

April 1, 2015

Apollo Global Management LLC

Winter Is Coming: Sell APO Into 1Q Earnings

Industry View	Stock Rating	Price Target
In-Line	Underweight	\$23.00

Lowering 1Q divi estimate by 38% to 30c; we're now 38% below consensus. Risk is that dividends may skew towards our bear case in 2015-16 with APO largely through its harvesting mode.

Near-term we see downside risk to APO shares with our 30c dividend estimate in 1Q that is 38% below consensus and 64% lower than 1Q14's 84c div. Our 2015 dividend of 1.96c is 6% below consensus and we see downside risk of ~36c if the cash performance fees held in Fund VI escrow are not released this year (we expect this is released in 4Q15, but if timing is pushed out then our 2015 divi declines to 1.60c which is 23% below consensus). While we see long-term value in APO, given the firm's strong track record of above average market returns, we think the stock will likely underperform peers over the next 12 months due to a declining cash earnings and dividend trajectory. Also see our 1Q Alts preview here: **US Asset Managers: Summer of Realizations: Buy BX and CG into 1Q Earnings (01 Apr 2015)**.

1Q divi expected to be the lowest since 2Q12. If this trend persists, there could be a disconnect between near-term share-price performance and longer-term fundamentals. APO's high dividend yield (9.6% currently on cons 2015 divi) is a core part of the APO investment appeal in the short-term, until the outlook for cash earnings improves after another deployment cycle or incremental scaling of the credit business. We see downside risk to consensus dividend estimates and we're 6% below in 2015 (with downside bias to our estimate) and 13% below in 2016.

No PE Monetizations Announced in 1Q: APO did not announce any PE exits in 1Q in which they can take cash carry. Yes APO exited Sprouts but that's held in the Fund VI escrow which is not released until the portfolio value exceeds 115% of cost (last at 104% in 4Q and likely declines further in 1Q with the Sprouts exit). We're estimating 3c in cash carry for PE in 1Q as we bake in potential dividend recaps in portfolio companies. APO announced sales of Brit Insurance and Great Wolf in 1Q which we estimate could generate 21c of cash carry but we do not expect these to close until 2Q or 3Q.

CNS Monitoring fee expired in 4Q, drops to zero in 1Q: this drives a 29% decline in credit mgmt fee revenues in 1Q15, worth 8c to EPS. We're relatively less concerned about this as it's been expected for some time now and does not impact cash earnings or the dividend... but presents headline risk to reported EPS.

Founder and significant shareholder lock-ups expired March 29, could

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Apollo Global Management LLC (APO.N, APO US)

US Asset Managers / United States of America

Stock Rating	Underweight
Industry View	In-Line
Price target	\$23.00
Shr price, close (Mar 31, 2015)	\$21.60
52-Week Range	\$31.59-20.02

Fiscal Year Ending	12/14	12/15e	12/16e	12/17e
ModelWare EPS (\$)	1.42	1.88	2.15	2.27
Prior ModelWare EPS (\$)	-	1.86	2.07	2.22
P/E	16.6	11.5	10.1	9.5
Consensus EPS (\$) [§]	1.64	2.01	2.25	-
Div yld (%)	12.3	9.1	8.7	8.1

Unless otherwise noted, all metrics are based on Morgan Stanley ModelWare framework
[§] = Consensus data is provided by Thomson Reuters Estimates
e = Morgan Stanley Research estimates

QUARTERLY MODELWARE EPS (\$)

Quarter	2015e		2016e		2016e
	2014	Prior	Current	Prior	
Q1	0.55	0.38	0.36	0.58	0.60
Q2	0.52	0.54	0.56	0.55	0.57
Q3	0.12	0.42	0.43	0.43	0.45
Q4	0.23	0.51	0.53	0.51	0.53

e = Morgan Stanley Research estimates

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potentially see insider share sales post black-out period in May: this is worth 7.6% of sharecount, which could pressure the shares near-term. While it's possible none could sell, history suggests partial selling.

