

KKR Macro Update: New World Order

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Conclusions

- We See a Square Root Recovery, Not a V-Shaped One
- The U.S. Consumer in Aggregate Is in Good Shape, But High Unemployment Weighs on the Fed
- The Fed's New Average Inflation Targeting Warrants Investor Attention
- U.S.-China Tensions Will Remain Heated, but We Still View Asia as an Opportunity
- We Are at an Inflection Point for 'Traditional' Asset Allocation

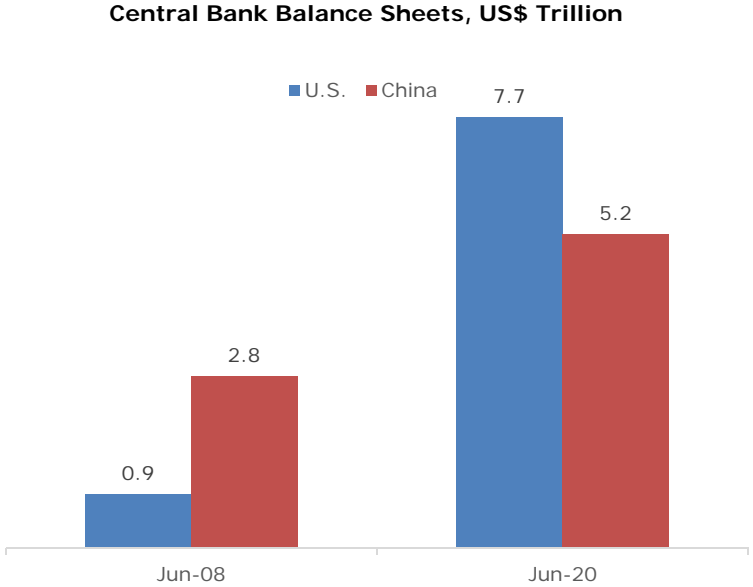
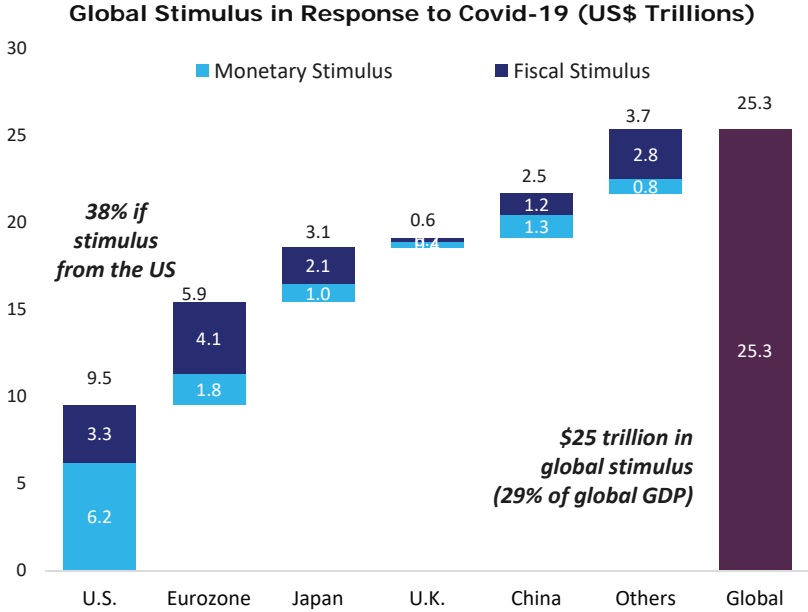
Section I: GDP Growth

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Record Stimulus, With the Fed — Not the Bank of China — Leading the Charge

29% of Global GDP Worth of Stimulus to Battle COVID-19

In 2008, China Led the Way. Today, However, the U.S. Is the Most Stimulative



As at July 24, 2020. Source: Cornerstone Macro, <https://www.imf.org/en/Topics/imf-and-covid19/Policy-Responses-to-COVID-19>.

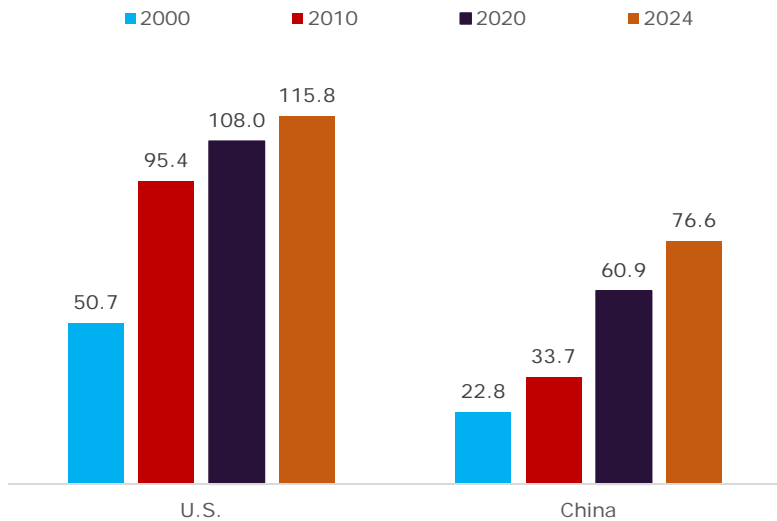
Data as at June 30, 2020. Source: PBoC, Federal Reserve, Haver Analytics.

Overall, Given Heavy Debt Loads and High Unemployment, We Now Envision More of a Square Root Recovery Than a V-Shaped One

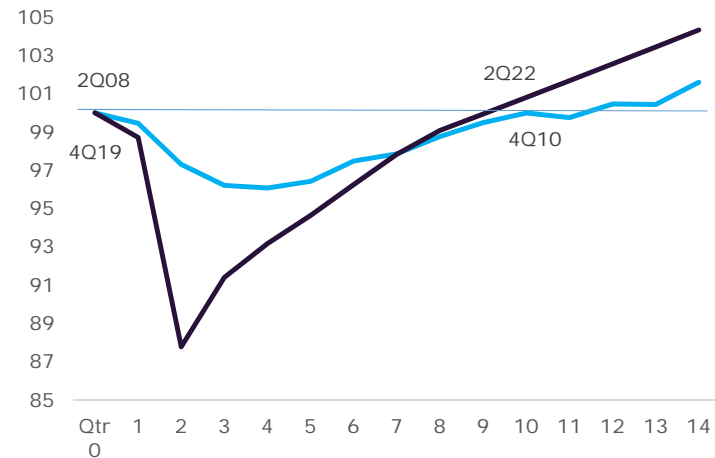
Global Growth Will Continue to Fall As Global Debt Continues to Rise

Near-Term Economic Trends Are Quite Constructive. However, We Ultimately See More of a Square-Root Recovery Than a Traditional V-Shaped One

Gross Debt to GDP, %



U.S. Real GDP (Pre-Crisis Level = 100)



Data as at April 14, 2020. Source: IMF, Haver Analytics.

