S&P Capital IQ

CONTENTS

Apollo Global Management, LLC NYSE:APO

FQ2 2016 Earnings Call Transcripts

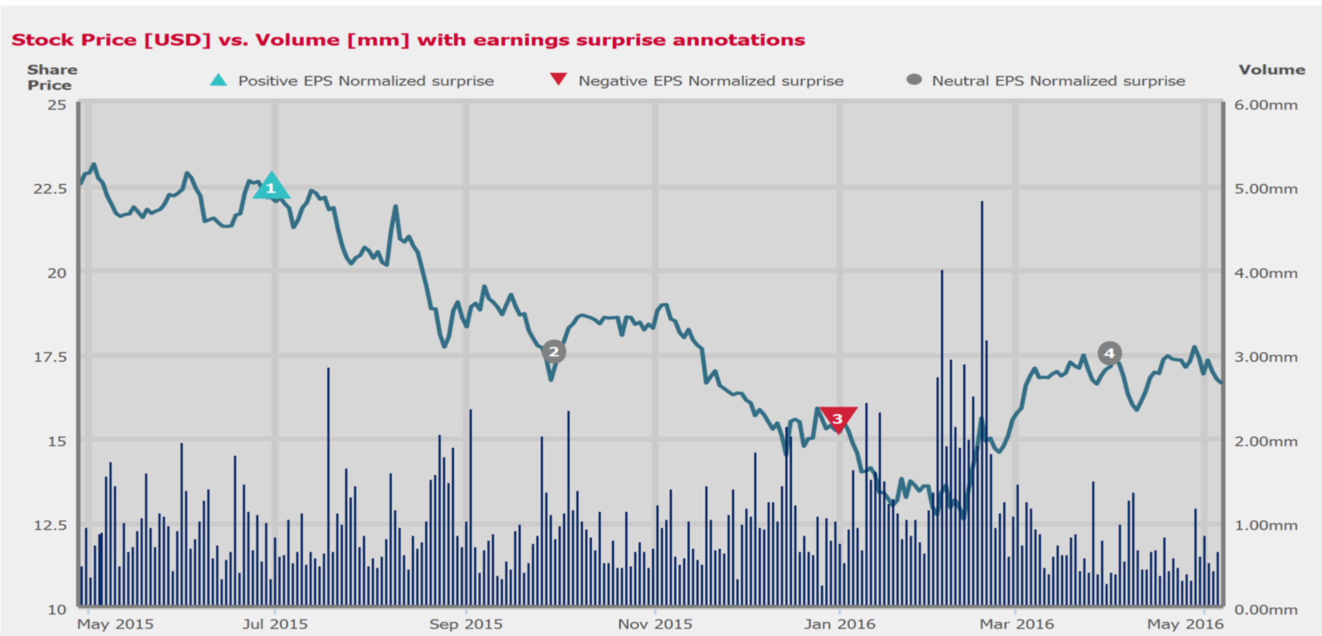
Wednesday, August 03, 2016 2:00 PM GMT

S&P Capital IQ Estimates

	-FQ2 2016-			-FQ3 2016-	-FY 2016-	-FY 2017-
	CONSENSUS	ACTUAL	SURPRISE	CONSENSUS	CONSENSUS	CONSENSUS
EPS Normalized	0.20	0.98	▲390.00	0.37	0.81	1.84
Revenue (mm)	307.00	660.45	▲115.13	367.20	1173.21	1634.39

Currency: USD

Consensus as of Aug-03-2016 1:35 PM GMT



- EPS NORMALIZED -

	CONSENSUS	ACTUAL	SURPRISE
FQ2 2015	0.35	0.38	▲8.57 %
FQ3 2015	(0.11)	0.26	NM
FQ4 2015	0.26	0.08	▼(69.23 %)
FQ1 2016	0.04	(0.18)	NM

Call Participants

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Presentation

Operator

Good morning, and welcome to Apollo Global Management 2016 Second Quarter Earnings Conference Call. [Operator Instructions] I would now like to turn the call over to Mr. Gary Stein, Head of Corporate Communications.

Gary M. Stein
Head of Corporate Communications

Great. Thanks, operator. Welcome, everyone. Joining me today from Apollo are Leon Black, Chairman and Chief Executive Officer; Josh Harris, Co-Founder and Senior Managing Director; and Martin Kelly, Chief Financial Officer.

I'd like to remind you that today's conference 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 to assess the financial performance of the business, and are reconciled to GAAP figures in our second quarter earnings presentation.

earlier this morning, we reported GAAP net income of $0.91 per share for the second quarter ended June 30, 2016. Economic net income totaled $0.98 per share during the quarter, and distributable earnings to common and equivalent holders totaled $0.40 per share, $0.37 of which was declared for the quarter's distribution and will be payable to shareholders later this month.

If you have any questions about any information provided within the earnings presentation or on this call, please feel free to follow up with me or Noah Gunn.

With that, I'd like to turn call over to Leon Black, Chairman and Chief Executive Officer of Apollo Global Management.

Leon D. Black
Founding Partner, Chairman & CEO

Thanks, Gary, and good morning, everyone. I'm pleased that we have the chance to speak with all of you today. This call provides us with an opportunity to highlight what we've been able to achieved in Apollo through the first half of 2016, punctuated by our strong second quarter results which delivered meaningful asset growth, significant capital deployment and our most profitable quarter in nearly 3 years, fueled by solid performance across all our businesses.

During this call, I'll first provide some high-level commentary regarding Apollo's investment activities, and then Josh will provide you with details regarding our asset growth and investment performance. Martin will conclude our prepared remarks with some brief comments regarding Apollo's financials before we take your questions.

