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APO - Q1 2018 Apollo Global Management LLC Earnings Call

EVENT DATE/TIME: MAY 03, 2018 / 2:00PM GMT

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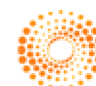

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CORPORATE PARTICIPANTS

Gary M. Stein *Apollo Global Management, LLC - Head of Corporate Communications*

Gary Parr

Joshua J. Harris *Apollo Global Management, LLC - Co-Founder, Senior MD & Director*

Martin Bernard Kelly *Apollo Global Management, LLC - CFO*

Scott M. Kleinman *Apollo Global Management, LLC - Co-President & Lead Partner of Private Equity*

CONFERENCE CALL PARTICIPANTS

Alexander Blostein *Goldman Sachs Group Inc., Research Division - Lead Capital Markets Analyst*

Allison Taylor Rudary

Brent Dilts

Brian Bertram Bedell *Deutsche Bank AG, Research Division - Director in Equity Research*

Brian Wu

Christopher Meo Harris *Wells Fargo Securities, LLC, Research Division - Director and Senior Equity Research Analyst*

Devin Patrick Ryan *JMP Securities LLC, Research Division - MD and Senior Research Analyst*

Gerald Edward O'Hara *Jefferies LLC, Research Division - Equity Analyst*

Glenn Paul Schorr *Evercore ISI, Research Division - Senior MD, Senior Research Analyst & Fundamental Research Analyst*

Michael J. Cyprys *Morgan Stanley, Research Division - Executive Director and Senior Research Analyst*

Michael Roger Carrier *BofA Merrill Lynch, Research Division - Director*

Patrick Davitt

PRESENTATION

Operator

Good morning, and welcome to Apollo Global Management's First Quarter 2018 Earnings Conference Call. (Operator Instructions) This conference call is being recorded. I would now like to turn the call over to Gary Stein, Head of Corporate Communications.

Gary M. Stein - *Apollo Global Management, LLC - Head of Corporate Communications*

Great. Thanks, operator. Welcome to our First Quarter 2018 Earnings Call, and thanks for joining us. As usual, joining me this morning are Josh Harris, Co-Founder and Senior Managing Director; and Martin Kelly, our Chief Financial Officer. In addition, I like to introduce a few other members of our team that are here in the room, including our Co-Presidents, Jim Zelter and Scott Kleinman, as well as Gary, our Senior Managing Director. Jim, Scott and Gary will be available to provide insight during the Q&A portion of today's call.

As a reminder, this call may include forward-looking statements and projections, which do not guarantee future events or performance. Please refer to our most recent SEC filings for risk factors related to these statements.

We'll be discussing certain non-GAAP measures on this call which management believes are relevant in assessing the financial performance of the business. These non-GAAP measures are reconciled to GAAP figures in our earnings presentation, which is available on the Apollo website. Also, note that nothing on this call constitutes an offer to sell or a solicitation of an offer to purchase an interest in any Apollo fund.

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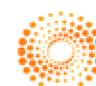

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Earlier this morning, we reported distributable earnings to common and equivalent holders of $0.46 per share, which drove a cash distribution of $0.38 per share for the first quarter. This quarter's distributable earnings were primarily driven by fee-related earnings, or FRE, of $0.32 per share.

Lastly, we reported an economic net loss of $0.30 per share for the first quarter of 2018, principally driven by unrealized mark-to-market depreciation within our private equity business.

Lastly, you may have noticed the earnings presentation we issued this morning has a new look and feel. This is part of a broader brand refresh recently launched by Apollo featuring a new visual identity, including a streamlined logo and a re-launch of our corporate website. We believe this new approach reinforces our strong brand equity and position as a leading investment management franchise.

With that, I like to turn the call over to Josh Harris.

Joshua J. Harris - *Apollo Global Management, LLC - Co-Founder, Senior MD & Director*

Thanks, Gary, and thanks all of you for joining us this morning. As we reflect on the momentum of our business, we wanted to share our perspectives on a few important multiyear trends, some of which were masked in the first quarter results, principally due to lower transaction fees and volatility in marks.

First, we continued to drive strong growth in fee generating assets under management, which is being fueled by strategic capital initiatives and traditional fund raising. Second, we believe the growth trend in fee generating AUM is underpinning strong growth in management fee revenues and scalability of our business model is driving expanding margins and fee-related earnings. These metrics have been on a positive trajectory for several years and we believe this will continue. And finally, we believe we continue to build long-term value in the portfolios we manage and we will opportunistically monetize investments as appropriate.

Now, I like to cover each of these topics in more detail. At the end of the first quarter, our fee generating assets under management sit at $182 billion, capping a 7 year run of 21% compound annual growth since our IPO. We believe this result is powerful evidence of Apollo's model at work where we are pursuing strategic capital initiatives and driving growth, while also raising larger opportunistic funds by continuing to deliver excellent investment performance to the investors in our funds.

Over the last 12 months, our strategic capital initiatives and organic fund raising activity have collectively generated $30 billion of fee generating net inflows across the platform, and we have conviction that strong growth is sustainable since there are several known catalysts already in view and others are on the horizon.