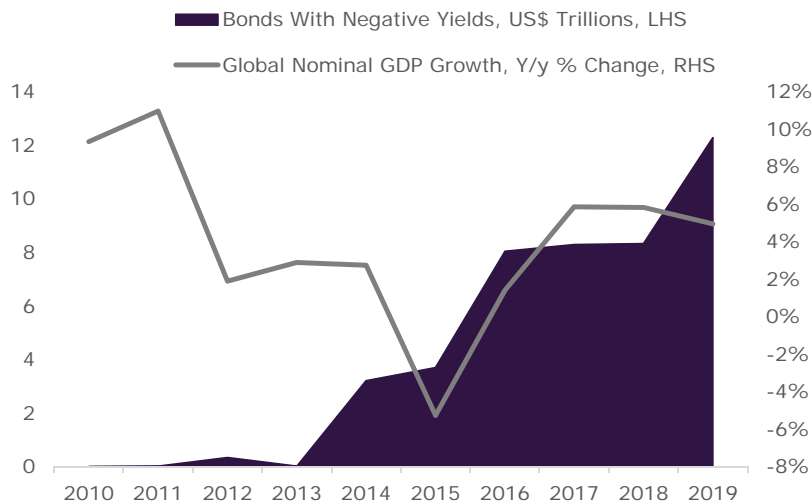
GDP = Gross Domestic Product. Bloomberg consensus estimates as at June 12, 2020. Source: KKR Global Macro & Asset Allocation analysis.

Bigger Picture, We Think We Have Entered a Structurally Slower Growth Environment...

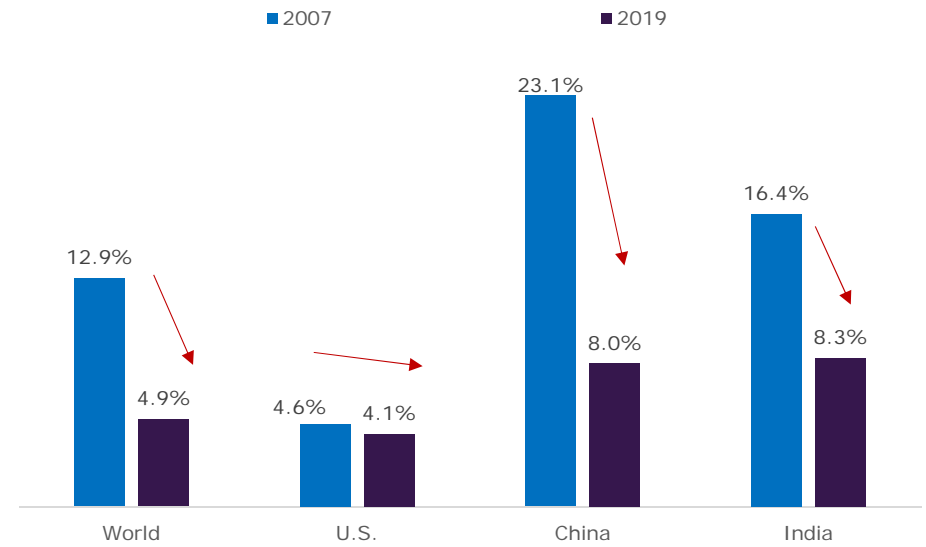
Even Before COVID-19, the Amount of Negative Yielding Securities Had Ballooned at the Same Time Nominal GDP Had Been Cut in Half

We Believe That Investors Are Underestimating How Much Nominal GDP Has Slowed in Recent Years

Global Supply of Bonds with Negative Yields and Nominal GDP Growth



Nominal GDP Growth, US\$, Y/y % Change



Data as at March 2, 2020. Source: Bloomberg.

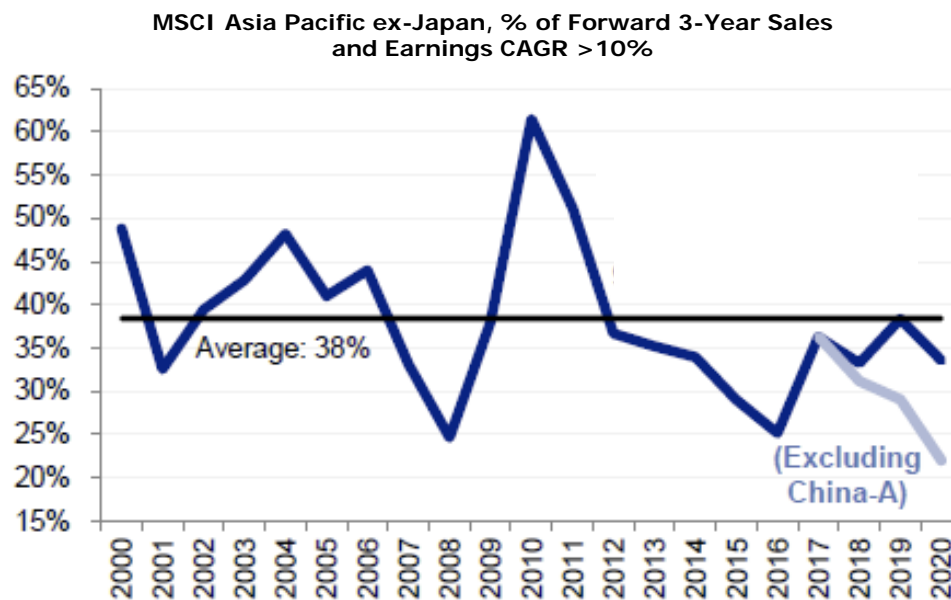
Note: China and India in local currency. Data as at November 21, 2019. Source: IMFWEO, respective national statistical agencies.

...Which Has Substantial Implications For the Capital Markets

The Number of Companies That Can Structurally Grow Has Slowed



Even In Asia, Growth Has Slowed



Data as at August 3, 2020. Source: Datastream, I/B/E/S, Goldman Sachs Global Investment Research.

Data as at August 3, 2020. Source: Factset, MSCI, Goldman Sachs Global Investment Research.

