year ago when the balance sheet represented less than \$4 per share. This growth was primarily driven by strong appreciation in the value of Athene as well as the significant increase in the value of our net carried interest receivable which is nearly quadruple from its [trough] level of \$0.58 per share in March 2016 to \$2.16 per share today.

Regarding our cash distribution, the \$0.39 per Class A Share we declared today for the first quarter was primarily driven by fee related earnings which benefited from continuing growth in our management fees and in part from lease proceeds. One final note with regard to taxes, you will notice that our ENI tax rate for the quarter was lower than normal, largely due to the mix of income earned during the period which contained a higher concentration of pass-through carry and investment income.

With that, we'll now turn the call back to the operator and open up the line for any of your questions.

Question-and-Answer Session

Operator

[Operator Instructions] Your first question comes from the line of Alex Blostein with Goldman Sachs.

Alexander Blostein

So the first question just to guess that lead to the question around timing of Fund VIII realizations, the funds actually moving through its kind life cycle very nicely, I would say much faster than you guys expected. So on prior calls you gave higher level of use and when you could start to realize some of the earlier investment, so maybe just an update that will helpful?

Josh Harris

I think like, I just sort of some of the prepared remarks that I gave which was that, we are -- the average life [appears] but certainly some of the earlier investments now are approaching 5 years and that's around when you start to harvest and there is a definitely a lot of things right now that we're looking at, so I would expect that distributions will ramp up starting next year. The other thing that I would point out is that, we bought that portfolio as we mentioned at a 5-multiple point discount, and really when we look at the -- the companies themselves are doing well, revenue, EBITDA and aggregate was up mid single digit year-to-year for the portfolio and much of the accretion in that 5-multiple discount remains still not in the marks. So if you think about that 5-multiple point discount really only 1-multiple point has been introduced into the marks that's what our process has put in there. So we expect there is not only realization upside in that portfolio, but return to cash but also there is this more significant upside coming from that portfolio. I mean obviously it depends on the economy and the markets that now specific companies do but we feel like there's still a lot of value creation left, even as we start to realize.

Alexander Blostein

Got it. Thanks for that. And I guess just as a follow up, it's a little bit of a bigger picture question but, several years ago at the Investor Day you guys kind of talked about aspirationally \$250 billion to \$300 billion in AUM, you are 240 and change today. So just taking a step back, I guess how do you guys think about that still as a target and that the

ultimate number is higher, can you just talk about the kind of scope and scale and kind of where the incremental growth opportunities could be for Apollo today and any incremental investments that you need to make to kind of support significantly higher level of growth?

Josh Harris

Yes. I mean what I would say is that, obviously, we're ahead of pace relative to growth there and what we didn't think traditionally is that the core business is growing AUM at high single digit to low double digit just on its own. And then, we have this, what I call, the R&D lab which kind of adds value sporadically and stair steps the growth. Certainly that occurred during the financial -- when there is a big financial pullback, we tend to raise a lot of capital and we did that during the last financial crisis. And then, obviously the creation of a theme where we managed the asset, added a lot of value there. And then, now we have Athora I mean, I think the one that's sort of out there right now that's really clearly focused today is Athora. We have raised the capital. It gives us a lot of buying power in Europe and there is -- it's in industry that in terms of insurance that really needs the capital infusion. And so, we see a lot of opportunity in Athora. We see a bunch of opportunities as we move our product line from what I would call higher alpha generating credit into, what I call yield, which is call it 5% to 10%. That's an area that we have a number of products that are making real headway. Like, I told, we have one in particular total return that really, it's just about finding investment opportunities, not finding capital. We are almost having to turn capital away. And then, our hedge fund product has been performing very well. That is we have optimism that will grow.

And so, we see opportunities really across our platform. And we are investing. When we throw the number of \$1.30, right, that includes we are setting aside a bunch of operating expense or G&A to invest in really proprietary origination around the world and Europe and in the U.S., and even a little bit in Asia where we are trying to go off the run and outside the markets. Whether it would be middle market origination in Europe, whether it would be enhancing other products that might be more akin to a GE Capital in terms of asset based lending, whether it would be energy credit. We are building up in that number. We've already set aside a bunch of money to invest in its origination. Because, what we are finding is that the capital there is really there for us. Our investors really trust us. So, we just need to keep delivering on the investment returns. And so, anything in the public market today is overvalued because of the quantitative easing that's going on, central bank wise. So, we have got to get off to run. And so, we are trying to stay ahead of the

wave of money that hits the market and really develop arbitrage opportunities in credit. And so, that's really what's going on.