Since founding Apollo 26 years ago, we have gone through 4 economic cycles, and we have demonstrated time and again that some of the best investments or funds have ever made have been when markets appear to be at their worst or most volatile. It is during these periods of dislocation when others are often sidelined that we can leverage our integrated platform, deep industry knowledge and capital markets expertise, coupled with the long-dated nature of our funds capital to make attractive investments that we believe will deliver meaningful returns to our investors. We tend to thrive during these periods of volatility and uncertainty and during the second quarter, which transpired against a highly unpredictable market backdrop, we were extremely active on the investment front and we also generated strong financial results. During the quarter, the funds we managed together with new co-investment partnerships, deployed or committed more than $7.5 billion in aggregate investments across Apollo's platform. The vast majority of this activity was driven by our private equity business as Fund VIII has been experiencing a heightened investment pace. While I'm pleased to note that this quarter marks our record for private equity deployment at Apollo, I'm even more pleased that we've continued to maintain our value-oriented discipline, despite the robust pace of activity, which is one of the fundamental tenets of our investment style. I would like to point out that a number of the deals we've recently announced or completed have been in the works for many months or even years in certain cases and is somewhat of a coincidence that all of these deals have gotten to the finish line at around the same time. At a point when equity market values are at or near all-time highs and private equity deal valuations remain elevated at more than 10x enterprise value to EBITDA, the average creation multiple of Fund VIII remains at approximately 6x adjusted EBITDA, more than 4 turns below the industry average. At the end of June, Fund VIII was 56% committed, and if we account for the Outerwall transaction that was announced recently, the fund is approximately 60% committed. We are gratified the fund has been able to acquire a number of high-quality companies, particularly when considering the discipline we have maintained in an otherwise robust valuation environment. Moreover, the construction of our Fund VIII portfolio, including the low average creation multiple and what we believe to be prudent investment selection, has helped the fund move into a carry earning position at a rather early stage, given that the companies have been in the portfolio for about one year on average. We believe we have several competitive advantages at Apollo that have enabled us to source and complete or announce a number of deals over the last few quarters. We have a willingness to tackle complexity and create solutions to uncover value. We have a proven ability to privately place debt and preferred securities to support the financing of our fund transactions and the size of Fund VIII, coupled with strong unlimited partner relations, has allowed has to step up for larger transactions or investments that can be scaled over time. To provide a bit of color on Apollo's latest private equity activity, I'd like to mention a few of our recently completed or announced transactions. The most notable completed transaction during the second quarter was the opportunistic buyout of ADT, which highlighted our ability to embrace complexity, utilize creative financing and execute a large transaction. In a very Apollo-esque deal, the funds we manage were able to combine ADT, the leading alarm services company with Protection 1, an existing Fund VIII portfolio company, resulting in the largest sponsor back transaction so far this year, with an aggregate enterprise value of approximately $15 billion. Through our broker dealer-affiliate, we were able to provide a creative financing solution despite a very difficult backdrop earlier in the year. This included accessing sizable, nontraditional sources of debt and preferred equity capital. Other transactions completed during the second quarter included the opportunistic buyout of The Fresh Market, a high-end specialty grocery retailer; NKBM, one of Slovenia's leading financial institutions; and follow-on investments in a couple of existing portfolio companies. In addition to these completed transactions, several new investments were announced during the second quarter with an aggregate equity commitment of $1.8 billion. The largest announced transaction was the buyout of Diamond Resorts International, which manages a leading network of more than 420 vacation destinations across 6 continents. In addition, during the quarter, funds managed by Apollo announced the simultaneous acquisitions of 2 lifting services businesses: AmQuip and Maximum Crane. This transaction just closed last week and served as a good example of our willingness to embrace complexity, given the challenges of acquiring 2 different businesses from 2 sellers at the same time. Beyond these deals, we have a very robust pipeline of potential new investment opportunities that could continue to propel the commitment level of Fund VIII forward in the near to medium term.

Before I turn the call over to Josh, I'd just like to emphasize how well positioned, I believe, the Apollo platform is today. I've already discussed our private equity business, and I'd also like to highlight our credit platform. As one of the world's leading alternative investment managers, we are poised to benefit from a number of secular tailwinds, including the deleveraging of the bank and reregulation of financial institutions, coupled with persistently low rates that are forcing institutional and retail investors alike to scour the globe for yields. All of these fundamental drivers played to our strengths at Apollo and over the last decade, we have created what we believe is the largest and most diverse alternative credit platform in the world with $134 billion of assets under management, which is up more than $20 billion since this time last year. Given the breadth and depth of our credit business, we are able to offer investors a variety of investment solutions across asset classes in the risk-reward spectrum, ranging from yield-oriented solutions with mid-single-digit returns, all the way up to opportunistic solutions that can offer mid- to high-teen types of returns. Most importantly, we have built an extraordinary team at Apollo with an extremely deep bench of talent throughout the firm.

With that, I'd like to now turn the call over to Josh.

Joshua J. Harris
Co-Founder, Senior MD & Director

Thanks, Leon. During my remarks, I'd like to touch on 2 important topics: growth and investment performance. First, with respect to asset growth and fundraising. During the second quarter, we generated inflows of more than $16 billion, which included $8 billion of inflows from a diverse set of investment solutions and mandates across all of our business segments; $8 billion of inflows associated with Apollo asset management Europe, or AAME, which Martin will explain in a moment. Within private equity, we generated $2.5 billion of inflows from equity co-investment capital to help finance the ADT transaction, and we also raised an additional $200 million from our second natural resources fund during the second quarter. Just last week, we closed on an additional $500 million, bringing total commitments for ANRP II, the national resource fund, to $2.7 billion and fundraising remains underway. This is roughly 50% greater than our last fund at this point.

Within credit, we had inflows of $4.6 billion during the quarter, excluding the aforementioned AAME assets. And notable drivers included $2.3 billion of incremental new assets related to Athene, which grew its total assets to $68 billion during the quarter, up from nearly $66 billion as of March. This growth resulted from new flow of business, from reinsurance clients as well as the successful launch of new retail products. Our credit inflows also included an additional $800 million for MidCap, our middle-market direct origination platform, bringing total assets under management to nearly $7 billion there. Based on its current capital base, MidCap now has a capacity to grow its assets to approximately $10 billion as it originates new middle-market loans. New add-on managed account commitments totaled $400 million during the quarter, and our pipeline remains strong as we are in active dialogue for additional mandates. As of June, we managed more than $18 billion of AUM for dedicated strategic managed accounts. We raised an additional $200 million for our total return strategy during the quarter. To date, we've been awarded mandates totaling more than $1 billion in strategy and there are additional investor allocations in the pipeline. Total return is designed to take advantage of the sourcing and underwriting capabilities of the entire liquid end of Apollo's credit business, and it is becoming an increasingly important strategic platform.

In total return, we believe we have been able to create a superior and differentiated products in the marketplace that when compared to traditional fixed income investments, targets greater returns and lower duration in exchange for modestly less liquidity. Since its inception, total return has significantly outperformed traditional high-yield and bank loan mandate. And it has also provided our clients with downside protection during periods of market volatility.