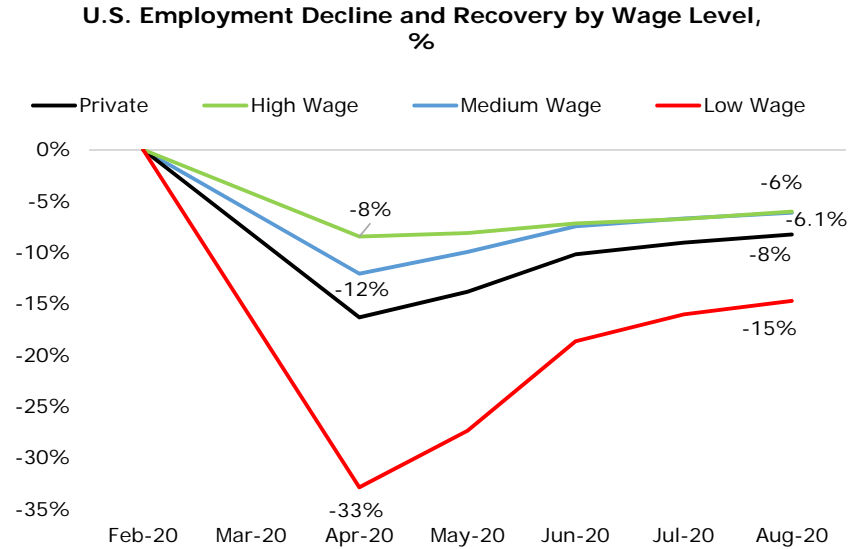
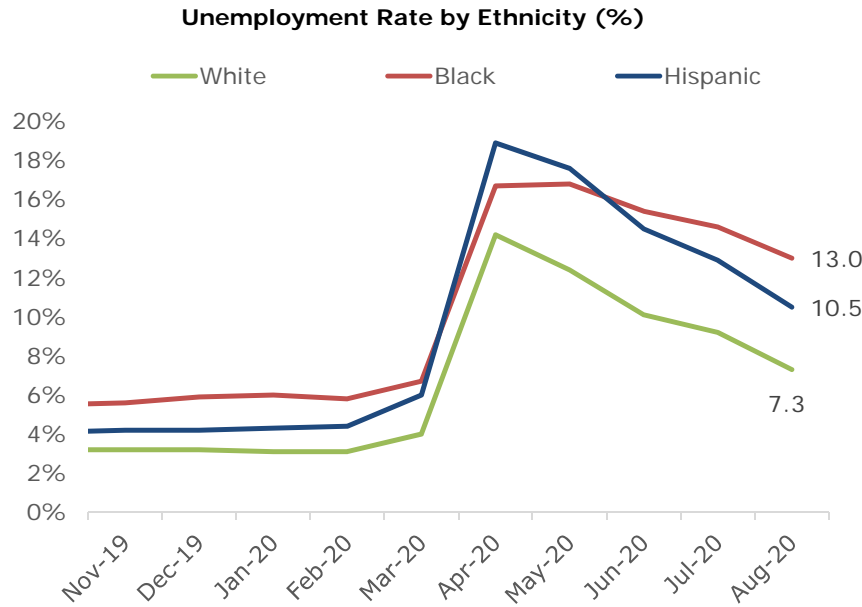
Section II: The Consumer

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Heavy Unemployment Weighs on the Fed's Psyche

Minorities Have Experienced a Tougher Job Market During the COVID-19 Pandemic

Racial Inequality and Socioeconomic Inequality Have Reached Record Levels, Which is Likely to Affect Policy and Politics



Data as at August 31, 2020. Source: Bureau of Labor Statistics, Haver Analytics.

Note: High-Wage = Information Services, Utilities, Finance, Prof Services And Mining/Logging; Medium-Wage = Wholesale Trade, Construction, Manufacturing, Education/Healthcare, Transport; Low-Wage = Retail Trade, Leisure/Hospitality. Data as at August 31, 2020. Source: Bureau of Labor Statistics, Haver Analytics.



The Health of the Consumer — Savings Is Actually Going Up

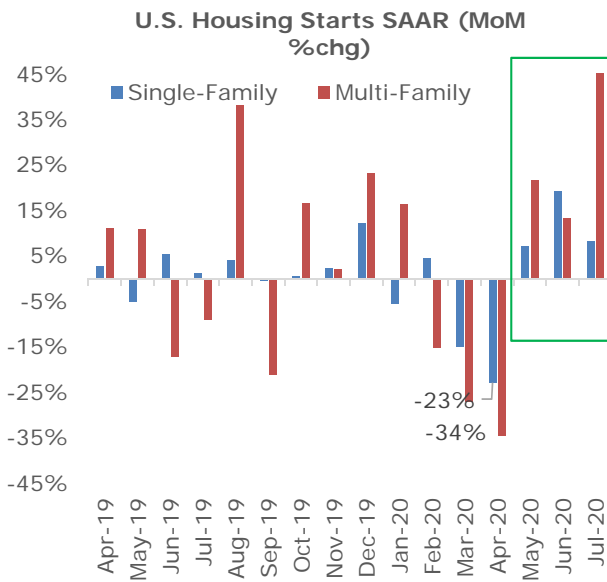
U.S. Household Disposable Incomes Have Actually Risen During the Coronavirus, Thanks to Massive Government Transfers

	Dec-19	Jun-20	US\$ Change	% Change
Disposable Personal Income	11,116	11,617	501	4.5%
Private Sources	9,030	8,407	-623	-6.9%
Government Social Benefits	2,086	3,210	1,124	53.9%
- Personal Consumption Expend.	9,927	9,071	-856	-8.6%
- Other Items (interest expense, etc.)	388	338	-49	-12.8%
= Personal Saving	801	2,208	1,407	175.6%
Memo: Savings Rate	7.2%	19.0%		11.8%

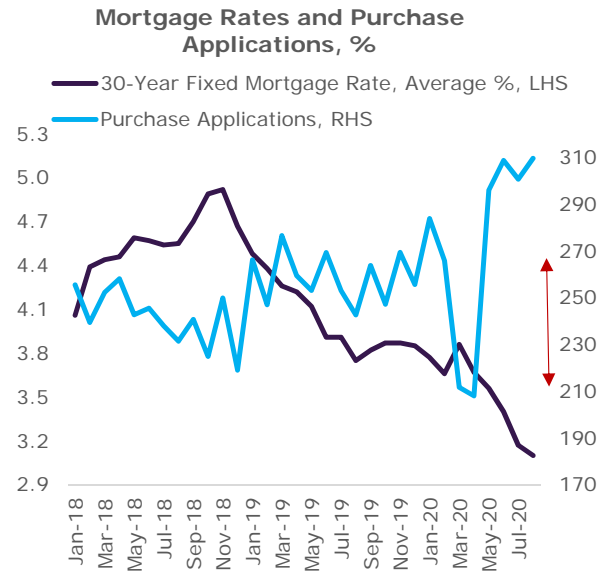
Data as June 30, 2020. Source: Bureau of Economic Analysis, Haver, KKR Global Macro & Asset Allocation analysis.

Many Parts of the Economy, Including Housing, Could Continue to Thrive...