Where we could be wrong: higher than expected divi could be driven by 1) dividend recap that may not be reported in the press/loan data services, for which we pencil in 3c, 2) greater monetization of APO's GP stake in funds beyond the beyond the 4c that we model in 1Q for realized investment income, 3) dividend payout greater than 90% of cash earnings using on-balance sheet cash or funded through debt issuance (which we think is highly unlikely), 4) greater than expected management fee-related earnings which we estimate at 19c pre-tax, 15c after-tax, 5) greater net realized cash performance fees from the credit business which we model at \$50m or 12c pre-tax.

Changes to our Estimates: Lowering 1Q divi by 38% to 30c and lowering 1Q EPS estimate by 7% to 36c. Our 2015-16 dividend estimates decline by 15%/6% to \$1.96/\$1.88 (that's 6%/13% below cons).

Apollo Global Management (APO, \$21.60, Underweight, PT \$23)

Less attractive risk-reward as largely through cash harvesting vs peers; long-term potential in unlocking value from Athene but still early days



Source: Thomson Reuters, Morgan Stanley Research

\$23

Based on DCF and sum-of-the-parts; back into implied multiple

Bull \$32

11.3x 2016e Bull Case EPS

Returns more in-line with historical. Fundraising +50% and deployment +25% above base case; faster Athene asset growth; carry taxed as ordinary income.

Base \$23

10.7x 2016e Base Case EPS

Below historical returns with rising allocations to alternatives: 5% fee-paying AUM CAGR, declining pace of harvesting investments; ramp to full corp. tax rate in 2019-20.

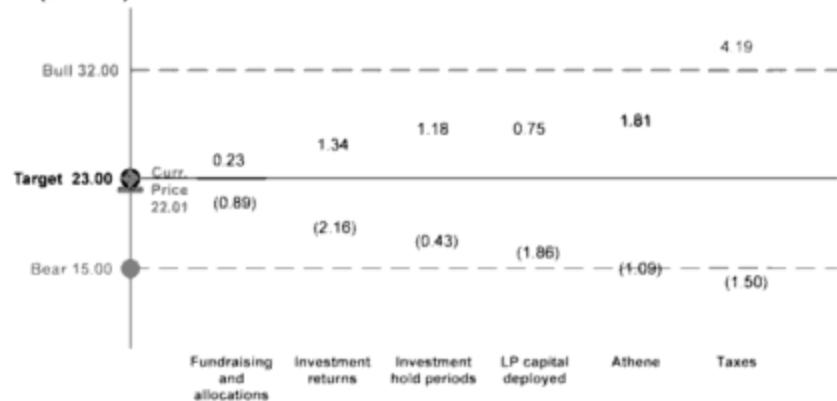
Bear \$15

11.1x 2016e Bear Case EPS

Challenging exit and investing environment: negative near-term marks on accrued performance fees, delayed exits; returns well below historical average, slower capital deployment and weaker fundraising environment; full corp. tax rate in 2018.

Exhibit 1: Bull to Bear Drivers

Impact (\$/share)



Why Underweight?

- **Less upside relative to our Overweight stocks**, driven by Apollo's early cycle skew. We see lower cash earnings over the next several years as APO harvested its investments earlier than peers (80% thru harvesting vs peers at 45-65% thru) which leaves less upside at this point in APO's cycle.
- **Athene catalyst longer tailed** with IPO potentially delayed to 2016 but we would look to get more positive as cash monetization approaches.
- **Expect lower fundraising** at 19% of AUM in 2015-16 vs. peer average of 30%; this drives fee-paying AUM CAGR of 5% in 2014-17 (below peer avg of 11%)
- Founder and significant shareholder lock-ups expire March 29th (worth 7.6% of share count) could weigh on the stock near-term

Key Value Drivers

- **Athene:** IPO as early as 4Q15 but most likely in 2016, resolution of internal control weaknesses, strategic actions should accelerate already strong asset growth; and shifting earnings profile toward fee-related earnings
- **Strategic actions:** including acquisitions to further scale the credit and real estate businesses

Potential Catalysts

- Stronger fundraising
- Continued pace of realizations
- Strategic actions
- Potential share buybacks

