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The Carlyle Group LP (CG)

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MANAGEMENT DISCUSSION SECTION

Operator: Good day, ladies and gentlemen and welcome to The Carlyle Group Third Quarter 2016 Earnings Conference Call. At this time, all participants are in a listen-only mode. Later, we will conduct a question-and-answer session and instructions will follow at that time. [Operator Instructions]

I would now like to introduce your host for today's conference call, Mr. Daniel Harris. You may begin, sir.

Daniel F. Harris
Managing Director & Head-Public Investor Relations, The Carlyle Group LP

Thank you, Kevin. Good morning and welcome to Carlyle's third quarter 2016 earnings call. In the room with me on the call today are our Co-Chief Executive Officers, David Rubenstein and Bill Conway, and our Chief Financial Officer, Curt Buser. Earlier this morning, we issued a press release and detailed earnings presentation with our third quarter results, a copy of which is available on the Investor Relations portion of our website.

Following our remarks, we will hold a question-and-answer session for analysts and institutional investors. To ensure participation by all those on the call, please limit yourself to one question and return to the queue for any follow-ups. Please contact Investor Relations following this call with any additional question. This call is being webcast and a replay will be available on our website.

We will refer to certain non-GAAP financial measures during today's call. These measures should not be considered in isolation from or as a substitute for measures prepared in accordance with Generally Accepted Accounting Principles. We have provided reconciliations of these measures to GAAP in our earnings release.

Any forward-looking statements made today do not guarantee future performance and undue reliance should not be placed on them. These statements are based on current management expectations and involve inherent risks and uncertainties, including those identified in the risk factor sections of our annual report on Form 10-K that could cause actual results to differ materially from those indicated. Carlyle assumes no obligations to update any forward-looking statements at any time.

With that, let me turn it over to our Co-Chief Executive Officer, David Rubenstein.

David M. Rubenstein

Co-Chief Executive Officer & Director, The Carlyle Group LP

Thank you for joining today's call to discuss The Carlyle Group's results for the third quarter of 2016. We hope to convey four primary messages on today's call, the first two of which I will cover, and the second two of which Bill will cover.

First, Carlyle again delivered a strong distribution for our unit holders of $0.50 per common unit. Second, as a result of the positive momentum created by our solid quarterly performance as well as the ongoing investment pace of our largest funds, we are at the beginning of a multiyear fundraising period in which we expect to raise approximately $100 billion of new capital for our next generation of funds.

Third, our existing portfolio of $56 billion in remaining fair value in our carry funds continues to strengthen and appreciate thereby positioning us well to deliver future earnings. And fourth, we have decided to focus our GMS platform on global credit and we will spend much more of our energy and resources into enhancing our capabilities in this area.

And first, let me address our results for the quarter. The third quarter followed a consistent pattern to that of our second quarter with a high level of realized proceeds, attractive cash earnings, and solid appreciation across our main carry funds. Specifically, Distributable Earnings for the quarter were $228 million or $0.66 per unit, resulting in a per common unit distribution of $0.50. Year-to-date, we have distributed $1.39 per common unit and since our IPO, we have distributed an average of approximately $0.47 per quarter.

Our quarterly distribution was driven once again by a high level of realizations from our carry funds. Specifically, we realized proceeds for investors of approximately $6.6 billion for the quarter and more than $19 billion in the last 12 months. And while we remain active sellers of assets that we believe are right for sale, we also continue to have a large portfolio of mature investments for which we can and will build value and monetize over time.

This pace for realized proceeds is roughly consistent with our pace over the past five years and the gains we produced are generally consistent with our historical average MOICs. This quarter, we invested $1.6 billion from our carry funds, bringing the rolling 12-month total to $12.5 billion. While the quarterly amount is less than we have deployed on average over the past 12 months, we have recently announced a number of significant investments which are expected to close in the coming quarters.

Turning to fundraising this quarter, we raised a gross $3.2 billion or $1.8 billion net of the hedge fund and hedge fund upon the redemptions that we have expected and referenced in past quarterly calls. Year-to-date, we raised gross capital of $10.3 billion and we believe that we remain on track to raise about $15 billion in gross new capital in 2016, despite having a smaller number of funds in the market versus peak fundraising periods.

Specifically this quarter, we closed our new long-dated private equity fund Carlyle Global Partners at $3.6 billion. This fund will invest limited partner capital over longer-time horizon, frequently 8 years to 10 years in a typical private equity fund and it has already invested or committed $1.1 billion in equity across four transactions.

We launched our global infrastructure and our new mid-market credit funds at our September Investor Conference. We continue to attract capital for our fourth generation distressed investing fund and fully expect to hit the hard cap at $2.5 billion in the foreseeable future. And we also closed one new CLO during the quarter.

In addition, we continue to attract capital and scaling up a number of other strategies including Core Plus real estate and AlpInvest Secondaries and managed accounts. Of course, we believe this fundraising progress and our prior success is due in part, to the track record of Carlyle generally and to the firm's overall high global brand value.

But there's no doubt that there is a clear and growing global appetite for alternative investments, and Carlyle, as well as other large alternative investment firms, is a beneficiary of this trend. We expect that this appetite would likely continue for some time.

Turning to the second message that I mentioned at the outset, we have a substantial but quite realistic fund-raising opportunity over the next four years, enhancing our potential for both fee-related earnings and fee-earning AUM growth. Beginning this year and accelerating into 2017 and 2018, we will enter a four-year period where we expect to raise the next generation of our funds, many of which will be larger in size than the current generation. We reasonably expect to raise approximately $100 billion in new capital during this period, starting what we hope will be an even larger investment and value creation cycle.