This year transactions that have already been announced by Athene and Athora are expected to generate at least $25 billion of future inflows. Both companies are continuing to execute their strategies of pursuing accretive acquisitions to grow their businesses, which has the added benefit of growing Apollo's business since we are their strategic asset management partners.

Looking forward, Athene's balance sheet will approach the $100 billion mark following the closing of the announced Voya transaction and Athora's balance sheet will be appropriately $15 billion following recently announced deal activity that will expand their European footprint to include Belgium in addition to Germany and Ireland. These transactions are expected to close later this year subject to regulatory approvals.

In addition to Athene and Athora, we continue to explore opportunities to establish new strategic capital initiatives, several of which are a direct result of our deep expertise in insurance, where we are broadening our dialogs across the sector.

In terms of traditional fund raising activities, we have numerous initiatives in the market today and others are expected to launch in the coming month. As we mentioned on the prior call, we have launched a new strategy called Hybrid Value, which will more formally integrate the expertise of our private equity and illiquid credit investment teams by focusing on capital solutions, structured equity and noncontrolled stressed and distressed investments. The strategy will target net returns in the low to mid-teens with downside protection, which we believe provides a highly

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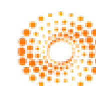

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differentiated solution to investors' portfolios. The current size for the inaugural vintage of this strategy is $3 billion -- the current target size, and we expect a first close during the second quarter.

Next, our natural resources franchise is continuing to perform well, with the ANRP II experiencing very strong returns to-date. Since the $3.5 billion fund is currently 75% committed or invested, we expect to launch fund raising for a successive fund vintage shortly and would anticipate first closing around year end.

We are also seeing heightened interest for customized managed accounts across our credit business as well as the broader platform. These dialogs are with a mix of new investors as well as with current investors that are seeking to expand their existing managed accounts. During the quarter, we took in mandates totaling $1.4 billion and the pipeline of dialogs is quite active. We anticipate that a few of these conversations will likely turn into mandates during 2018.

Lastly, one of our newer innovative credit products worth highlighting is called Apollo Capital Efficient, or ACE, which has been designed to solve the specific yield requirements of European insurers. We believe ACE serves as a great example of how we are leveraging our deep expertise in credit and insurance to create compelling investment solutions for European insurance companies.

Given the overall momentum in these strategic capital initiatives and our various fund raising efforts across the Apollo platform, we believe we are well positioned to continue to grow our management fee revenues and fee-related earnings. As you know, we believe FRE is one of our most important financial metrics since it is the foundational component of our quarterly and annual cash distribution and is largely based on recurring management fees generated from long-dated and permanent assets we manage.

Management fees have comprised appropriately 90% of our fee-related revenues historically and have been growing at a compound annual rate of 8% over the last 5 years. This growth in management fees has been augmented by an ongoing focus on efficiency, cost discipline and operating leverage, which has driven margin expansion across the platform and led to a 14% compound annual growth in fee-related earnings over the same timeframe.

We believe there's a high degree of visibility supporting a continuation of these trends that will lead to a sustainably higher level of FRE as we progress to 2018 and beyond. This visibility is being driven by recent impending catalysts, including the commencement of Fund IX and the aforementioned Voya transaction. Collectively, the net addition of more than $35 billion of fee generating AUM from these items alone will add approximately $270 million of net annualized management fee revenues. We believe additional upside will be provided over time from other growth opportunities across the platform.

My comments this morning have largely covered the growth of our fee generating asset and the positive impact of this growth -- that this growth has on our fee-related revenues, margins and earnings. However, it's also important to emphasize the long-term value we believe our investment teams are creating in the funds we manage.

In private equity, for example, from 2015 to 2017 the funds we managed deployed nearly $20 billion largely from Fund VII. The fund is off to a great start, and despite the decline in marks in the first quarter, Fund VIII has appreciated 25% over the past 12 months.

It's worth noting that this is still a relatively young fund with an average life of an investment at just over 2 years versus our historical average hold period of approximately 4 years. As this fund matures, we believe it is building value in its portfolio that we expect will be monetized over time and deliver cash distribution.

Our long run track record in traditional private equity is strong, with 39% gross and 25% net IRR since inception. We have a value oriented and contrarian investment philosophy that dictates we are determined buyers and opportunistic sellers. Because of our historic ability to drive strong returns over a long period of time through various economic cycles, we believe Fund VII will ultimately follow the same pattern of differentiated performance.

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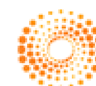

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Finally, we continue to analyze the merits and the market valuation of a C corp conversion. As we discussed on our last call, there is a tax cost involved as our current structure is tax efficient. It's worth noting that each alternative asset manager has a different mix of earnings and strategy, so the analysis around conversion varies by company. As these announcements by our peers are absorbed by the market, it's possible that the positive attributes of converting to a C corp will materialize in the form of greater shareholder value such as an expansion in valuation multiples and broader investment ownership -- or investor ownership.

