



**PSERS PRIVATE INVESTMENT PROGRAM**

**Recommendation for Investment in  
KKR 2006 Fund L.P.**

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## **KKR 2006 Fund L.P.**

### **A Global Franchise Crafted Over Three Decades**

Kohlberg Kravis Roberts & Co. L.P. (“KKR”; also referred herein as the “Firm”) pioneered the leveraged buyout industry in 1976. They have remained one of the world’s largest and most successful private equity firms across three decades of economic cycles and private equity market changes. Their name is synonymous with the successful execution of large, complex leveraged buyout transactions; a commitment to building market leading companies; a focus on operational value creation; a vast network that includes financial, corporate and political leaders worldwide; a reputation for integrity and fair dealing; and excellent investment returns.

KKR has developed a strong track record of partnering with management teams and building successful businesses across a broad range of industry sectors. Today, they are a leading global private equity firm with offices in New York, Menlo Park, London, Paris, Hong Kong and Tokyo. They are currently raising capital for KKR 2006 Fund L.P. (the “2006 Fund”), KKR’s twelfth investment fund. Since KKR believes that the competitive position of the 2006 Fund in seeking investment opportunities increases with the size of the 2006 Fund, there is no limitation on the aggregate amount of commitments to the 2006 Fund. The 2006 Fund will focus primarily on investments in the U.S. and Canada, and will build on their 30 years of private equity experience.

KKR is a global private equity firm differentiated by their:

- Exceptional Long-Term Performance
- Experienced Investment Team
- Deep Industry Knowledge
- Expertise in Building Value in Complex, Global Businesses
- Global Reach
- High Standards of Excellence Based on Best in Class Processes
- Creativity and Innovation

### **Deep Industry Knowledge**

KKR has a focused investment approach designed to address the complexities of investing in global businesses. Their investment professionals are organized into industry teams charged with being experts in their respective fields. Their expertise in specific industries has led to proprietary investment opportunities.

KKR currently focuses on nine industries globally: Chemicals, Consumer Products, Energy and Natural Resources, Financial Services, Health Care, Industrials, Media and Communications, Retail and Technology. Each team is led by a Member supported by other KKR executives. The teams work together across their offices, and hold frequent conference calls to share ideas and identify potential acquisition candidates. They periodically review the industries on which they focus and make adjustments based on their economic outlook and the potential for attractive investment returns. Former operating executives such as Clive Hollick in media, Ken Freeman in health care, Sir Deryck Maughan in financial services and Michael Marks in technology have recently joined KKR to augment their industry teams and lend an operating perspective to their investment analyses.

## Expertise in Building Value in Complex, Global Businesses

Their success in achieving high multiples on invested capital depends on, among other things, their ability to select quality opportunities, pay reasonable prices and drive value in the businesses they acquire. They strive to forge strong partnerships with highly motivated management teams who put their own capital at risk. They seek out companies with strong business franchises, attractive growth prospects, defensible market positions and the ability to generate high returns on investment. They typically focus their efforts on situations where they can invest a meaningful amount of capital in a business with a sustainable competitive advantage, and where the value of the business can be enhanced through their involvement.

Their strategic approach to building businesses and creating value for their limited partners begins the day they identify a potential investment and continues throughout its life cycle. The major components of this approach are:

- *Active and Expert Board Involvement.* When they complete a transaction, the real work begins. Their success lies in actively working with management teams to assist them in formulating plans to drive growth and enhance profits. This often includes leveraging their industry knowledge, accessing their wide network of resources (including their expert advisors) and recruiting seasoned operating executives.
- *Operational Focus.* They provide management teams with additional operational expertise and resources to meet their objectives. One of the key levers in driving operational improvements in their companies is their relationship with Capstone Consulting and Capstone Europe, consulting firms with which they have an exclusive relationship.
- *Support Long-Term Growth Plans.* Their investment approach is predicated on helping companies deliver growth over the long term. They are patient investors and they encourage their portfolio companies to invest for future competitiveness; to improve operating efficiencies; to make strategic acquisitions; and to incentivize employees by giving them ownership in the business.
- *Innovative Financing Techniques.* Once they have identified a potential investment, they work to create innovative financing structures that give them a competitive advantage in winning transactions and that provide ongoing financial flexibility to their portfolio companies.

They have a set of internal processes to drive accountability, focus and prioritization during the ownership period. These include a Portfolio Management Committee, 100-Day Plans, monthly and quarterly monitoring reports and annual evaluations of each investment.