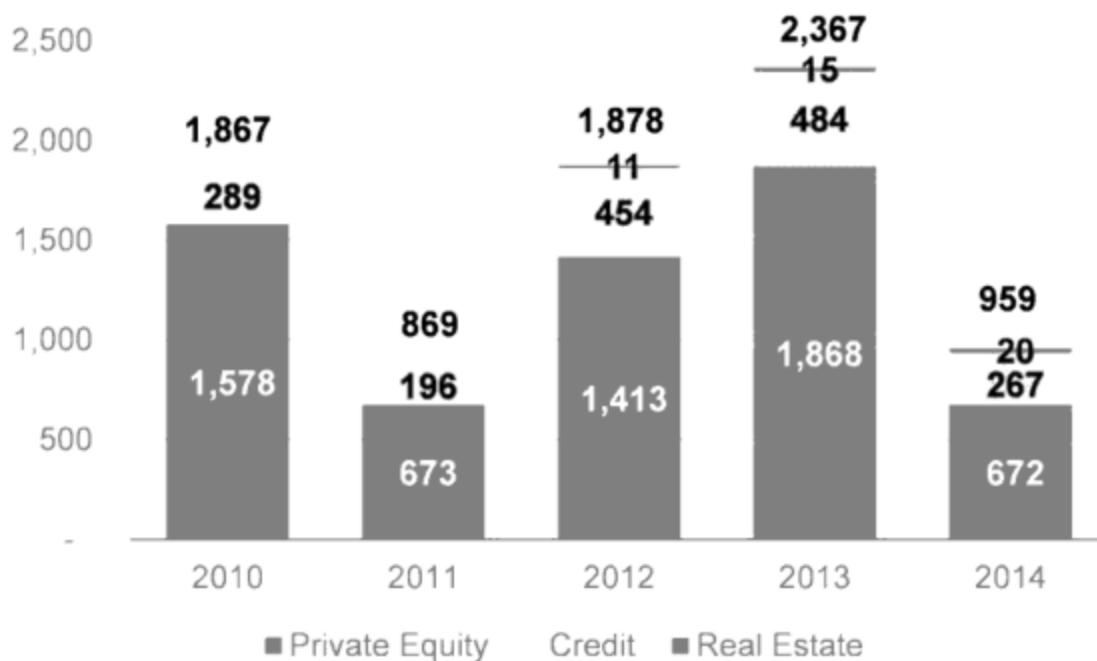
Risks to Our Price Target

- **Upside:** Better FPAuM growth, capital deployment accelerates, better returns
- **Downside:** declining valuations reduce cash earnings (fewer exits or lower multiples); slower deployment

Headwinds for APO

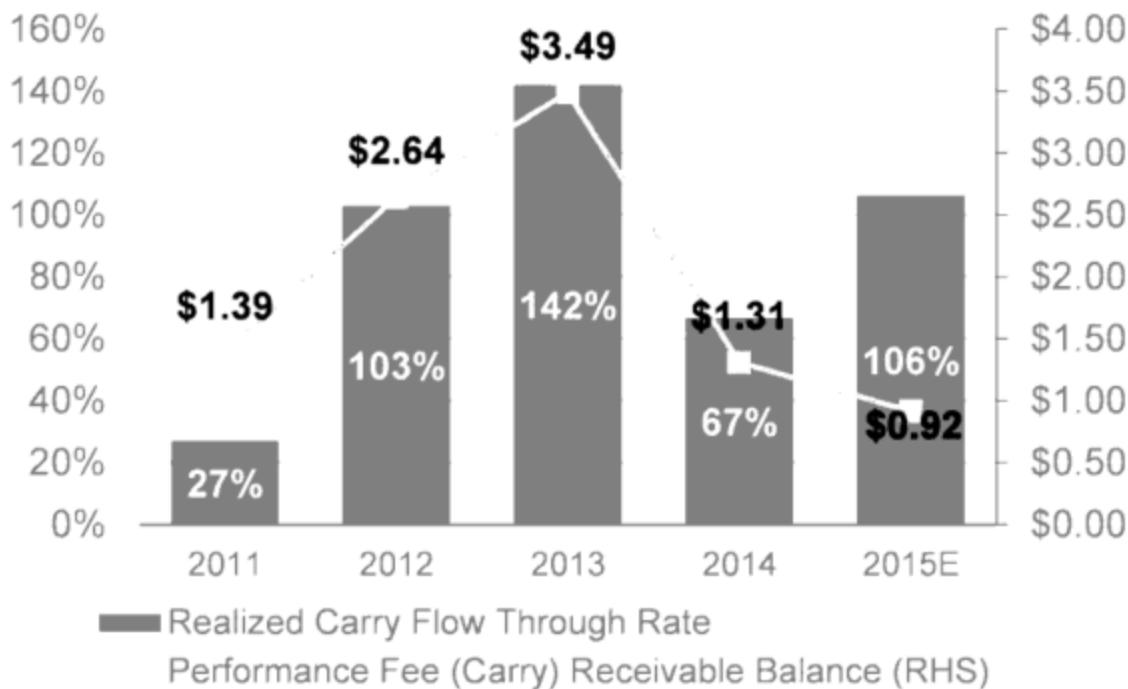
Declining performance fee (carry) receivable balance: this balance sheet receivable represents the amount of performance fees that could be realized in cash if the fund investments were liquidated. During 2014 the balance declined from \$3.49 in 2013 to \$1.31/share with about 70% of the beginning of period balance realized in cash in 2014 worth \$2.33 to cash earnings. A similar 70% realization rate during 2015 would imply cash performance fees of \$0.90 in 2015. This suggests downside risk to our \$1.39 realized cash performance fee estimate (our est implies a 106% realization rate). Deployment in Fund VIII set to pick-up in 2015 (~7% invested and almost 20% committed) but realizations are still a few years away.