One of the items we are continuing to monitor very closely is the sustainability of any value creation since converting to a C corp is essentially a one-time decision and permanent decision. We do not have a specific time table for making a determination, but we remain committed to maximizing long-term shareholder value. As we noted before, we welcome your feedback on this important topic.

With that, I'll now turn it over to Martin for some additional comments.

Martin Bernard Kelly - *Apollo Global Management, LLC - CFO*

Thanks, Josh, and good morning again, everyone. Starting with our cash distribution, the $0.38 we declared today was driven by the relative cash flow stability of our fee-related earnings and was complemented by realized performance fees principally generated from Fund VIII monetization activity.

Focusing on the economic financial performance of the first quarter, we generated fee-related earnings of $133 million or $0.32 per share, which was offset by 2 factors including the reversal of net performance fees and associated investment losses of $136 million or $0.33 per share primarily due to unrealized mark-to-market depreciation in Fund VIII. And Athene-related depreciation during the quarter drove $74 million or $0.18 per share of unrealized losses between our balance sheet investment and carry arrangements. The net result of these items drove a pre-tax economic loss of $105 million or $0.26 per share or an economic net loss of $121 million or $0.30 per share post-tax.

Starting with FRE, the first quarter result was roughly flat year-over-year, but down quarter-over-quarter primarily due to the moderation of transaction and advisory fees. Transaction fees typically correlate with the level of capital deployment activity in a given period, and while the funds we manage deploy capital into new investments during the quarter, these particular investments were not large enough to warrant the need for equity co-investment or meaningful financial syndication, activities which usually generate fees.

Management fees were also sequentially lowered due to the cessation of management fees from Fund VI as well as the absence of some catch-up fees in credit. We believe this decrease in management fees will be short-lived as the quarterly run rate is expected to increase by approximately $50 million to $55 million from Fund IX alone, with modest incremental expense beginning in the second quarter.

For added perspective, on Page 7 of our earnings presentation you'll see that we've laid out the trajectory of our historical fee-related earnings growth, including a bridge to our first quarter results, and an illustration of the expected impacts around this near-term system.

Next, I like to provide some context behind the quarter's investment performance, which was principally responsible for the reversal of performance fees and associated equity method or GP investment losses. While the credit and real assets businesses produced positive returns in the first quarter of plus 1% to 2%, the private equity portfolio was down 3% overall. The blended private equity mark for the quarter represents significantly diverging outcomes in the portfolio as publicly traded investments were down 16% while private investments were up 4% percent.

The primary source of volatility on the public side was ADT, which had its initial public offering in January and subsequently traded down during the quarter. Excluding the mark on ADT, the blended return on the portfolio would have been approximately 500 basis points higher at plus 2%. We believe the quarter's performance is quite idiosyncratic given the outsized 38% quarter-over-quarter swing in ADT's valuation.

Despite the decline, Fund VIII's inception to-date gross and net IRRs of 26% and 18% respectively continue to be strong and the team is optimistic regarding the long-term value proposition offered by ADT and the other 30-plus investments in the fund.

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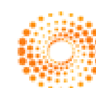

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As it relates to the quarterly mark on Athene, the fair value decreased by approximately 8% quarter-over-quarter due to the lower trading price of its stock, partially offset by a modest reduction in the liquidity discount on the shares held on our balance sheet.

As I mentioned, the net impact of the decline in value on our economic earnings was an unrealized loss of $0.18 per share for the quarter. Despite the depreciation in the quarter, we believe strategic investments like Athene serves to make our balance sheet stronger. During the quarter, we received additional shares of Athene to satisfy a performance fee receivable from AAA. We had the option to monetize these shares, but we elected to increase our ownership position in the company as we believe it is a compelling investment and to further align ourselves with a strategic partner. As a result, we now hold 19.2 million shares of Athene in aggregate, which translate into nearly a 10% economic stake.

To provide further context on the topics of unrealized marks and a growing Athene investment, we included Page 16 in today's earnings presentation. This page illustrates the recent growth we have experienced in our net performance fee receivable balance resulting from strong investment performance in 2017 and the components of the decline in the first quarter which included the additional investment in Athene.

Looking a bit more broadly at our balance sheet, we now hold $1.2 billion of cash and treasuries and an additional $500 million undrawn revolver against $1.4 billion of debt, providing us with a conservatively capitalized financial position with ample liquidity.

Our cash balance reflects the issuance of our second perpetual preferred stock security during the quarter. The transaction was well received with gross proceeds of $300 million at [6.38%]. We were pleased by the outcome as it allowed us to diversify our capital structure even further by adding additional permanent financing at an attractive rate.

We this enhanced flexibility, we continue to pursue strategic capital initiatives, evaluate potential M&A transactions, fund other growth initiatives and immunize share dilution of employee-related compensation.

Our debt structure now includes 30-year senior notes which raised gross proceeds of an additional $300 million at 5% during the quarter, which was used to refinance outstanding term loans. We are again pleased with the outcome of the transaction as it enabled us to access new institutional fixed term income investors and diversify our maturity profile.