In addition, they have built significant resources to improve and add value to their portfolio companies:

- They have an exclusive relationship with Capstone Consulting and Capstone Europe, consulting firms that concentrate on helping KKR portfolio companies define strategic priorities and implement operational changes. Capstone consultants specialize in multiple industries, including chemicals, consumer products, industrials, health care, media, retail and technology. While they do not require their portfolio companies to engage Capstone, most portfolio company managers embrace Capstone's involvement given its operational expertise and bottom-line focus. Capstone executives are compensated directly by the portfolio companies and through equity sharing arrangements with KKR. As a result, their economic incentives are aligned with the incentives of KKR, the limited partners and the management teams. Capstone Consulting currently has 12 consultants in the U.S. and Capstone Europe has six in Europe.

- They have a roster of active Senior Advisors who have held leading executive roles in major U.S. and European corporations. These advisors help the investment teams evaluate new opportunities and many serve on the boards of directors of the portfolio companies where they are able to complement their expertise with their industry experience. Five Senior Advisors also participate on their Portfolio Management Committee, which monitors the performance of all their investments.
- Fisher Capital is an insurance advisory firm formed by Jim Fisher after the successful sale of American Re-insurance, a former KKR portfolio company where Jim was CFO. Jim and his team work solely with KKR and help them analyze, create value in and operate their insurance industry investments. Jim is Chairman and CEO of Bristol West, and serves on the boards of directors of Alea Group and Willis Group.
- KD Capital is an advisory firm formed by Foster Duncan to support their efforts in the energy and natural resources industries. They have known Foster for many years through their extensive activity in the energy sector. Foster was formerly Executive Vice President and CFO of Cinergy Corp., a large integrated electric and gas company with regulated public utilities in Ohio, Indiana and Kentucky, and several diversified commercial businesses. Foster was also CEO and President of Cinergy's Commercial Business Unit and was involved in the sale of Cinergy to Duke Energy.

## **Global Reach**

KKR has a global network of professional relationships, which includes CEO's of the largest companies, political leaders, co-investors, advisory institutions and other intermediaries that they believe is without equal in the private equity industry. They have direct relationships with approximately two thirds of both the Fortune 500 and Global 500 companies. This network provides access to exclusive investment opportunities, valuable sources of knowledge during due diligence and significant resources when they are building and exiting their portfolio companies.

Most of the investments they consider are multi-national in scope and require coordinated diligence efforts across different markets. They have acquired businesses based in Europe, such as MTU Aero Engines and Legrand S.A., where their relationships and ability to assess U.S. operations were instrumental in their valuation analyses and ability to prevail in competitive bids. Similarly, they have sourced investments in North America such as Avago Technologies and Toys 'R' Us, where they were able to analyze worldwide operations with a globally coordinated KKR/Capstone diligence team.

They have also recently established a presence in Asia with offices in Hong Kong and Tokyo. Two senior KKR executives, Joseph Bae, a Member from their New York office, and Justin Reizes, a Director from their London office, moved to Hong Kong to initiate this effort. They are in the process of hiring additional executives in the region and have recently added David Liu and Ming Lu as Managing Directors in their Hong Kong office. Sir Deryck Maughan, former Vice Chairman of Citigroup, Chairman and CEO of Salomon Brothers and Chairman of Salomon Brothers Asia, has also joined them as Chairman of KKR Asia. They expect that the 2006 Fund will invest a portion of its committed capital in Asian companies, particularly in advance of the formation of an Asian-focused fund by KKR.

## **High Standards of Excellence Based on Best in Class Processes**

KKR is committed to high standards of management excellence and business ethics that have resulted in quality relationships with their business associates and contributed to the overall stability of their investment team. KKR's culture is defined by a spirit of teamwork and mutual

trust across all of their offices. Their professionals share information across industry groups and geographies and take a long-term view of the business of each portfolio company.

Over the past 30 years, they have refined their internal processes for making investment decisions and driving value creation within their portfolio companies. They have a single Investment Committee consisting of six of their most experienced executives that approves all investment decisions globally, and advises the investment teams on analyzing and executing new investments. After an investment is made, their Portfolio Management Committee assumes responsibility for working with the individual investment teams to monitor performance. Beginning with a 100-Day Plan that details the steps necessary to achieve the strategic and operational goals of each portfolio company, the investment teams update the Committee with monthly financial reports, quarterly financial and operating reviews and an annual memorandum on whether a portfolio company will continue to compound at an attractive rate of return. Each investment team, sometimes accompanied by the portfolio company's senior management, presents in person to the Portfolio Management Committee on average twice per year. They have also established an Operating Committee consisting of seven senior Members of the Firm to oversee the day-to-day management of KKR.