Lastly, as we noted last quarter, we commenced the fundraising process for the third vintage in our financial credit investments fund series, a credit draw down product which focuses on insurance-linked securities. I'm happy to note that we held a first closing of approximately $400 million during the second quarter.

Now, turning briefly to our investment performance. The funds we manage delivered solid results across each of our businesses during the quarter, with private equity up 3.1%, credit up 3.7% and real estate up 2.2%. The 3.1% appreciation in the private equity funds we manage was driven by strong performance among our funds private portfolio company holdings, public debt positions, as well as energy investments. In a few minutes, Martin will provide some additional details regarding our private equity funds, but I would like to call your attention to Fund VIII's performance in the quarter. Fund VIII is our $18.4 billion, 2013 vintage fund that is actively deploying capital and already performing well as Leon noted. In fact, even though Fund VIII has been invested for about 3 years and its current investments only have an average holding period of approximately 1 year, the fund appreciated by approximately 8% and crossed its 8% preferred return hurdle during the second quarter, enabling the fund to accrue carry for the first time. This is a significant milestone for a 2013 vintage fund, particularly given the earnings power it represents over time. In credit, the investment performance of the funds we manage was also quite strong during the quarter, up 3.7% on a gross basis and up 3.3% on a net basis, excluding the non-sub-advice assets of Athene. If you look at some of the core strategies within our credit business, our drawdown funds generated gross returns of 6.4% during the quarter, bolstered by investments held in our European principal finance business as well as a rebound within the energy sector. Our liquid performing funds, which represent approximately 1/3 of our credit assets, also performed well and delivered a 3% return during the quarter.

With that, I will turn it over to Martin for some comments on our financial results.

Martin Kelly
Chief Financial Officer

Thanks, Josh, and good morning again, everyone. Starting with our economic earnings for the quarter. The $395 million or $0.98 per share of total ENI in the quarter was driven by strong performance in our Management Business and even stronger performance in our Incentive Business. In the Management Business, we earned $137 million of economic income, up from $82 million in the prior quarter. The increase was driven by rising Management Business revenues, principally resulting from fees earned in connection with sizable co-invest activity. The increase in Management Business revenue offset higher Management Business expenses, which rose sequentially primarily due to an increase in non-compensation related expenses.

In the Incentive Business, we earned $322 million of economic income, representing a significant rebound from an economic loss in the prior quarter. The sequential increase was driven by 2 primary factors. First, the positive fund performance across business Josh mentioned, drove strong carried interest income across several funds, which included Fund VIII crossing its preferred return threshold and earning 80-20 catch-up carry. Approximately $87 million or nearly 45% of the quarter's total net carry income was generated by Fund VIII. At the end of June, Fund VIII had the potential to earn approximately $30 million more in net catch up before reverting to the conventional 20% carry accrual. Fund VIII is in the somewhat unique position of being carry generating while still deploying a considerable amount of its capital. For this reason and given the dynamics of marching forward in time to keep pace with the preferred return hurdle as well as uncertain future portfolio it marks. It's possible that the funds net IRR could fluctuate within or out of catch-up carry territory over the coming quarters.

The other primary driver of Incentive Business economic income during the quarter was the increase in the evaluation of Athene. This valuation was driven by significant business growth in Athene's, reinsurance and retail channels and continued progress towards its initial public offering. In addition and in connection with the process of preparing for Athene's IPO, Athene received feedback from a range of sources, which supported our view of an increase in value relating to recent developments at Athene. Upon adjusting for these recent developments, Athene's fair value increased by approximately 20%. This resulted in a $101 million unrealized gain within other income as well as $69 of unrealized net carried interest income from AAA and related accounts, driving an aggregate contribution to second quarter ENI of approximately $0.40 per share. Across the $17 billion of private equity fund capital that we currently have in the ground, only $2.5 billion or 15% of our invested capital is in public equity securities. And so although the value of these public equity securities declined this quarter, the performance of these holdings is not necessarily representative of the board of fulfillments of our private equity funds. As Josh touched on earlier, investment performance in our credit business was also strong during the quarter, which in turn, drove a significant amount of carry and lead to an increase in carry-generating AUM. The carry income was primarily generated from our opportunistic drawdown funds as well as our credit hedge funds.

Lastly, on the Incentive Business, there was a discretionary incentive pool compensation accrual in the quarter of $13 million within realized profit-sharing expense, which drove an elevated profit share ratio in the quarter. As a reminder, the firm takes a long-term view with respect to the discretionary components of incentive compensation and will monitor its overall level relative to the firm's incentive-based earnings over an extended period of time.

With regard to our cash distribution. The $0.37 we declared today was driven by the relative cash flow stability of the Management Business and the upside it can create by leveraging the firm's integrated platform as it relates to sourcing, financing and executing sizable transactions. Earlier on the call, Josh described some of our inflows during the quarter. Included within that figure is approximately $8 billion of assets related to what we referred to as a apollo asset management euro, or AAME. We have been building out AAME over the past year as a centralized investment and risk management capability for regulated balance sheets in Europe, including certain of the insurance and banking platforms already owned by the funds we managed. For the time being, AAME is primarily operating as a utility, providing services on either a cost or low margin basis. While the profitability of this venture is currently more limited, we believe this will be more accretive over time, given the opportunities we see across Europe to acquire other regulated balance sheets and the value, we believe, can be created through more efficient management.

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

Question and Answer

Operator

[Operator Instructions] Your first question comes from the line of Devin Ryan with JMP Securities.

Devin Patrick Ryan
JMP Securities LLC, Research Division

Maybe starting on AAME as you just touched on. You're just trying to think about your plan to market that strategy. It seems pretty differentiated. And then maybe if you can -- I know it's early days and there's not a big contribution, but can you just help us think about the potential market for that business or just the market share that you could take from through these insurance companies?

Joshua J. Harris
Co-Founder, Senior MD & Director

Yes, I mean, I'll take extra crack at it, Josh. It's a huge market. You're talking about kind of all of -- kind of -- like all of the existing insurance company liabilities and for that matter, noninsurance company liabilities, bank liabilities in Europe. So it's trillions of dollars. So the market share is really small, I mean it's infinitesimal. That not really a market share issue. In terms of how we're going to market it, I would say that we continue to sort of study that and think about it and there are certainly, multiple ways we could go. Certainly, if you look at the Athene model, the MidCap model, the permanent capital model, that might be a way that we would orient or we might raise LP capital directly, but we're continuing to work that out. But so far, there's a lot of opportunity. The opportunity comes from, there is 0 cost liabilities in Europe. And so if you know how to manage the assets, you can make -- it's a great time to try and accumulate those liabilities.