As we raise these funds, we should start to see growth in Fee-Related Earnings precisely at the time that we anticipate our current generation of funds will be in harvest mode, with their investments creating the opportunity for further increases in Distributable Earnings for our unit holders. All of this, of course, will depend on our investment performance which fortunately continues to be strong.

In sum, we continued to execute well this quarter, had yet another quarter in which we have produced an attractive level of distributions for our fund investors and our unit holders and we have positioned the firm to deliver solid and growing earnings in the future.

Bill?

William E. Conway

Co-Chief Executive Officer, Director & CIO, The Carlyle Group LP

Thank you, David. To continue with our third major message mentioned by David, we've continued to execute on our mandate to invest our limited partners capital wisely, create value in our portfolio and ultimately, realize investments at healthy rates of return. This is particularly true with respect to appreciation in our newer funds, those funds that will drive earnings in the future.

On the investing front, we are being selective, but thanks to the breadth and diversity of our global platform, we continue to find attractive opportunities. During the quarter, we made three new private equity investments in Europe; the Cupa Group, a global manufacturer of roofing slate based in Spain; exocad, a German computer aid design software company and AA Ireland, an Irish roadside assistance provider. We invested more than $300 million in a variety of real estate projects. We are particularly focused on areas like senior living and rental properties, categories that we believe will benefit from demographic tailwinds to drive demand.

And NGP invested approximately $700 million in various natural resource opportunities in high quality basins like the Permian Basin and the Eagle Ford. We also recently signed transactions totaling more than $4 billion in equity commitments that we expect to close and deploy in future quarters.

Turning to our portfolio, our carry funds appreciated 3% in the quarter and 9% year-to-date, buoyed by continued strong performance in natural resources, and our current generation of regional buyout funds. This 9% appreciation compares to 5% year-to-date appreciation in the MSCI All Country World Index, and 6% year-to-date for S&P 500. A few large funds in particular merit a mention, and all are off to strong starts.

In corporate private equity, Carlyle Partners VI, our $13 billion U.S. Buyout fund, has committed or invested a little less than 60% of its capital. Carlyle Partners VI appreciated by 7% in the quarter after rising 15% in the second quarter. We are still very early in the fund's development and still have a substantial amount of capital to invest, but so far so good. Carlyle Asia Partners IV, a $3.9 billion fund, has invested or committed approximately 55% of its capital and appreciated by 15% on the quarter after rising 5% in the second quarter.

In real assets, U.S. Real Estate VII, a $4.2 billion fund, appreciated by 5% in the quarter after rising 7% in the second quarter. And also within that Real Assets, NGP X, a $3.6 billion fully-invested fund, appreciated by 15% in the quarter, after rising 16% in the second quarter.

Moreover, we just closed early in the fourth quarter, the partial exit of Centennial Resources, a Permian Basin company. In that single transaction, NGP X will return cash of approximately 17% of the total equity invested by the entire fund. And NGP XI, a $5.3 billion fund, is also off to a strong start, although it is very early days for that fund as well.

Lastly, we continue to be active sellers in the quarter. We generated total realized proceeds of $6.6 billion and we're especially active in the public markets where we generated $3.8 billion of realized proceeds. Specifically during the quarter, we fully exited 11 publicly traded investments, including Axalta, NXP Semiconductors, Qube Logistics and 58.com. We also sold partial stakes in other public positions in CommScope, CVC in Brazil, three investments in China, and in the Bank of Butterfield which completed its IPO in September.

Outside the public markets, we exited a number of investments through trade sales including Sagemcom, a French high-tech and broadband company in Europe III; Vogue International, a hair care company in Carlyle Partner VI, and a portion of our interest in Duff & Phelps in our first financial services fund.

In the NGP funds in which we have an economic interest, NGP realized proceeds of slightly more than $650 million and expects to returns somewhere between $1.5 billion and $2 billion in proceeds to investors throughout the course of 2016. And we realized more than $650 million in asset sales and operating proceeds from our real estate portfolios in the United States, Europe and China. In short, our core business has performed well, we continue to find opportunities to put capital to work, we've taken good care of the portfolio and have delivered strong returns.

Turning to the final message of this call, the strategic direction of Global Market Strategies or GMS. As you know, in certain areas of the firm, our performance has not met our or our investors' expectations. And when our performance fell short, it is critical for both our fund investors and for the firm that we deal with the consequences.

As a result, we recently undertook a strategic review of our GMS business segment and have made several important decisions that we believe will help us better serve our investors and should over time increase this segment's profitability.

We have committed to develop our already substantial credit business into a scalable world-class platform. To help us move towards that goal, we recently announced the hiring of Mark Jenkins in the newly created position of Head of Global Credit. Mark joins us from the Canada Pension Plan Investment Board, where he built and led the credit platform. We have also reorganized our credit business by function to enhance collaboration across product lines, industries, and geographies.

We are also expanding actively in several areas, thanks to the strong performance of our existing credit strategies. Our distressed debt investing group, which has achieved a blended Gross Internal Rate of Return of 21% over three funds is close to raising its fourth fund, which is already more than two times the size of its predecessor. Our Energy Mezzanine credit team is also close to fully raising its second fund, which is more than twice the size – twice as large as its predecessor. And we are increasing our activity in direct lending through our business development company, separately managed accounts, and new credit strategies.