### **Creativity and Innovation**

KKR has consistently set new standards of achievement in the private equity industry. They have been the lead investor in some of the largest, most complex buyout transactions that have been completed. They also have a record of accomplishments that distinguishes them as creative and innovative investors. These include leading the U.S. private equity industry during the past 30 years in a series of firsts: the first large buyout of a public company, the first billion dollar buyout, the first buyout of a public company by a tender offer and the first billion dollar leveraged build-up.

They have continued this legacy of achievement; for example:

- The structure they used to acquire Texas Genco was particularly innovative for its use of a complex power hedging program that allowed the company to lock in significant future cash flows, reduce risk in the transaction and execute a favorable financing package, all of which allowed them to create immediate value at the company.
- Their investment in International Transmission Company (ITC) was the largest investment to date by a private equity firm in an electric transmission business, and created the first and largest truly independent transmission company.
- In Canada, they have completed four transactions in four different industry groups making them one of the most active U.S.-based private equity firms in that country. They have completed the three largest leveraged buyout transactions in Canada: Masonite, Shoppers Drug Mart and Yellow Pages Group. They also invested in Canadian General Insurance, a Toronto-based property and casualty insurer.
- KKR has set new standards in international markets as well. In 2002, they executed one of the most complex corporate carve-outs in Germany when they acquired from Siemens seven separate businesses, renamed Demag Holding, with annual sales of €3.4 billion and over 20,000 employees. They undertook a similarly complex corporate carve-out transaction with their recent acquisition of Agilent's semiconductor products business, renamed Avago Technologies, whose manufacturing assets are based principally in Singapore and Malaysia. KKR and Capstone worked extensively with management to restructure, rebuild and selectively outsource Avago's finance, human resources and information technology functions resulting in over \$100 million of annual savings. In addition, they re-domiciled the company in Singapore, resulting in a highly efficient tax structure.

## MANAGEMENT TEAM

KKR has benefited from continuity in their management and investment professionals throughout their long history. Henry R. Kravis and George R. Roberts, founders of KKR, are active investors and managers of the Firm. As members of the Investment, Portfolio Management and Operating Committees, they contribute their collective 70 years of buyout and management experience, together with other senior Members, to selecting and building all of the Firm's portfolio companies and to guiding the strategic direction of the Firm. Collectively, their Members have over 270 years of accumulated private equity experience spanning three decades. They have built their firm with the intellectual capital of their investment professionals and they are guided daily by the depth and breadth of their collective knowledge.

They currently have 68 investment professionals dedicated to sourcing, analyzing, executing and managing investments, including 23 Members, five Managing Directors, six Directors, 14 Principals and 20 Associates. In addition, they have 10 other senior executives who focus on finance, information technology and fund administration. Their investment professionals come from a broad spectrum of backgrounds including private equity, operations, strategic consulting, investment banking, merchant banking and finance. They hail from 10 countries and collectively speak 11 languages.

### Members

**Henry R. Kravis** (Age 62, New York) co-founded KKR in 1976. During more than 35 years, he has participated in the financings of over 150 businesses in diverse industries making him, along with George Roberts, one of the world's most experienced private equity investors. Currently, he participates in all the investment activities of the Firm and serves on the Investment, Portfolio Management and Operating Committees. He is also a member of the board of directors of Legrand and PRIMEDIA. Prior to founding KKR, Mr. Kravis was a Partner in the Corporate Finance Department of Bear Stearns & Company, where, with Messrs. Kohlberg and Roberts, he pioneered the use of leverage in acquisitions. He earned a B.A. from Claremont McKenna College, and an M.B.A. from Columbia Graduate School of Business.

**George R. Roberts** (Age 62, Menlo Park) co-founded KKR in 1976. During more than 35 years, he has participated in the financings of over 150 businesses in diverse industries making him, along with Henry Kravis, one of the world's most experienced private equity investors. Currently, he participates in all the investment activities of the Firm and serves on the Investment, Portfolio Management and Operating Committees. Prior to founding KKR, Mr. Roberts was in the Corporate Finance Department of Bear Stearns & Company, where he became a partner at 29 and where, with Messrs. Kohlberg and Kravis, he pioneered the use of leverage in acquisitions. He earned a B.A. from Claremont McKenna College, and a J.D. from the University of California (Hastings) Law School.