Exhibit 2: EOP Gross Performance Fee (Carry) Receivable Balance (\$MM)



Source: Company Data, Morgan Stanley Research

Exhibit 3: EOP Net Performance Fee Receivable Balance Per Share vs. Realized Carry Flow Through Rate



Note: Realized carry flow through rate is calculated as the net realized carry for the period as a % of the BoP net performance fee (carry) receivable balance; Source: Company Data, Morgan Stanley Research

Exhibit 4: Net Performance Fee Receivable Balance Per Share Roll Forward

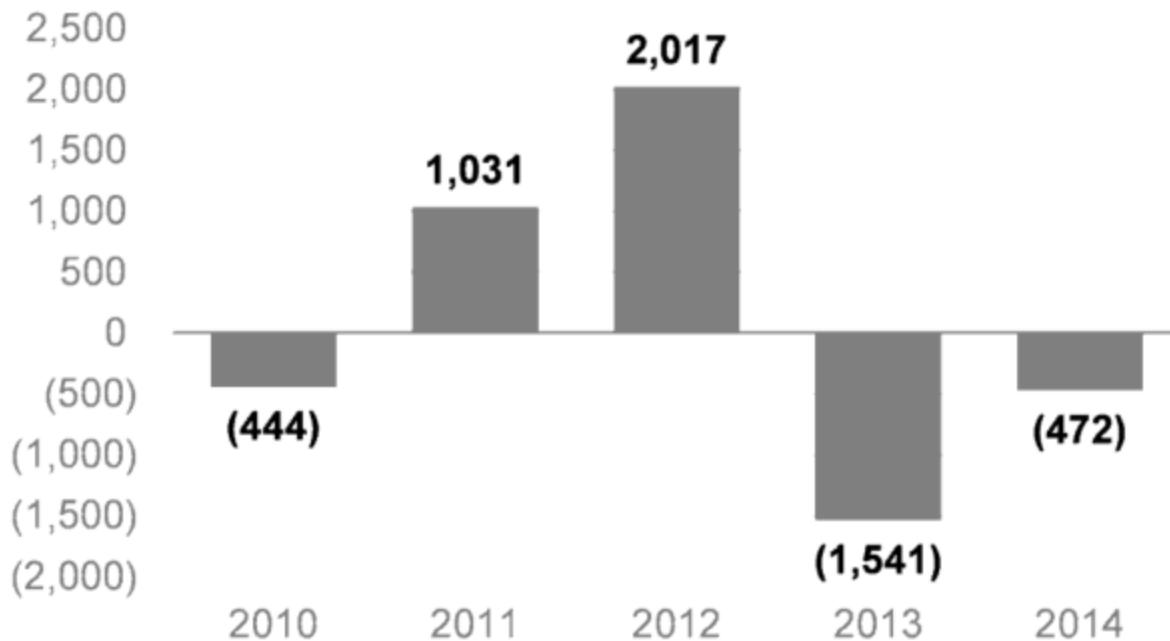
Net Performance Fee (Carry) Receivable Balance Rollforward					
	2011	2012	2013	2014	2015E
BoP	\$3.41	\$1.39	\$2.64	\$3.49	\$1.31
Add: Fund Apprec	(\$1.10)	\$2.68	\$4.60	\$0.15	\$1.00
Less: Realized Gain	(\$0.92)	(\$1.43)	(\$3.75)	(\$2.33)	(\$1.39)
EoP	\$1.39	\$2.64	\$3.49	\$1.31	\$0.92