We have also decided to reduce our exposure to shorter-term trading businesses, areas where frankly we have not performed well. Earlier this year, we announced that we're winding down Diversified Global Asset Management and our liquid alts business. You've also previously heard our announcement that we are selling our 55% stake in ESG back to its principals. That transaction is expected to close in the next week or so. And by the end of 2016, our total hedge fund assets under management should reduce to approximately $1 billion.

With these decisions, we are deepening our commitment to global credit, an area where there is strong LP demand and where our investment track record is consistent with the high standards we have set for ourselves for nearly 30 years. These decisions will entail some cost on the short run, but we firmly believe they will better position us to serve our fund investors well and ultimately increase the firm's profitability.

In closing, our core business remains strong and is getting stronger, and we have made several important decision to put our firm on a path to improved performance, enhanced growth, and strengthened earnings in the coming years.

Let me turn it over to Curt Buser, our Chief Financial Officer. Curt?

Curtis L. Buser

Chief Financial Officer & Director, The Carlyle Group LP

Thank you, Bill. I'm going to make four general comments before discussing our specific segment results. First, we once again posted solid cash earnings for our unitholders. Distributable Earnings were $228 million in the quarter, marking the fourth quarter of the past six quarter, where our Distributable Earnings were more than $225 million. We generated net realized performance fees of $186 million and Fee-Related Earnings of $31 million.

Second, our latest vintage funds are performing well and should drive our next generation of realized carry over time. As Bill mentioned, many of our current vintage carry funds are producing great results and are in an accrued carry position. These funds are beginning to support our net accrued carry balance, which stood at approximately $1.2 billion at the end of the quarter, approximately in line with the prior quarter. Another way to think about it, year-to-date in 2016, we have generated $490 million of net realized performance fees, while our net accrued carry has declined only $145 million or so since the end of last year. We continue to generate accrued carry with appreciation in our underlying funds, even as global equity markets have been difficult to navigate.

Third, our Fee-Earning Assets Under Management and Fee-Related Earnings will grow with our next major fundraising cycle. We continue to be active sellers of our fund investments, and over the last 12 months, we've realized $19.1 billion from our carry funds for our fund investors. As you know, as we exit those investments, we generally stop collecting management fees on that invested capital. Fortunately, this exit process is also the basis for realizing net performance fees. Combined with some asset outflows in our hedge funds and related products, overall fund management fees were $52 million lower compared to last year's third quarter.

Also contributing to decline in management fees was a $32 million decrease in catch-up management fees due largely to the smaller number of funds in the market this year relative to 2015. Our catch-up management fees are likely to shift higher during the next major fundraising cycle. We expect to see fund management fees start to stabilize and then grow as our next major fundraising cycle begins in late 2017. By extension, we would expect Fee-Earning Assets Under Management and Fee-Related Earnings to noticeably increase beginning in 2018.

Fourth, as anticipated last quarter, our Fee-Related Earnings declined from the first half of 2016 driven by Global Market Strategies. Losses in GMS have been driven by our hedge funds and commodities operations. We're focused on improving the operational and financial performance of GMS over the next several quarters and years. In addition, we continue to focus on managing our expense base and will continue to be extremely diligent in this area. For example, our total cash compensation for the first three quarters of 2016 is down 9% relative to the first three quarters of 2015.

Also during the quarter, we agreed to transfer our ownership in ESG back to its management team in exchange for termination of all remaining earn-out obligations related to our investment. ESG had no material impact on Fee-Related Earnings in the quarter and the disposition will also not result in a material gain or loss.

Moving on, we generated $54 million in Economic Net Income during the third quarter, or $0.21 per common unit (sic) [Adjusted Unit] (19:13) after-tax. Included in this quarter's result, in our general, administrative and other expenses for both U.S. GAAP and Economic Net Income is a $100 million reserve for ongoing litigation and contingencies that is excluded from Fee-Related Earnings and Distributable Earnings. As of today, this is only a reserve and we have not had cash expenses. Excluding this, our Economic Net Income would have been $154 million, reflecting the strong appreciation in various carry funds that are either in full carry or moving through their carry waterfall.

Now, let's turn to a review of our business segments. Let me start with Corporate Private Equity, which had a great quarter with Distributable Earnings of $209 million, up from $178 million a year ago. Fee-Related Earnings in Corporate Private Equity were $17 million this quarter, down from $29 million in the third quarter of 2015 reflecting the cyclical fall off in catch-up management fees from $21 million in the third quarter of 2015 to none in the current quarter.

Net realized performance fees of $168 million were roughly $30 million higher than a year ago. During this quarter, Corporate Private Equity had meaningful realizations in five different funds, highlighting the diversity of CPE segment. Importantly, Carlyle Partners VI had its first exit during the quarter in Vogue. And while this transaction did not generate realized carry for us, it was a great first exit at a substantial gain and sets a solid base of cash return to our fund investors.

Shifting to Global Market Strategies, as we noted last quarter, results in GMS were likely to move lower this quarter. Distributable Earnings in GMS were $4 million in the quarter, net of the $5 million loss in Fee-Related

Earnings already discussed. Net realized performance fees were $8 million in the quarter, largely reflecting realizations from our credit business, primarily the BDC.