Operator

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

Mike Carrier

Maybe first one, Josh, just on Fund VIII and the exit and the distribution outlook. Just trying to understand, you mentioned where you guys have deployed in terms of around five times multiple versus the industry. Are there any other nuances in the portfolio when we compare this one versus the prior funds? And how we should be thinking about the process of exiting some of those investments, whether it's in the private markets or in the public markets? Just trying to gauge potential over the next three years and if there is any nuances relative to that?

Josh Harris

First of all, there -- in some cases, they are bigger company, I mean, it's a bigger fund. So, you go like a company like ADT, which is bigger company; you have Rackspace. You have many companies that were public companies once where for whatever reason, whether it would be, the portfolio is too broad and not understood by the public markets or whether it be, we've built the companies over time such as ADT where we took a grab where we've really added a lot of extra, half to the company and changed the company strategy or in some cases we had the portfolios where they owned a lot of different things and the company itself wasn't even -- the corporate structure didn't even make sense. I won't say publically what those companies are. And so, in many cases, we're able to reposition the company, change it materially and then reintroduce it into the public market. So, they are bigger companies. The fact that we bought the portfolio so cheaply has allowed us to put less leverage on the companies.

And then, I would say, particularly the portfolio is less cyclical than it has been in the past, which is less -- if you look at the mix between services, business services, healthcare and more cyclical things, and chemicals, not that we walked away from those cyclical businesses, but it just happens to be very less cyclical. And so that would be another attribute. So, I would say, look, -- and then there is very -- I mean, obviously, our average over history has been about a third distressed for control where we've bought companies

through the debt markets. And in this case, it's only 5%. So, there is a very little distress in this fund. I think we've been able to prove to, I think our investors very clearly that distressed, non-distressed, obviously a great stressed environment helps us but we're able originate off-market transactions at low multiples without that distressed market and that these funds will clearly do it. So, all those things I say

So, I think it's sort of a good story relative to our past funds in terms up bigger and some cases better companies and less kind of distressed. And then, I think also last think I would say is that in this fund we sell a lot of these corporate buildups where we've really added a lot of -- many of these companies have made them bigger. So that's what I would talk, would say. Generally speaking, the public market and the debt markets tend to be greater than 50% of our exit. And so, obviously, that's going to be important. That's [indiscernible] market for us. But that's not the only way we can exit. Clearly, we can exit to strategic buyers. When you create a portfolio of five or six times EBITDA, right, you can exit to a financial buyer at a much higher price because that's all you need. So, even if the equity markets don't go so well, the debt markets hanging in there will be another backstop to our ability to exit. So, that would be may be how I would size it up.

Mike Carrier

And then, just as a follow-up, just on the credit side. So, with AGER or I guess Athora just how those opportunities are setting up relative to what you saw at Athene? It seems like there is little bit more competition but it seems like it's still more in the U.S. versus Europe. And then just broadly with rising rates, potentially we're seeing in the U.S. and may be in Europe, how does that factor in to that the upside or the opportunity?

Josh Harris

Yes. I'd say, there are opportunities, both in the U.S. and in Europe. So, not an either or. And I think that there is always competition. I don't -- my sense is that it's not that there is any more or less competition -- there is or was. In terms of rising rates, over time, clearly, rising rates helps financial institutions. So, key to much of this is spread. And so over time, if rates rise, over many years that will take some of the acute pressure off of insurance companies and banks and other financial institutions. But I don't -- first of all, my outlook is -- I don't know what yours, thinking about rates, but I think that the quantitative easing globally continues, certainly in the U.S. will be at least trying to -- they have been raising rates, and obviously U.S. is trying to reduce the Federal Reserve's balance sheet. But,

there is still, between Japan and the ECB and everyone else, you're still going to have a lot of quantitative easing. Well, it's not clear to me how much rates will go up. Maybe they'll go up, maybe the long end of the curve will go up some, short end of the curve will go up some, but I don't think there is going to be the huge rate increase, unless we see inflation. And right now, notwithstanding the robust economic growth, we haven't seen that.