Approximately 2 years ago, we launched a share repurchase program that authorized up to $250 million of aggregate repurchases. Through the end of March, we have cumulatively spent $150 million of capital on this initiative by repurchasing roughly 5 million shares to immunize employee-related share dilution as well as an additional 2 million shares in open market transactions.

We intend to continue the net share settlement program to mitigate dilution resulting from employee stock plans.

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

QUESTIONS AND ANSWERS

Operator

(Operator Instructions) Our first question comes from the line of Glenn Schorr of Evercore.

Glenn Paul Schorr - *Evercore ISI, Research Division - Senior MD, Senior Research Analyst & Fundamental Research Analyst*

Wonder if you could just help us outline the fee structure for some of these new products, Hybrid Value, ACE and maybe the new assets taken on for the deals in both Athene and Athora?

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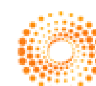

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Martin Bernard Kelly - *Apollo Global Management, LLC - CFO*

Sure. So we haven't been public with any of this. I would expect Hybrid Value to be sort of in line with traditional drawdown PE funds. And on Athora, we similarly don't plan to make that fee rate public yet. I would say the platform is formative and the fee rates are similar in context to Athene Asset Management, but also different in the sense that there's a base fee rate which we expect to be lower, driven by the fact that these platforms need to have treasury securities as a duration. But we'll have the opportunity to own sub-investment or sub-advisory fees over time, which we expect will be meaningfully accretive over time.

Operator

Our next question comes from the line of Michael Carrier of Bank of America.

Michael Roger Carrier - *BofA Merrill Lynch, Research Division - Director*

Josh, maybe one for you just on Fund VII. I think whenever any of the big funds have a sizable investment it tends to be the spotlight with ADT. So I just wanted to get your sense. When you look at Fund VII across the 30 portfolio companies or so, what's going on in terms of like the revenue, the EBITDA trends? The performance overall still looks very good when we look at it relative to like history and it's still, like you mentioned, a young fund. So just trying to gauge sort of like the one investment that's kind of in the spotlight versus everything else that's going on and what that means for the future, like kind of realization potential of the fund.

Joshua J. Harris - *Apollo Global Management, LLC - Co-Founder, Senior MD & Director*

Yes. So I think first of all, we just had our big portfolio review. We do it once or twice a year, a couple of times a year. And so we went to every company. And pretty much the fund is in great shape as evidenced by the 25% unrealized return that we reflected in the comments. And I'd say, it's pretty broad-based across the portfolio. There are very few issues. And I would say that the revenues and EBITDA are growing in line with GDP, about plus low single digits. But as we reflected to you all, very consistent with our strategy of buying stuff at under 6x EBITDA when the market is paying over 10x EBITDA. And by the way, even with ADT, while we -- while the market has obviously kind of moved the stock of ADT kind of relative to its IPO, that's still a great investment for us and marked up, I want to say, 1.4x times or something, which you can read in our financial statement. So I think it's a good situation. And, look, at the end of the day, the ebb and the flow of market value when you have more than 50 companies across multiple portfolios certainly does create some quarterly volatility. But long run, we think that the fundamentals of ADT in that portfolio are quite good and we're actually quite positive. I would say that when we look at the multiple on that fund relative to fair value today, it's about 7.4. And when we started, it was 5.7. So we think we're building value in that portfolio. It's still like well south, well south of anything -- any of the S&P 500 or any of the kind of industry tops.

Michael Roger Carrier - *BofA Merrill Lynch, Research Division - Director*

Okay. Thanks a lot.

Joshua J. Harris - *Apollo Global Management, LLC - Co-Founder, Senior MD & Director*

Thanks.

Operator

Our next question comes from the line of Devin Ryan of JMP Securities.

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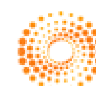

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Devin Patrick Ryan - *JMP Securities LLC, Research Division - MD and Senior Research Analyst*

Maybe just a follow-up on ADT. I know it's been a big win for Apollo here, but more recently just in the public markets it has been a tougher run. And so trying to think about -- I know every investment kind of has its unique characteristics, but this was a fast turnaround from being a public company into the private markets, back out to the public market. So I'm curious if there's any kind of lessons to be learned from that or does that change the trajectory for any other investments for Fund VII. I've seen some reports of some other investments that maybe were public not too long ago that have come back to the public markets. So I'm just curious about that.

Joshua J. Harris - *Apollo Global Management, LLC - Co-Founder, Senior MD & Director*

Look, I'll sort of illustrate it. And I have presented Scott Kleinman today -- wants to add on. I think that ADT, we've grown ADT. We've changed the trajectory of the earnings and the cost structure and the capital intensity of the business. And so we went public. And obviously, the public markets require more convincing. And I think sometimes you don't always get it right, exactly. You rely on underwriters and you use your best judgment. We believe in the long-term fundamental value of ADT. And certainly, we have other companies that we've taken out of the public markets and we're certainly going to do our best to -- when we exit to -- whether it's -- if it ends up being to the public markets. But certainly there are other exit alternatives. To do that at the right time after the appropriate seasoning and value creation -- which we think we did in ADT, but obviously the market hasn't fully -- doesn't fully agree with that or -- so I think that -- that's what I would say. I don't know if you have anything to add.

