

## — PARTICIPANTS

### Corporate Participants

**Dan F. Harris** – Managing Director, The Carlyle Group LP (Corporate Private Equity)

**David M. Rubenstein** – Co-Chief Executive Officer, Co-founder Washington, DC

**William E. Conway** – Co-Chief Executive Officer, Co-founder Washington, DC

**Adena T. Friedman** – Chief Financial Officer, Managing Director Washington, DC

### Other Participants

**Howard H. Chen** – Analyst, Credit Suisse Securities (USA) LLC (Broker)

**Kenneth B. Worthington** – Analyst, JPMorgan Securities LLC

**Robert Lee** – Analyst, Keefe, Bruyette & Woods, Inc.

**Marc S. Irizarry** – Analyst, Goldman Sachs & Co.

## — MANAGEMENT DISCUSSION SECTION

Operator: Good day, ladies and gentlemen. Welcome to The Carlyle Group Third Quarter 2012 Results Conference Call. At this time, all participants are in a listen-only mode. Later, we will conduct a question-and-answer session and instructions will follow at that time. [Operator Instructions] As a reminder, this conference is being recorded.

I would now like to turn the conference over to today's host, Daniel Harris. Sir, you may begin.

### **Dan F. Harris, Managing Director, The Carlyle Group LP (Corporate Private Equity)**

Thank you. Good morning and welcome to Carlyle's third-quarter 2012 earnings call. My name is Dan Harris and I'm the Head of Public Market Investor Relations at Carlyle. With me on the call today are our Co-Chief Executive Officers, Bill Conway and David Rubenstein; and our Chief Financial Officer, Adena Friedman.

If you have not received or seen the earnings release, which we published this morning detailing our third-quarter results, it is available on the Investor Relations portion of our website or on Form 8-K filed with the Securities and Exchange Commission. Following our prepared remarks, we will hold the question-and-answer session for analysts and institutional unitholders. This call is being webcast and a replay will be available on our website immediately following the conclusion of today's call.

We will refer to certain non-GAAP financial measures in today's remarks, including distributable earnings, economic net income and fee-related earnings. These measures should not be considered in isolation from or as a substitute for measures prepared in accordance with generally accepted accounting principles. Reconciliation of these non-GAAP financial measures to the most comparable measures calculated and presented in accordance with GAAP are included in our earnings release.

Please note that any forward-looking statements provided today do not guarantee future performance and undue reliance should not be placed on them. These statements are based on current management expectations and involve inherent risks and uncertainties that could cause actual results to differ materially from those indicated including those identified in the Risk Factor

section of our registration statements on Form S-1 and such factors may be updated from time to time in our SEC filings. Carlyle assumes no obligation to update any forward-looking statements.

With that, let me turn it over to our Co-Chief Executive Officer, David Rubenstein.

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**David M. Rubenstein, Co-Chief Executive Officer, Co-founder Washington, DC**

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Good morning and thank you for joining us today. I'm pleased to report that Carlyle had a very strong quarter. We continue to see attractive opportunities for investments by and distributions from our funds. During the third quarter, we announced or completed a large number of what we believe will be highly attractive investments. We saw valuations increase appreciably. We continued our industry-leading pace of realizations and distributions and we continued our strong fund-raising pace. And thus, we are very pleased with the quarter's results, but our performance should always be viewed over the long term at a minimum on a rolling 12-month basis.

With this type of long-term perspective in mind, we should also note that we are quite pleased with our year-to-date results. During our remarks, as we have done each quarter, we will focus on the underlying activities that drive distributable earnings, which we've always viewed and continue to view as the most important metric by which to evaluate the current and future strength of our business.

I say current metric, because distributable earnings clearly show the results of our recent investment performance. And I say future metric, because current distributable earnings reflect profitable realizations for our fund investors. And when these investors receive distributions, they tend to reinvest with us. And by doing so, they restart the cycle, enabling us to invest, create value and distribute more to our investors. In turn, we can produce distributable earnings to our unitholders.

Of course, we cannot guarantee that our having significant amounts of capital to invest will always produce an attractive level of distributions to our investors and then to our unitholders. But we believe our ability to produce strong and consistent distributions is second to none in our industry and we remain confident in our ability to continue this record into the future.

In sum, we focus on our ability to make attractive distribution to our investors and in turn to our unitholders and we believe our record in being able to do so is the best metric by which to judge our current and our future performance.

Now, let me turn to a few highlights. First, our year-to-date pre-tax distributable earnings on a pro forma basis are \$512 million with \$206 million generated in the third quarter. We continue to be pleased with our cash earnings performance.

Second, we announced a quarterly distribution of \$0.16 per common unit. Year-to-date, our pro forma post-tax distributable earnings per common unit are \$1.52 and distributable earnings per common unit, since we priced our IPO on May the 2nd, are \$0.91. While we don't know precisely how we will perform during the fourth quarter, we are optimistic that we'll be able to deliver an attractive year-end catch-up distribution.

Third, we have now invested \$4.6 billion in equity across our carry funds year-to-date, including \$1.6 billion equity in the third quarter. We announced additional transactions during the third quarter with more than \$4 billion in new equity commitments, which should close in the fourth quarter or early in 2013.

Fourth, as previously disclosed, our overall carry fund portfolio has appreciated 11% since the end of 2011, 18% in the last 12 months and 3% in the third quarter. We saw particularly strong appreciation in our U.S. buyout funds.

Fifth, we have realized \$11.9 billion in net proceeds for our fund investors so far this year, including a very strong \$5.1 billion in this quarter, arising from 117 investments across 34 carry funds. We expect that our diverse portfolio investments, with varying maturities, will continue to produce solid distributions to fund investors in the years ahead.

Sixth, as we have discussed and anticipated in last quarter's call, our fundraising continues to be strong in a challenging market. During the quarter, we closed on \$3.4 billion in new commitments for our carry funds, our hedge funds and new CLO, bringing our year-to-date total of new commitments for our funds to \$9.4 billion. Over the last 12 months, we have raised \$10.8 billion in new capital commitments.

I wanted to take a moment now to highlight the continued growth of our Global Market Strategies business. As I mentioned last quarter, investors continue to be in search of yield and we've continued to expand our GMS product offerings in response to investor demand. For example, during the quarter, we closed a \$615 million CLO, our third new-issue CLO of the year. At the end of the third quarter, we managed nearly \$17 billion in CLOs.