So, I think that -- first of all unclear that rates will rise. If they do, I think it will be many, many years -- many of these problems are very, very acute. And rate increases won't them; they just are fundamentally challenged, financial institutions that need to deleverage. But over many years, it will help the financial institutions, if rates go up.

Operator

Our next question comes from Glenn Schorr with Evercore ISI.

Kaimon Chung

This is Kaimon Chung in for Glenn Schorr. Actually recent announcement on the acquisition of the majority stake in Catalina. Can you just spare little time talking about what the deal is, what your plans are for them and what it means for the Company? Is it the same game plan for that non-life insurance with Athene and so what's the opportunity?

Martin Kelly

So, with respect to Catalina, yes, they put out a press release a week or so ago announcing that they were going to be selling some stakes to Apollo managed funds. So, when the transaction is complete, the funds managed by Apollo will control the equity of Catalina; management will still own a sizable stake as well. Catalina is a really interesting company. It's been around for 10 years. It has been growing at a pretty rapid clip and is one of the largest players in the space of acquiring run-off portfolios of non-life, both in the U.S. and Europe. And we see significant opportunity with the really limited competition. I would note that it is a bit difference in terms of the investments. And you should think about Athene or Athora and that we are not -- today, we are not managing the assets directly of Catalina. So, I would think about it more as a fund portfolio opportunity at this point in time, but lot of upside there.

Kaimon Chung

Just as a follow-up. Can you give us maybe your updated thoughts on tax reform as it stands? I know it's kind of early but how it impacts your firm, your credit business and maybe in particular Athene and Athora?

Josh Harris

Yes. I think we are obviously, like everyone else, watching what comes out of Washington. And it's got -- without seeing the legislation itself, you can go in so many different directions. So, we will probably not speculate on it but as soon as it actually comes out -- if it comes out, we will definitely be very, very focused on and be much more able to elaborate on what it means to us.

Operator

Our next question comes from Bill Katz with Citigroup.

Bill Katz

Just circling back to the discussions about sort of high single low double-digit organic growth in the core business. Can you give us a sense of where you're seeing the best demand from the LP perspective? And maybe give us updated thoughts in terms of penetrating a little bit more into the retail channel as well.

Josh Harris

So, I mean, look, the LP community, I said yield, so what's happening is that, to put it all over the place, I mean, we're growing the whole range of products. But, the one that sticks out the most is as yield -- as rates have come in, right, like the ability of the most of the LP community or much of the LP community are -- pension funds or other liability managers where they have increasing costs, even some of them that don't are focused on just the inability to make real returns to fixed income. And so, as they look to branch out of fixed income, they look at obviously equity and alternatives private equity, but they also look at, okay, how can we earn more on our credit -- how can we invest more in fixed income store and kind of the old five, six, seven, eight that we used to be comfortable with. So, there is the alternatives basket within the context of our investors, is still well smaller than fixed income or the equities book.

And so, this provides a great way for them to earn enough return to keep up with their targets or there liabilities. And the only way you could do is going after run off market. As I

talked about, whether it be structured credit CLOs, whether it'd be middle market origination, whether it'd be insurance type liabilities that people don't understand, energy credit where you need special expertise, aircraft leasing. We're looking at lots of segments in the context of the real economy that aren't necessarily priced to perfection because the central bank money can't flow through the market and hit those sectors. And so, that's one big area that's going on. We're also seeing a lot of demand for direct origination, Europe as I mentioned. So that would be what I would say.

The last thing is, clearly, the search for return, right, opens up a lot of the private -- whether it would be infrastructure, whether it would be our traditional private equity energy investing, some of our competitors have raised core products. But, everyone is looking -- the run in equity is also -- there are many of our LPs that are saying, well, the future of return on equities might be not that traditional percent 8% or 6% to 8% that we used to count on, might be lower because as the central banks raise rates, equity prices could -- they might not go down but they might -- we sort of borrowed from the future return by having rates so low. And so, people are looking to get even out of their own equity book and into alternatives. And so, really as I said, for us, it's all about income we show with the product, we raise lots of money. And so, for us, it's all about building expertise in these various areas, so that we can deliver outsized returns and then we will raise the money. So, we're seeing a lot of demand there as well.

Bill Katz

Okay. It's helpful. And then, just to follow up, I know you don't want to comment on taxes, taking that as in terms of your structure. But if you were -- if the industry would have faced some pressure about interest expense deductibility, I've been asking this to your peers as well, what's your stance on the economics for the LBO model?