Devin Patrick Ryan
JMP Securities LLC, Research Division

Okay, great. That's helpful. And then, just on Fund VIII, great to see it moving to carry generating. If you can give any detail just around, were there specific investments that have been driving the performance that you've had kind of a couple of nice quarters? And is it fundamentals improving within those businesses that's driving the marks or the marks being kind of pulled up by something going on in the public comparable side?

Martin Kelly
Chief Financial Officer

So, it's Martin, Devin. It's a general seasoning of money that's in the ground across the investments that were made. Across DE, more broadly than just Fund VIII, we benefited from energy markups during the quarter, and that had an effect on Fund VIII as well. But it was -- the contribution of energy as it relates to Fund VIII was less pronounced than it was more broadly it fits with the portfolio.

Yes, I can hit the business. The underlying business of the companies in the portfolio is sort of trending to what we had planned. The revenues are -- both revenues and EBIT are both up sort of single digit, low single digit on a LTM basis, 12 months [indiscernible] . But it's still early days. The company's -- each company has its own situation, each is being managed according to its own plan. It's hard to sort of benchmark marks against the broad index, but we feel good about the structure of the portfolio. Yes, just to give, EBITDA for the nonenergy stuff quarter-on-quarter -- year-on-year is up about 5% across our private equity firm. That gives you kind of a sense of why kind of on aggregate that we're realizing -- start to realize value.

Operator

Your next question comes from the line of Craig Siegenthaler with Crédit Suisse.

Craig William Siegenthaler

Crédit Suisse AG, Research Division

So it was nice to see the $6 billion of capital deployed in the quarter, and we saw some fairly sizable transaction with ADT and Fresh Market. But Apollo is one of the few key shops we're actually, seeing a high level of capital deployment and some of your peers are complaining about high public equity prices and slowing global economy. So how do you guys respond to this contra trend and really that we've seen an increase in your pace of investments here in P8 [ph] ?

Leon D. Black
Founding Partner, Chairman & CEO

Well, this is Leon. I think we respond through reactions and performance. The proof has been in the pudding. Basically, we have put a lot of capital to work, and we also have a robust pipeline today of deals that we like. There's no assurance that they will be executed. But right now, we're going at a very nice pace. We hope that will continue. We're most pleased that is the fact that we're doing it in an Apollo-esque way. We understand that some of our peers feel it's a high-priced environment. We've always felt it was a high-priced environment, and that's how we have always operated by dealing with complexity, by dealing with the stress, by dealing going down roads others don't and that's why not only have we put a lot of capital to work, but we put it to work at 4 multiples lower than what the average of our peers are doing. So basically, I think our value-oriented mantra has worked for us and continues to work. And our whole team and culture here has been attuned to doing deals that are outside of what our peers are doing and what the rest of the market is doing. Just to remind you all, we probably do over our 26-year period, about 1/3 of our transactions have been in distress during volatile times. The entry there has been at a 5 multiple. We do a lot more complex carve-outs than anybody else. Our entry there is at about a 6 multiple, and then the 9 industries that we cover in-depth here with our 360 professional investors across the Apollo platform will help each other. We're willing to go a little higher, maybe to 7.5x, but that's why, at the end of the day, we've been able to find things and keep to our culture investing at much lower multiples than what our peers are doing.

Craig William Siegenthaler
Crédit Suisse AG, Research Division

Got it, Leon. And just my follow-up. So we finally had some clarity in the second quarter on the Department of Labor rule. I'm sure you guys probably were disappointed on the one point, but the rule ended up including index annuities. And I noticed several suits out there and the insurers are involved, but if the rule is implementing as is in April 2017, how should we think about the impact to Athene, which I believe, is one of the largest underwriters of index annuities in the U.S.?

Joshua J. Harris
Co-Founder, Senior MD & Director

Yes, you're right in terms of your comments with respect to their presence in the annuity space. Generally speaking, it's tough for us to comment on Athene's business given the fact that they've got their S1 on file and they're in a quiet period. I would note that they did hold an investor update call back in June. And in that call, they presented a slide talking about the DOL, and you can find that on the AAA website. The one point I would make is that they did show a pie chart there that indicated that only 34% of their new flows in the first quarter of 2016 were subject to the DOL. So I think their exposure there is coming down over time.

Leon D. Black
Founding Partner, Chairman & CEO

Yes, I'd actually like to add to my long-winded list of the last answer because I've reflected on the question more. I think the other things we have going for us, frankly, is we have a very large fund with the backing of great supporters, which allows us to do larger deals like ADT. It is also great to have all of those LPs and supporters because not only are we able to commit a lot of capital, but we are able to offer co-investment to our LP constituency. Finally, just going to our integrated platform, I think we're able to be creative on financing when times are tough in the credit markets. So those are part of the secret sauce as to why, I think, we've been able to generate a lot of deal flow and why we have a robust pipeline now.

Operator

Your next question comes from the line of Mike Carrier with Bank of America Merrill Lynch.

Michael Roger Carrier
BofA Merrill Lynch, Research Division

Martin, first on the fee-related earnings, I guess, just the outlook, like when I think about the transaction -- level of transaction fees, it seems like from a deployment co-investment, the outlook is still pretty acumen and it was something that tough to forecast. And then also just given you guys' comments on Fund VIII at 60%. So we think about going into 2017, any potential new timing or how we should be thinking about fund raising heading into next year?

Martin Kelly
Chief Financial Officer

Sure, so I'll take the first question, Mike, and then I'll hand over to Josh for the second. I think on the fee-related earnings comment, we've gone from a period of time when we had relatively low deployment and not much co-invest to a more robust deployment environment and we earn -- we can earn fees in a couple of different ways when we take in co- invest capital and we do financings that are accretive when we place the debt. So in the case of 82 [ph], we earned a transaction fee and we also earned a debt placement fee. I think it's certainly reasonable to expect that we can expect to earn more of those fees, but it's dependent on a, getting deals done; and b, then being large enough to sort of warrant the use of company's capital. So I think there should be more, but it's difficult to predict on a quarter-by-quarter basis.

Joshua J. Harris
Co-Founder, Senior MD & Director

And on the fund, I mean, as we noted, the fund was approximately 56% committed at the end of the second quarter and factoring in recent deal activity, we're 60% committed at this point presuming those deals close. We've been -- funds have been invested for about 3 years. So it's about 20% a year. Typically, private equity funds begin the fundraising process for successive funds when they cross the 70% threshold. But obviously, it's difficult to predict exactly when that will be.

