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The Carlyle Group, Inc. (CG)

Morgan Stanley Virtual Financials, Payments and CRE Conference

CORPORATE PARTICIPANTS

Kewsong Lee
Chief Executive Officer & Director, The Carlyle Group, Inc.

OTHER PARTICIPANTS

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

MANAGEMENT DISCUSSION SECTION

Michael J. Cyprys

Analyst, Morgan Stanley & Co. LLC

Before we get started, I've been asked to direct your attention to important disclosures on the Morgan Stanley Research Disclosure website at morganstanley.com/researchdisclosures. If you have any questions, please reach out to your Morgan Stanley sales representative.

Good afternoon, everyone. Welcome back to Morgan Stanley's Financials Conference. I'm Mike Cyprys, equity analyst covering brokers, asset managers and exchanges for Morgan Stanley Research. Welcome to our fireside chat with The Carlyle Group. We're excited to have here with us live in person, Kewsong Lee, CEO of The Carlyle Group. As many of you know, Carlyle is a global investment firm with about $260 billion of client assets under management.

Kew, thanks so much for joining us live today.

Kewsong Lee

Chief Executive Officer & Director, The Carlyle Group, Inc.

Oh, it's great to be here. Great to be doing this live and in person.

QUESTION AND ANSWER SECTION

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

Now, is this one of your first in-person meetings?

Kewsong Lee A
Chief Executive Officer & Director, The Carlyle Group, Inc.

This is – well, it's not my first in-person meeting, but this is my first in-person conference. So it's special for Morgan Stanley.

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

Oh. Well, thank you. Thanks. It's been about six months, Kew, since your Investor Day where you guys shared a number of multiyear targets. What would you say the investor feedback has been so far? How would you summarize that and how is the business performing against those targets more broadly?

Kewsong Lee A
Chief Executive Officer & Director, The Carlyle Group, Inc.

Sure. So let's take a step back. I've been challenging our firm to think bigger, perform better, move faster. We've laid out our priorities to scale our existing businesses, move into adjacencies and then institutionalize the firm. And the target just to remind everybody was to generate $800 million of FRE over four years, $1.6 billion of DE, get to 40% FRE margins and raise $130 billion plus in AUM. So as I sit here today, take a step back. We're doing better than I expected.

I'm really excited about the firm firing on all cylinders. I think our management team is executing exceptionally well. Then finally, I would say, this environment, while there's uncertainty and certainly challenges, it creates a ton of opportunity and the tailwinds for our business are strong. So I take a step back and basically say I feel really good about where we are. I think we're ahead of plan. And I fully expect us to keep generating more and more positive momentum the more we get into the plan.

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

Great. And I certainly want to come back to those targets. We're going to dig into them across the different ones that you laid out. But I know you guys are on the road meeting with investors whether it's virtual road, perhaps more so than in-person. But certainly curious, any perspective on how that is transitioning here? But as you're speaking with LPs today raising some of your latest funds, what are some of the common themes that you're hearing from LPs and what unmet needs do they have?

Kewsong Lee A
Chief Executive Officer & Director, The Carlyle Group, Inc.

Sure. So I'm going to be very careful not to talk about any specific funds for obvious reasons. But in general, we're seeing LPs basically like all investors struggling in a low interest rate environment to figure out where do they drive returns. So in general, alternatives, private markets where the outperformance has been. So we're seeing basically secular flow into our asset class. So that's very, very big picture. Second, they're trying to do more with less in terms of GP. So there's consolidation. So let me just make point something out. If you go 10 years ago at Carlyle, 24% of our LPs were in three or more distinct strategies at Carlyle. Then last year, it was 64%; end of first quarter, 73%. So you can see we're doing more and more with our LPs and they – that's another way of seeing is the flip side of them doing – wanting to do more and more with us.

And then finally, LPs now – this is a real asset class. I don't know why we keep calling it alternatives. These are massive quantums of dollars that need to be very responsibly managed. And they're looking for very sophisticated GPs, because they're planning on a multiyear type of a basis across a full breadth of strategies around the world. And there are only a handful of us who can really meet those needs. And so, you're seeing LPs continually wanting to do more in alternatives. You're seeing LPs wanting to do more with the few GPs that they feel are very close and strategic relationship with. And they're looking for sophisticated GPs that are appreciative of what their needs are, trying to figure out solutions over a multiyear timeframe across a broad range of strategies.