Flow Through Rate (%): Represents % of BoP Carry Balance that is Realized in Cash					
	2011	2012	2013	2014	2015E
Realized Carry	26.9%	103.0%	142.0%	66.8%	106.2%
Total Carry	-32.3%	193.5%	173.9%	4.3%	76.2%

Note: Realized carry flow through rate is calculated as the net realized carry for the period as a % of the BoP net performance fee (carry) receivable per share balance; Source: Company Data, Morgan Stanley Research

Fee-paying AUM outflows in credit: net outflows to fee-paying AUM in credit of -\$475m in 2014 or -0.5%, improved vs outflows of -\$1.5b in 2013 or -3.1%. In our forward look we expect this stabilizes and build in solid growth from Athene. All in, we're expecting about ~\$13b in gross fee-paying inflows in each 2015-16, and on a net basis (net of outflows) we're expecting net inflows of \$9.2b and \$6.1b in 2015-16. Additionally, we're baking in \$3b of additional sub-advised assets from Athene in each 2015-16. Potential upside to estimates if APO successfully scales the newly announced sub-advised relationship with Oppenheimer, but it's still early days and details of the product remain light (questions around specific type of credit products, liquidity provisions for retail, economics, risk mgmt, etc).

Exhibit 5: Net Organic Fee-Paying AUM Flows in Credit (\$MM)



Note: Net organic flows in credit are calculated by summing the subscriptions/capital raised, distributions and redemptions lines in FPAuM roll forward table; Source: Company Data, Morgan Stanley Research

Founder and significant shareholder lock-ups expire March 29th: this is worth 7.6% of share count which could pressure the shares near-term. While it's possible none could sell, history suggests partial selling.

CNS Monitoring fee expires in 4Q14, drops to zero in 1Q15: We flag as a headline risk given the magnitude with an expected 29% decline in credit management fee revenues in 1Q15. This is worth 8c to 1Q15 EPS. But, we're not as concerned about this falling out of the run rate in 1Q15 because it's been expected for some time now and does not impact cash earnings nor the dividend.