Martin Kelly

Again, I think it's so hard to really react to that. Is there going to -- are there going to be lower corporate taxes, at what level, will interest deductibility be limited, what are the other changes that will occur. I mean, I think clearly, changes in fundamental things like that will create lots of volatility, lots of companies that get hurt by that, lots of companies who get helped by that. And we tend to thrive in volatility. I think when you look at the private equate model, the public markets are levered just over three times and private marks are levered just over five times. It's really not on the margin, it certainly will impact the cash

flows of more levered companies. But, I don't believe -- I don't personally think that -- I think if there is big changes to the structure of our tax rate, I think that will provide a lot of interesting opportunities for people that get ahead of that and adjust to it. And I think certainly, we have demonstrated the ability to do that. And I don't think that it will fundamentally change the private equity model.

Operator

Our next question comes from Patrick Davitt with Autonomous Research.

Patrick Davitt

Just one quick follow-up on the creation multiple conversation. Would your experience -- given your strength, would you expect the exit multiples to generally be at market then, so that if we are going to move from a 5x discount to a 4x discount, should we expect that to get to zero by the time you exit?

Martin Kelly

It's really hard. I mean, I think that's just unfortunately too broad of question. In other words, like, each company has its own unique story, its own unique situation. And the comparables to that company, the ability of us to exit into the market changes like every day. And so, certainly, we think we bought the portfolio at a significant discount to fair value. Whether that -- what the ultimate exit multiples are is really hard to predict. I mean, I'll say that certainly in our prior funds, we have exited at many multiple point accretions to where we bought these funds. whether we will get a full-5, that's hard to predict.

Josh Harris

And I'll just say, another math that we use internally is, can we double our investors' money or will we. And if you do that in Fund VIII and nothing more, nothing less, then that creates about \$8 of gross carry over the fund life. So, obviously, more would be more. We are about a quarter of the way through that in terms of what we've recognized today through our ENI earnings. So that's a way to frame what the outcomes might be.

Martin Kelly

And what I'll say -- I mean, to me, we have done about 2.5x, over our history. It's a little shade under 2.5x, so the double, which is what the LP community wants. We have always

over-delivered that. And I would expect Fund VIII to be no different, to be honest with you. But at the same time, it's very hard to predict. We are off to a very fast start.

Patrick Davitt

And then, quick follow-up. Could you remind us of the economics on a store -- has there been any change to that with the rebranding?

Josh Harris

No, we haven't really aid much around the economics at this point. Over time, we expect to make that more clear. But for the time being, the assets said that are being managed through Athora, a lot of the assets are portfolio company assets from our private equity funds, where we're managing or helping to advise on the balance sheets there. And it's generally been sort of cost plus, up to this point. There are some assets under management for the former Delta Lloyd portfolio and there the basis points is around 10 basis points earning on those assets. But as Athora grows and as additional incremental assets, I think we would expect fee rates to be incrementally higher, but at this point, haven't disclosed any of that.

Martin Kelly

Relative to the U.S. model, when you look at the European model, there is more leverage in the European model, roughly double, but the fee rates are lower and the assets are more -- the flexibility is a little more constraint. So, I think, we haven't said beyond that but certainly we do see this as a really potentially important growth opportunity for us.

Josh Harris

And the future outcomes will depend on what portfolios are acquired. But clearly, anything that is done is going to be done in an accretive way.

Operator

Our next question comes from Chris Harris with Wells Fargo.

Chris Harris

I just want to follow up on that earlier question regarding where Fund VIII is valued versus the market. I guess, we really haven't discussed why Fund VIII is still valued at pretty big

discount to the comps. Just wondering, if you could elaborate on that, because it seems like the portfolio companies are doing extraordinarily well.

Josh Harris

We didn't actually -- just to be clear, Fund VIII -- I mean, Martin will speak about our FAS process, our mark-to-market presence. But what we said was that we bought the private equity market acquired companies of our size, like greater than \$500 million, so even smaller, at about [indiscernible] it is having that multiple. And we value, and we create our portfolio at about 5 multiple discount to that. That doesn't really speak to the comps. And then, we said that we thought we bought our portfolio, we got it in a good price that we thought we had created our portfolio at its discount because of our ability to source things and change their strategies. What we didn't say, to be clear, is that its marked at a discount to the comps because that -- why don't you talk about our FAS process?