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

Q

And what would you say Carlyle is doing to bring in to the firm these new fund LPs versus re-ups from existing ones?

Kewsong Lee
Chief Executive Officer & Director, The Carlyle Group, Inc.

A

Sure.

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

Q

Can you touch upon any sort of differences on the retail versus the institutional side of that?

Kewsong Lee
Chief Executive Officer & Director, The Carlyle Group, Inc.

A

Sure. So it's interesting. We have about, [indiscernible] (00:04:58), close to 2,700 LPs. And we're very big. We've been around for a long time and in a ton of countries. Yet, just last 12 months, we brought in close to 100 brand new LPs we've never done business with. So there are new LPs out there that we continually are bringing into the Carlyle family, so to speak. Obviously re-ups are very strong in this environment, particularly when it's a virtual environment with Zoom. They are – or WebEx or whatever. They are gravitating towards those GPs that they feel comfortable with, that they trust, that they know have delivered for them in the past. So I think that's to our advantage.

And so, for a whole bunch of environmental reasons – but the asset class is growing and you're seeing more and more interest obviously from retail. And if you break down our statistics, I'd say about 45%, call it about half of our business comes in from pension funds. And about 10% to 15% right now are coming in from what we call retail, high net worth, et cetera. And my guess is over time, obviously, that will grow, but it's not an easy path. But clearly, there's a huge opportunity set of capital there.

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

Q

So 100 new LPs just in the past year?

Kewsong Lee
Chief Executive Officer & Director, The Carlyle Group, Inc.

A

Past – latest 12 months.

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

Q

That's quite impressive. Any sort of color around how you've been able to do that particularly over Zoom, and any sort of update on what the travel situation is

[indiscernible] (00:06:32)

Kewsong Lee
Chief Executive Officer & Director, The Carlyle Group, Inc.

A

Sure.

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

Q

Are you guys traveling around the world or starting to?

Kewsong Lee
Chief Executive Officer & Director, The Carlyle Group, Inc.

A

Yeah. So it's really interesting to see how our business is going to be affected with the reopening. I would say if you go back a year, personally as a CEO, I was nervous when – obviously when COVID happened. Oh, my gosh, what's going to happen to our business, how do we do fundraising, what's going to happen with management team meetings. I got to tell you, our team, our firm adjusted incredibly well. Overnight, boom, we went virtual, and we raised more money last year than almost any other year. And we hadn't really – we didn't really have any physical LP meetings. Right?

And so it just talks to the effectiveness of that platform, but also the hard work of our people, the relationships that they have, and just the power of our brand and our institution and basically, our LPs wanting to make sure they're dealing with a safe pair of hands during times of change and turbulence. And we have incredibly strong distribution arm led by terrific person where it's one of the power – is one of the power alleys of Carlyle is distribution. And we – it's a direct force that has all these relationships with our LPs, and we're nurturing it, investing in it, and that's the basis for why we keep bringing in new LPs into Carlyle strategies.

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

Q

Well, speaking of raising capital, you're looking to raise meaningful amounts of capital in the next couple of years. You've outlined a target to grow your fee-earning AUM, which implies, call it, a 5% to 6% growth CAGR in the next couple of years. How much of that would you say is from new initiatives versus existing and where might you be conservative on that growth target?

Kewsong Lee
Chief Executive Officer & Director, The Carlyle Group, Inc.

A

Sure. Well, look, I put out $130 billion plus as our target. I focus more on the plus. I think two things are happening. First, the schedule for when we are going to market with our strategies has accelerated. And second, just a general comment on fundraising, our strategies are being very well-received. The performance is strong. And I'm seeing very good demand. And like I said earlier in my commentary to you, it's better than we planned. Right? So, when you put those two things together, I think it all informs me when I say focus on the plus of the $130 billion, and I think there's more upside risk than there is downside risk at this point in time.

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

Q

Great. Any sort of color you would care to elaborate on the new versus existing strategies there?

Kewsong Lee
Chief Executive Officer & Director, The Carlyle Group, Inc.

A

Well, the – when you look at the – what's really driving our AUM build, it's going to be taking our very large existing strategies and scaling them up even more. Right? So, whether it's US buyout, Asia buyout, Europe buyout, whether it's our secondaries fund, our US real estate product, all of these funds tremendously successful. They're all growing 30%, 40%, 50% over predecessor funds, right? So, without giving you the exact breakdown, a big chunk of our AUM strategy is being driven by just scaling our best platforms which is kind of the first pillar of our strategic plan, just scale and accelerate the growth of our strengths and those are our existing businesses.