In early October, we announced the purchase of a 55% stake in Vermillion Asset Management, a commodities investment manager with \$2.2 billion of assets under management across three strategies. We can now offer our limited partners the differentiated opportunity to invest directly in various commodity strategies, as well as to provide exposure to the agriculture, energy and infrastructure sectors in our carry funds.

We believe by combining Carlyle's expertise in global platform with the experience of direct trading strategies employed by Vermillion, we'll provide our fund investors with new opportunities to allocate capital to more liquid commodity strategies. With the addition of Vermillion, our hedge fund partnerships will have total AUM of \$12 billion across three distinct strategies, long/short credit through Claren Road Asset Management, emerging market opportunities through the Emerging Sovereign Group and now commodity strategies through Vermillion.

In the past two years, through a combination of organic growth and bolt-on acquisitions, AUM and our GMS platform, including the recent acquisition of a 55% interest in Vermillion, has increased more than 2.5 times from \$12 billion to over \$32 billion and GMS is now a significant contributor to the firm's overall asset base and earnings. We will continue to search for avenues of growth in this segment.

Moving on, I wanted to remind everyone that we believe we have four drivers of our business at Carlyle, fundraising, investing, appreciating the value of the portfolio and exiting. Collectively, we call these drivers the Carlyle engine. I would like to address in most of my remaining comments the fundraising element of this engine.

Despite the fact that large parts of the world experienced economic slowdown over the summer, we raised \$3.4 billion during the quarter, bringing our total of new capital raised to \$9.4 billion for the year. This figure compares favorably to the \$6.7 billion we raised during all of 2011 and we expect additional new commitments in the fourth quarter.

In other words, we have raised 40% more in the first three quarters of 2012 than we did in all of 2011. For this reason, we are pleased with the fundraising year-to-date, particularly considering the challenging fundraising market that we have discussed on previous calls.

Let me provide some additional color on our current fundraising efforts. First, we have had subsequent closings in our latest U.S. buyout fund, Carlyle Partners VI, in our Energy Mezzanine Fund, in our distress fund and in our Real Estate Credit Fund. And, yesterday, we had a final closing of \$1.1 billion for our mid-market U.S. buyout fund, Carlyle Equity Opportunity Fund. We expect the final close this year as well on Carlyle Energy Mezzanine Fund.

Like Carlyle Equity Opportunity Fund, the Energy Mezzanine Fund will exceed \$1 billion in size. For both of these funds, we exceeded our fundraising target and we also brought into our investor base a good many investors new to Carlyle.

Second, Carlyle Partners VI, our flagship U.S. buyout fund, is the fund about which we are asked the most for it is our largest fund in the market. It is targeted at \$10 billion. We are on pace to achieve our size, goal and also to do so on the schedule we set out for this fund. Third, we continue to see robust inflows into our hedge fund strategies. We had approximately \$380 million in new net subscriptions in the quarter for our hedge funds and we've seen \$1.7 billion in new net subscriptions year-to-date.

Fourth, we expect to have a first closing on our fourth Asian buyout fund before the end of the year and have a number of new funds, which will start fundraising late this year or early in 2013. And fifth, we have recently started to gain traction within our Alpinvest fund of funds business on raising capital for our new commingled secondaries fund.

One last anecdotal comment on fundraising, in September, we held our Annual Washington Investor Conference for our fund investors. Nearly 700 investors participated from around the world. This is the largest such gathering organized by an alternative investment management firm for its investors every year. This was our 18th year holding such an investor conference.

Bill Conway and I, along with our Chairman, Dan D'Aniello, have attended all 18 of these conferences. For the first time since the Great Recession began, we collectively sense this year a real uptick in the interest level of our fund investors in committing capital to alternative investments and perhaps more importantly to our alternative products. And since the conference, we have in fact seen real follow-up with our investors on a great many of our funds. We firmly believe additional commitments will follow, but of course only time will tell.

Let me close with brief comments on Hurricane Sandy and its impact on Carlyle and then on to the election and its impact on private equity. Like other U.S. companies, we have been very engaged in monitoring the impact of Hurricane Sandy on our business. Of course, our first priority has been the safety and security of our employees and those of our portfolio companies. While a number of our employees experienced hardship, associated with lack of power, water or access to communications, thankfully none experienced serious injury.

I'm also pleased to let you know that none of our companies reported any substantial damage to their facilities, properties or operations. Like others, some of our companies have experienced power failures and logistical challenges at certain sites related to the storm and certain of our companies will undoubtedly report slower sales for a few days related to the storm.

Other parts of our business, particularly those companies involved in infrastructure, construction and logistics could well see increased business activity in the short-term, associated with the rebuilding. Fortunately, as a global firm, with a highly diverse set of funds and investments, we do not believe the hurricane will have any meaningful impact on our firm's overall performance.

Now the election, today in a nutshell, let us just say that we do not believe that the election will produce impactful changes on Carlyle or in the private equity world in the near-term, but as an American citizen, we hope, of course, that the U.S. government will begin to address seriously the mounting fiscal and financial issues facing the country.

As a result of the election, as we all know, we have the same President as we have before and each house of Congress is controlled by the same party as before though in slightly different percentages. Overall, this is not seen to be a formula for rapid resolution on key issues facing the country, but hopefully some real progress will be made.

The lame duck session in December will focus on fiscal cliff issues and while Carlyle, like all companies, would like to see a satisfactory resolution of fiscal cliff issues. We do not believe any such resolution will focus on private equity in any specific way nor do we believe anything likely to happen in the lame duck will impact private equity or Carlyle in anyway, which was disproportionate to the way it will affect any other type of company in the country.

After the lame duck, we expect that comprehensive tax reform will likely be on the agenda of the new Congress and the President. However, we expect that any comprehensive reform will take at least two years. In the context of this reform, carried interest taxation and a great variety of other issues will no doubt be addressed, but our best judgment and information about what will happen on carried interest taxation does not yet enable us to say how this or any other issue of interest to firms like ours will ultimately be resolved. Perhaps in a few months or sometime in the next Congress, greater clarity on these issues will be possible.

Let me now turn it over Bill Conway. Bill?