Moving to Real Assets; Real Assets produced Distributable Earnings of $10 million, compared to $47 million a year ago, with the differential largely attributable to a large exit and realized carry in our first power fund in 2015 that did not recur in 2016, and due to lower Realized Investment Income. Fee-Related Earnings were $14 million, down from $20 million a year ago, due to a fall off in catch-up management fees and we had Realized Net Performance Fees of $11 million in the current quarter. During the quarter, the $14 million in Realized Investment Loss reflects the loss from Urbplan, which is our consolidated real estate investment in Brazil that we previously discussed and was partially offset by investment gains in real estate and natural resources.

In Investment Solutions, we generated Distributable Earnings of $6 million in the quarter, with $5 million in Fee-Related Earnings as compared to $3 million in Distributable Earnings a year ago. Our AlpInvest business is making solid progress toward raising its latest vintage secondary fund which has a $6 billion target and which should drive higher management fees over time. And we have several other products at both AlpInvest and Metropolitan Real Estate that could possibly impact results in the future. While overall financial results are a smaller proportion of our results today, this is a segment in which we see upside over time.

One final comment on our unit repurchase program that we launched in the middle of the first quarter. We purchased approximately 1.1 million units in the third quarter for total price of about $17 million, and for the first three quarters of the year, we purchased about 3.3 million units for a total of $54 million. That leaves us with approximately $146 million available in the program for unit purchases in coming quarters.

With that, let me turn it back to David for some closing comments.

David M. Rubenstein

Co-Chief Executive Officer & Director, The Carlyle Group LP

Thank you, Curt. To summarize, Carlyle had another strong quarter in which we produced high levels of Distributable Earnings. Moreover, because of the strength of our portfolio and our investment performance, combined with the potential to raise even more significant amounts of money, we are well-positioned to deliver future earnings. Lastly, we made several decisions in the last couple of quarters that should help position the firm to perform even better in the future for our limited partners and for our unitholders.

Now, we're ready to take your questions.

QUESTION AND ANSWER SECTION

Operator: [Operator Instructions] Our first question comes from Ken Worthington with JPMorgan.

Kenneth B. Worthington
Analyst, JPMorgan Securities LLC

Q

Hi. Good morning and thank you for taking my question. I appreciate Carlyle kind of pivoting GMS focus from the hedge funds to credit. I think in hindsight, your late-to-hedge funds made significant investments and it didn't end well. So, a couple of questions with regard to the focus on credit. Maybe one, why are you not late to credit to as well? I guess, Bill mentioned that there was demand – or that there is demand for credit from LPs. I recall that there is demand from your clients for hedge funds as well. So, why is this different?

Two, is there something more fundamental in terms of why you think you'll be successful on the credit side, and maybe why you weren't in hedge funds? Three, how does your vision for credit compare with the credit businesses of your publicly traded peers? And then lastly – I'm sorry for being a pig here, do you plan to build or buy? Thank you.

William E. Conway
Co-Chief Executive Officer, Director & CIO, The Carlyle Group LP

A

Well, I think you've made the great use of your one question, Ken. So, let me try to take them. First of all, do we think we're late on credit? The answer to that would be, well, I wish we were further along than we are. I don't think we're late really. We've got about a $30 billion credit business. In the CLO business, we're I think number two and we're probably about the biggest issuer each year now of CLOs. So, in that part of the business, we're very strong.

We have an excellent distressed business. As I mentioned in my prepared remarks, we're on our – raising our fourth fund and the first three funds all went to carry with an average Gross IRR of over 20%. So, we feel pretty good about our distressed business. Not as big as I'd like it to be, but it's very successful. We have an Energy Mezzanine business, we have a BDC, we have a lot of the pieces. I think that we should scale better, we should be bigger, and I think with Mark joining us, I think, he'll help us do that.

I admit it's going to take some time, too. This is not all going to happen all at once. I would point out that – and this ties maybe back to your question about hedge funds as well, that the difference on our credit businesses now is they're really focused on the private markets rather than the public markets, areas where we think we have a very good expertise. In the private equity business, for example, it is virtually impossible for the equity to do well and the debt not to do well. And so, I think they tie together.

Our vision is to build our credit business into one of the finest credit businesses in the world. We think, with the base we're starting from, the global network we have – we have 700 investment professionals around the world, we're confident we will be able to build it into what our dreams are. Maybe when we started the hedge fund business, we had high expectations about that business as well. And in fact, early in the time we own the hedge funds, they were wonderful performance for us, having made hundreds of millions of dollars in 2011 and 2012 in that rough approximate timeframe, they performed very well. Now, of course, they're not and I mentioned in my remarks that it look to me like the assets at the end of the year in the hedge funds are going to be – are in the range of $1 billion.

In terms of building or buying, I would think so far, we'll primarily build. Mark is running the segment. I have a lot of confidence in him. So, if he had a spectacular idea in the buying segment, I think we'd look at it. But I think our focus is probably going to be starting out on building.

Kenneth B. Worthington
Analyst, JPMorgan Securities LLC

Q

Okay. Awesome. Thank you for all those answers to my one question. Thanks.

William E. Conway
Co-Chief Executive Officer, Director & CIO, The Carlyle Group LP

A

You bet.

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

Michael Anthony Needham
Equity Research Associate, Bank of America Merrill Lynch

Q

Hey. Good morning, everyone. It's Mike Needham in for Mike Carrier. On the upcoming fundraising cycle, can you maybe drill down into the drivers and timing of the next generation funds coming online? You have a break out in the last investor presentation, but I was wondering if anything bigger could happen in 2017? And then some of the fundraising you're planning apart from the next big – next generation funds?