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

Q

And so when you think about, I guess, that plus side of your target...

Kewsong Lee
Chief Executive Officer & Director, The Carlyle Group, Inc.

A

Sure.

[indiscernible] (00:10:08)

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

Q

...fair to say that that's coming more from the existing strategies, scaling perhaps a little bit bigger and sooner?

Kewsong Lee
Chief Executive Officer & Director, The Carlyle Group, Inc.

A

I think it's both. It's our existing strategies, bigger and sooner. And don't forget, we've got great initiatives going on in global credit, where we're seeing great success not only in our dominant CLO business, but also our illiquid strategies like our opportunities fund where we've raised close to $5 billion over just the past three years. We've launched new initiatives in infrastructure credit. We've got new initiatives coming in real estate credit. We've also grown through acquisition. Look at Carlyle aviation finance which has done really well even through COVID. So, it's a combination of the existing that's successful becoming even bigger with a real drive and a focused way to pick out very scalable and new areas for us to grow.

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

Q

We'll certainly come back to global credit in just a few minutes. But just maybe taking it up a notch, with raising more assets comes more management fees.

Kewsong Lee
Chief Executive Officer & Director, The Carlyle Group, Inc.
A

Yes.

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

And I think the expectation is more fee related earnings from that as well. You've laid out a target of – a goal of $800 million for 2024 versus, call it, just under $500 million in terms of what you put up in 2020. So, I guess a two-pointer question here is can you talk about the largest contributors to that fee-related earnings target that you laid out? And as T&E comes back, in terms of the – into the run rate there, how do you think about the moving pieces and any sort of offsets?

Kewsong Lee
Chief Executive Officer & Director, The Carlyle Group, Inc.
A

Yeah. I mean, look, the biggest driver of it is going to be scaling our existing fund strategies up, right? So if they're growing 30%, 40% from predecessor funds, you're going to see – and we're not driving operating expense at nearly that rate. You're going to see tremendous operating leverage and flow through. And so, that's going to be where you see a bunch of FRE pickup. Second, our capital markets business, that's just pure, what I would call, gravy because it's a team that's already been built out. It's financing fees and transaction fees that we hadn't been picking up that we ought to have been from portfolio companies and from our new deals. So I think that's going well. And then quite frankly, global credit, these are higher margin businesses because they are much more – there's much more operating leverage when you scale those strategies. They're more liquid than private equity. So I think you're going to see big FRE pickup there.

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

Great. Why don't we shift gears a little bit, talk about the deployment opportunities? You have about $75 billion in dry powder today across your platform. Can you talk about where you're seeing the most compelling opportunities to put capital to work? And also, I'd be curious, any perspectives you have on the return of big LBO activity, just given some of the large transactions in the press?

Kewsong Lee
Chief Executive Officer & Director, The Carlyle Group, Inc.
A

Yeah. Some of these deals we've done. Look, I mean, the great thing is our platform is so large, so global across all industry sectors, we kind of have a very good read on anything and everything that's happening in the private equity space. I would say, it's both large deals, more traditional deals like the Medline deal that was recently announced. But also, past year, we've done a tremendous amount of growth investing as well. And if you take a step back, the regions where we're busiest are – we're actually – we're busy in Americas. Europe is picking up in a strong way. We've always been busy in China, and India, we deployed close to $1.5 billion just in the past year in India. And Japan, we've been in Japan for over 20 years and it's always a steady source of deals for us. So, that's geographically. But industry-wise, it's got to be healthcare and tech. But I'd make the statement, every deal is a tech deal now.

Right. Every industry is being affected by tech. And so I don't know how you define tech. But clearly, the technological disruption that's occurring across all industries is creating a tremendous amount of deal flow. And then finally on the whole growth investing, we've got just amazing sector expertise. And what we've been doing very quietly is figuring out how to drive our deal flow through that platform. And when you marry that sector expertise with our global platform and the resources we have, be it capital markets, human capital assessment, procurement strategies, digital help for these portfolio companies, it's a terrific formula for entrepreneurs and these growth companies wanting to partner with us, so that we can help drive their growth. So the issue for us is not really the dry powder in the sense that everybody is worried about dry powder, but they're not really focused on the fact that the opportunity set has really expanded.