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**William E. Conway, Co-Chief Executive Officer, Co-founder Washington, DC**

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Thank you, David. I'd like to start by offering a few thoughts on the overall economic environment and then move to our new investments, the state of our portfolio and our recent exit activity. As you know, we collect and analyze data from our 200-plus portfolio companies, providing us insight into the state of the global economy.

In the United States, the economy continues to expand at a stable, yet unsatisfyingly slow rate. We are seeing some interesting trends. Capital spending and industrial production declined in the third quarter, showing continued caution by corporate management teams, who have taken action to reduce inventories and limit unused capacity. In contrast, we have seen a notable acceleration in fixed residential investment and stronger than expected household spending.

We remain cautiously optimistic that the combination of very low interest rates, the strengthening housing market and the benefits of significant domestic energy discoveries will provide a catalyst for stronger U.S. economic growth over the medium term. The trajectory of our internal data on Europe changed during the quarter. Rather than steep declines has had been the case for most of 2012, recent data suggest signs of stabilization. One of our proprietary European indicators, which accurately predicted about five months in advance the European contraction that began in October 2011, is currently showing signs of modest growth.

Conditions remain challenging, but our recent data are more favorable than what you read about in the headlines. To be clear, we aren't seeing strong evidence of a recovery, but European economies are not falling off the cliff, rather we believe we're witnessing a mild contraction.

Our perspective on China has not changed materially since the second quarter. Incoming data had been volatile with months of apparent stabilization followed by periods of renewed deceleration. We believe it is better to focus on longer-term trends.

China is experiencing two secular shifts. First, it is moving from an export oriented economy heavy on infrastructure investment to an economy where domestic final sales will make a progressively larger contribution of growth. Second, it is adjusting to a slower long-term rate of growth. Thus,

we're observing uneven performance in different sectors. Some have slowed; some are contracting; others continue to grow rapidly.

Elsewhere in the world, we see surprisingly rapid growth in household spending in Brazil, but in Japan, we are seeing a worrying decline in industrial output. We're monitoring Japan closely to determine whether the decline is limited to Japan or has broader implications. Keep in mind that the economic environment is not the same as the investment environment. In fact, we think this is a great investment in which to invest on a very disciplined basis even with weak and mixed macro growth signals.

In the third quarter, we invested \$1.6 billion in 86 new and follow-on transactions in 16 countries across 24 distinct carry funds. In addition, we announced, but had not yet closed as of September 30, 10 transactions in four countries with over \$4 billion in additional equity commitments across seven distinct carry funds. We expect these transactions to close in the fourth quarter or in the first half of 2013. Rather than walking through each of the larger corporate deals that we announced in the quarter, we have included an appendix on page 31 of the earnings release.

You will note that more than half of these investments and virtually all of the larger ones were made in the United States with 62% of the equity for the committed transactions in the U.S. industrial and manufacturing sectors. There is a reason for this. To put it bluntly, we believe that the best place in the world to invest today is the United States. I have already mentioned the very low interest rates, the strengthening housing market and the revolution in the U.S. energy markets, which will lower cost and drive growth in U.S. manufacturing.

Additionally, America possesses inherent attributes, attributes that are so often taken for granted like freedom, the rule of law, general trust in our regulatory agencies, our infrastructure, capital markets, universities, medical systems, silicon valley, et cetera, all of which, even given the many obvious improvements needed, are across the board highly advanced and systemically well-working.

As we consider opportunities in other domestic economies – developed economies, even those with weak economies at present, we believe that investing in marketing-leading companies in those economies continues to make sense. Thus, we announced investments in a leading small engine manufacturer with significant operations in Japan, a software company based in Germany and an apparel company based in Italy.

Notwithstanding the slowdown in China and other emerging markets, we continue to be bullish on particular types of investments in emerging markets. In this quarter, we announced two transactions in China as well as two public to private transactions of Chinese businesses; two investments in Brazil; one in Turkey; and we completed our first investment in Southeast Asia. Each of these investments will, hopefully, benefit from the strong and growing middle class in their market.

We continue to be active in real estate investing, putting nearly \$340 million to work in the quarter. We see signs of a recovery in the U.S. housing sector, which is consistent with our view that during the recession there was an underinvestment in housing that affected all aspects of the housing sector. And today pent-up demand is creating attractive investment opportunities in the multi-family development, hotel and senior living sectors.

As David mentioned, we recently held our Annual Investment Conference and a number of our investors asked two questions. The first was, why are we, Carlyle, pursuing all these deals when our competitors, both private equity and corporate, seem much less active? We responded. First, we have a larger corporate private equity business than many of our peers with more than 260 of our 600-plus investment professionals engaged in buyout and growth investing, dedicated to finding the best investments around the globe. This has been our core business for 25 years and our

global reach and network helps us to find investments, where others can't. And our experience gives us the comfort to pursue investments where others won't.

Second, the timing of some of these investments is coincidental. Examples of this are DuPont Performance Coating, Hamilton Sundstrand and Philadelphia Energy Solutions, all of which we've been working on for over a year. Our business is lumpy by nature.

Third, in other transactions, we created tactical advantages over our competitors. For example, we were the only investor in serious discussions with Sunoco about the Philadelphia refinery. In Hamilton Sundstrand, United Technologies was selling three different business units. We believe that they received bids from multiple strategic investors for each of these businesses, but Carlyle and BC Partners, our partner on the deal, were the only ones interested in buying all three units, giving us the edge.

Another example is Genesee & Wyoming. We have been interested in the short-line railroad sector for years and we thought a creative way to invest in this area was to provide capital to Genesee & Wyoming, helping them to buy RailAmerica, creating an even stronger combination.

Fourth and finally, our transactions benefit from incredibly low-interest rates. As an example, the weighted average cost of our debt on the recent Getty Images investment was only 5.25%. The high-yield market has become a low-yield market.

The second question that many investors asked at the conference was how do I invest in this transaction? Our investors – our fund investors are eager to put money to work. Many of their other investment options look unattractive, annualized public equity returns, even including dividends, over 10 or 15-year period have returned mid-single digits or below. Treasuries are paying next to nothing. The yield on high-grade corporate bonds is at historic lows. Investors need a place to achieve attractive returns and we're providing them with solutions.

Turning to portfolio performance, our overall carry fund portfolio appreciated by 3% in the quarter and is up 11% year-to-date and 18% year-over-year. Finally, in terms of exits and distributions to our fund investors, we realized proceeds of \$5.1 billion for the quarter, bringing total realized proceeds to \$11.9 billion year-to-date.