Michael Roger Carrier
BofA Merrill Lynch, Research Division

Okay, that's helpful. And then this is a follow-up. I guess, just on the Athene gain in the quarter I just wanted to -- I know you mentioned a couple of things that were more may be specific to Athene. But when you think about the kind of the DOL aspect, you guys mentioned growth and I think when we look at the comp group, you didn't see much of a move. So I just wanted to -- I don't know, maybe flush out or understand how to be thinking about maybe what happened in the quarter but probably more importantly just going forward?

Martin Kelly
Chief Financial Officer

Sure. So I guess, the events in the quarter are the new management team is in place and doing well. The organic growth in the business across each of the channels is stronger than planned and the readiness for the IPO is progressing nicely with the registration process in terms of incremental readiness. And so our view is and Athene's view is that a premium to the comp set that we'd identified is warranted and that's being supported by advice that we've had from outside advisers. So we need to translate that into numbers, I guess, it's back to a 1.2x multiple on book and around 50% premium to the comp set. And coincidentally, the 1.2x multiple is where capital was raised 2 years ago.

Operator

Your next question comes from the line of Ken Worthington with JP Morgan.

Kenneth Brooks Worthington
JP Morgan Chase & Co, Research Division

First on AAME, I know you've given some description. Could you further flush that out? I'm still a little uncertain about what AAME is? And then maybe in those comments, can you talk about really providing a service for a fee or how does it make money? I assume it's not a carry fund maybe it is a carry fund. Anyway, that's #1.

Joshua J. Harris
Co-Founder, Senior MD & Director

Yes, so it's an entity be we set up. So we have various insurance companies and banks that are in and around our platform in various funds. And it's an entity that we've set up. So each of -- -- one of the ways we add value to those companies is rather than each of them having their own specific team. In certain cases, it makes sense for them to -- -- for us to consolidate all of those teams and come out with a new better team that's integrated and centralized. And in doing that, both save costs, but at the same time, allow for, in our opinion, better and more thoughtful investment performance versus each smaller entity having a specific team. And so AAME, if you will, is an entity that is set up to manage certain assets of our European investments, where it's logical and makes sense. And at the same time -- so that capability both benefits our investors, but at the same time allows us to make more thoughtful acquisitions of other assets as well as possibly manage incremental capital outside our investor pool. And so that's AAME in a nutshell.

Leon D. Black
Founding Partner, Chairman & CEO

And I guess, I'd say at the outset, the thought was that AAME would mostly be servicing our existing portfolio companies, and that's why we're saying it would be a cost or at a very low margin. But the hope, over time, is that it would also engage in incremental activity that could create value on new investments that may or may not be portfolio investments and on those, there could be meaningful fee increments to the entity.

Kenneth Brooks Worthington
JP Morgan Chase & Co, Research Division

Awesome. Yes, was that mean to the other ends that I was trying to go towards new, you got that perfectly. And then, on see -- I don't know if you can answer this, but like on Athene, you mentioned that the assets were up a bunch. There was new business, material business growth. You mentioned some new products. Could you flush that out again? I know they are in the registration period so it may not be possible but I'll try anyway.

Gary M. Stein
Head of Corporate Communications

Yes, it's tough for us to do, Ken, as you pointed out given the quiet period and also importantly Athene hasn't reported their own Q2 results yet. So I think until they do that, it's tough for us to comment. You can certainly look at their Q1 results relative to last year, and you'll see strong growth in reinsurance flows and you'll see strong growth in new sales driven by new products that they released earlier this year.

Leon D. Black
Founding Partner, Chairman & CEO

Yes, in retail. If you're jogging on your morning run in front of Bloomberg, you'll see a fair amount of advertising for Athene in an approach to retail, which is new for them, which is working so far.

Kenneth Brooks Worthington
JP Morgan Chase & Co, Research Division

Excellent, okay. Then just maybe lastly on MidCap, raised more capital. Based on the business environment and conditions, how quickly can they deploy what you raised? I think you said $800 million, if I heard correctly. Is that an amount of capital given the leverage that can last them a year, 2 years, 6 months? How long until they possibly can work through that capital??

Martin Kelly
Chief Financial Officer

So just framing with what they've done in the first 6 months of the year, they originate loans and then syndicate down a proportion so -- what they call a hold level. That's been about $2 billion on a year-to-date basis. And then the runoff on the book has been about $1 billion. So that sort of adding it 2x the runoff and if you annualize it, that's about $2 billion net growth for you.

Joshua J. Harris
Co-Founder, Senior MD & Director

Yes, I think we said that they're at $7 billion of AUM and we said in the comments that they could go to approximately $10 billion based on the current market conditions and so that would be few more years of growth.

Operator

Your next question comes from the line of Glenn Schorr with Evercore ISI.

Glenn Paul Schorr
Evercore ISI, Research Division

Just curious, I wanted to flush out your comments relate to the $80 million or so gain in unrealized gain in credit. I think you mentioned you're paying principal finance rebound and energy and liquid performing funds. But curious what asset classes may be underneath? And I'm trying to get at how much of it's rebound in energy prices? How much of it is just you bought well and credits improved in the quarter? That would be helpful.

Martin Kelly
Chief Financial Officer

I think energy is a de minimus component of that plan if -- most of it in dollars -- about half to total dollars was coming out of EPS, which itself is driven wisely by European real estate positions. And then, a portion came in at our structured credits funds, SCRF III, which actually came in to carry this quarter and created some nice carry. And the rest was sort of sprinkled across the liquid performing parts of the business, including the credit fund and others with related credit hedge funds.

Glenn Paul Schorr
Evercore ISI, Research Division

Excellent, that's good. And then just a follow-up. In your capital deployment comment, within credit, you mentioned NPL's and longevity assets. Just curious if you give a little more color on each where they're coming from, the types of assets, the bank balance sheet, the downsizing and what kind of expected returns there?

Joshua J. Harris
Co-Founder, Senior MD & Director

Yes, it's coming across like kind of our entire platform. So I think it's pretty hard, like to answer that question the way you framed it. I mean, it's coming across nonperforming loans, coming across incremental buys in our performing credit business, which is yield. As I think you're aware, the second quarter experience much volatility, and it's coming across some of our opportunistic businesses. So it's sort of like, if you just look at our platform, it's pretty broad.