Change in the environment is just creating opportunity. And if there's one thing I would say it's – it used to be that we thought about the opportunity set from technology and changes in healthcare coming from the growth side. But COVID has basically made all CEOs and all companies think about how they need to use digital more effectively in their businesses. So we're seeing incumbents in mature businesses unleash big operational and other types of opportunities by more readily adopting things that they otherwise wouldn't have done pre-COVID. And so the opportunity set almost has expanded or doubled in terms of its both the mature and incumbent companies, as well as the newer growth interesting disruptive companies.

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

I could ask some follow-ups, but I want to keep going along here.

Kewsong Lee A
Chief Executive Officer & Director, The Carlyle Group, Inc.

Keep going.

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

But that's fascinating.

Kewsong Lee A
Chief Executive Officer & Director, The Carlyle Group, Inc.

Right.

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

Maybe just shifting over to Europe portfolio.

Kewsong Lee A
Chief Executive Officer & Director, The Carlyle Group, Inc.

Yeah.

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

Today, you posted some very impressive returns there over the last 12 months I think in private equity, 50%-plus returns, credit 30% or so, helping drive your accrued carry balance to a record $3.2 billion. Can you just give a little bit more color around the attribution of performance within your portfolios? And then looking forward, how do you expect returns to sort of trend in whole periods relative to what you guys have put up historically speaking?

Kewsong Lee
Chief Executive Officer & Director, The Carlyle Group, Inc.

A

Great question. So, the attribution, I would say, is diverse, widespread. It's across US, Asia, Europe. It's across private equity, real estate, our solutions business, our credit opportunities business. Basically, all our businesses are performing, I'm proud of our team, exceptionally well. The mix between public versus private in our portfolio, about 20% are public. So, clearly as public markets go up, you're seeing values go up in that section of our portfolio.

But our private companies are all – I mean, look, every fund has a deal or two that we wish was doing better. But in general, these companies are performing, they're growing, their margins are expanding. And so, there's fundamental value creation occurring. And so, one thing to remember at least at Carlyle, Mike, is 80% of our returns is driven by EBITDA growth and cash flow generation, 80%. And the rest being multiple expansion and financial leverage. So, 80% of our increase in value is driven from what I would call very fundamental top line, bottom line, capital efficiency type of things.

And so, when you have a formula, it drives returns because we're making these companies better. We're making these companies perform in a very fundamental sustainable way. You can see that we feel really confident about a continued path regardless of whether markets are strong or not, regardless of whether the environment is doing this or that. If we can drive that fundamental value creation at these companies with the type of improvements we're talking about, that's what's really driving the type of appreciation numbers that you're alluding to.

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

Q

And any sort of perspective or views on the outlook for returns for what you're investing today relative to history?

Kewsong Lee
Chief Executive Officer & Director, The Carlyle Group, Inc.

A

Well, you tell me what interest rates and inflation will be now. Look, it's the $64,000 question as to what's going to happen to general economy, what's happening in markets, et cetera. And to a certain extent, our valuations will be comped to trading multiples, right, because of valuations, et cetera. But I'll just go back to – look, we partner with great management teams. These are great companies and our resources are enormous. Our investment teams are incredibly experienced and we set up a really aligned structure with these companies. And so, quarter-to-quarter, who knows what happens with fluctuation. But basically, if we can just stay focused on driving the fundamental performance improvements of these businesses, I'm highly confident we're going to create the appreciation.

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

Q

Well, speaking of appreciation and performance, back at your Investor Day, you outlined a path to I think it was about $800 million in performance fee revenues by 2024.

Kewsong Lee
Chief Executive Officer & Director, The Carlyle Group, Inc.

A

Right.

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

Last year, you put up about $250 million. So...

Kewsong Lee
Chief Executive Officer & Director, The Carlyle Group, Inc.
A

Right.

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

...expectations for a large amount of growth there. Which funds do you anticipate are going to be the biggest contributors to those performance fees? And given the pace of the recovery here, is it possible that you can hit those numbers sooner?

Kewsong Lee
Chief Executive Officer & Director, The Carlyle Group, Inc.
A

Yeah. I think it's very possible. I think there's definitely upside to the numbers that we gave in terms of quantum, but also when we get to these types of numbers. When you look at carry, it's going to come mostly from private equity. And within our Global Private Equity, I would say it's going to come mostly from US buyout, Asia buyout, Europe buyout, US real estate. Those are the main drivers of carry income.