Model Summary

Exhibit 6: APO Model Summary

Apollo Global Management Income Statement (\$MM)							Apollo Global Management % Growth						
	2012	2013	2014	2015E	2016E	2017E		2012	2013	2014	2015E	2016E	2017E
Revenues							Revenues						
Management Fees	773	927	1,217	1,015	1,074	1,113	Management Fees	35.0%	19.9%	37.3%	-16.6%	5.8%	3.8%
Performance Fees	2,291	2,895	407	695	830	909	Performance Fees	-654.0%	31.6%	86.0%	68.7%	21.0%	9.5%
Investment Income	120	102	66	126	154	183	Investment Income	2276.7%	-14.8%	-36.0%	92.7%	21.9%	18.8%
Other Income	21	52	68	12	12	13	Other Income	43.2%	145.9%	29.6%	-82.5%	0.2%	7.4%
Total Revenue	3,116	3,978	1,757	1,839	2,079	2,216	Total Revenue	43.2%	27.7%	-55.8%	4.7%	12.6%	7.1%
Expenses							Pre-tax Income (Economic Income)	644.0%	30.2%	64.0%	12.2%	17.1%	7.3%
Compensation	1,217	1,534	723	697	774	837	Net Income (Economic Net Income, or ENI)	558.9%	34.1%	77.7%	34.5%	16.8%	7.5%
Non-Compensation	257	302	266	274	293	292	EPS	-541.7%	31.4%	-77.7%	32.1%	14.5%	5.5%
Total Expenses	1,473	1,836	969	972	1,056	1,129	Average Diluted Share Count	3.9%	2.1%	1.5%	1.8%	2.0%	2.0%
Pre-tax Income (Economic Income)	1,634	2,128	756	856	1,002	1,076	Dividends Per Share	73.2%	103.3%	-26.7%	-32.2%	-4.2%	-6.3%
Tax Rate	10%	7%	25%	17%	15%	11%	Cash Earnings Per Share (DE Per Unit)	93.4%	119.6%	-30.1%	-30.4%	-4.2%	-6.3%
Tax Expense	159	149	168	92	110	116							
Net Income (Economic Net Income, or ENI)	1,475	1,979	546	764	883	960							
EPS	\$ 3.82	\$ 5.03	\$ 1.42	\$ 1.88	\$ 2.15	\$ 2.27							
Average Diluted Share Count	386	394	400	407	415	424							
Dividends Per Share	\$ 1.94	\$ 3.94	\$ 2.89	\$ 1.96	\$ 1.88	\$ 1.76							
Cash Earnings Per Share (DE Per Unit)	\$ 2.04	\$ 4.48	\$ 3.13	\$ 2.18	\$ 2.09	\$ 1.96							
Pre-tax Income													
FRE (Mgmt Business)	223	331	578	359	396	414							
Net performance fees (Incentive Business)	1,411	1,797	178	497	606	662							
Investment income	-	-	-	-	-	-							
After-tax Income Per Share													
FRE	\$ 0.38	\$ 0.58	\$ 1.01	\$ 0.71	\$ 0.76	\$ 0.78							
Net Performance Fees	\$ 3.44	\$ 4.44	\$ 0.41	\$ 1.17	\$ 1.39	\$ 1.48							
Core Investment Income	\$ -	\$ -	\$ -	\$ -	\$ -	\$ -							
EPS	\$ 3.82	\$ 5.02	\$ 1.42	\$ 1.88	\$ 2.15	\$ 2.27							
Balance Sheet (\$MM)	2012	2013	2014	2015E	2016E	2017E							
Cash	946	1,078	1,204	1,494	1,956	3,083							
Investments	466	510	857	1,076	1,211	1,419							
Other	3,044	3,626	2,116	1,890	1,870	2,056							
Total Assets	4,456	5,214	4,176	4,460	5,038	6,558							
Debt	738	750	1,034	1,016	1,016	1,016							
Other	1,719	2,006	1,344	982	731	1,374							
Total Liabilities	2,456	2,756	2,379	1,986	1,767	2,390							
Total Equity	2,002	2,457	1,799	2,461	3,371	4,168							
Leverage Ratios													
EBITDA / Interest Expense	23.4	64.9	64.8	41.0	40.8	38.9							
Debt / equity	0.37x	0.31x	0.57x	0.41x	0.31x	0.24x							
Cash Earnings Walk (\$MM)	2012	2013	2014	2015E	2016E	2017E							
Pre-Tax Income (Economic net income)	1,634	2,128	756	856	1,002	1,076							
Less: Net performance fees	(1,291)	(1,566)	(89)	(370)	(452)	(479)							
Less: Investment income (loss)	(120)	(102)	(66)	(126)	(154)	(183)							
Less: Other income	-	(9)	(23)	-	-	-							
Fee related earnings (APO Method)	223	331	578	359	396	414							
Add: Realized perf fees, net of related comp	552	1,479	931	567	538	467							
Add: Investment income (loss) realized	-	108	64	62	47	47							
Less: Athene capital and surplus fees	-	(110)	(228)	-	-	-							
Add: Equity-based comp (non-cash item)	69	66	107	72	72	76							
Add: Dep and amt (non-cash item)	10	11	10	10	10	10							
Add: Other	(21)	(13)	(32)	-	-	-							
Cash Earnings (DE) (pre-tax)	\$ 633	\$ 1,871	\$ 1,436	\$ 1,079	\$ 1,064	\$ 1,014							
Add: Interest expense	37	29	22	27	27	27							
Total EBITDA (Excludes MTM Gains)	870	1,901	1,462	1,097	1,090	1,040							
Less: Realized Net perf fees and inv income	(552)	(1,566)	(995)	(629)	(585)	(514)							
Fee and Yield EBITDA (ex eqty-based comp)	318	314	457	460	505	527							
Cash Earnings Per Share to Public Fleet													
Net FRE	\$ 0.66	\$ 0.50	\$ 0.67	\$ 0.76	\$ 0.82	\$ 0.86							
Net realized cash carry	\$ 1.36	\$ 3.71	\$ 2.29	\$ 1.27	\$ 1.17	\$ 0.99							
Realized investment income	\$ -	\$ 0.27	\$ 0.16	\$ 0.14	\$ 0.10	\$ 0.10							
Performance													
Mkt Appreciation / Bp ALM ex Dry Powder	17.8%	18.5%	2.0%	7.1%	5.5%	5.2%							
PE Appreciation	39.2%	41.2%	2.6%	14.5%	15.9%	16.5%							
RE Appreciation	3.6%	1.4%	-0.7%	8.3%	8.5%	23.0%							
Credit Carry Fund Appreciation	30.7%	8.8%	2.6%	7.6%	8.8%	7.9%							