Glenn Paul Schorr
Evercore ISI, Research Division

Okay. And you mentioned the volatility in the quarter provided some great opportunities that you are always ready to jump on. Should we keep our expectations at bay barring another crazy event in the quarter? In other words, would you consider this an exceptional capital deployment environment in the second quarter?

Joshua J. Harris
Co-Founder, Senior MD & Director

I wouldn't say it was exceptional. I think that it was strong and we still have a robust pipeline. I think it's very difficult -- the problem is it's very difficult to predict the ebb and the flow and the investment business. I mean, certainly, when there's volatility, it's helpful. When there's pullback, it's helpful. But even if there's not pullback, I think we've demonstrated the ability to continue to deploy. Like as Leon said, in private equity, we're 60% invested after 3 years in what is possibly one of the most aggressively priced environment that I remember in my 26 years in the business and yet our platform is able to continue to churn out deal flow and certainty when there's a pullback and the financing market shutdown, that helps, but we're just doing it quarter after quarter. And then in credit, certainly, it helps when there's a volatility but between our structured credit business and our yield business and total return, the long-term trends of the deleveraging of the banks, the financial sector, we've positioned ourselves to be in products which -- -- where we don't we need volatility to deploy. But it was a good quarter but I wouldn't say it's an exceptional quarter, I think it's just work to continuing to chug away.

Operator

[Operator Instructions] And your next question comes from the line of Robert Lee with KBW.

Robert Andrew Lee
Keefe, Bruyette, & Woods, Inc., Research Division

Just kind of curious on maybe looking at fund raising a bit. I mean, I'm interested in maybe trying to get updated on some of the drawdown in PE strategies, your fund raising for, obviously, you mentioned FCI IV, you mentioned ANRP is ongoing. I mean, if I look at -- those look like EPS is pretty much fully invested. We see PF2. I'm not sure if you're raising another credit opportunity fund because I know 3 had some performance issues but that's pretty much invested. So can you maybe update us on some of the fundraising initiatives and drawdown in PE land?

Leon D. Black
Founding Partner, Chairman & CEO

Sure, So it's Martin. I'll start it now, and I'll hand it to Josh. In DE, it's ANRP 2, the natural resources fund and special situations, which is small, but we think potentially important over time for us. And we touched on that last quarter. In credit, it's the third generation of some of that what we call are flagship funds, FCI III, which is underway with the first close. APF3 is in fundraising now, has not had a first closing. We'll likely get one done by year-end, but unlikely in Q3. And then, it's other sort of what you'd expect across the platform, total return, CLO's, continued managed accounts.

Joshua J. Harris
Co-Founder, Senior MD & Director

Yes, I mean, I say the sort of -- I think you might identify the flagship and drawdown funds and then you got certainly, some of the products that are perpetually open. The hedge fund, it's been performing incredibly well. And we're -- we're starting to see some, notwithstanding some of the negative vibes towards hedge fund products, our performance is really setting us apart . We're starting to see some traction there. I'd say that the total return fund where we can add a bunch of returns to BB, BBB crossover type product and pulling duration for a small amount of incremental lockup, a quarterly lockup versus a daily lockup for most mutual funds.That's also starting to resonate with investors and the performance has been quite good there. And so what we're trying to do is set up a series of products that allow -- and then our yield business starts -- overall yield business where we just are constantly taking in money and growing in our CLO business as well. We're trying to set up a series of products that allow us to not just be dependent on the next big drawdown to fund even though it's certainly, our drawdown funds, our flagship funds are quite unique in terms of how they perform and they're big pops, if you will. They propel our growth forward, but we're trying to set up a series of these other legs to allow us to just continually grow our assets, and I think we're getting some traction there.

Leon D. Black
Founding Partner, Chairman & CEO

Obviously, we'd be remiss just to underscore Fund IX and PE is looming somewhere on the horizon although at 60% committed and where at 70%, you can go out and raise it, but we can't predict with any exactitude when that will be but somewhere..

Joshua J. Harris
Co-Founder, Senior MD & Director

And last thing I would say is the managed account business also continues to chug along. So as I think we mentioned in the comments, we're at about $18 billion there and those come in, $400 million chunks, $200 million chunks, $700 million chunks. And so again, they're little lumpy, but we continued to land those and we have a nice pipeline there as I mentioned in my remarks.

Robert Andrew Lee
Keefe, Bruyette, & Woods, Inc., Research Division

Great. And I did have a -- excuse me, a follow-up on going back to the AAME, I guess, there's been a lot of questions on the call today. But I guess, it strikes me that pretty similar to what you do for Athene here in the States, the services, maybe the types of services you're providing and you do charge, Athene does pay whatever the number is in basis points as opposed to making kind of more utility like at least at this point in Europe. I mean, is that more because of just the nature of the companies you're servicing being portfolio companies versus something that you helped start up with Athene?

Leon D. Black
Founding Partner, Chairman & CEO

I think you hit it exactly, but it's really starting out with existing portfolio companies. But over time, it should morph to, hopefully, more like an Athene structure.

Operator

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

Alexander Blostein
Goldman Sachs Group Inc., Research Division

Questioned, maybe it's a little early but as we think about the realizations from Fund VIII, just given the improved performance and the pretty quick pace of deployment. At what point in time do you guys think you could start begin to aggregate some of the positions and I guess, crystallizing and monetizing the carry?

Joshua J. Harris
Co-Founder, Senior MD & Director

Yes, unpredictable and certainly -- and the investments are year old on average. Having said that, we're always looking at -- if the markets continue to be robust and the thing continues to mature, you're certainly going to start to see some of that, but it's really hard to be specific there.

Alexander Blostein
Goldman Sachs Group Inc., Research Division

Would it be reasonable I assume if you do start to see faster realizations and the fund is still in investment period. You guys would just totally deploy it as opposed to kind of return it?

Joshua J. Harris
Co-Founder, Senior MD & Director

Well, the way the funds work is you can't really make that decision in that way. There's an 18-month recycle provision, which sort of more than allows kind of you recycle the capital if you realize investment within the context of 18 months and you do -- at that point you would realize carrying profit. So certainly, when you sell an investment and again, you realize the carrying profit that gets distributed -- that gets realized. So I think having said that, certainly, if it's within 18 months -- it's recycled, if it's after 18 months, it's permanently sold and it goes out of the capital base and that's the way it works.