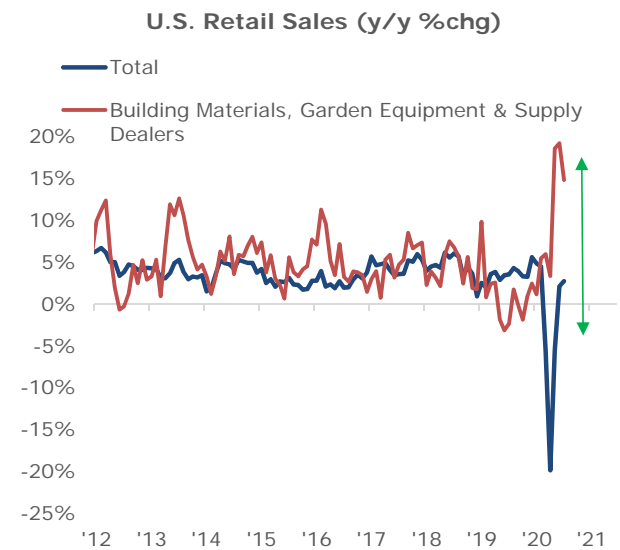
Multi-family Starts Have Taken Off While Single-family Remain Resilient



Lower Mortgage Rates Is Correlated with Stronger Purchase Applications



Home Improvement and Nesting As a Theme Is Staying Strong, Outpacing Overall Retail



Data as at August 18, 2020. Source: Census Bureau, Haver Analytics.

Data as at August 18, 2020. Source: Bloomberg.

Data as at July 31, 2020. Source: KKR GMAA, Haver, Bloomberg, NAR, BEA, FRB, Census Bureau



Investing Themes: More Conviction

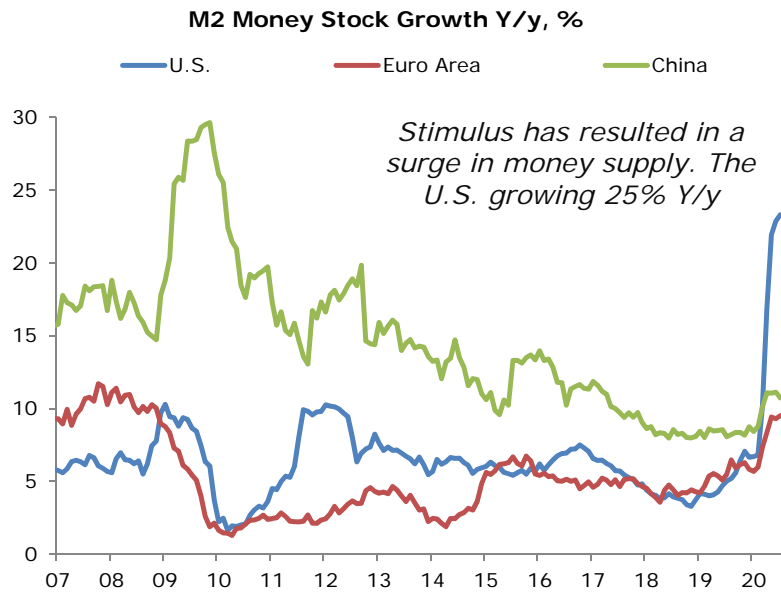
- Personal Safety
- E-Commerce/Digitalization
- Resiliency/Preparedness
- Nesting
- ESG/Infrastructure
- Health & Wellness/Preventative Care
- Savings/Tax Deferral
- Potential Reversals of Globalization, Urbanization, and the Sharing Economy

Section III: Central Banks and Inflation

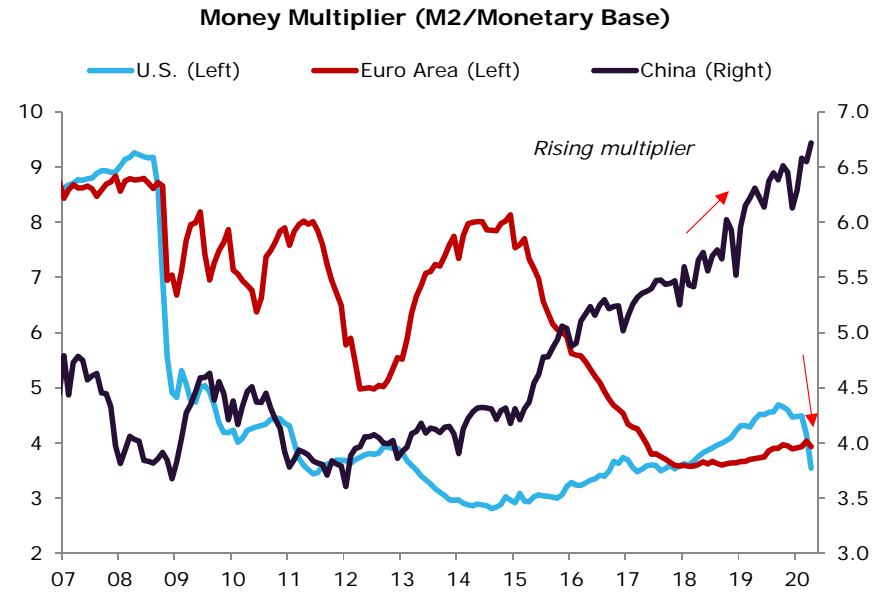
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Money Supply Is Up, But the Money Multiplier, Which We Think Is the Key, Has Actually Gone Down

The U.S. Money Supply Is Booming, But...



...The Money Multiplier Is Not. We Expect It to Remain Sluggish in the Near-Term

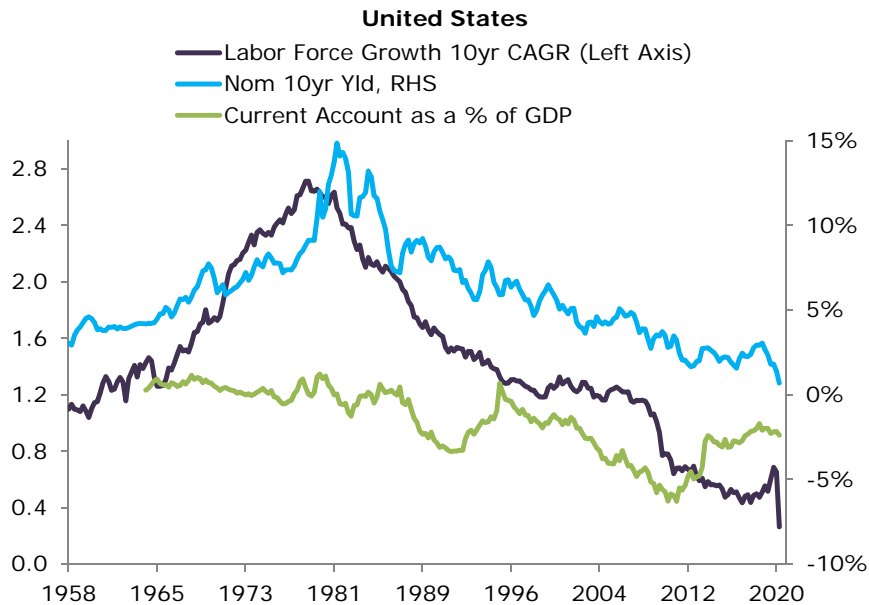


Data as at July 31, 2020. Source: BEA, Federal Reserve, Haver Analytics.