And then, we do have some [indiscernible] (00:20:15) in credit fund, which has got I think close to $100 billion of accrued carry in it, et cetera. But it's pretty well diversified across our platform. But the private – the Global Private Equity strategies are the ones that are going to be the real drivers of that carry.

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

Okay. Expanding your capital markets business is another focus of yours. You've outlined that at your Investor Day. Can you just elaborate a bit more on the strategy there?

Kewsong Lee
Chief Executive Officer & Director, The Carlyle Group, Inc.
A

Sure.

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

And what's the biggest contributor would you say in terms of the expectation for – I think it's a 3x increase in transaction revenues that you're expecting – and is there any sort of aspirations for third party in here as well?

Kewsong Lee
Chief Executive Officer & Director, The Carlyle Group, Inc.
A

Yeah. The aspiration is there.

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

Okay.

Kewsong Lee
Chief Executive Officer & Director, The Carlyle Group, Inc.

A

We're not doing it in full force yet. We're focusing on, what I would say, the building blocks and the easy stuff, which is the existing deal flow in our portfolio companies. I'm really happy with the progress we've made there, integrated a capital markets team. It has always existed for the past, well, I don't know, decade, but we never really put them all together to say, let's figure out a way to partner and help our deal teams and help these portfolio companies and earn a fee as we do that.

And if you think about it, they're so well positioned to be able to help these portfolio companies because they're working side by side with our deal teams. And so, the companies actually want their value-added services. And so, it first starts with just how do we earn fees off of our existing flow, off of our existing portfolio companies, and then at some in time that will obviously migrate to incorporating third party.

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

Q

And when you think about the targets you've had laid out for transactions on the capital markets side, does that embed any sort of third party in there?

Kewsong Lee
Chief Executive Officer & Director, The Carlyle Group, Inc.

A

Yeah. Whether it does or not, let me answer the question this way. The targets that we laid out at our Investor Day, I would be shocked if we don't hit those targets within the first half of our strategic plan, because the progress has been so tangible and so strong right out of the box. Now, it's going to be correlated to deal activity, deal flow, right? So, to the extent M&A volume stops, to the extent we have a slowdown, yes, it's going to affect our ability to earn fees in capital markets. But assuming there aren't any big issues or changes, I expect continued steady progress there, which is doing better than I would've thought.

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

Q

Okay. Maybe shifting gears over to your credit business...

Kewsong Lee
Chief Executive Officer & Director, The Carlyle Group, Inc.

A

Sure.

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

Q

...another very big area of focus at Carlyle. Can you just talk about what's left to build out at this point relative to where you'd like the platform to be? And as you think about your $80 billion AUM target, which I think is for 2024, which strategies are going to be the largest contributors there?

Kewsong Lee
Chief Executive Officer & Director, The Carlyle Group, Inc.

A

Okay. So, there's always work to do. But if we take a – let's go back a bit. About five years ago, this credit platform was very different. It was in hedge funds, a bunch of isolated, more boutique type of strategies. And it was earning maybe $10 million, maybe $15 million of FRE, maybe. And there were a lot of issues with it.

Come five years forward, it's a balanced platform, it's got liquid, illiquid and hard asset strategies. We've got about $56 billion of AUM, generating call it $100 million of FRE. And we're looking to double that over the next handful of years, as we laid out at our Investor Day. So, we feel really good about the platform and what we've built and how we've transformed it. And with the patience of all of our shareholders, I think it's paying off because you can clearly see the growth in FRE and we think the momentum will take it even further.

What's going to drive continued growth, we're a dominant player in the CLO business. So, we're top 3. And you're seeing a ton of reissuance, reset and new activity in CLO business right now, as you know. And so, that's very strong. Second, in our illiquid business, particularly in credit opportunities, we've made huge strides. And like I mentioned earlier, in just the past three, four years, we've raised already over $5 billion from zero. And it's a strategy that's performing exceptionally well. I think that can continue.

We've launched the infrastructure credit strategy, which to-date I think is closed on – close to a $1.5 billion, already deployed well, it's performing well. And I think in light of where the world is, where rates are, and the shifts that I see in traditional fixed income investors as they look for ways to find return in illiquidity, this strategy is going to be very appealing. And so, I see continued growth there. Now, in terms of – and by the way, we've done things through acquisitions along the way, [ph] you witnessed (00:25:25) Carlyle Aviation. And so, to the extent there's an interesting acquisition to add on to our platform, we'll carefully think about that.