Martin Kelly

When we buy a company at many multiples less than where the market is, there are different reasons for that. And you need time to address the issues in the companies that you find, some of that's capital structure, some of it is operating performance and that just takes time. And so, with an age of under two years, we're still actively working through many of the names in the book. And that's going to take -- it is going to take three, four, five years, potentially longer from here to do that and complete it. So, we value things where we see an exit price today taking into account all the relevant market data that we can, it's close objective. But yes, there is a value creation time frame that we have our way through.

Chris Harris

Okay. That's helpful. And then, just a quick question on the expenses. I think your management based expenses are tracking up around 7% year-on-year so far year-to-date. How should we be thinking about the growth rate as we enter 2018? I know you have got Fund IX coming on; I'm not sure if that influences anything.

Martin Kelly

Sure. Our margins are up, our FRE margin for this year to date is 50%. And if you take out the lease buyout gain, sort of non-recurring item, it's 48%. That's slightly higher than

where it was last year, and last year had a lot of transaction fees. So, we have been able to grow organically the firm, management fees were up 10% year-on-year, comp is up about 7% and non-comp is up about 2%. So, there is real operating leverage that's being created. As we look into 2018, we are very focused on margins. And clearly, Fund IX will provide an uplift in revenues without a lot of additional direct expenses. And then, to Josh's point, we will likely take some of that and invest it in areas where we see compelling growth. But, we do it in a way that is margin accretive relative to where we are this year.

Josh Harris

We are seeing operating leverage, and we are very focused on it. And the reality is, you don't need -- I mean, certainly in the context of IX, we are always looking to enhance our team but there is a lot of operating leverage in raising your next private equity fund.

Operator

Our next question comes from Michael Cyprys with Morgan Stanley.

Michael Cyprys

I just want to follow up on, Martin, the point you were just making about investments to the business, putting to work some of the additional revenues that you get from Fund IX. If you could just maybe talk about what some of those compelling growth opportunities might be, where you might see you invest in the business for the next couple of years?

Martin Kelly

Okay. Some of this will be repetitive. I think that within the -- most of it will be across our credit platform where we are increasingly seeking to go off the run and outside the market in terms of generating yield and opportunistic but more yield origination capability. So that could range from creating a middle market lending presence in Europe, similar to the one that we have in the U.S. It could be investing in any number of, what I'll call, asset-based financing businesses. Aircraft leasing would be an example of that type of business where we already have a significant presence. It could be investing in areas like insurance and/or financial institution lending, and/or energy where we already have a significant capability. It could be expanding our emerging markets presence and enhancing our capabilities there. And then, it could be also looking at expanding our alternatives in a private equity

expertise whether that'd be adding to our existing team in energy or whether it would be getting into infrastructure which we talked about before and/or real estate and real assets. And so those are the types of things that we're going to be investing in.

And this has been an ongoing -- this is in -- we don't talk about it a lot. It is really part of our strategy is to be able to deliver investments that are added significant arbitrage or discount relative to the yield they generate per unit of risk in the credit markets and/or in the alternative private equity markets the same thing. In order to do that, you need to stay ahead of the competition in terms of origination and that's been the key to our model. And so really -- and by the way, what happens in the financial markets is that people copy right away. And so, you need to keep moving and keep adding and keep ahead of everyone, which is what we try to do, which is why we're marginally obtuse on these calls, in terms of specifically talking about that.

Michael Cyprys

Okay, thanks. Just as a quick follow-up, maybe you could just talk a little bit about data and technology front. Just how your investment process today is that incorporating that and how you kind of see the evolution of your investment process, say over the next five years, given changes technology, growing amounts of data and how you're thinking about integrating that over the next couple of years?

Josh Harris

Sure. So, I will take this. Yes. We're spending a lot of time on this. We're investing significantly in technology across the platform, both within our businesses and then across the infrastructure of the fund. And so, beyond the investment decision process, which I will speak about in a minute, it allows us to operate portfolio companies more effectively, allows us to sort of do things offensively and defensively, and allows us to more effectively operate the fund. So, at the fund level, we've invested in warehouses and data scientists across our businesses that allow us to collect and analyze information across the companies that we own. And that allows us to operate companies more effectively and also informs decision process for new investments. And then, in credit, it allows us to aggregate risk and report information to a pace in a more useful fashion. And then it allows to grow the funds favorably, which you see in our margins.