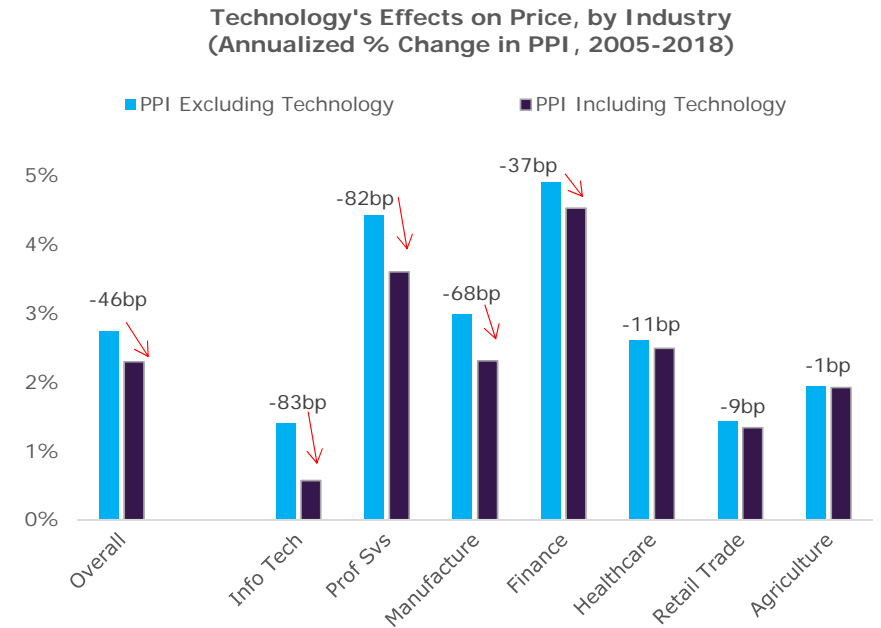
Data as at July 31, 2020. Source: BEA, Federal Reserve, Haver Analytics.

Beyond Technology's Downward Pressure On Inflation, There Are Other Forces to Consider

There Is a Strong Historical Relationship Between Demographics and Inflation



Technology's Effect on Prices by Industry Has Been Significant in Recent Years



Data as of June 30, 2020. Long-term changes represented as 10-year compound annual growth rates. Source: Bureau of Labor Statistics, Bureau of Economic Analysis, Haver.

Note: In the BEA's input-output data (I-O), we identified technology-related inputs as follows: computer and electronic products; broadcasting and telecommunications; data processing, internet publishing, and other information services; and computer systems design and related services. We identified as closely as possible Producer Price Index (PPI) series for each industry in the I-O, including all four technology inputs. The weightings were multiplied by technology's PPI to arrive at the contribution to each industry's PPI. For each industry's PPI minus technology, we subtracted the tech contribution from PPI and divided it by one minus technology's weight. Data as at 2005 through 2018. Source: KKR Global Macro & Asset Allocation calculations, Haver Analytics, BEA, BLS, Vanguard.

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Not Surprisingly, The Fed Has Ramped Up Its Effort

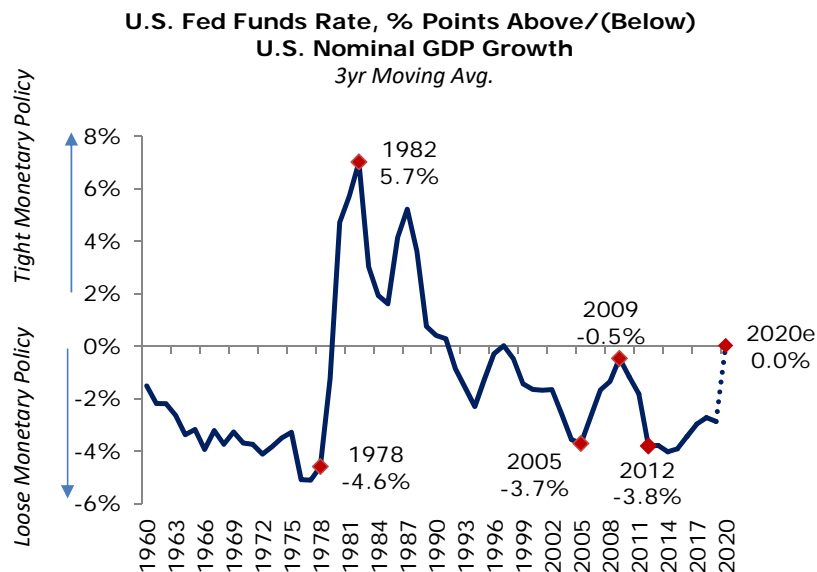
At the annual Jackson Hole summit, held virtually in 2020 in late August, **the Federal Reserve shifted its focus towards “flexible form of average inflation targeting”** from a stated two percent annual inflation rate.

- **The inflation rate has only reached two percent for six months during the last 10 years**, despite the U.S. reaching a generational low in its unemployment rate in 2019.
- **Importantly, though, the new mandate will not rely “on a mathematical formula to equal the average”**, so the Fed has a lot of wiggle room to decipher what average means over the cycle.
- Central bank committee members believe that inflation is so structurally low that this change reflects their belief **“that a robust job market can be sustained without causing an outbreak of inflation.”** This statement is important because it reveals two things.

With Real Rates So Negative, Now Is the Time to Think About Yield, Cash Flow, and Collateral

The Government Has Focused on Stimulating Nominal GDP Through Monetary Policy. This Strategy Makes Us Want to Overweight Cash Flowing Assets with Upfront Yield

Record Stimulus by the Federal Reserve and Treasury Are Finally Lifting Inflation Expectations



Data as at June 30, 2020. Source: BEA, Federal Reserve, Haver Analytics.

Data as at September 3, 2020. Source: Bloomberg.

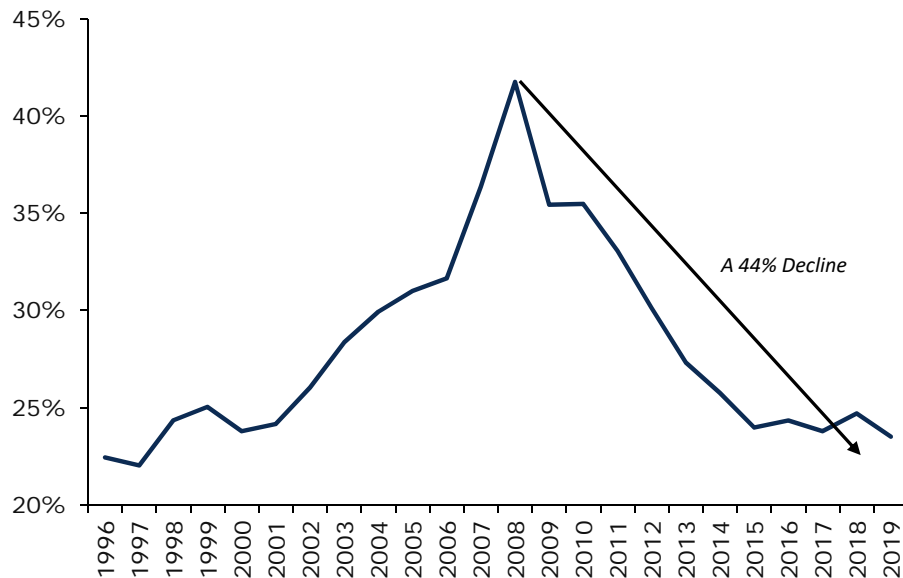
Section IV: China

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How Should We Think About Globalization? Our Message Remains the Same