Scott M. Kleinman - *Apollo Global Management, LLC - Co-President & Lead Partner of Private Equity*

Yes. No, I would just echo Joshua's comments. We feel really good about ADT specifically. I don't think you can extrapolate from that the broader portfolio. We look at every company and think long and hard about the timing of exit and the right path for exit. And I don't think you want to take too much from the current trading performance. Ultimately, ADT's performance is quite strong and we would expect the market to eventually catch-up to that.

Joshua J. Harris - *Apollo Global Management, LLC - Co-Founder, Senior MD & Director*

And ADT was 2 years old when we took it public relative to our investment horizon. It wasn't -- had we -- it wasn't -- we weren't in any rush. So we're also happy to, if the market doesn't reflect, hold on.

Devin Patrick Ryan - *JMP Securities LLC, Research Division - MD and Senior Research Analyst*

Yes, got it. Thank you. Helpful, guys.

Joshua J. Harris - *Apollo Global Management, LLC - Co-Founder, Senior MD & Director*

Thanks, Devin.

Operator

Our next question comes from the line of Alex Blostein from Goldman Sachs.

Alexander Blostein - *Goldman Sachs Group Inc., Research Division - Lead Capital Markets Analyst*

Just a follow-up question around Voya and Athora. So heard you on the fees obviously, but I was wondering if you guys talk to the incremental FRE margins you expect to see from both of these transactions. And I guess broader, as you think about the opportunity set for Athene and Athora, how does that compare versus, I would say, a year ago as we're thinking about potentially more activity here on the forward?

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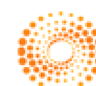

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Joshua J. Harris - *Apollo Global Management, LLC - Co-Founder, Senior MD & Director*

Yes. So I'll start the first one and then I'll pass to Gary Parr for the second part. Both of them are very, very high margin. We don't actually disclose the specific margins. But once you build the cost structure, you're adding revenues and you're not adding a lot of costs. So they are over time -- I mean, honestly, Athora is just beginning and so I don't want to overplay too much the effect on this year's earnings, but it will be marginally accretive and over time significantly -- when you're building the platform, clearly there's costs associated with it. In Athene's case, obviously the -- you've got a fully built out platform. Voya is going to add $19 billion of AUM and that's at 30 bps, which we've announced. And plus you've got whatever we can sub-advise, which today -- which was about 20% pre-Voya. And then you get the underlying economics of those funds. And then obviously as the assets of Voya -- of the variable annuities become fixed annuities, Athene also gets those. And then we manage the assets that Athene gets. And so that will be accretive over time and growing from Voya's point of view and from Athene's point of view. In terms of the more strategic assets of your transaction, I like to have Gary Parr, who is on the phone, answer that.

Gary Parr

Yes. At a high level, we continue to look for creative ways to expand our permanent capital. So Voya is a particularly good example where we saw a dilemma in the insurance industry and that is the old run off blocks of variable business. They shouldn't -- those blocks shouldn't be in a public company really. We think they should be in a private arena. So we also saw that they were attached to fixed annuities, which were attractive to Athene. So we bundled a transaction that was good for Voya, obviously good for Athene and good for Apollo. Now that we have the platform of a variable capability and venerable, once we close, which as we had said would be midyear -- when we have that capability, it just adds to the array of things we can look at and consider. And it is the case that there are other companies that have variable blocks that they need to address. There are some other aspects of just the life in annuity industry that are feeling -- continuing to feel margin pressure that plays to some of our advantages. So we'll continue to look for creative ways to do material transactions such as Voya.

Joshua J. Harris - *Apollo Global Management, LLC - Co-Founder, Senior MD & Director*

There's other types of insurance that we're looking at where we feel like similar strategies can be effective.

Alexander Blostein - *Goldman Sachs Group Inc., Research Division - Lead Capital Markets Analyst*

Great. Thank you.

Gary Parr

Thank you.

Operator

Our next question comes from the line of Bill Katz of Citi Group.

Brian Wu

This is Brian Wu in for Bill Katz. We notice the pace of dry powder deployment's growth quarter-over-quarter. Could you guys provide some details on what's driving that and maybe what the challenges or opportunities are for deployment in the current market backdrop?

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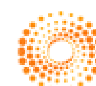

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Joshua J. Harris - *Apollo Global Management, LLC - Co-Founder, Senior MD & Director*

And so, Scott, why don't you -- it's really PE.

Scott M. Kleinman - *Apollo Global Management, LLC - Co-President & Lead Partner of Private Equity*

Yes. I would say PE deployment was a little bit slower in the first quarter, a little bit off our normal pacing. I don't see that having any longer term repercussions. We're looking at Q2 back more normal, on normal track. So...