Around the investment decisions process within PE, we have developed relationships with

specialized providers of data and technology, and they provide analytics and information that are customized to particular industries. And so that ranges from robotics and apps through to mainframe enhancement and some legacy platforms. And so, there is clearly -- there is a lot going on, there is risk, there is opportunities, lots of changes, but we're trying to embrace that across the businesses as well as at the firm level.

Operator

Our next question comes from Craig Siegenthaler with Credit Suisse.

Jordan Friedlander

Good morning. This is Jordan Friedlander filling in for Craig. I want to follow up on Bill's question earlier on retail. I know you already have some retail product offerings including mortgage REITs, BDC, and some other credit fund products. But, would you ought to further penetrate this channel by building out new products such as maybe real estate REIT or interval funds?

Martin Kelly

Yes. Look, we're always looking at opportunities like that where we can get to what we perceive to be sticky low cost capital and certainly we have some of that in the commercial real estate area. And so, certainly, we're always looking at what there are new public structure or other structures that are kind of available and interesting and where we feel like we can generate arbitrage and good rates of return for those investors and where their needs meet our capabilities. And so, we certainly are looking at that. We also obviously, I'll just point out, just to go back through it, we -- today, we're between 10% and 15% retail. It's the reach to retail investors through a variety of different channels from obviously just public companies, [indiscernible] companies to high net worth channels to we wholesale to other credit providers and we reach -- for most of our funds, we reach high net worth, we have high net worth channels that invest. Then obviously, the ones that -- so the 10 -- between 10% and 15% does not count Athene. We're clearly -- their whole business is built on annuities to retail clients. And so, if you include that, obviously the number -- that would be another 30% of our assets. And so, we have quite a different approach to retail, maybe than what you're hearing on some of the other calls. I mean, the other issue for us truthfully is that there is so much institutional demand for our products that -- again, it's not about the sort of real need to reach more and more capital, isn't as acute right now. But

certainly, where retail provides -- where retail understands our products and provides sticky, long-term capital and we feel like we have capabilities that overlap with that we're going to -- we're not, we're very much intent with taking retail capital.

Operator

Our next question comes from Brian Bedell with Deutsche Bank.

Brian Bedell

Maybe to circle back on the Fund VIII realizations, Josh, and then thanks for all the color on that. As you think about the macro, or I guess, my question is, how do you think about the interplay between the macro environment and then trying to improve the valuations on those portfolio companies, realizing obviously it's -- each position is different, but, kind of in line with what Martin was saying on the three to four to five-year time periods, valuations up to where you think they ought to be, would you seek -- if your deal in the macro got worse or you got something that is going to happen within next year, would you accelerate that realization, not fully try to capture the entire economics out of that?

Martin Kelly

So, the way we think about it, really is -- first of all, we do have a macro overlap for how we think about our portfolio. And certainly it's not locked on us that we're in year eight / going into year nine of an economic cycle that interest rates are historically low, that valuations are historically high. And certainly that is something that while we don't have a crystal ball, pushes us to look very hard at where we can monetize things. So, we're definitely in tune with the macro environment. And right now, I would say, there is a -- it does orient you towards looking hard now. So, the way we actually put that into practice is on a bottoms up basis, where we look at every single company and we look at not just where we bought it but where we could -- so, everyday that you don't sell, you buy. And so we look at every single company and we say, can we generate private equity returns for our investors from where we could sell this company. And if the answer is yes, we keep it; and if the answer is no, we sell it.

And certainly, what we do within the contract of those portfolio reviews and we had one very recently. We literally sat around for entire day with the entire private equity team and went company by company is we orient around average ultimate, we orient around interest rate adjusted, market condition adjusted multiples, right, as the ultimate exits. So,

we might be able to sell a company today at a high multiple. But, when we look out into the future and we decide not to sell it, we normalize for what we expect the environment to be. And so, what that does obviously is it puts pressure on the math, because we can't predict continued momentum in the marketplace. So that inherent approach puts pressure on the -- our kind of our selling. And once we created a lot of value, we're oriented towards selling and that's the way that we do it.

Brian Bedell

And then you could also accelerate the IRRs I suppose, if you are selling those faster, even if you're not hitting the 2 or 2.5 MOICs, is that something in that consideration.