Cross-Border Capital Flow Trends, a Traditional Proxy for Globalization, Are Reversing as Protectionism Ramps Upwards

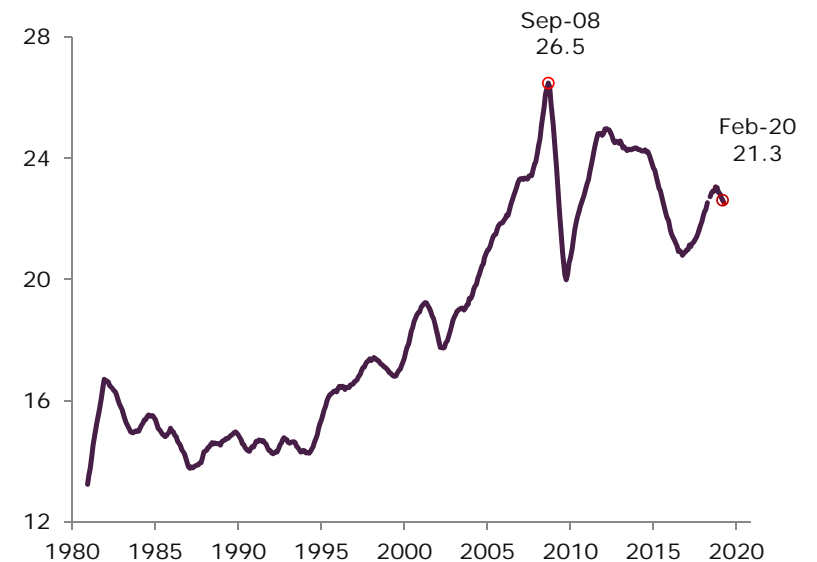
Global Cross Border Bank Lending as a % of GDP



Data as at December 31, 2019. Source: Haver Analytics.

Trade as a Percentage of Global GDP Peaked Several Years Ago

Global Merchandise Exports as a % of Global GDP



Data as at February 28, 2020. Source: IMFWEO, Haver Analytics.

Expect More Internal Consumption (aka Domestic Circulation) Across All of Asia, Not Just China

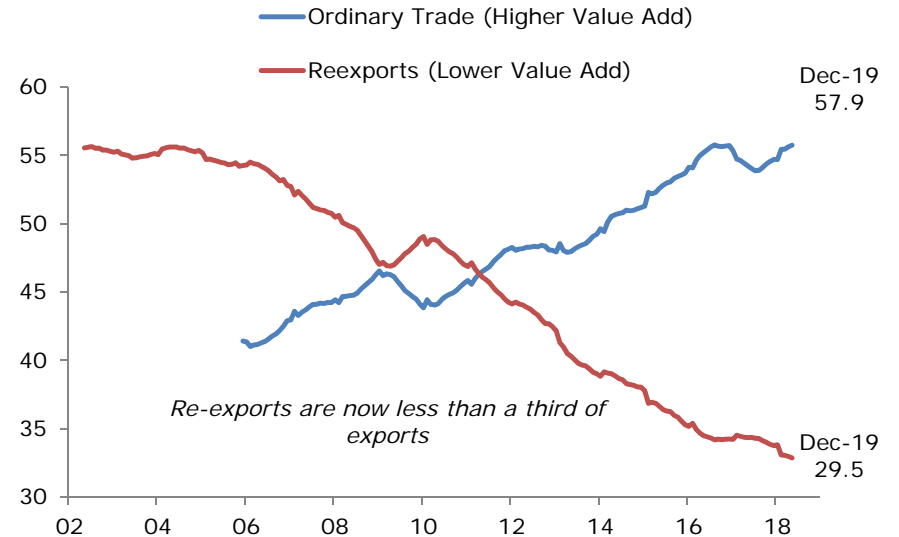
Importantly, Trade Is Becoming a Smaller Part of China's Economy

Trade Continues the Rebalancing Towards Higher Value Added

China: LTM Trade as a % of GDP



China % Total Exports, 12mma



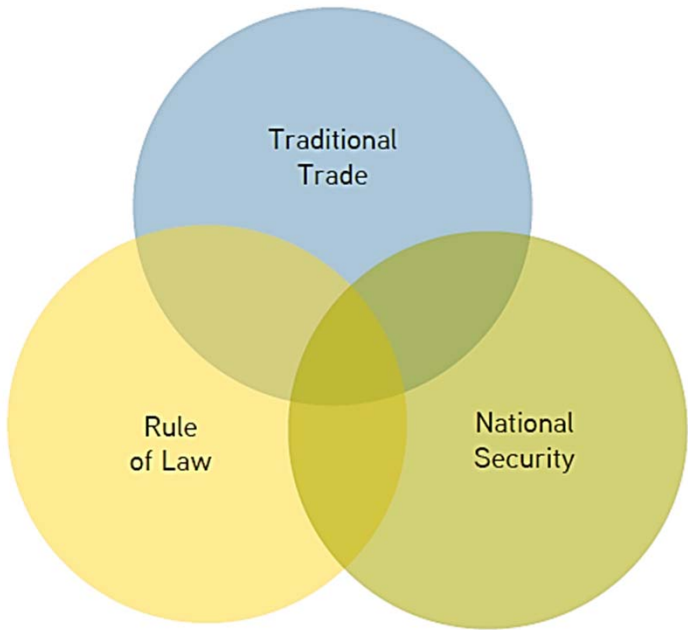
Data as at June 30, 2020. Source: China Customs, Haver Analytics.

Data as at December 31, 2019. Source: China Customs, Haver Analytics.