Our third-quarter realization activity reflects the diversity of our platform with proceeds from 117 investments and 34 carry funds. This quarter, we generated proceeds from secondary sales, sales to both financial and strategic investors and dividends from some of our strongest cash flow generating companies.

Secondary sales, including block sales of publicly traded stock, including slightly more than \$1 billion from the sale of Kinder Morgan stock in Carlyle Partners IV and our Energy Funds, \$721 million sale of stock in China Pacific Insurance Company in Carlyle Asia Partners I and \$367 million from the sale of our final ownership stake in Dunkin' Brands in Carlyle Partners IV.

Upgrade sales included Talaris and our third-year buyout fund to GLORY, a Japanese company, AMC movie theaters from Carlyle Partners III to Dalian Wanda of China and Three Rivers Natural Resources in Carlyle/Riverstone IV to Concho Resources, a U.S. corporate buyer.

As an example of the dividend, our fund investors also benefited from Booz Allen's dividend of \$6.50 per share on our ownership of about 90 million shares of Booz Allen stock. Our portfolio now stands at \$62 billion in fair value of carried work and – of capital work in our carry funds. Of this \$62 billion, \$16 billion is held in publicly traded equities and \$31 billion represents transactions originally made in 2008 or earlier. As we said last quarter, we have a diverse portfolio that is ripe for monetization, providing us opportunities for future significant realization.

I will now turn to Adena to discuss our financial results.

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**Adena T. Friedman, Chief Financial Officer, Managing Director Washington, DC**

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Thank you, Bill. Carlyle posted a strong quarter of \$196 million in post-tax distributable earnings or \$0.63 per unit and post-tax economic net income of \$204 million or \$0.66 per unit. As said earlier, Carlyle declared a quarterly distribution per unit of \$0.16, our first full quarterly distribution since the IPO in May. Over the past few quarters, our distribution to public unitholders totaled \$0.27 compared to our post-IPO distributable earnings of \$0.91 per unit.

Looking forward to yearend, we intend to payout a catch-up distribution to all the unitholders based on the level of post-tax distributable earnings generated since our IPO. Our intention is for our total distribution to unitholders in 2012, including our fixed distributions and year-end catch-up, to payout a range of 75% to 85% of post-tax, post-IPO distributable earnings, absent any unusual cash requirements from acquisitions that paid on our fund investments.

As a reminder, we expect that we will announce the catch-up distribution in our fourth quarter earnings release in February 2013 with the cash distribution to follow in March. Comparing our results to prior periods, we posted pre-tax distributable earnings \$206 million compared to \$115 million in the second quarter of 2012 and \$244 million in the third quarter of 2011.

Our realizations in carry-generating funds increased in the third quarter versus the second quarter this year, whereas the third quarter of 2011 also experienced strong carry generating realizations.

Over the last 12 months basis – on the last 12-month basis, distributable earnings of \$748 million are roughly unchanged compared to the prior 12-month period with net realized performance fees up 7% from the prior year and fee-related earnings down 14% over the same period due to unfavorable foreign exchange adjustments, long-term growth initiatives and firm preparations for the IPO, driving operating U.S. dollar denominated expenses higher.

Carlyle's third-quarter 2012 pre-tax economic net income or ENI of \$299 million compares to an economic net loss of \$57 million in the second quarter of 2012 and a loss of \$191 million in the third quarter of 2011. The positive comparison is largely attributable to portfolio appreciation during the third quarter, driving positive performance fees versus portfolio declines in the second quarter of 2012 and the third quarter of 2011.

On a last 12-month basis, ENI of \$808 million is lower versus the prior year of \$1.2 billion due to strong portfolio appreciation in the recovery period following the financial crisis. The recovery in portfolio values resulted in both Carlyle Partners IV and Carlyle Partners V, surpassing their preferred total returns in the fourth quarter of 2010 and the first quarter of 2011 respectively, causing accumulative catch-up of performance fees in those periods.

Moving to our key metrics for the quarter, as of quarter-end, Carlyle had total assets under management or AUM of \$157 billion, up from \$156 billion in the second quarter of 2012 and \$147 billion at the end of the third-quarter 2011, while fee-earning AUM of \$115 billion compared to \$112 billion in the second quarter of 2012 and \$113 billion at the end of the third-quarter 2011.

As our engine hums along, we will have a natural regulator on the growth of our AUM. There are four key factors that drive changes in AUM in our carry funds, fundraising, changes in portfolio value, exit activity and firm-level acquisitions, whereas new fund commitments drive AUM up. They're made at the equivalent of a one-time value to reflect the purchase price of the investments made with that capital – that committed capital.



In contrast, our successful exits are hopefully at valuations well above the entry price, many times at two plus times value, and therefore, results in a greater relative decline in AUMs. Specifically looking over the past 12 months, while our fundraising efforts have been quite successful over the period with \$10.8 billion raised in new commitments, our exit activity has driven distribution of \$15.2 billion. Other contributing factors to AUM are changes in portfolio value and acquisitions.

Our carry fund portfolio appreciated 18% over the last 12 months. We made two CLO group acquisitions, both of which drove our overall AUM up year-over-year. Overall, our AUM grew by \$10 billion in the last year, but many factors played a role. Our AUM roll-forward on page 21 of the release provided additional information regarding the changes.

Turning to the firm's four segments, our Corporate Private Equity segment produced distributable earnings of \$145 million, positively impacting Corporate Private Equity in the quarter for large block sales in Kinder Morgan, Dunkin' Brands, SS&C and China Pacific Insurance Company, in addition to several closed private sale transactions.

Year-to-date distributable earnings from the Corporate Private Equity segment of \$326 million accounts for 65% of firm-wide distributable earnings thus far in 2012.

Third quarter private equity ENI of \$177 million resulted from 5% appreciation of the portfolio in the quarter as well as strong realizations across 16 funds. For the year-to-date, the portfolio has appreciated 12%.

Corporate Private Equity ended the quarter with \$53 billion in total AUM and \$37 billion in Fee-Earning AUM. Fundraising continues for our latest vintage U.S. buyout fund, Carlyle Partner VI as well as multiple other Corporate Private Equity funds.