Alexander Blostein
Goldman Sachs Group Inc., Research Division

Got you. And then just a quick numbers question around FRE, not sure if I missed it, but obviously, very elevated level of kind of transaction adviser fees and expense were little bit elevated as well. If we were to exclude that activity and understanding you could repeat itself, but probably a little bit more unusual. So what's kind of run rate FRE that you guys stand at heading into the third quarter?

Martin Kelly
Chief Financial Officer

So I would just take the transaction. If you simply want to back out transaction fees, just back out difference between Q2 and Q1.

Alexander Blostein
Goldman Sachs Group Inc., Research Division

Got it. Okay, but the expense run rate is kind of what it is, there's nothing unusual there?

Martin Kelly
Chief Financial Officer

Comp quarter-on-quarter was flat and I would expect that will -- obviously, subject to year-end compensation though. That will be in the area of where it is now for the rest of the year. We have not -- we haven't made many hiring decisions this year. Our headcount is up very modestly. And so while we had a bit of step up in comp from last year into this year, I think the run rate from here on average is pretty predictable. And then, on non-comp, we had a couple of not individually significant, but sort of cumulatively they increased the run rate going into Q2 and so that should step down a bit again next quarter. But all of this sort of underpins our expectation to pay $1 a share from the Management Business.

Joshua J. Harris
Co-Founder, Senior MD & Director

Right. I mean, in other words -- it certainly transaction fees are unpredictable, but they happen, right? And the reality is we will pay them out. When we're talking about $1 a share, we're excluding the ongoing transaction fee. So you have upside from those which you're seeing in this quarter. You also have upside certainly from the incentive income, which is largely not included -- which is not included -- largely not included in the $1/share. So I think all those things are upside but because of the focus on quarterly performance -- we don't include them, but having said that, I think over time, they certainly have repeated and we would expect them to repeat.

Operator

Your next question comes from the line of Chris Kotowski with Oppenheimer & Co.

Christoph M. Kotowski
Oppenheimer & Co. Inc., Research Division

I wondered, can you give us the breakdown on ADT? How much came from Fund VIII and how much came from co-invest? And then, is your -- are your economics on the co-invest primarily the transaction fees? Or do you have carrier rights retained there too?

Leon D. Black
Founding Partner, Chairman & CEO

So we don't have carry on that capital and then the transaction fee -- we charge a placement fee on the debt and that was 30% of the total, thereabouts and the rest was a transaction fee charge on the value of the acquired business, a portion to the amount of capital that came in through co-investment.

Christoph M. Kotowski
Oppenheimer & Co. Inc., Research Division

Did you give us the breakdown between what's on from Fund VIII and what from co-invest?

Joshua J. Harris
Co-Founder, Senior MD & Director

The equity breakdown, yes, we said it was $2.5 billion of co- invest that was included in the inflows this quarter, and you can assume about $1 billion from our funds.

Operator

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

Brian Bertram Bedell
Deutsche Bank AG, Research Division

My question for maybe Josh and Leon, but I know it's always hard to answer but just to get your sort of view on -- and sort of where we are in the credit cycle in terms of the deployment in fund data as both of you guys mentioned at a fixed multiple. I mean, did you ever think you'd be able to get that type of entry most of all in this type of highly valued environment. And then, as we move forward from here and we do deploy more in Fund VIII, can you envision raising another fund ahead of the next credit cycle? Or is that just too [indiscernible]?

Joshua J. Harris
Co-Founder, Senior MD & Director

I'll start, and then Leon can add. Look, I think it's -- the credit spreads and levels are not as you would -- not very exciting. They're at kind of like all-time lows. But what's driving that is 0 interest rates and what's driving that is quantitative easing around the world. So the real question you're asking is what's going to happen? When are the central banks can raise rates and we don't really have a crystal ball in here, but I would say that I don't really see that happening as much as I don't like the level of credit spreads. I think we all need to just be accustom to the fact that we could be in the 0 rate environment for a prolonged period of time. I think a lot of that's going to depend on kind of how the economies themselves do and that's unpredictable. But I think you have to go into this kind of being cautious and trying to find ways to deploy capital where even if things go wrong and rates go up and the credit cycle turns against you, you still are okay and make some money. But I think my personal base case is that this could go on for a period of time and I think -- and so that's really what you're asking. In terms of your second question on PE, look, I think we've been honing for 25 years now -- 26 years, we've been working hard to hone our craft as perdition's private equity in terms of finding deals that other people can't do. And I think certainly, we're getting better at it in terms of being able to source transactions that don't seem to be consistent with the current evaluation environment, whether that be because we're fluent arranging financings that other people can't, whether that would be buying into distressed dips, whether it'd be corporate carve-outs. And interestingly, more recently, as you guys have seen, we found some public companies where each have a different view than the market. And so I guess, my honest answer would be I'm actually quite proud of the job the team has done in a really tough environment. And we're quite differentiated and you hear it. We listen to the other calls, and we're aware that other people are saying, "Well, we're not finding a lot of deals and the market's overvalued." So forth and so on but you just look at the multiples we're paying and the reality is that's not the case for us. So we are quite differentiated from what you're seeing out there and I'm very proud of the model and the team and the platform that we've built to be able to do it.

Leon D. Black
Founding Partner, Chairman & CEO

Just to underscore Josh's last point, if you look at the numbers from your last 4 PE funds going back to 2000, with each fund, we've actually widened by 1 multiple the difference between us and our peers in terms of putting capital to work. So Fund V, we are 1 multiple better; Fund VI, 2 multiples; Funds VII, 3 multiples; and now Fund VIII, there is a difference of 4 multiples versus the average in terms of our deployment of capital. I don't know how long he can keep that trend going into 5x and 6x and 7x, but just going to Josh's point that there's been an evolution of honing the skills that our whole team is imbued with that culture. And so we are gratified. I think our returns have been first in class in PE, but what I'm more proud of is that we've gotten them by taking less risk and paying lower multiples.

Brian Bertram Bedell
Deutsche Bank AG, Research Division

That's very perspective. Maybe just to switch gears, Josh, on the -- you talked about total return product in the liquid performing credit area. Can you talk about the fund raising market opportunity there, say over the next intermediate long term maybe 2 to 3 years in terms of which marketplaces do you think you have an opportunity to really gain substantial market share?