In terms of what's left to do, we recently announced that we are going to move into real estate credit. Again, we're going to do it thoughtfully. And we're going ask for patience, because we're not going to rush into this. And we're going to build it out the right way. But it's clearly a big scalable strategy and it fits in really well to our platform approach.

And I really want to emphasize, when we sell and propose private credit solutions to our LPs, it is a solutions-oriented platform-based approach. And we're playing the long game here. And I fully expect that with the right patience, with the right hard work, these are strategies that will continue to propel our growth.

And of course, Mike, you know this, private credit is just growing faster and it's much smaller than private equity. But I could easily see allocations from the broader LP community continuing to flow into private credit just because of their need to find every little bit of return that they can in their portfolios.

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

Q

Now, as you're building this out, to what extent could M&A be a part of the growth profile here? I mean, it's already has been to some degree with the aviation platform. But as you look out, is there any appetite there?

Kewsong Lee
Chief Executive Officer & Director, The Carlyle Group, Inc.

A

Yeah. Look, we did in aviation. We clearly made several years ago an important acquisition in Fortitude, our insurance platform. We are very open to using our capital to acquire externally, but for the right reasons. We like to buy permanent capital. We like to buy recurring FRE businesses. We want to buy things that are big and can be even bigger and easily scalable. So, that lends you to think about – that pushes you to think about if we're going to use acquisitions to think about it in credit or in real estate and not private equity. But it's expensive now and so we have to be very thoughtful because the last thing I would say is we're not going to do anything that is dilutive. I want to do things that are going to increase the drivers that can move the needle for us of earnings, particularly FRE, but it's got to be done in an accretive way, a strategic way, whereby you can see a real path for our shareholders.

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

Q

You mentioned Fortitude, that acquisition bring you into the reinsurance business. Maybe you could talk a little bit about the strategy there, why it makes sense for Carlyle and how you think about the longer-term opportunities...?

Kewsong Lee
Chief Executive Officer & Director, The Carlyle Group, Inc.

A

Yeah. So, Fortitude has about $40 billion of AUM. From Carlyle's perspective, it's performing great; 15% ROE, we've rotated about $5 billion of Fortitude's assets into Carlyle's strategies. That's on schedule, maybe even ahead of schedule. And I actually think there's even more upside there in terms of where we eventually get to.

And Fortitude now has a pipeline where they're looking at doing more reinsurance transactions, more acquisitions. And as Fortitude grows, the asset base that ought to be managed by Carlyle will just grow as it rotates assets over to us. So, if Fortitude grows, Carlyle will grow. And that's the whole notion of how we're doing it.

We're doing it in a very deliberate, thoughtful way. We're doing it differently than others. Our approach I think is more B2B. It's more diversified in terms of risk. And we're focused on legacy liabilities and we're not needing to generate or originate new policy. I think it's also an approach, which is regulatorily more friendly in terms of how we've designed it.

And so, I'm very bullish on where the prospects are for not only Fortitude, but other insurance-related solutions as it relates to our growth. Because taking a step back, this is an industry with trillions of dollars of liabilities that if structured in the right way and managed in the right way is an enormous opportunity for our industry.

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

Q

And how much capacity would you say Fortitude has today to do deals? And are there any deals...

Kewsong Lee
Chief Executive Officer & Director, The Carlyle Group, Inc.

A

Sure.

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

Q

...built into your FRE targets that...

Kewsong Lee
Chief Executive Officer & Director, The Carlyle Group, Inc.

A

Sure.

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

Q

... [indiscernible] (00:30:11) you spoke about?

Kewsong Lee
Chief Executive Officer & Director, The Carlyle Group, Inc.

A

Zero deals built into our FRE targets. So, all of our FRE targets in our strategic plan that we outlined does not take into account any of these external growth initiatives that I've mentioned. And in terms of Fortitude's excess capital, I don't know the exact number, but it's $1 billion, $1.5 billion, something like that, of excess capital. And so, it is more than appropriately reserved and has capacity to grow.

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

Q

Great. Maybe shifting gears a bit more a higher level. It's always interesting hearing Carlyle's perspectives given the portfolio of companies the vast number you have around the world. I think it's over 200 or so, I think with particularly a large number in Asia as well...