For Carlyle Partners VI, specifically, we have now received commitments of \$3.7 billion in capital, which is on plan with our expectations when we launched the fund in the first quarter of 2012. We have not yet turned on the fees, because the predecessor fund, Carlyle Partners V, is still investing in new deals and, therefore, the commitments into Carlyle Partner VI are not yet included in our Fee-Earning AUM.

Fundraising remains challenging across the industry, but we are pleased with our progress year-to-date and expect to see flows into our funds continue during the fourth quarter. Global Market Strategies or GMS, which David focused on earlier, ended the third quarter with \$28 billion in Fee-Earning AUM and \$30 billion in total AUM.

These results do not reflect the October 1 acquisition of a 55% interest in Vermillion Asset Management, which added \$2.2 billion in total in Fee-Earning AUM to the asset base. Distributable earnings were \$28 million for the third quarter and \$83 million year-to-date, which accounted for 17% of Carlyle's overall distributable earnings thus far in 2012. Within GMS, during the third quarter, we raised our third and largest new CLO in 2012 with \$615 million in new assets and have raised over \$1.6 billion in new CLO assets year-to-date.

Our GMS carry funds appreciated 2% in the quarter and are now up 17% year-to-date. Our first generation Energy Mezzanine Fund will close with over \$1 billion in commitments and has been in active in energy investing during the quarter.

Net subscriptions into our GMS hedge funds were \$397 million and do not reflect any impact from the 55% interest in Vermillion. Our hedge funds ended the quarter with \$9.8 billion in total assets under management, up from \$9.6 billion in the second quarter of 2012.

Moving onto real assets, distributable earnings for the quarter were \$31 million and \$80 million year-to-date. In terms of fund performance, our real estate funds experienced 5% appreciation in

the quarter and 12% year-to-date. Our Energy funds declined 3% in the quarter, but have appreciated 6% year-to-date.

Asset deployment in our latest U.S. real estate fund, which had its final close in December 2011, continues at a rapid pace with 42% of the fund already deployed or committed. We recently started fundraisings for our next-generation Asia Real Estate fund and we expect new fund launches across the real estate platform to occur in 2013. In addition, as noted earlier, we continue to evaluate options to enhance our energy offerings.

Our last segment is the Fund of Funds Solutions. Distributable earnings were \$3 million for the quarter. As noted previously, we have also begun to see a pickup in fundraising in this segment and expect to have a first close in Alpinvest commingled secondary fund V in the fourth quarter. We continue to focus on ways to develop this business and expand the offering set to both current and potential new clients.

Now, moving to expenses, excluding performance fee-related compensation expenses, our operating expenses were \$205 million, down from \$213 million last quarter and \$212 million in the third-quarter 2011.

Base compensation expenses declined 8% since the third quarter of 2011 due to changes in bonus accruals related to shifts in compensation associated with the IPO, partially offset by additional hires. Third-quarter G&A of \$69 million increased \$13 million when compared to the third-quarter last year, primarily due to unfavorable foreign exchange adjustments, but also influenced by higher fundraising costs and a continued build-out of firm-related infrastructure associated with the IPO.

Interest expense of \$5 million declined from \$15 million in the third-quarter 2011, primarily due to the redemption of the [indiscernible] (36:27) in the fourth quarter of 2011 and first-quarter 2012 as well as debt paid down during the second quarter with proceeds from the IPO.

Moving to the balance sheet, at quarter end, we had \$770 million in cash and \$500 million in the loan payable. Our net accrued performance fees are approximately \$1.2 billion as of quarter-end and on-balance sheet investments attributable to unitholders are \$216 million at quarter end.

In summary, we are pleased with our third-quarter results of \$0.63 per common unit of distributable earnings and \$0.66 per common unit of economic net income. And we are excited about the future prospects of the recent investments we chose to make this quarter and how they will benefit our engine in the years to come.

With that, let me turn it back to David for some concluding remarks.

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**David M. Rubenstein, Co-Chief Executive Officer, Co-founder Washington, DC**

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Thank you, Adena, and thanks to all of you for listening today. As I think you heard this morning, Carlyle's engine was active and successful throughout the third quarter. We raised \$3.4 billion. We invested or committed over \$5.6 billion. Our carry fund portfolio appreciated 3% and our realized proceeds totaled \$5.1 billion. We are confident – actually very confident about the state of our business today and quite optimistic about the future direction we are heading.

We are now ready to take your questions.

**QUESTION AND ANSWER SECTION**

Operator: [Operator Instructions] Our first question is from Howard Chen of Credit Suisse. You may begin.

**<Q – Howard Chen – Credit Suisse Securities (USA) LLC (Broker)>**: Hi, good morning, everyone.

**<A – Adena Friedman – The Carlyle Group>**: Good morning.

**<A – David Rubenstein – The Carlyle Group>**: Good morning.

**<Q – Howard Chen – Credit Suisse Securities (USA) LLC (Broker)>**: David, you touched on the broad-based success you've seen in fundraising across the variety of strategies, but I was curious on a relative basis, do you feel or are you seeing any meaningful differences amongst those fund families, where is fundraising proving to be incrementally more or less challenging today?

**<A – David Rubenstein – The Carlyle Group>**: Well, I think that, clearly, people like or investors like funds that have track records. So, if you've got a long track record, it's obviously easier to raise money for a track record, like Carlyle Partners VI, so obviously sixth generation.

Second, it's easier to raise money today, where there's some kind of fixed income or some distribution that's more regular than just a typical private equity fund and I think our success in raising Energy Mezzanine Fund reflects that. It's an equity fund, but also has a current coupon in effect from some of the investments.

Clearly, all of the funds that we have today are ones that have made some resonance with investors, but nothing happens overnight. Even Carlyle Partners VI with a track record of 25 years can't be raised in a few months. So, I'd say, overall, investors are coming back into the market, they recognize that alternative investments probably produce better returns for them than any other kind of alternative – or any other kind of an investment, but nobody is, overnight, just making large commitments that would welcome fundraisers heart. It does take some time.

I think, overall, we're now quite pleased with the interest level of our investors in re-engaging, sometimes I'd say a year ago or so, some investors were not as interested in making new commitments, now I think that they are, but still you really have to work to get it.