Joshua J. Harris
Co-Founder, Senior MD & Director

Yes -- no, I think it's really -- it's the core pension fund and sovereign wealth funds that we're typically in dialogue with and that are supporting most of our products, but I think it's also retail. And again, like it's hard to make -- making a safe 6 to 8 is actually quite -- and taking less risk in this environment when you have the ability -- if you buy a BB or BBB -- let's say buy a BBB high-yield investment, you're going to make 4 and you're going to have duration. So if you can go to someone and say, okay, instead of 4, I'll give you 6 to 8, I'll pull in duration." So in case, the central banks do decide to raise rates which we all inevitably worry about and have to think about years protecting because of your floating rate, but instead of daily liquidity, you need to give me quarterly liquidity. That's attractive to our core clients. It's also quite attractive to high net worth individuals and other individuals that don't have a lot of places to put their money in. So we think long run, it's going to be a very large product for us. It's performing quite well. We've now been added for 3 years, and we found is that there's lots of boxes to check with the track records and 3 years of performance in this and that. And we're checking all those boxes at the tail end of that, and we're starting to see the potential investor demand open up having gotten through all that and the performance is quite good. So it's just a product that we think is better for our investors and better for retail and it's quite differentiated versus what's out there. And we're at a size where we can play in off-the-run in credit differently than some of the very large branded players who are just multiples and multiples the size of us. And they just can't play in that area because they're too big. And so this is an area that we think we can take some market share.

Brian Bertram Bedell
Deutsche Bank AG, Research Division

And what's your penetration in retail right now? Is there a strategy to get deeper in the warehouses?

Joshua J. Harris
Co-Founder, Senior MD & Director

Yes, so -- I mean, I think what we've been saying on pretty much repeatedly, we're investing in the marketing resources we need to attack retail in multiple ways. Certainly, the warehouses are a part of it. Certainly, issuing -- in some cases having permitting capital vehicles in public markets and certainly, the non-warehouses. So I think like we're doing all of that and it's just -- we have -- we've always been great manufacturers of return, and increasingly, we're just now making those products available and suitable for retail, which is different. And then, obviously, you're aware of the sub-advisory stuff that we've done that we've announced between Opco and Wedell & Reed and things. So I think like that's another way. But at the end of the day, all of these ways, there's not 1 magic bullet, it's building up the process and the people and the systems to be able to like service the retail client base and communicate with them effectively.

Operator

Your next question comes from the line of Patrick Davitt with Autonomous.

M. Patrick Davitt
Autonomous Research LLP

So Fund VIII is going to be a big driver of ENI while it's in this 80/20 catch-up and beyond. When we think about marking that, should we think about any 1 index or industry concentration or some broad kind of weighted index of credit energy, the MSCI and the S&P in trying to kind of look at how that moves each quarter?

Joshua J. Harris
Co-Founder, Senior MD & Director

It's really hard to answer that. I mean, the answer is if you look at all of our historic returns, we've crushed the indexes. It's not even close. Having said that, you can look at our historic returns and they're in the mid-20s net and in the mid-30s to high 30s gross. So having said that, obviously, we're not saying you should model that. Certainly, we underwrite to a 20% gross return. We've exceeded that and then I guess, you can look at historical private equity benchmark returns. But the reality of private equity is that the top quartile performers do way better than the average performers. That's just the reality of the numbers. So you guys can look at all the data and so forth and if you want to look at indexes, you look at the top quartile private equity performers, but the reality is we've been better than that. So I don't know how to really predict it other than to give you all the data that's available as I just did and have you just consult it.

Gary M. Stein
Head of Corporate Communications

Just to clarify, we're underwriting to 20% net -- 25% gross.

M. Patrick Davitt
Autonomous Research LLP

Okay. And I meant more kind of like directionally quarter-to-quarter like if oil moves 20% a quarter, is that going to move it a lot? Or if credit moves 5% a quarter, is that going to move it a lot then over the long run? I understand what you mean over the long run.

Joshua J. Harris
Co-Founder, Senior MD & Director

It's -- first of all, we don't have a big -- we have a very small -- it's 5% in energy. So we're under-weighted in energy right now and so it's not really -- energy certainly, moves it up and down but not -- it's not any different than any of the other sectors that we're in. And if you look at all the investments, they're all -- it's pretty broad, right? It's pretty broad. It's becoming a bit less cyclical [indiscernible] history. So it's really hard. I mean, what I would do is, obviously, you always have to look at the major investments as best you can and try to figure out how that comparable companies are doing. If you want to look at -- look, the reality is the S&P 500 on a quarterly basis does move up and down from our evaluation. It's really hard to get away from that, but that obviously doesn't, in the long run, hasn't been consistent with our performance. We've done way better than that.

Operator

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

Nicholas D. Stelzner
Morgan Stanley, Research Division

This is Nick Stelzner filling in from Mike Cyprys. Just a quick question on the $10 million of AUM with future management fees potential. Can you elaborate on the funds and strategies those represent? And is it just deployment that will turn on the fees? And I guess how you're thinking about the time frame and types of environment needed to put that to work if those fees turn on?

Martin Kelly
Chief Financial Officer

Sure. It's almost exclusively within our credit business, and a decent amount that is from managed accounts that where the money's been raised and the money needs to be put to work. I don't think there's any -- certainly, nothing of significance. That's a fund that's waiting to switch on. It's really based on deployment. And then, you can look at the deployment that we've -- in credit, that we've have made in the last quarters going back in time. So it's challenging, as Josh mentioned, given the rich credit environment and so you just need to come up with a run rate based on what we've done over time. But it's multiple quarters of deployment to sort of run through that.

Nicholas D. Stelzner
Morgan Stanley, Research Division

Okay, that's helpful. Just one other quick question. Fund VIII now 60% deployed, sounds like Fund IX is looming. I think you successfully scaled your prior PE funds. If you think about the size of the next fund, how should we think about the puts and takes around scaling there?

Leon D. Black
Founding Partner, Chairman & CEO

I don't think you can ever predict but I think the good news is that there's been a lot of realizations in the last few years. So many LPs have a good amount of cash to deploy. The good news is they seem to be giving more of that cash to top performers. But when you go out for fund raising, you never know what the outcome is going to be. I think we're already a very large fund. It's really hard to predict how much more of that will scale.

Operator

We have reached the allotted time for questions and that concludes the Q&A portion of today's call. I will now return the floor to Mr. Gary Stein for any additional or closing marks.

Gary M. Stein
Head of Corporate Communications

Thanks, operator. Thanks, everyone, for joining us today. As we noted, if you have any follow-up questions, please feel free to give me or Noah Gunn a call.

Operator
This concludes today's conference call. You may now disconnect.