Curtis L. Buser
Chief Financial Officer & Director, The Carlyle Group LP

A

Well, in 2017, some of our larger funds are likely to be in the market at the latter part of the year. Again, it depends on how fast they are able to invest the current generations of funds. We have three very large private equity funds that we anticipate sometime by the end of 2017 will be in the market. That would be our next U.S. generation buyout fund, our European buyout fund, and our Asian buyout fund, and I suspect not far behind that will be our Japan buyout fund.

Those will be our four big buyout funds and we have thought it might not be ideal to have them in the market at the same time. On the other hand, when they're out of capital, it's necessarily to raise new funds. We have found that some investors are interested just in U.S. buyout or just in Asian buyout or U.S. buyout. And so, it's not necessarily that they're cannibalizing each other. And also, because these funds have long track records, they have a reservoir of investors who are pretty interested in going back into them.

So, those would be the main things that, I would say, will be driving the fundraising process over the next couple of years, but we have many other funds that, in 2018 and beyond, will be coming into the market. And I'd say, in our U.S. Real Estate business as well, which is quite large, our next generation of U.S. Real Estate opportunistic fund will be in the market, and it's actually doing some pre-marketing now and the reception to that is likely to be pretty good. So, I think, our track record is good in these funds, but I think as good as our track record is, we can't be superhuman. If there are no interest in any private equity funds, then we're not going to be raising large sums.

On the other hand, as I tried to say on my opening remarks, it seems as if the conundrum that investors face today, which is low interest rates and low returns on public equity and fixed income investments, is driving them to alternative investments. Over the last 10 years or so, the gap between public equity returns and alternative investments or particularly private equity, has been roughly 800 basis points, on average. I'm not talking about top-quartile versus average, but average versus average. And if we can continue to get those kind of averages, people are going to put more and more money into these alternative investment funds because they're so much better than anything else people can get.

Final point on this, that larger source of new capital that's coming into our market is really – are two, I would say. One is the sovereign wealth funds. The sovereign wealth funds had roughly $1 trillion around 2003 total. By 2020, it's expected that they'll have $9 trillion to $10 trillion. So, the biggest source of capital and they are putting very large sums into our kind of investment vehicles. And then family offices and individual investments, they are dramatically increasing their investments in alternatives, and I suspect they will be important investors for us and for our peers. So, I don't know if that directly answers your question, but we are pretty optimistic that we can get to the approximately $100 billion over the next several years, because there is likely to be a fair amount of demand for our products, and our track record has been pretty good so far.

Michael Anthony Needham
Equity Research Associate, Bank of America Merrill Lynch

Q

Okay. Yeah. Thank you.

Operator: Our next question comes from Craig Siegenthaler with Credit Suisse.

Craig Siegenthaler
Analyst, Credit Suisse Securities (USA) LLC (Broker)

Q

Thanks. Just as a follow-up on the last question. So, if I add up U.S., Europe and Asia buyouts, and assume the next fund is 20% larger than the last, I think you get about $25 billion of capital. And then I heard what you said about U.S. Real Estate in Japan, that helps, but what other kind of product sets may kind of get up to $100 billion.

Curtis L. Buser
Chief Financial Officer & Director, The Carlyle Group LP

A

Okay, all right.

Craig Siegenthaler
Analyst, Credit Suisse Securities (USA) LLC (Broker)

Q

And then – can you hear me okay?

Curtis L. Buser
Chief Financial Officer & Director, The Carlyle Group LP

A

Yes, I can. Well, let's go through our various segments. I focus a bit on Corporate Private Equity. So, Corporate Private Equity, I mentioned the big four funds, but we have some others like our financial service industry fund and so forth. But let's talk about energy and natural resources, and also real estate. In energy and natural resources, we have several funds that are likely to be in the market again, and our power fund is doing quite well. We'll probably have another power fund in this period of time that we're talking about. Our international energy fund will probably have another fund during this period of time that we've talked about. In NGP, we'll have another fund during this period of time as well.

We also are raising our infrastructure fund and the first generation of it will probably be raised before this period of time is over, and we may be into the second generation by the time this four-year period is over. In terms of our real estate fund, I did mention that our next opportunistic real estate fund is likely to be – pretty likely to be bigger than the previous one. And we've been raising these opportunistic funds every couple of years, and I suspect by the end of this period of time, this four-year period of time that I mentioned, we might be into the next opportunistic real estate fund. So, generally, I'd say, if you take a look at everything we have, about a third will be in Corporate Private Equity, about a third in real estate and energy.

And then, we have two other segments. GMS, which Bill addressed earlier which is our global credit business, and that will be roughly 10% to 15% of everything we're likely to raise during this four-year period of time. And Mark Jenkins and his team, and it's a pretty good size team and they have many different funds, and they'll be starting some funds that are probably – will be announced in this period of time, will expand our credit business a fair bit. And then Solutions, our Alpinvest business, which is the largest part of Solutions, is doing quite well right now. They're doing well in their Secondaries fund. They have a couple other products that they're going to announce soon. And so, I think those are the variety of different products.

Also, let me say that there are some products that I don't know about today that are likely to be raised during this four-year period of time. In Carlyle's history, we do come up every year or two with some new ideas, and we aren't just always raising successor funds, and I'd be disappointed if we didn't have some new funds that kind of do things that are different than what we've done before. So, for example, our Carlyle Global Partners fund was something we didn't really have a few years ago. And now, we have a $3.6 billion fund that does long-term private equity investing.