**<Q – Howard Chen – Credit Suisse Securities (USA) LLC (Broker)>**: Great. Thanks a lot, David. And then, Bill, switching over to the meaningful step-up in deployment, I realized any one quarter's results can be lumpy and impacted by things like timing. But is this quarter's pace sustainable from the context of capacity of your investment team? I'm just trying to gain a sense of, if we roll forward 12, 18 months, it's reasonable to think that deployment activity can trend higher from the capacity of you and your team?

**<A – Bill Conway – The Carlyle Group>**: I think the teams – Howard, I think the teams have the capacity to invest at this pace and conceivably even higher. I would say that the U.S. team, which led a lot of the transactions done in the third quarter, they were very busy and now they have to actually close the deals that have already been agreed, which they'll be doing over the next three or six months. I would say over time, I'm counting on other funds, other than U.S. buyout fund to step-up their level of investing.

**<Q – Howard Chen – Credit Suisse Securities (USA) LLC (Broker)>**: Great, thanks. And then, just continuing on deployment, Bill, you put a lot of money in the ground this quarter and amongst that activity did a few non-proprietary deals. I was just hoping you could comment on the pricing

environment for deals that aren't purely proprietary sourced and how you gain comfort with your value creation expectations exiting investment committee?

**<A – Bill Conway – The Carlyle Group>**: Well, I would say, Howard, that it's interesting that the combination of available financing, relatively low rates, the global network and what we think we can do with the companies, has not led to any reduction in our expected rates of return on the new investments that we're making.

I think one of the things that gives us a lot of comfort is that we've been doing this for 25 years. On over that period of time, we've made hundreds of investments, not that they're all worked out as you know, but I think, generally, we've got a lot of confidence in what we've done. I would also say that I wouldn't trade places with any of the firm when it comes to the deals we've done and the portfolios that we have at Carlyle now.

**<Q – Howard Chen – Credit Suisse Securities (USA) LLC (Broker)>**: Understood, thanks. And then, just finally from me, just touching on something you've mentioned a few times now with respect to the financing environment. I think you gave an example with respect to Getty Images and the attractive financing there, Bill. We realized what that's being fueled by in terms of the [ph] accommodators (42:35), central banks, but at what point do you become concerned and you see these signals that it gets a bit frothy and what you do in that scenario? Thanks.

**<A – Bill Conway – The Carlyle Group>**: I would say, Howard, I'm concerned now that the markets are extremely frothy that we've never seen rates this low. I would say the underwriting standards of the banks though are probably not as loose as they were in 2008, 2009 – 2007, 2008, 2009 period, but anytime we've got rates at these very, very low levels.

Remember what's fueling this that the central banks print all this money and investors everywhere are seeking return and yield. And, first, they go to the sovereigns and then they drive down the rates on U.S. treasuries, Japanese JGBs, German bonds, you name it. And then they start looking through other asset categories. They'll go to high-yield corporate bonds and we've – I saw earlier this week, I think, a 10-year [ph] BBB was done at 233 (43:44), it's just – you'd have to be not very aware not to be watching what's happening.

And I think from the standpoint of Carlyle's responsibility to our limited partners and our unitholders, we've responsibility to really take advantage of this while it's being offered. And on the other hand, we also have the responsibility to be positioned for the fact that it's not going to go on forever. And so, for example, you're not just trying to borrow money and use the benefit of these short-term very low rates or in the short run very low rates, but also you're trying to make sure that you have covenants that give you extreme flexibility that you have revolvers that can be used maybe for a time when things aren't as cheap as they are today.

**<Q – Howard Chen – Credit Suisse Securities (USA) LLC (Broker)>**: Great. Thanks for the thoughts and for taking all the questions.

Operator: Thank you. Our next question is from Ken Worthington of JPMorgan. You may begin.

**<Q – Ken Worthington – JPMorgan Securities LLC>**: First, in terms fundraising as well, you're in the market with CP VI, you mentioned Asian buyout with the first close coming and I think European buyout CP IV will start fundraising soon. So, how does, being in the market, fundraising your big flagship products at the same time, impact the ability to kind of meet or even exceed the fundraising goals? It feels like it would make things more challenging given market conditions, but I'd figure you'd know that and maybe there's actually even synergies out there, so would love to hear your comments.

**<A – David Rubenstein – The Carlyle Group>**: Okay, thanks for the question. First, these funds have long histories to them. They are not first funds and, therefore, they have an embedded investor base and as you know, typically investors re-up with a fund that's been reasonably successful. So, if we were raising three funds of this size that had no track records with them, I'll be more nervous.

Second factor is that the funds have all done pretty well relatively speaking and in absolute terms as well and, therefore, I don't think it's going to be as difficult to raise these funds as it might be for some other organization that might be trying to raise three funds at the same time with a track record that might not be as good as this.

Third, what we're now seeing is an influx of new investors into the private equity world or alternative world. And that is not only sovereign wealth funds, which are stepping up and they can invest large sums, but a high net worth individuals, particularly those who are being rounded up in feeder funds not unlike with your organization or other organizations now have a pretty good business rounding up high net worth individuals, putting them together in a so-called feeder fund and investing in our funds. And that's a business that we're seeing kind of increased fairly dramatically.

So, we also have a very large fundraising team and it's a large world. So at any given time, yes, these fundraising teams are figuring out where the best place is for our fund hedge to go. And since we have about 1,400 existing institutional investors from which to pick, plus new investors, it's not as challenging as it might seem. On the other hand, I don't want to make it sound like it so easy that when we get our targets, nobody will tell me what a great job I've done.

**<Q – Ken Worthington – JPMorgan Securities LLC>**: Okay. Thank you very much there. And then, just a little bit more of the high level, how do you address or manage reputational and brand risk when making investment decisions? And I'm not sure this is totally related, but Chemring has kind of made it into the press, maybe give us some background there, but I am really after kind of the brand and reputational risk and how you think about that in the investment process.

**<A – Bill Conway – The Carlyle Group>**: Let me take that if I can, David and Ken, Carlyle, obviously, values our good name. It's our biggest asset. A lot of times when our investment professionals or fundraisers go to see someone, I want them to be able to put their business card down and [ph] it says (48:00) the Carlyle group on it and I want people to really think well that's a first-class organization.