Martin Kelly

I mean I think it's all in the hopper. I think that certainly MOIC and rate of return are both very important.

Brian Bedell

And then, just lastly, maybe just an update on the partnerships with OppenheimerFunds in the retail credit products and whether you're looking other similar types of opportunities?

Martin Kelly

So, sitting here today, we've got partnership with Waddell, which has been growing very nicely and also partnership with K2 Funds. [Ph] We no longer have a partnership with Oppenheimer. So, really just focused on Waddell and K2 at this point. And they continue to grow and be well received. And as Josh talked earlier about the total return strategy being a really attractive product, it's true for retail as well. And so that's really where we're seeing lot of growth and momentum through those advisor relationships.

Operator

Our next question comes from Ken Worthington with JP Morgan.

Ken Worthington

Just quickly, Martin, what were catch-up fees again? I know you mentioned them, I missed it. And how much of that was in credit?

Martin Kelly

Hi, Ken. It was \$12 million in Q3, there was a little bit in Q2 as well and it was all in credit.

Ken Worthington

All credit, okay. Thank you. And then, Josh, just follow-up on I think on Mike's question earlier in the call. On Athora, how far are part of the buyers and the sellers of insurance assets and properties in Europe? Are they really far, are they kind of close, is there anything for us to consider that would kind of bridge that gap and get us to see more of these deals getting done?

Josh Harris

Yes. I mean I think, I'm hopeful that we can get some stuff done over the next 6 to 18 months. I don't know if there is -- I think that we raise the capital because we perceive there to be significant opportunities. These things are very complicated. They are regulated. It takes a long -- there is a lot of moving pieces. It's not like you can just go in there and buy these things. There is a huge amount of complexity and negotiation and you have to be super careful and handle very appropriately with all parties including protecting the alternate policy holders. I think it's hard to just, unless you're known for having the capability to do this, it's hard to just go and do it. And secondly, once you are known, it's still complicated to get it done. So, it's not easy, but that's one of the reasons why we gravitate towards it because it takes a lot of scale, but I think that it's -- I think we are well situated right now.

Operator

Our next question comes from Devin Ryan with JMP Securities.

Devin Ryan

Maybe a follow-up for me as well. You touched on real estate and infrastructure as areas of investment, and understanding one of obtuse around the opportunities in real assets. But at a high level, because I know some of these are harder for us to model. Is there anything big growing that could move the needle over the next year? And any color you can give us around some of those things we are looking at organically or maybe even thinking about inorganically would be helpful.

Josh Harris

Look, I think that I would say that clearly we have been putting together team in these areas and we are going to approach this in a very Apolloesk way where we -- right now, there is a tremendous need for capital in the infrastructure and real assets arenas but at the same time, there is commodity stuff that everyone can do, has been bid to pretty high prices driven by lots of capital to do that kind of stuff. And so, we are working painstakingly to develop an edge that allow us to do things that are different, similar to how we do private equity where we're either able to assess things that other people can't or execute transactions that other people can't or absorb execution risk that other people aren't willing to. And so all that takes time to build capability. So, that's the way we are approaching it. I think certainly our credit business in real assets is growing a lot and we are investing in it. And so, that's really how I'd answer it. I don't know how to -- deals come and go and it's hard to predict some -- there is not some big elephant looking out there right now.

Devin Ryan

Quick follow-up here. [Multiple Speakers] And maybe I'll just ask a quick math question, this is not a tax question. Leon noted earlier in the year that 20% corporate tax rate could be a level where it's pretty much a wash to be a C-corp. And I know there are some shifts occurring in earning stream and maybe qualifying incomes increasing. So, I just want to think about that rate directionally. Would that 20% threshold be moving much lower or was that over the cycle comment? I know it's complicated but just trying to think about that directionally.

Martin Kelly

So, what was said is that blended tax rate today, over the cycle, as best as we can model it, and not specific to any quarter or year is sort of 10% to 15%, like sort of low teens, mid teens type area. And so, if you end up taxing the whole income stream in a single tax rate, call it 20%, there's going to be tax leakage, it's going to be dilutive but the benefit may be there in the sense of a different shareholder base. So, at 20%, it's -- it will have to come down to 15% or something like that to be close to a breakeven on paper.