Joshua J. Harris - *Apollo Global Management, LLC - Co-Founder, Senior MD & Director*

Yes. Look, at the end of the day, there's the ebb and the flow of the deployment cycle, of the realization cycle. Sometimes you have a stock where you believe in it, it doesn't perform in the stock market. And so the reality is there can be these quarterly fluctuations. But from a -- as Scott says, like our -- from a fundamental long-term point of view, we feel like we're going to be back on pace.

Brian Wu

Great. Thank you.

Scott M. Kleinman - *Apollo Global Management, LLC - Co-President & Lead Partner of Private Equity*

Thanks.

Operator

Our next question comes from the line of Michael Cyprys of Morgan Stanley.

Michael J. Cyprys - *Morgan Stanley, Research Division - Executive Director and Senior Research Analyst*

On C corp conversion, you mentioned something that -- you're thinking about maybe it's a way to enhance shareholder value. But just curious, are you thinking about any potential change to your capital management policy maybe as a way to enhance shareholder value, maybe paying a fixed distribution in line with FRE growth and using other cash generated for buybacks. What sort of the drawback is that sort of approach and just generally how are you thinking about any sort of tweaks or refinements to your capital management?

Joshua J. Harris - *Apollo Global Management, LLC - Co-Founder, Senior MD & Director*

Yes. I'd say that we have sort of paid out the bulk of our earnings and we continue to do that. What we said is that if we have -- we have a highly cash accretive business. There's not a lot of need for capital other than for GP stakes and acquisitions and investments. And certainly, we're sitting with an investment grade capital structure with $1 billion, $2 billion of cash. And selectively we're going to pursue investments in acquisitions as we've done in the past. If we found something that was compelling enough, we might. And we've always said that we look at the dividend as important and -- but if we needed to stop the dividend, we would look at the -- we do that if the ROI on an acquisition that required capital was in our opinion attractive enough to merit that. But given the cash accretiveness of our model and the amount of cash on our capital structure, we haven't had to do that. And so we don't see that happening in the future, but we reserve the right to talk about it, if it makes sense. And the reality is -- I'll just say one more thing. We don't think our -- I think we've said repeatedly and I'm not -- I don't mean to come across as gripeing about it, but we just think that the ROI of our own stocks and the dividend flow out of our own stock and the upside out of our own stock is incredible attractive investment, so we just haven't seen something that would warrant that. And then relative to buybacks, I think what we've said is that we don't want to shrink the flow, but we've done is -- what we're doing strategically is neutralizing the employee dilution with buybacks. And so

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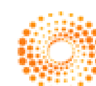

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we're going to keep on that path. Clearly, we reserve the right to change all of that, but that's kind of where we are. And I don't -- right now we don't see any reason to change it.

Michael J. Cyprys - *Morgan Stanley, Research Division - Executive Director and Senior Research Analyst*

Okay. Thanks.

Operator

Our next question comes from the line of Brent Dilts of UBS.

Brent Dilts

Thanks. Good morning, guys.

Joshua J. Harris - *Apollo Global Management, LLC - Co-Founder, Senior MD & Director*

Good morning.

Brent Dilts

On the topic of growth, so at the 2014 Investor Day you had said you didn't think (inaudible) would get much larger than where it was at the time. Today it's about 50% bigger. So could you talk about your outlook for growth in that segment over the next few years, just given where you are with Fund IX starting to turn on fees, but Fund VIII and ANRP II (inaudible) and like would this an update in harvesting here?

Joshua J. Harris - *Apollo Global Management, LLC - Co-Founder, Senior MD & Director*

Yes. What we said is -- obviously, we were sitting with an $18 billion fund, and even though we were performing well and had performed well, we didn't expect that we would raise the largest fund in history. And so we didn't want to set that kind of expectation and we said that -- so we exceeded expectation and we now sit with a $25 billion fund. We were able to deploy the $18 billion fund in 3-1/2 years, so that merited us taking down a $25 billion fund. And so we went forward. But we -- and I think during Investor Day, we also said that we didn't expect blistering growth, that we felt credit would be our growth engine and that was growing kind of high single digit or low double digit sort of organically. But that given the scale of private equity, we saw it being incremental growth. And we did talk about other products such as natural resources. And as I mentioned in my opening remarks, we've added Hybrid Value, which we think is in the middle of the capital structure and it's sort of a -- not as competitive and really plays to the strength of our integrated model between credit and private equity. And so we think we have a competitive advantage. And over time, we're going to add products where we think we can outperform the market in terms of returns. But it's not going to be -- it will be -- I think it will be low to mid single digit growth, not high single digit growth because of just the scale of what we're doing already.

Brent Dilts

Okay, great. Thanks, Josh.

Operator

Our next question comes from the line of Brian Bedell of Deutsche Bank.