The thing that we have done perhaps more in the last few years than in the early years of Carlyle is now on every investment that we make. We'll have a checklist done on the various CSR issues, labor, the environment, anything, Foreign Corrupt Practices Act, will employ far more consultants to do things. Now, there is no guarantees, you've got hundreds of portfolio companies and you've got more than 1,000 people working for Carlyle all over the world. There aren't guarantees, but I think we have done a tremendous amount to try to ensure that we're playing by the rules and I think also we've come to the belief that playing by the rules is a good business. It's not bad business, it's good business, doesn't make it tougher to do business and it's a good thing.

On the Chemring situation, I think that they've been putting out the various releases on the timing, obviously, at a certain time and on a certain price, we had a certain interest in clearing up the transaction, could be put together. Based upon the information we received or the information we didn't receive, we just decided this has gone long enough and at this time, we're not interested in pursuing it.

**<Q – Ken Worthington – JPMorgan Securities LLC>**: Okay, great. Thank you very much.

Operator: Thank you. Our next question is from Robert Lee of KBW. You may begin.

**<Q – Robert Lee – Keefe, Bruyette & Woods, Inc.>**: Thanks, good morning. Just had a couple of quick questions. First, maybe looking within GMS, where you've had some good success in the fundraising, your hedge fund strategies, could maybe dive a little bit deeper just – I don't know is there anyone or two specific strategies? Maybe it's one or two within Claren Road that's kind of accounting for the lion's share of the net subscriptions or is it pretty broad based?

**<A – David Rubenstein – The Carlyle Group>**: I would say – Adena will help me on this, but I would say that it's – Claren Road is the biggest of the hedge funds and it's got multiple strategies within that hedge fund and different investors are looking for different exposures there. The main fund to Claren Road closed earlier this year to new investors. It can still take additional commitments from existing investors, so that is a factor. I don't know, Adena, if we've mentioned anything on any of the specific funds.

**<A – Adena Friedman – The Carlyle Group>**: In terms of the specific funds, we do have funds that are in the significant fund table in terms of performance and size, but I would say generally, Rob, that the insights have been ESG has definitely had a very good year in terms of net inflows and Claren Road has as well, despite the fact that the master fund is in fact closed to new investors. So it has been relatively broad based. Remember that that each of those fund groups has multiple strategies. So, there's no one strategy that's dominating right now and mainly, because frankly the master fund which is the largest fund is not currently open.

**<A – Bill Conway – The Carlyle Group>**: Let me add a point to that. When we acquire these hedge funds, we do so in part, because we think they have a good track record and they will add to our firm's overall value, but we also think that we can help them with fundraising. They all typically have raised money before, but they wouldn't have the assets they have, but many of them don't have the international fundraising base that we can often help them with.

And so we have found with each of these that we have brought investors to them and those investors are reasonably satisfied with the performance and sometimes they increase what they already have with them. So, we think that we'll be able to do this as well with Vermillion as soon as that's closely a part of our firm as it is now, but we haven't yet started really doing fundraising for them.

**<Q – Robert Lee – Keefe, Bruyette & Woods, Inc.>**: Okay, great. And maybe a question on the AlInvest, I mean you mentioned and we've clearly seen a nice pickup in capital formation there. But I think when you first did the transaction, one of the things that, I think, you guys talked about was the ability to take their expertise and kind of apply it may be broadly across the firm in terms of doing more, I don't know, strategic accounts or multi-asset class products and I think you have that.

**<A – David Rubenstein – The Carlyle Group>**: Yes.

**<Q – Robert Lee – Keefe, Bruyette & Woods, Inc.>**: I forget which state it was, Wisconsin or one of them. Are you seeing – are you starting to see more of that, is that starting to impact their inflows more of those kind of broader-based relationships?

**<A – David Rubenstein – The Carlyle Group>**: Yes. To remind everybody, we have this relationship and we own this organization, AlInvest, that we bought from two Dutch pension funds, but they cannot invest in any of our funds and we don't see any of the things that they do in terms of what they decide to invest in.

However, we are able to help them in fundraising and as you suggest, what you're referring to is the Michigan Municipal Employee Retirement System, MERS, and we were helpful in introducing MERS to AlInvest and they did become an investor with them. What AlInvest does is it has three large commingled funds, one in secondaries, one in fund investments and one in direct investments or so-called co-investments.

They are beginning to build the business around so-called managed accounts that isn't going to be gigantic for them, because they already have a gigantic commingled business, but the managed account business is a business that is one that they are beginning to build and I think that will have a lot of growth potential and we are helping them on that because we have a fair amount of expertise within their fundraising group and how to help with managed accounts. Does that answer your question?

**<Q – Robert Lee – Keefe, Bruyette & Woods, Inc.>**: Yes, it does. And just to confirm, I think, if I remember correctly, the original terms of the transaction, the assets they raise now, you have a greater future participation in at least any performance fee generations to the extent that's part of the fee structure, is that correct?

**<A – David Rubenstein – The Carlyle Group>**: You have a good memory.

**<Q – Robert Lee – Keefe, Bruyette & Woods, Inc.>**: Okay. Let's see – I think – oh, and last one maybe for, Adena, I don't know to what extent you could maybe just provide some color if there is any kind of already known or announced realizations in Q4 that we should be thinking about as we look at our [ph] DE (54:27) forecast for the quarter?

**<A – Adena Friedman – The Carlyle Group>**: Well, we have continued to remain active in terms of realizations and in terms of some of them, we will be realizing proceeds for LPs on other dividend types of situations like we did with Booz Allen, those are just recent LPs, but they are really return of capital to them. In terms of exits, we have done additional secondaries and those are generally publicly available and I think that obviously we don't – we are not going to give you any projections over the rest of the quarter, but we have remained active so far this quarter.

**<Q – Robert Lee – Keefe, Bruyette & Woods, Inc.>**: Right. Great. Thanks for taking my questions.

Operator: Thank you. Our next question is from Marc Irizarry of Goldman Sachs. You may begin.

**<Q – Marc Irizarry – Goldman Sachs & Co.>**: Great. Thanks. Just a question on carried interest taxation, obviously it's been a long dated issue. When you think about compensation for employees in the private equity business, if you will, and just your franchise that you've built in your sort of overall firm equity that you can provide, how should we think about if at all that the changes in carry taxation could affect the way you think about compensating private equity professionals?

**<A – David Rubenstein – The Carlyle Group>**: Well, of course, we don't know that there's going to be any change anytime soon and I would point out that under numbers that are apparent from the President's budget numbers and CBO, the amount of money that would be picked up by carried interest taxation being changed from capital gain to ordinary is a modest amount.