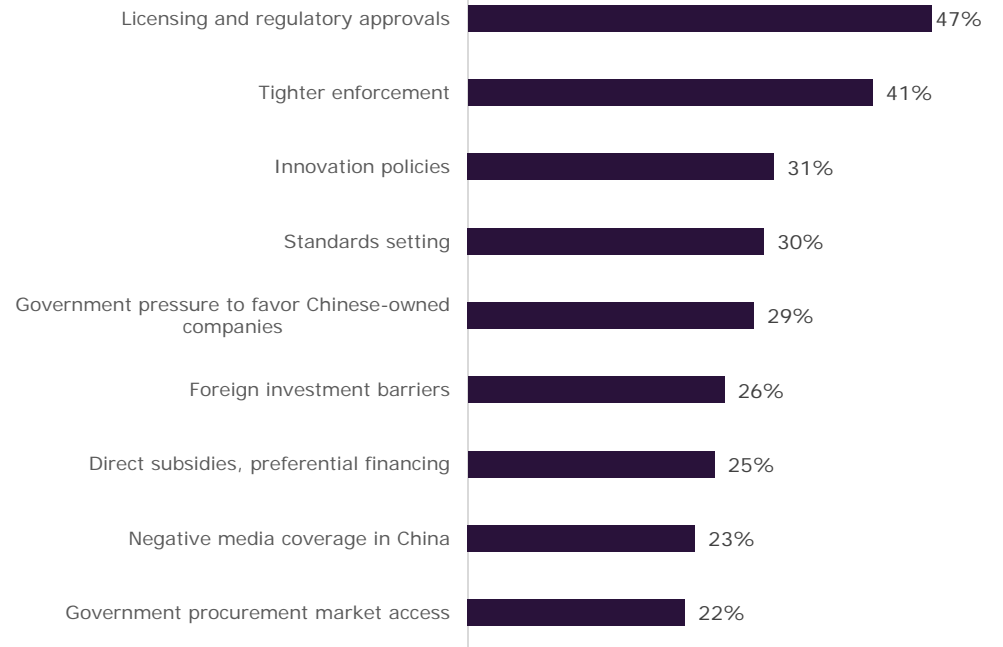
Key Point: Understanding the Nuances of Policy Is Now of Paramount Importance

National Security Is Now Bundled With Rule of Law and Trade Negotiations

Global Multinationals Are Having a Harder Time Navigating the Business Environment in China



What are the most important concerns of operating in China these days?



Data as at May 29, 2019. Source: KKR Global Macro & Asset Allocation analysis.

Data as at June 2019. Source: US China Business Council Member Survey.

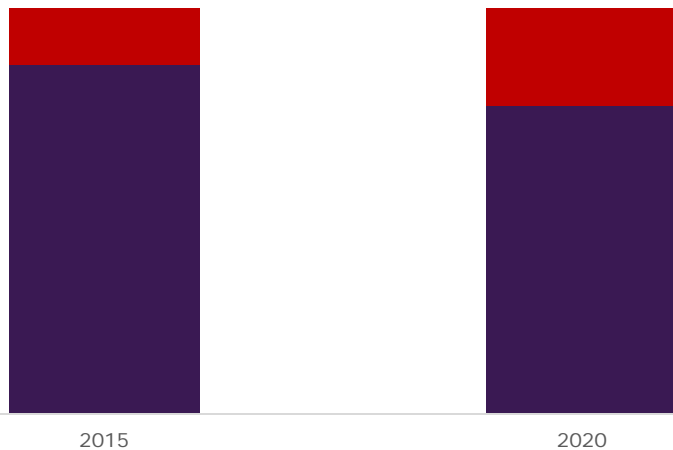
Longer-Term, Global Supply Chains Are Poised to Change

Almost 25% Member Companies Have Reduced Or Stopped Planned Investment in China in the Last Year, A Historic High For This Survey

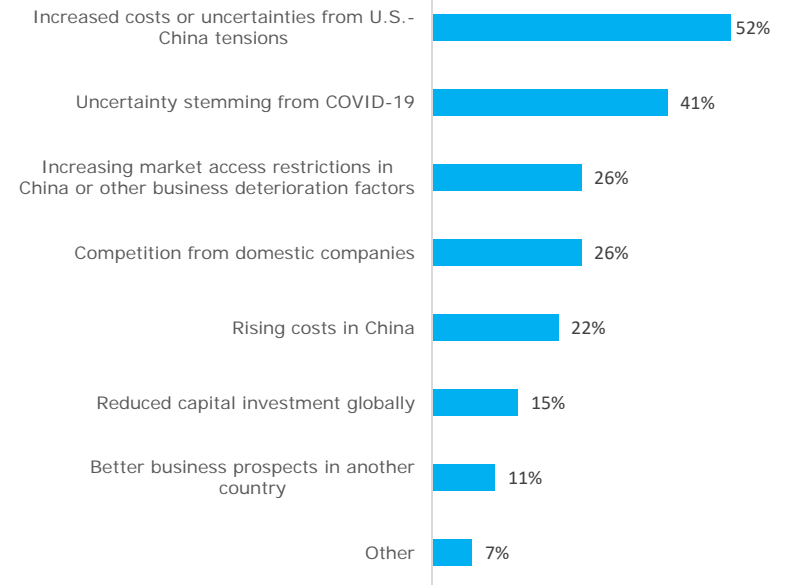
The Top Reasons for Curtailing Investment in China Are Increased Costs or Uncertainties from U.S.-China Tensions and COVID-19

Did Your Company Reduce or Stop Planned Investment in China in the Past Year?

■ No ■ Yes



2020 USCBC Survey: Why Did Your Company Reduce or Stop Planned Investment in China in the Last Year?



Section V: Valuation and Expected Returns

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Under Almost Any Traditional Metric, Equities Appear Fully Valued. However, Interest Rates Do Matter

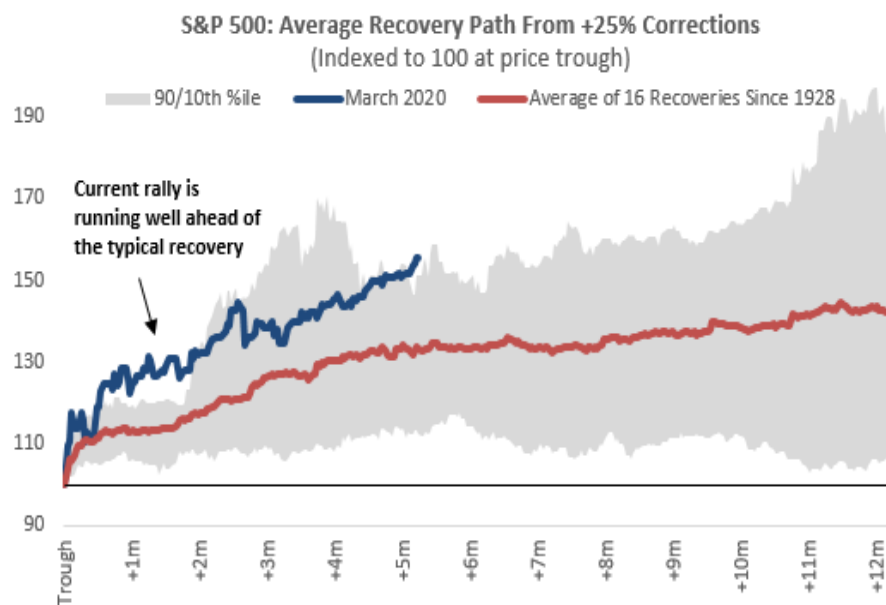
The Market Looks Expensive on All Metrics Except Interest Rate Adjusted Metrics. Importantly, Though, Interest Rates Do Matter

Valuation Metric	S&P 500 Aggregate Index	
	Current	Historical Percentile
U.S. Market Cap/GDP	207%	99%
Forward P/E	23.2x	98%
EV/Sales	2.5x	98%
EV/EBITDA	13.1x	95%
Price/Book	3.4x	87%
Cyclically Adjusted P/E	26.7x	87%
Cash Flow Yield	7.2%	84%
Free Cash Flow Yield	4.2%	50%
Yield Gap vs. 10-Year UST	367 Basis Points	26%
Median Metric		87%

S&P 500 data from 1976 apart from FCF yield which is from 1990. Credit market data from 1997, equity risk premium from 2001 and government bond data from 1921. Data as at June 17, 2020. Source: Goldman Sachs.