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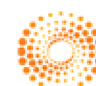

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Brian Bertram Bedell - *Deutsche Bank AG, Research Division - Director in Equity Research*

I appreciate the comments on the C corp conversion. Maybe just I'll add a little bit more there. Maybe if you can just talk about the complexity for you guys do this. Obviously, KKR came out with a little bit of a different situation. Every company is unique of course. But as you think about -- I think you said 15%, so 15% to 16% dilution on ENIs last quarter will be the proforma. And as you think about what kind of valuation improvement you would need -- you would think you would need to see sustained to do this. And then also just on KKR's simplified reporting structure, where they are limiting the ENI and focusing more on DE and changing the comp a little bit. Just your views on whether you think that makes -- that type of reporting structure makes sense for Apollo and the industry?

Martin Bernard Kelly - *Apollo Global Management, LLC - CFO*

Sure. So, Brian -- so I -- so what we said last quarter was looking at 2017 full year our reported 8% blended ENI tax rate would have been 5% under the new tax code or 23%. And so that's sort of the rough order of magnitude of the leakage at the company level. It obviously doesn't consider the shareholder level because that's a further derivation of that. I think it is a very complex topic. I think the complexity comes in: Do you convert all or part of the structure? Is the conversion a taxable transaction or a nontaxable transaction? And then ultimately to Josh's earlier comment, are we convinced that we get a sustainable uplift in the multiple over time? And so we continue to study it hard and spend time on it, but it's very complicated and a onetime decision. We would expect that the multiple uplift would -- on the [hauling stream] is a couple of [tons], but if you were to isolate that FRE, it's double that. So you need a meaningful uplift to justify it. That's why we continue to do a lot of work on it.

Joshua J. Harris - *Apollo Global Management, LLC - Co-Founder, Senior MD & Director*

Yes. Obviously, the math is relatively straightforward. If you've got 15% dilution or whatever, you'd have to think that on the overall multiple you get more than that. And the key on a sustainable basis over time. And so we just have to -- we're studying it. We're watching what others are doing. And I think others going first is helpful. We have to see what happens over time. In terms of the focus on DNI, that's a good focus, management company DNI, total DNI, cash flow. I mean, obviously from an earnings view, we are -- we do report earnings and we are committed to report earnings and we think it's a great reflection of our best view. But as you can see with this quarter in something like ADT obviously, when stock market might take a different view of something, that can affect your reported earnings. But it's unrealized. These are unrealized marks. And from our point of view, volatility in markets while they might create unrealized mark-to-market losses, generally that's been very, very positive for us over time because that's when we get to step-in with lots of our locked up capital and buy stuff. And so there's a -- so for us ultimately what we're really looking at is cash flow, DNI, predictable DNI out of the management company and then total DNI, which is very reflected by FRE. FRE is very, very close to cash flow out of the management company. And so we're going to try to continue to emphasize that more, but we're probably going to keep reporting everything because we want to be very transparent and allow people to look at whatever they want to look at.

Brian Bertram Bedell - *Deutsche Bank AG, Research Division - Director in Equity Research*

Right, right. Okay, great. That's helpful. Thank you.

Martin Bernard Kelly - *Apollo Global Management, LLC - CFO*

Okay. Thanks, Brian.

Operator

Our next question comes from the line of Gerry O'Hara of Jefferies.

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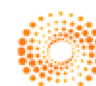

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Gerald Edward O'Hara - *Jefferies LLC, Research Division - Equity Analyst*

Perhaps one more on the permanent capital vehicles. You're now in the closing of the Aegon transaction here in Q2. So I thought maybe you can discuss what means of growth this provides for the European insurance platform. And I don't know if there's any ability to leverage this platform across multiple regions, but any kind of additional commentary there would be helpful.

Gary Parr

So a couple of thoughts. As Martin referred to earlier, we're building out the capabilities at Athora and building the platform to build -- to do multi countries. Specifically, Ireland gave us a reinsurance platform through Ireland that is helpful for capital management and efficiency, for example. There were some product capabilities embedded in that as well. There was some variable capability in fact or the equivalent of variable that's a European version. That's not a business line we want to keep in, but there were some technical abilities that will help us to do other transactions. So think of that as another building block for giving us expertise and capability along with now the Generali transaction giving us a base in Belgium, where we see Belgium as being just as we see Germany, having a number of opportunities. And it's particularly helpful to have your first base, have the platform from which you then consolidate.

Operator

Our next question comes the line of Chris Harris of Wells Fargo.

Christopher Meo Harris - *Wells Fargo Securities, LLC, Research Division - Director and Senior Equity Research Analyst*

So as you know, short-term interest rates are up a lot. Wondering if you guys could help us understand your exposure to that, like do underlying portfolio companies have a lot of floating rate debt and are you guys seeing any stresses in the portfolio as a result of these moves in rates? It seems like no. But just if you can elaborate on that, that will be great.

Joshua J. Harris - *Apollo Global Management, LLC - Co-Founder, Senior MD & Director*

Yes, we're not. First of all, most of our credit portfolio is floating rate, nearly all of it. So when short-term rates go up, we actually just make more return from a PE point of view. We're generally hedged. And also the leverage in our PE portfolio is very, very reasonable. It's under 4x. And so short-term fluctuations in rates generally isn't moving the needle between the lower leverage and the hedging that we've done relative to our cash flow.