Josh Harris

But again, a lot of that depends on the treatments of different types of the income. And I

don't even know that how to kind of really answer it ,because, what Martin is saying 100% accurate. If there is blanket rate, there is not today and I don't think anyone is talking there being a blank rate in the future. So, I mean, again, and what you're deductions are -- and so like again it's -- I mean, we're not trying to be argumentative in terms of mirroring, but it's really hard to predict it right now.

Operator

Our next question comes from Robert Lee with KBW.

Robert Lee

I guess, Josh, I was curious about, you talked about where you kind see the opportunities that you certainly highlighted, some in the U.S. and Europe. I guess just because it wasn't included, could you maybe update us on your opportunities or your thoughts around Asia? I mean, clearly, that's a region of the world where a lot of your peers have raised a lot of capital through a lot of effort and you guys really seem to be little bit quiet about opportunities there.

Josh Harris

We are, I mean -- but, we have a whole team in Asia, we got a team in Hong Kong, we have a small team in Singapore, we have people in China, we have people in Australia, India, we have a big team in India and doing credit and real estate business. So, we have a number of businesses, primarily our credit and real estate, so special situations like lending and structured equity. And today, the overall business is less than 5% of our assets. And I would say that we're value oriented, creditor right oriented investors and there is a fair -- and control investors in the case of our private equity funds. And so, in each case there are just cultural and structural impediments, whether it'd be the legal and regulatory environment or the ability to transact on a control basis in certain countries that just make our business may be smaller than other programs that might be more oriented towards growth, equity or momentum investing or minority investing or take a less value for it. If you're willing to -- some of the values in Asia are high. And so if you are willing to pay a high price but you think you're going to get a higher price in the IPO or something, that would open up an awful lot of Asia, and you want to take a minority stake and kind of wing it, that would open up kind of a lot of investing from our point of view. But it's just not who we are, like we need to know that we're getting in an at a great price. And so that just

limits the flow, but it doesn't mean that we're not investing in Asia. And we certainly have real franchise in India and increasingly a franchise in real estate and credit around Asia and a more limited approach in private equity that's opportunistic.

Robert Lee

I appreciate that color. And then, maybe just one follow-up I guess, December, it will be about a year where you announced that the Gary Parr was joining the firm and I guess he joined in early this year. Just kind of curious, could you maybe update us on how his role has kind of evolved, where you kind feel like maybe there's been the most impact on kind of how you think about things or do things that can help us get a sense of his impact on the business?

Josh Harris

Gary comes with a vast reservoir of financial institution experience, like that's where he spent his entire carrier. Clearly, that skill set is applicable across -- and we're doing a lot of stuff, whether it would be in insurance, whether it would be in banks, whether it would be financial services, and we ourselves are asset managers. So, I would say that experience comes across like all of our businesses. He helps us in private equity, he helps us in credit with that expertise, and certainly relative to the strategy of our own firm, in terms of evaluating different opportunities where we should invest, whether we should make acquisitions or not make acquisition, all of that is very helps. So, he has been an enormous help to the firm. And anyway, he has been a good addition.

Operator

Our final question this morning will come from the line of Gerald O'Hara with Jefferies.

Gerald O'Hara

Thanks for squeezing me in. Clearly, a lot of focus on the insurance components within the permanent capital vehicles but I was hoping you might just be able to close up the call I suppose with a little bit of an update around midcap as it continues to grow and what the opportunity set might be there kind looking forward and what the geographic reach of that vehicle is if you could remind us. Thank you.

Martin Kelly

So, midcap is growing, it's diversifying its business away from healthcare across a much broader set of asset classes. It's originating business nicely, so it's on par with what's defined and said. The challenge it's had this year is refi activity has been high, and so paydowns have taken away some of the net growth. But we're being careful what's underwritten and taking what we perceive to be good quality risk. And it's a good, established platform with increasing access points to origination. So, it's picking up but a little bit more slowly than what we planned.

Operator

And with that, I will hand our program back over to Gary Stein for any additional or closing remarks.

Gary Stein

Thanks, operator. Thanks, again, everyone for joining us today. As I noted earlier, if you have any questions regarding the earnings presentation or anything that was discussed on this call, please feel free to give Noah Gunn or me a call. Thanks very much.

Operator

Ladies and gentlemen, thank you for joining the Apollo Global third quarter 2017 earnings conference call. This will conclude our conference call this morning. You may now disconnect and have a wonderful day.

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