So, if you're a creative organization, as we think we are, and you have a lot of investors that want you to keep coming up with new products, I think, we are likely to come up with some number of new things that our investors would be interested in. So, $100 billion sounds like a lot, and it is, but we've raised roughly that in the previous four-year period of time when we had our high fundraising period of time. So, it's not that heroic to do that, and I'm clearly comfortable that we can get there.

Craig Siegenthaler
Analyst, Credit Suisse Securities (USA) LLC (Broker)

Q

Thank you, David.

Operator: Our next question comes from William Katz with Citigroup.

Jack Keeler
Analyst, Citigroup Global Markets, Inc. (Broker)

Q

Hi. Thanks for taking my question. This is Jack Keeler filling in for Bill. Just a question on the longer-term private equity fund, and I guess, longer-term funds in general. Just curious on what you're seeing in terms of investor appetite for the longer dated capital versus, let's say, the more traditional carry funds you've historically raised?

David M. Rubenstein
Co-Chief Executive Officer & Director, The Carlyle Group LP

A

Well, let me start and Bill will follow. The longer-term funds are still a relatively small part of the overall private equity market because not every investor is willing to let people hold onto assets for eight years to 10 years. But there's a fair amount of valid interest in it and it may grow, but still the bulk of what we've done is shorter term. But the longer-term things tend to be ones where you have current yield as well as some capital appreciation.

And we've done four transactions; Bill might discuss what we've done in that fund already. And I suspect that the sovereign wealth funds which don't have to pay out money quite as regularly as public pension funds will be big drivers of this kind of longer-term investment business, because they really have enormous amounts of capital and they can afford to have investments grow for quite some time. So, we see it as a reasonable growth business, but it's not going to replace the traditional Corporate Private Equity anytime soon in my view. Bill?

William E. Conway
Co-Chief Executive Officer, Director & CIO, The Carlyle Group LP

A

Yeah. Couple of thoughts. First of all, the fundraising and the investment pace kind of have to always tie together on this type of thing. The fundraising was from just about 10 investors, they were mostly sovereign wealth funds, they were – as David said longer-dated, people thought about the long-term investing. The terms of these longer dated funds tend to be a little different than the terms of the other Corporate Private Equity funds. They sometimes will have lower hurdles. They may have, as David said, longer investment periods. They tend to have not a commitment fee on the commitment, but they tend to have a satisfactory fee on the capital once it's deployed. So, they're a little different, some advantages for us, some advantages for the LPs, and obviously, we were able to find pretty significant demand.

The other side of it is, can you find a place to put the money to work? And I would say that we don't necessarily think that the longer dated fund will have a lower rate of return than the standard buyout funds, it may or may not. The differentiating factor is really maturity and time that the investment might well be held. I know in our time in Carlyle, we've had many companies that we owned in our private equity business that we wish we could have held forever, but unfortunately, our model really required us to sell them.

In terms of a couple of examples of funds that are – the first four investments we made in the longer dated fund, one was a large portfolio of corporate aviation assets that we bought from a big seller. It was a business that really tied a lot to the other businesses that Carlyle knows. As you know, we've had a big business in aerospace for a long time. So, we're able to use the expertise we had in some of our aerospace team to help us vet the value of these assets in this pool of leases and sales, and various other pieces of equipment associated with corporate aviation. And the second one was a kind of an investment in content, media content, very long term licenses to show replays of shows or syndications both United States and globally. It's a very long lived asset, I'd say, both of those have that in common.

There certainly is a lot of demand. What we have to be careful of is that maybe some people would like us to put the longer dated fund just in competition with the buyout funds, and really the big thing is that it's a much longer investment period usually.

Jack Keeler
Analyst, Citigroup Global Markets, Inc. (Broker)

Q

Great. Thanks for taking my question.

Operator: Our next question comes from Chris Kotowski with Oppenheimer.

Chris Kotowski
Analyst, Oppenheimer & Co., Inc. (Broker)

Q

I wonder if you can give any color around the litigation charge and/or reserve and help us put a breadbox around it. And historically, I guess, since most of the activity, business activity is conducted within funds, usually the funds are liable for any litigation. So what made you take a charge at the – or the reserve at the parent?

Curtis L. Buser
Chief Financial Officer & Director, The Carlyle Group LP

A

Chris, thank you. This is Curt. So as you know, we have a number of contingent matters, all of which we've previously disclosed and discussed in our public filings. These matters are in different stages of resolution. Some of them are in their early stage, some of them are middle or later stage. Each still has a pretty wide range of possible outcomes with one-end typically being zero. But this wide range makes it difficult to come up with a precise estimate for the outcome.

That said, we thought it was appropriate to increase our reserve and accordingly, we recorded a $100 million charge. And that went both through our GAAP earnings and Economic Net Income. And because of the nature of these matters, we're really limited in what else that we can say. I would encourage you again to look at the public filings where we've talked about these matters before.

In terms of the second part of your question, firm versus fund, I think that's made fairly clear in the public filings in terms of the distinction between those two.

Chris Kotowski
Analyst, Oppenheimer & Co., Inc. (Broker)

Q

Okay. Well, never mind. I'll get in the queue. Thanks.

Operator: The next question comes from Glenn Schorr with Evercore ISI.