**Paul E. Raether** (Age 59, New York) has been with KKR for 25 years and during that time has been actively involved with numerous portfolio companies. He played a significant role in the development of Beatrice Companies, Bruno's Inc., Cole National Corporation, Duracell, Flagstar Companies, Fleet/Bank of New England, IDEX Corporation, KSL Recreation, Masonite, PT Components, Randall's Food Markets, RJR Nabisco, Seaman Furniture, Shoppers Drug Mart, Stop & Shop Companies, Storer Communications, Inc., Walter Industries and Wometco Enterprises. Currently, he is on the Board of IDEX Corporation, KSL Recreation and Masonite. He is a member of the Industrials industry team and a member of the Portfolio Management Committee. He started his professional career in the Corporate Finance Department of Reynolds Securities. Prior to joining KKR, he was a Vice President in the Corporate Finance Department of Blyth Eastman Dillon & Company. He obtained a B.A. from Trinity College, and an M.B.A. from the Amos Tuck School of Business Administration at Dartmouth College.

**Michael W. Michelson** (Age 54, Menlo Park) has been with KKR for 25 years and during that time has been directly involved with numerous portfolio companies. He played a significant role in the development of Accellent, Alliance Imaging, Amphenol, AutoZone, Beatrice Companies, Dillingham, Golden West, Jazz Pharmaceuticals, KinderCare Learning Centers, Lily Tulip, M & T, Malone & Hyde, Fred Meyer, Owens-Illinois and Union Texas Petroleum. He currently serves on the board of directors of Accellent, Alliance Imaging and Jazz Pharmaceuticals. He heads the Health Care industry team. Mr. Michelson is also a member of KKR's Investment Committee and chairs the Operating Committee. Mr. Michelson began his professional career with the law firm of Latham & Watkins in Los Angeles, where he was involved in a broad corporate practice while specializing in management buyouts. He has an A.B., Cum Laude, from Harvard College, and a J.D., Cum Laude, from Harvard Law School.

**James H. Greene, Jr.** (Age 55, Menlo Park) has been with KKR for 20 years. During this tenure he has been involved with numerous investments including Accuride, Avago Technologies, Intermedia Communications, NuVox (NewSouth Communications), Owens-Illinois, Randall's Food Markets, RELTEC, RJR Nabisco, Safeway, Shoppers Drug Mart, Stop & Shop Companies, SunGard Data Systems, Tenovis and Zhone Technologies. Currently he is on the board of directors of Accuride, Alliance Imaging, Avago Technologies, Nuvox, SunGard Data Systems and Zhone Technologies. He is a member of the Technology industry team. Prior to joining KKR, Mr. Greene had 14 years of banking experience as a Vice President of Bankers Trust Company in Los Angeles where he was involved in large corporate lending, management buyout financings and other merger and acquisition transactions, including KKR transactions. He has a B.S. from the University of Pennsylvania.

**Perry Golkin** (Age 52, New York) has been with KKR for 20 years and during that time has been directly involved with numerous portfolio companies. He played a significant role in the development of Alea Group Holdings, American Re-Insurance, Bristol West Holdings, Canadian General, First Interstate, Fleet/Bank of New England, PRIMEDIA, Rockwood/Dynamit Nobel, Walter Industries and Willis Group. Currently, he is on the board of directors of Alea Group Holdings, Bristol West Holdings, PRIMEDIA, Rockwood Holdings and Willis Group. He is a member of the Financial Services industry team. Mr. Golkin is a member of the Portfolio Management and Operating Committees. He also plays a key role in managing KKR's investor relationships, as well as in raising new funds for the Firm. Prior to joining KKR, Mr. Golkin started his professional career with Price Waterhouse & Co., became a certified public accountant and taught accounting at the University of Pennsylvania Wharton School. Later, he was with the law firm of Simpson Thacher & Bartlett in New York, where he was involved in a broad range of corporate financings including mergers, acquisitions and management buyouts. He has a B.S., Summa Cum Laude, from the University of Pennsylvania, an M.S. from the Wharton School, and a J.D. from the University of Pennsylvania Law School.

### **Conclusion/Recommendation**

Based upon the successful track record and experience of the principals and the recommendation of PSERS' consultant, Portfolio Advisors, staff recommends that the Board invest an amount equal to 25 percent of the committed capital, but not to exceed \$300 million plus reasonable normal investment expenses, in KKR 2006 Fund L.P. The final terms and conditions of the investment must be satisfactory to the Investment Office, the Office of Chief Counsel, and the Executive Director.