Operator

Our next question comes from the line of Patrick Davitt of Autonomous Research.

Patrick Davitt

A couple of questions on ACE. One, is this going to be the only product like it in the market; and two, what asset bucket will it fall in for the insurance companies with the idea of getting to an addressable market for this product?

Scott M. Kleinman - *Apollo Global Management, LLC - Co-President & Lead Partner of Private Equity*

Well, as Gary and others have said this morning, between Athene, which is US-focused, and Athora, European-focused, there's just a different regulatory regime in terms of constructing a fixed income and insurance dedicated portfolio. So for us, obviously we have a lot of experience in Athene in the US. It's more of an NAIC portfolio. It's largely investment grade. In Europe, there are different constraints under the regulatory regime

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under Solvency II that we just really extracted that knowledge and that experience. And in addition to using it for our own balance sheets, we're really making that intellectual capital now available to others. So it's really insight on portfolio construction. It's insight on various asset classes and the manner in which those will be treated. So for us, it's just really a logical expansion of our proprietary activities with Athene and Athora and logically expanding those to a very thoughtful and solid client business. So I think you'll see us constantly do more of that. And I think that we feel that we are the leading -- we have a leading edge and leading insight in that field.

Patrick Davitt

And it sounds like its -- is it more transactional than -- like a fee on AUM type situation?

Scott M. Kleinman - *Apollo Global Management, LLC - Co-President & Lead Partner of Private Equity*

Well, I just think it's a -- we have a variety of products in our credit platform. This will be an additional product that we roll out and have been rolling out. So it really is just a continued logical expansion of our product size.

Joshua J. Harris - *Apollo Global Management, LLC - Co-Founder, Senior MD & Director*

But it's not a permanent capital vehicle. In other words -- yes, I think you are on to the right structure. It's more of a -- this part of it -- I mean, obviously our [clients] would use this expertise, but relative to the products we are offering -- we are going to offer our clients. But generally they are going to be more managed accounts/possibly fund structures, not a permanent capital vehicle.

Scott M. Kleinman - *Apollo Global Management, LLC - Co-President & Lead Partner of Private Equity*

Yes, an evergreen product, but not a permanent capital per se.

Operator

Our next question comes from the line of Allison Taylor Rudary of Oppenheimer.

Allison Taylor Rudary

You've answered most of my questions. I just wanted to dig in a little bit to the hybrid credit strategy. You mentioned that the economics might look more at the drawdown fund, but is this strategy a permanent capital vehicle, could it morph into that and can it co-invest alongside your private equity or real asset businesses?

Scott M. Kleinman - *Apollo Global Management, LLC - Co-President & Lead Partner of Private Equity*

Sure. Yes. Now, this really is a fund product, so it's not really a permanent capital type vehicle. And it will be a -- it has a distinct strategy that fits into the Apollo ecosystem of products. So it's not really a co-investment vehicle to private equity per se. It's targeting a specific set of risk and return in corporate and other entities. And so it will be a very distinct strategy.

Joshua J. Harris - *Apollo Global Management, LLC - Co-Founder, Senior MD & Director*

So less -- probably on average less risky, more structured than private equity and a bit lower return. But still a good return.

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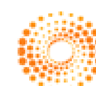

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Allison Taylor Rudary

Perfect. Thanks.

Operator

Our next question comes from the line of Michael Carrier of Bank of America.

Michael Roger Carrier - *BofA Merrill Lynch, Research Division - Director*

Just a quick one, Martin, on the follow-up. Just in terms of the incentive comp, I don't know if there was anything unusual this quarter and maybe it was just given the -- that may have been unrealized on the revenue side. But it just seemed a little unusual in terms of how we look at that.

Martin Bernard Kelly - *Apollo Global Management, LLC - CFO*

Yes, Mike, that's it. We had a realized profit share cost of -- on the gains that we took of mid 40s, 43% I think it was, 44%. And then on the unrealized losses, which exceeded the gains, we had a lower profit share cost, which is driven by Fund VIII. And Fund VIII we accrue -- if you recall, Fund VIII has a cash and a stock component to its profit share. We accrue the cash and the stock cost comes later. When you net the 2 together, it boils down to a negligible net number.

Michael Roger Carrier - *BofA Merrill Lynch, Research Division - Director*

Got it. All right, thanks.

Martin Bernard Kelly - *Apollo Global Management, LLC - CFO*

Yes.

Operator

Thank you. That concludes the Q&A portion of today's call. I will now return the floor to Gary Stein for any additional or closing remarks.

Gary M. Stein - *Apollo Global Management, LLC - Head of Corporate Communications*

Great. Thanks again for joining us today. As I noted earlier, if you have any follow-up questions, please feel free to circle back to Noah Gunn or myself. Iâ€™ll look forward to talking to you next quarter.

Operator

Thank you, ladies and gentlemen. This does conclude today's conference call. You may now disconnect.

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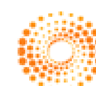

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