Kaimon Chung
Analyst, Evercore Group LLC

Q

Hi. This is Kaimon Chung in for Glenn Schorr. So capital deployment seemed a little light this quarter and I know you highlighted there are some transactions waiting to close. I'm not sure if I missed it, but can you just size the deals in the pipeline? And just bigger picture again, can you just talk about the current investment environment, how you're finding good investment opportunities given today's market valuations and what type of purchase multiples are you transacting at? Thanks.

William E. Conway
Co-Chief Executive Officer, Director & CIO, The Carlyle Group LP

A

You must have gone to Ken Worthington School of question-asking. Let me try. Capital commitments, that they were about $1.6 billion in the quarter. I would say on almost any metric of Carlyle's, it is difficult to judge our performance based on any one quarter. And so, I wouldn't say light or heavy or anything else, it's just, it's not so much random but it just can vary enormously by quarter.

In terms of the – I mentioned in my remarks we had $4 billion of committed transactions. These are not deals in the pipeline, if you will, these are deals that we're committed to do. And absent some really unforeseen developments, let's say, an antitrust issue or some global regulator said something, I think that those deals are all likely to close.

The biggest one which we did announce was the purchase of Atotech from Total and it was for a price of approximately $3 billion, so you can work out the size equity check that that would employ. That's a big part of it. We think that'll close some time in the beginning of 2017. We've got a variety of other deals from the pipeline, but I think that's the one I would call out.

In terms of purchase multiples that we're seeing, I would describe them as high. We are regularly beaten out by our competitors, and strategics, and the public market. I suspect whenever we win one, some of our competitors are saying, well, Carlyle really overpaid for that. And frankly sometimes when we lose, we're wondering what our competitors saw that we didn't see in a particular asset.

Generally, of course, the transactions that in order to work at relatively high multiples – and let me also say that this – you can't really generalize, I'd say multiples in Europe and Japan are a lot less than they are in the United States. I would say that we don't really invest in a macro environment anyway, we're really much more micro investing. We try to invest in what we can control, which is what companies do we buy, what price do we pay, and who do we pay to run those businesses for us. But, generally, I think multiples are high. And we – I think most people expect as long as interest rates stay low that multiples will stay high. Of course, there's no guarantee that that will be the case.

We're blessed that we have a big global investment team. They spend their time at both monitoring the existing portfolio as trying to find those spectacular deals we're going to turn into wonderful investments for our LPs and eventually our unit holders. But it's a – no doubt, it's a tough job and multiples are high. In terms of what that means for internal rates of return, time will tell. That will depend on what happens at the exit markets, what happens to each specific deal. We've been doing this for about 30 years. Frankly, the internal rates of return haven't varied that much over that period of time, but I would expect that with these high-asset prices, that they're likely in the future to be lower than they've been in the past, but we'll see what happens.

David M. Rubenstein
Co-Chief Executive Officer & Director, The Carlyle Group LP
A

Let me just add to that. Yes, EBITDA multiples today are somewhat higher than they were before the great bubble burst in 2007 or 2008. Well, interest rates are lower, so therefore, it's not really apples-and-apples. But the most important point that Bill is really addressing is that while returns might come down, investor expectations of returns coming down are pretty significant. In other words, investors, because they have so few other options, are actually saying, well, if the rates of return are lower than they were a couple of years ago, we're fine with that because we have nothing else that we can get better returns at.

So when money is coming into our industry dramatically into our funds, but it's because investors really don't see better alternatives. So even if our rates of return – other firms comparable with us, will have lower rates of return. I don't think investors would be unduly surprised or upset. They actually think that the rates of return that these multiples are likely to yield, are still very, very attractive.

Kaimon Chung
Analyst, Evercore Group LLC
Q

Thank you.

Operator: Our next question comes from Michael Cyprys with Morgan Stanley.

Michael J. Cyprys
Analyst, Morgan Stanley & Co. LLC
Q

Hey. Good morning. Thanks for taking the question. Just curious if you could elaborate a little bit on the Fee-Related Earnings trajectory? It seems like there's a number of moving pieces, say, over the next year with some of the hedge fund business-related exits coming up but then also, the monetization pipeline, which maybe could pressure Fee-Related Earnings. But then, as you're deploying some money, some pieces could be turning on in terms of fees. That's more the near term. And then, the longer term if you could just talk to, you mentioned $100 billion fundraising, how should we think about that benefiting Fee-Related Earnings to have some predecessor funds that stepped down and then what sort of fee rates can we think about for the products that you're planning to raise?

Curtis L. Buser
Chief Financial Officer & Director, The Carlyle Group LP

A

Michael, thanks for your question. So let me start with really a discussion of fee earning assets under management. I think really that's the driver of the core Fee-Related Earnings. So, if you think back first, I've talked about a number of core items that put some pressure on Fee Earning Assets Under Management, although in many of these cases, they don't have as much of a direct impact on fee-related earnings. So three items in particular. Our legacy energy funds where we have a small economic participation, has about $6 billion of remaining Fee Earning Assets Under Management as of September 30. That will run off, won't have much of an impact on earnings, but it will impact Fee Earning AUM.

Second piece that we have seen and we'll continue to see is the hedge fund. So, the hedge funds at their peak were about $15 billion of Fee Earning Assets Under Management. They now stand at about $5 billion and as Bill said in his remarks, we expect it will be about $1 billion by end of the year. So that's going to be some of your downward pressure in the fourth quarter and a lower number there going forward.