Kewsong Lee
Chief Executive Officer & Director, The Carlyle Group, Inc.

A

Close to 300.

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

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Okay. 300 now, a lot of deployment it sounds like. But given that that level of visibility that you have around the globe and particularly in Asia, through that lens, what are you seeing in terms of the global economic recovery pace here? How are things recovering and what's your take on the macro outlook?

Kewsong Lee
Chief Executive Officer & Director, The Carlyle Group, Inc.

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Okay. Look, there's clearly a recovery going on, a bounce back going on. America, the way we see it, it could be close to 9%. Europe's not far behind, a little bit later in terms of recovery stage, but closer to 6%. And obviously, China, Asia came out of this first, and they're growing at a healthy 5%, 6%. I make the comment that it is not yet a synchronous global recovery. Different regions are growing and coming out in different ways and different rates. And so, there's actually upside there to the extent that with vaccine and with continued progression, the recoveries that you start to see more of a synchronous type of recovery.

Now, obviously, going against that, cross cutting that are some of the geopolitical issues as well as now the specter of inflation. I know that's a question you're going to ask, so let me just answer it. Let me tell you what we're seeing versus what we believe. We do see price pressure in certain areas and certain parts of the supply chain, certain commodities, certain components, primarily related to consumer durables. But, we don't believe that there's going to be systematic uptick in inflation more longer term.

The way I think about it, stepping back just a year ago, we got hit by this thing that no one ever could have imagined called COVID. And it was a huge black swan event. And you're now in a place where the fed is accommodative. There's massive government stimulus. You're seeing a huge balance because of vaccine progress. And you're seeing the effects of technology creating opportunity. And so, to make conclusions off of longer term things like inflation, off of just what you're seeing at this moment in time, I think it's dangerous.

And so, we do see price pressure, but we're not yet of the view that this is going to translate into really high or stubborn rates of inflation. So, we think these need to settle out a little bit before we can really come to a proper discussion about what is happening. If anything, I think some of the trends we're seeing continue to be more disinflationary than inflationary that you'll see continue once you hit some type of equilibrium.

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

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If – I know there's a big debate out there in the marketplace around that. And let's say for argument's sake, we do enter in an environment where there is more sustained inflation, higher levels of interest rates, the fed hikes, and we're in that for a longer period of time, can you talk about how Carlyle's portfolio would sort of react through that and how that impacts your outlook for fundraising and growth in the asset class?

Kewsong Lee
Chief Executive Officer & Director, The Carlyle Group, Inc.

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Sure. So, our portfolio – we tend to pick companies that have business models that we think can push through these types of issues and risks. So, I'd start with that. And so, I can't tell you what the impact will be with respect to valuation multiples and what happens when markets correct. I can tell you these are scenarios and these are what ifs that we do run and what if this happens. But, in general, when you're backing a growth company that is growing 20%, 30% quarter-over-quarter because it's got a better business model, that's not going to really be held back if there's "inflation" because it's something different. It's something that's much more disruptive. And there are moats around these businesses that we try to buy. So, on a fundamental basis, I think our portfolio and the way we construct our portfolios are set up so that as best as we can, we're managing for that risk.

In terms of valuation multiples and how those companies are, look, it's not going to be a fun day in the markets when – if what you say happens happens. On the other hand, we're long-term investors, we back these companies and we're making money over a five, six, seven-year timeframe. So, are there temporary setbacks in an interim period of time when unrealized marks could go down? Sure. But over time, if these companies grow in value, like we think they ought to do, we're confident in our ability to eventually create that value. Right? So, over the long term, with that type of perspective, with all the resources we have, with the way we diversify our portfolios and construct these portfolios, yeah, it's not going to be a fun day when there are corrections, no doubt there will be, but longer term, I think we're okay.

Now, the other thing I would say is when there is volatility, when there is disruption, we've strategies that take advantage of it, credit opportunities or distressed businesses, we'll find opportunities to deploy. And so, last year during April, May, that's when some of our credit strategies really were able to take off or reposition their portfolios and trade in and out particularly in credit. And so, there's also opportunity that gets created when that type of dislocation happens.

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

I'm afraid we're going to have to leave it there. Thank you so much, Kew, for joining us today.

Kewsong Lee
Chief Executive Officer & Director, The Carlyle Group, Inc.

Mike, this is a great discussion. Thanks for having me.

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

Thank you.