Source: Company Data, Morgan Stanley Research

Valuation and Risks

Alternative Asset Managers: We value the stocks using a sum of the parts valuation supported by a discounted cash flow. Our DCF (COE of 11–14%, free cash flow = distributable earnings, terminal growth rate = 3% and betas benchmarked off BX's 1.6x) captures the long-term value of the business model, while the sum of the parts captures some of the shorter-term volatility. For our SOTP, we use 2016 "Core" FRE and apply a 15x multiple which is a 1-2 turn premium to传统s reflecting value in long term locked up capital; apply 12x multiple on BDC income share; use DCF to estimate future carry and apply discount rate to represent volatile nature of carry; 10% haircut on accrued carry; 10% haircut on B/S assets.

Apollo Global Management: Upside risks include better FPAuM growth, accelerated capital deployment, and better returns. Downside risks: declining valuations reduce cash earnings (fewer exits or lower multiples); slower deployment.

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(as of March 31, 2015)

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Equal-weight and Not-Rated to hold and Underweight to sell recommendations, respectively.

STOCK RATING CATEGORY	COVERAGE UNIVERSE		INVESTMENT BANKING CLIENTS (IBC)		
	COUNT	% OF TOTAL	COUNT	% OF TOTAL	% OF RATING CATEGORY
Overweight/Buy	1164	35%	331	43%	28%
Equal-weight/Hold	1466	44%	353	46%	24%
Not-Rated/Hold	100	3%	11	1%	11%
Underweight/Sell	605	18%	80	10%	13%
TOTAL	3,335		775		

Data include common stock and ADRs currently assigned ratings. Investment Banking Clients are companies from whom Morgan Stanley received investment banking compensation in the last 12 months.

Analyst Stock Ratings

Overweight (O). The stock's total return is expected to exceed the average total return of the analyst's industry (or industry team's) coverage universe, on a risk-adjusted basis, over the next 12-18 months.

Equal-weight (E). The stock's total return is expected to be in line with the average total return of the analyst's industry (or industry team's) coverage universe, on a risk-adjusted basis, over the next 12-18 months.

Not-Rated (NR). Currently the analyst does not have adequate conviction about the stock's total return relative to the average total return of the analyst's industry (or industry team's) coverage universe, on a risk-adjusted basis, over the next 12-18 months.

Underweight (U). The stock's total return is expected to be below the average total return of the analyst's industry (or industry team's) coverage universe, on a risk-adjusted basis, over the next 12-18 months.

Unless otherwise specified, the time frame for price targets included in Morgan Stanley Research is 12 to 18 months.

Analyst Industry Views

Attractive (A): The analyst expects the performance of his or her industry coverage universe over the next 12-18 months to be attractive vs. the relevant broad market benchmark, as indicated below.