If you eliminate the enterprise tax from consideration, you probably would pickup no more than \$10 billion over 10 years. We have – we projected to have \$10 trillion of additional debt over the next 10 years; this would pick up an insignificant amount. So, I don't think that it will be seen as a major revenue raiser and, of course, if other tax rates go up, capital gains rate were to go up and with the healthcare tax coming in, the amount of money that would be picked up by the change would be relatively less than the \$10 billion, maybe half of that, because of the differential being smaller.

In terms of compensating employees, obviously, we're in the same situation as other firms, so that if the rate were to change, we don't expect that people will leave our firm to go to our competing firm, because they'd have the same tax issues. Will people leave the private equity business and go to some other business? We can't say for sure. Obviously, it's a business that people like to do

for reasons other than just tax rates, but that's one of the concerns that we've always had about with this issue, the law of unintended consequences.

And so you don't really know whether if you change the way that taxed, whether the fact that the United States is the dominant private equity country in the world and dominant venture capital country in the world, whether that would change or not, we don't know and that's the debate the Congress has had. I expect that because these issues are so complicated, no resolution will occur in the very near-term. Again, it doesn't pick up that much revenue and it's complicated what the impact will be on these important industries. But, in terms of thinking about it, in terms of our compensation to our employees, we haven't had to really focus on it really, because we don't think any change is imminent. Bill?

**<Q – Marc Irizarry – Goldman Sachs & Co.>**: Great. And then just, if we – if you think about the fundraising environment out there today, David, I don't know, is the J-curve effect impacting fundraising for the bigger private equity funds? And as you sort of pick up, I guess, the investing pace, does that become maybe less of an issue in terms of, maybe some LPs are sidelined right now, maybe thinking some of the – getting the election, fiscal cliff behind us, maybe there'll be more investment opportunities going forward. Do you sense that maybe there is sort of a pickup in the fundraising that will happen as maybe your LPs think that money will be put to work even faster than it is today?

**<A – David Rubenstein – The Carlyle Group>**: Well, we hope that will be the case for sure. There is no doubt that the U.S. economy slowed down a bit in the second and third quarter compared to what had been projected. And I think some of that was uncertainty about where the election was going, and now that's resolved, I expect that people will say, okay, I'm not going to wait four more years for another President. I'm going to start doing capital expenditures and investing again.

I think the biggest complication in the fundraising market for private equity has been the mega funds and when I say mega funds, I mean funds above \$10 billion. I think it's very difficult today to go out and try to raise a \$12 billion, \$15 billion, \$20 billion fund and really nobody's really trying to do so. There's been a kind of feeling that those funds might have been too big to be deployed sensibly. And as a result, people who are raising their large U.S. buyout funds are really raising funds that are going to be lot smaller than those funds that were their predecessor funds and that is a major change in the industry as you probably know.

Historically, if you had a good fund, you would raise a successor fund that was bigger. Now if you have a good fund, you often raise a successor fund that is smaller. And Carlyle Partners V, for example, we have a top-quartile performer, it was a \$13.7 billion fund, we're out now raising a \$10 billion fund in a more normalized environment, years ago, we would be raising a much bigger fund. So, that's the biggest complication in the fundraising markets. It's just that investors tend to not want to be in gigantic funds as they were before and therefore, you have to offer things that are smaller and more diverse products, I think.

**<Q – Marc Irizarry – Goldman Sachs & Co.>**: Okay. And then, just one more, if I could, when you think about just building the diversification of your platform, how are you sort of viewing acquisitions at this point? There's some areas where you're focusing on building out sooner rather than later and how do you think about buying versus building in some of the areas where maybe you want to expand the business?

**<A – David Rubenstein – The Carlyle Group>**: Well, we don't have any preconceived notions. We look at each thing separately. Clearly what we have shown is that we are willing to make some acquisitions where we think we didn't have a presence that we thought was important to have, but we recognize though that you don't want to make acquisitions repeatedly if it's going to change dramatically the culture of your firm.



And one of our strengths is our one Carlyle culture and if you just spend all your time making acquisitions, you're not going to make sure – you're not going to have that culture as permeating in the organization as much as you might like. So, we don't want to make acquisitions that are going to change the culture or going to do things that are going to duplicate what we have elsewhere. So, we do it judiciously and while we've made a number of them in the grand scheme of things, most of the new assets that we have under management is really coming from organic growth or successor funds to our existing kind of businesses.

**<A – Bill Conway – The Carlyle Group>**: And I would also add that on – we call – we've used the word acquisitions, but really what happens in places like Claren Road, Vermillion, ESG, AlplInvest, is that they're not acquisitions as you might think about it. In those businesses, we typically acquire about 55% or 60% of the business. The people that have helped build those businesses to that point in time are our partners in helping to build the business even further.

They see Carlyle's global network, our fundraising capability and other things that can help them grow and perhaps be better and perform better, but they're not acquisitions in a normal sense. And I would also say that we are very culture sensitive. If we spend 25 years trying to build the Carlyle to what it is and I think it's – we don't want anything to destroy that culture at all.

And in another part of your question, I would say, in terms of organic growth versus acquisitions, it depends on the circumstance. I would say for example a business that we built from scratch was our Energy Mezzanine business. Two years ago, it really didn't exist. Mitch Petrick and the team at GMS recruited some people to begin to build the business. We did a couple of interesting deals. Fundraising teams went to work, the global network supported them. And 18 months or so later, we have a fund of about \$1.1 billion. And then, I think that's the kind of thing we can do when we've got all of Carlyle working together.

**<Q – Marc Irizarry – Goldman Sachs & Co.>**: Okay. Thanks.

Operator: Thank you. [Operator Instructions] I'm showing no further questions at this time. I would now like to turn the conference back over to Daniel Harris for closing remarks.

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**Dan F. Harris, Managing Director, The Carlyle Group LP (Corporate Private Equity)**

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Thank you all for participating. We look forward to talking to you guys in next quarter.

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**Adena T. Friedman, Chief Financial Officer, Managing Director Washington, DC**

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Thank you.

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**William E. Conway, Co-Chief Executive Officer, Co-founder Washington, DC**

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Thank you.

Operator: Ladies and gentlemen, this concludes today's conference. Thank you for your participation. Have a wonderful day.

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