Finally, AlpInvest. When we bought AlpInvest, we knew that those are large amount, about $10 billion or so of Fee Earning Assets Under Management that primarily came from its prior owners. That amount, we knew was not going to be replaced at the same fee-earning level. We're replacing that at a higher-fee earning level. So, you will see a decrease in Fee Earning Assets Under Management in solutions from that trend as it winds its way through, although that again is low yielding assets under management that is being replaced by higher yield in assets under management. That, plus, obviously, we've been acting at a very good pace, $19 billion over the last 12 months. And in the current period, we've been in somewhat, I'll say, for us, a bit of a lull in fundraising.

We're going to raise about $15 billion gross this year. And that's why David and them mentioned kind of we're embarking on the $100 billion new raise. That, it starts really – some funds will start to hit in early 2017, a lot of the bigger funds won't be until the end of 2017. When they turn on fees, it will really impact our Fee Earning AUM, that's when we turn the fees on. That will most likely be the end of 2017, the beginning of 2018, and that's what's going to then start to see a drive-up in 2018 is when you really see it coming through not only in fee-earning AUM, but also in fee-related earnings.

So, hopefully, that summarizes your question fairly well.

Michael J. Cyprys
Analyst, Morgan Stanley & Co. LLC

Q

Great. That's super helpful. And just any commentary around fee rates around different products that you're raising and just generally how you're thinking about overall deep pressure in the industry or discount for size, should I say?

David M. Rubenstein
Co-Chief Executive Officer & Director, The Carlyle Group LP

A

On fee pressure, so called, let me clarify or put it into three categories. There is the management fee, there is the carried interest, and there is the so-called deal fees and related kinds of things like that.

On the carried interest, there really hasn't been pressure on traditional private equity funds, at least we haven't seen it going below the 20%. A longer-dated fund might be different in some respects, but a traditional carried interest of 20% in their traditional private equity fund I think is pretty likely to be accepted. I don't think that's going to be reduced.

In terms of the management fee, the ongoing management fee on committed capital, it depends on the size of the fund. A smaller fund can have a 2% fee, a tiny fund might have even slightly higher. But most of the funds that we're raising are probably in the 1.5% range, maybe slightly higher in some cases. And the biggest funds might be between 1% and 1.5%. I don't really see the fee pressure changing that much from where it is today. In other words, I think there was some fee pressure after the Great Recession, and fees did come down somewhat, but I think they've stabilized at this point.

And I would add that it's actually the reverse of where the situation was just a few years ago. It used to be that the limited partners were demanding more fee cuts and so forth than they are today, in part because the interest in getting into the best fund is so intense, these funds are typically oversubscribed. That really what's happening now is sometimes there is the general partners are able to get exactly what they set out at the beginning to get and not really having any fee pressure.

To some extent, though, what is now more common in the industry than maybe 10 years ago is that if you come in early into a fund, there is a slight discount. And if you come in in size, there's a slight discount. In the early days of private equity, everybody paid the same fee whether you came in early, late, or bigger or smaller. Now, there are slight discounts for that, but I think they're compensating benefits to general partners.

The third type of fund is the deal fee, the so-called deal fee or the transaction fees. I think they have, to some extent, faded a bit. I think we were never dependent on it that much, and we never really got that much of those kind of fees relative to some other people in the industry. I don't think they're likely to come back. I think probably there are transaction fees, but relatively modest compared to what they might have been many years ago.

But anyway, I don't see ongoing fee pressure that's significant. I think in part, it's more the other way around. The larger investors really want to get into your funds, and there's a capacity problem for some of them, so they're willing to pretty much accept the terms that you often propose at the beginning.

Michael J. Cyprys
Analyst, Morgan Stanley & Co. LLC

Q

Great. Thank you. Appreciate all the color.

Operator: The next question is a follow-up question from Chris Kotowski with Oppenheimer.

Chris Kotowski
Analyst, Oppenheimer & Co., Inc. (Broker)

Q

Yeah. On the Investment Solutions business, I'd never reflected on it that much, but this quarter, because it's relatively small – financially in terms of the whole business, but this quarter, you had $36 million of realized carry and $36 million of realized performance fees. Is that just the nature of that business that all the carry gets paid out?

Curtis L. Buser
Chief Financial Officer & Director, The Carlyle Group LP

A

So, Chris, this is Curt. So on a net basis, we had about $1 million of net realized performance fees on Investment Solutions. You have to remember that when we bought the – and most of the carry that's coming off is from AlpInvest. We see this as a huge opportunity for us in the future. But what you have to remember is that most of the carry that's being realized today, we didn't buy. And so, while we have to consolidate these numbers, in the GAAP numbers, you will see a large amount of realizations and even in the non-GAAP you'll see large amounts, but it's pretty much either going to taxes or to the deal teams because our share of what is being purchased is really nothing of what's coming out.

Now, in a few years, so 2020, 2021, you'll start to see our portion of that going up and as a result, you're going to see Investment Solutions becoming a bigger part of our business.

Chris Kotowski
Analyst, Oppenheimer & Co., Inc. (Broker)

Q

Okay. Thank you.

Operator: And I'm not showing any further questions at this time. I'd like to turn the conference back over to our host.

Daniel F. Harris
Managing Director & Head-Public Investor Relations, The Carlyle Group LP

Thank you very much for joining us this quarter on the call. We look forward to talking to you next quarter. If you have any further questions, feel free to follow up with Investor Relations at any time.

Operator: Ladies and gentlemen, this does conclude today's presentation. You may now disconnect and have a wonderful day.