In-Line (I): The analyst expects the performance of his or her industry coverage universe over the next 12-18 months to be in line with the relevant broad market benchmark, as indicated below.

Cautious (C): The analyst views the performance of his or her industry coverage universe over the next 12-18 months with caution vs. the relevant broad market benchmark, as indicated below.

Benchmarks for each region are as follows: North America - S&P 500; Latin America - relevant MSCI country index or MSCI Latin America Index; Europe - MSCI Europe; Japan - TOPIX; Asia - relevant MSCI country index or MSCI sub-regional index or MSCI AC Asia Pacific ex Japan Index.

Stock Price, Price Target and Rating History (See Rating Definitions)



Stock Rating History: 3/1/12 : NA/I; 9/11/13 : O/I; 11/8/13 : E/I; 1/16/14 : NA/I; 2/26/14 : E/I; 5/12/14 : NA/I; 12/15/14 : U/I

Price Target History: 9/11/13 : 33; 11/13/13 : 34; 1/16/14 : NA; 2/26/14 : 34; 5/12/14 : NA; 12/15/14 : 24; 3/12/15 : 23

Source: Morgan Stanley Research Date Format : MM/DD/YY Price Target -- No Price Target Assigned (NA)
Stock Price (Not Covered by Current Analyst) Stock Price (Covered by Current Analyst) --
Stock and Industry Ratings (abbreviations below) appear as * Stock Rating/Industry View
Stock Ratings: Overweight (O) Equal-weight (E) Underweight (U) Not-Rated (NR) No Rating Available (NA)
Industry View: Attractive (A) In-line (I) Cautious (C) No Rating (NR)

Effective January 10, 2014, the stocks covered by Morgan Stanley Asia Pacific will be rated relative to the analyst's industry (or industry team's) coverage.

Effective January 10, 2014, the industry view benchmarks for Morgan Stanley Asia Pacific are as follows: relevant MSCI country index or MSCI sub-regional index or MSCI AC Asia Pacific ex Japan Index.

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INDUSTRY COVERAGE: US Asset Managers

COMPANY (TICKER)	RATING (AS OF)	PRICE* (03/31/2015)
Cyprys CFA, CPA, Michael J.		
Apollo Global Management LLC (APO.N)	U (12/15/2014)	\$21.60
Ares Management, L.P. (ARES.N)	E (12/15/2014)	\$18.54
KKR & CO. L.P. (KKR.N)	O (12/15/2014)	\$22.81
Oaktree Capital Group, LLC (OAK.N)	O (12/15/2014)	\$51.66
The Blackstone Group L.P. (BX.N)	O (12/15/2014)	\$38.89
The Carlyle Group L.P. (CG.O)	E (12/15/2014)	\$27.10
Graseck CFA, Betsy L.		
BlackRock Inc. (BLK.N)	O (05/12/2014)	\$365.84
Franklin Resources Inc. (BEN.N)	E (05/12/2014)	\$51.32
Invesco (IVZ.N)	E (05/12/2014)	\$39.69
QMA Asset Management Plc (QMA.MN)	O (11/18/2014)	\$18.64
T. Rowe Price Group, Inc. (TROW.O)	E (05/12/2014)	\$80.98
Whitehead CFA, Thomas		
AllianceBernstein Holding L.P. (AB.N)	E (05/12/2014)	\$30.87
Federated Investors, Inc. (FI.I.N)	U (05/12/2014)	\$33.89
Janus Capital Group Inc. (JNS.N)	E (09/29/2014)	\$17.19
Legg Mason Inc. (LMN)	E (05/12/2014)	\$55.20
LPL Investment Holdings Inc. (LPLA.O)	E (05/12/2014)	\$43.86
Virtus Investment Partners Inc. (VRTS.O)	E (05/12/2014)	\$130.77
Waddell & Reed Financial Inc (WDR.N)	E (05/12/2014)	\$49.54
WisdomTree Investments, Inc. (WETF.O)	O (06/09/2014)	\$21.46

Stock Ratings are subject to change. Please see latest research for each company.

* Historical prices are not split adjusted.