Equities Have Run Hard, But the Longer-Term Prospects Remain Solid

Relative to Past Cycles, We Are Now Ahead of Schedule in Terms of the Recovery



Data as at August 27, 2020. Source: Schiller, Haver Analytics, Bloomberg.

Each Recovery Is Different, But Our Work Shows a Lot of the Near-Term Appreciation Has Occurred. However, Longer-Term Investors Should Stay Invested and Add on Pullbacks

Historical S&P 500 Recoveries Following >25% Market Crashes

Trough Date	Initial 6 week Recovery	Return Following Initial 6-Week Recovery				
		+3m	+6m	+12m	+3yr	+3yr Annualized
Nov-29	18.0%	18.1%	(7.0%)	(28.7%)	(68.5%)	(31.9%)
Jun-32	8.9%	43.6%	53.2%	147.4%	121.7%	30.4%
Feb-33	17.7%	82.2%	54.4%	69.3%	136.4%	33.2%
Oct-33	15.1%	8.2%	(1.2%)	(3.7%)	74.4%	20.4%
Mar-35	16.6%	14.1%	31.2%	53.6%	8.6%	2.8%
Mar-38	20.7%	18.6%	34.4%	9.3%	(6.8%)	(2.3%)
Jun-40	11.0%	6.7%	5.4%	4.4%	25.4%	7.8%
Apr-42	11.6%	4.1%	11.5%	45.6%	79.0%	21.4%
Oct-46	0.6%	10.4%	(2.7%)	7.9%	13.6%	4.3%
Jun-62	9.9%	1.5%	15.1%	21.8%	49.7%	14.4%
May-70	5.4%	19.0%	24.9%	37.5%	38.7%	11.5%
Oct-74	15.5%	12.7%	28.3%	26.5%	32.6%	9.8%
Aug-82	20.4%	13.3%	23.9%	37.5%	49.4%	14.3%
Oct-87	3.2%	15.4%	9.2%	18.0%	38.9%	11.6%
Jul-02	12.0%	3.1%	(6.6%)	15.1%	36.3%	10.9%
Nov-08	23.8%	(10.5%)	(0.9%)	19.7%	35.0%	10.5%
Mar-20	28.2%	14.9%				
Geometric Mean	13.0%	14.8%	15.6%	25.4%	31.3%	9.5%
Median	13.5%	13.0%	13.3%	20.7%	37.5%	11.2%
Simple Average	13.2%	16.3%	17.1%	30.0%	41.5%	10.6%

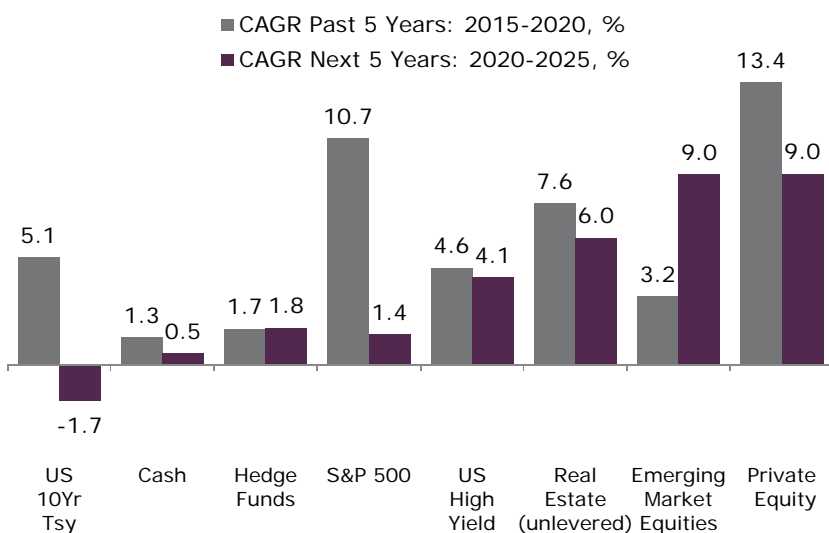
Data as at August 3, 2020. Source: Bloomberg.

A Lower Return Profile for Most Asset Classes on a Go-Forward Basis Will Likely Encourage More, Not Less, Risk Taking

We Generally Look for Lower Returns Across Many of the Asset Classes We Forecast

Our Work Shows That a Traditional 60/40 Portfolio Will Now Struggle to Deliver the Same Returns As in the Past. In Fact, Our Base Case Is Now Below One Percent Compared to 8.5% for the Past Five Years

Expected Returns by Asset Class, %



Return Assumptions	5 Year Outlook			Past 5 Yrs	
	Base	High Growth	Low Growth		
Stocks	1.4%	8.1%	-9.4%	10.7%	
Bonds	-1.7%	-3.5%	0.5%	5.1%	
Allocation		Expected Returns			Past
Stocks	Bond	Base	High Growth	Low Growth	5 Yrs
0%	100%	-1.7%	-3.5%	0.5%	5.1%
10%	90%	-1.4%	-2.3%	-0.5%	5.7%
20%	80%	-1.1%	-1.1%	-1.5%	6.2%
30%	70%	-0.8%	0.0%	-2.5%	6.8%
40%	60%	-0.5%	1.2%	-3.5%	7.3%
50%	50%	-0.1%	2.3%	-4.5%	7.9%
60%	40%	0.2%	3.5%	-5.4%	8.5%
70%	30%	0.5%	4.7%	-6.4%	9.0%
80%	20%	0.8%	5.8%	-7.4%	9.6%
90%	10%	1.1%	7.0%	-8.4%	10.2%
100%	0%	1.4%	8.1%	-9.4%	10.7%

Data as at June 30, 2020. Source: Bloomberg, Haver Analytics, Cambridge Associates, KKR Global Macro & Asset Allocation analysis.

High growth case is when inflation and interest rates rise. Low Growth case is when there is deflation risk and rates fall further or we do QE. Data as at June 30, 2020. Source: Bloomberg, Haver Analytics, Cambridge Associates, KKR Global Macro & Asset Allocation analysis.



Section VI: Conclusions

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Conclusions

- We See a Square Root Recovery, Not a V-Shaped One
- The U.S. Consumer in Aggregate Is in Good Shape, But High Unemployment Weighs on the Fed
- Average Inflation, While Bullish Near-Term, Comes With Some Longer-Term Risks
- U.S.-China Tensions Will Remain Heated, but We Still View Asia as an Opportunity
- We Are at an Inflection Point for 'Traditional' Asset Allocation