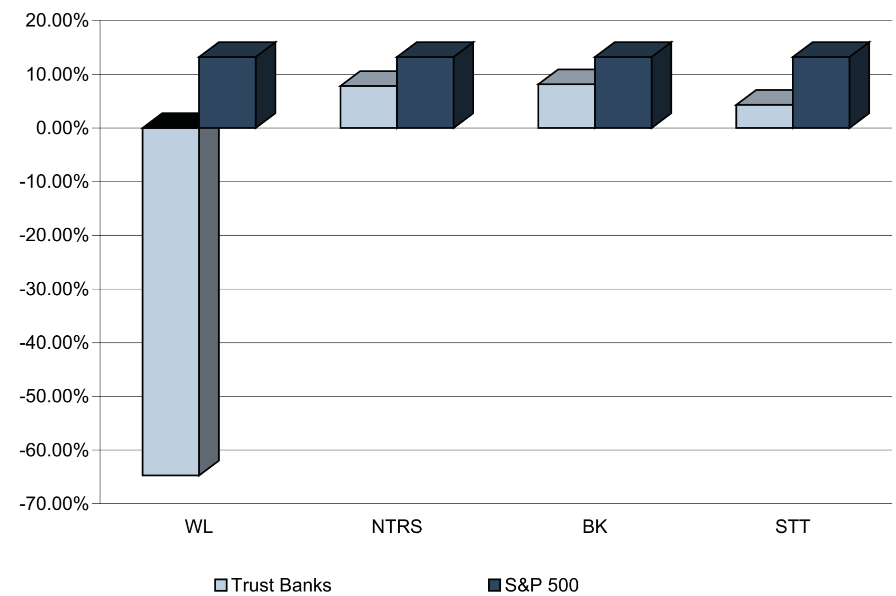
Asset Management Industry

Mercer Capital provides asset managers, trust companies, and investment consultants with corporate valuation, financial reporting valuation, transaction advisory, portfolio valuation, and related services. Call Matt Crow or Brooks Hamner at 901.685.2120 to discuss your needs in confidence.

Segment Focus: Trust Banks

In a year of rising equity markets and waning risk aversion, it probably comes as no surprise that the more conservative-oriented trust banks underperformed the broader indices for most 0f 2010. Much of the sector's gains in AUA (assets under administration) attributable to the bull run in the second half of the year were wiped out by rising treasury yields over the same period, punishing the trust banks with more conservative asset allocations. Quantitative easing has compounded the problem for many of these banks, as some have even been forced to waive their money market fees with short term interest rates hovering around 0%.

Total Returns for the 12 Months Ended 12/31/10



The recent (and ongoing) return of the retail investor to the stock market poses both a threat and opportunity to trust banks. On the one hand, this trend implies the commitment of more assets that trust banks can administer and charge fees on. At the same time, it is also indicative of a gradual resurgence in risk tolerance that could precipitate client asset flows out of custodial safe havens and into more exotic investment vehicles such as hedge funds and private equity firms. As a substantial percentage of trust banks' revenue is derived from high net worth individuals, retaining the assets of this critical customer base could be a challenge for these businesses if investor sentiment continues to improve.

Still, trust banks have a history of stability and tend to hold up reasonably well under most market conditions. The one exception, as noted in the chart above, is Wilmington Trust, which saw its stock decline upon the announcement of its merger with M&T Bank Corp. at a deeply discounted transaction price. Still the recent demise of WL is not indicative of any fallout or instability in these businesses as Wilmington's financial woes stem solely from the asset quality of its loan portfolio rather than its core trust operations, which have actually expanded over the last couple of years.

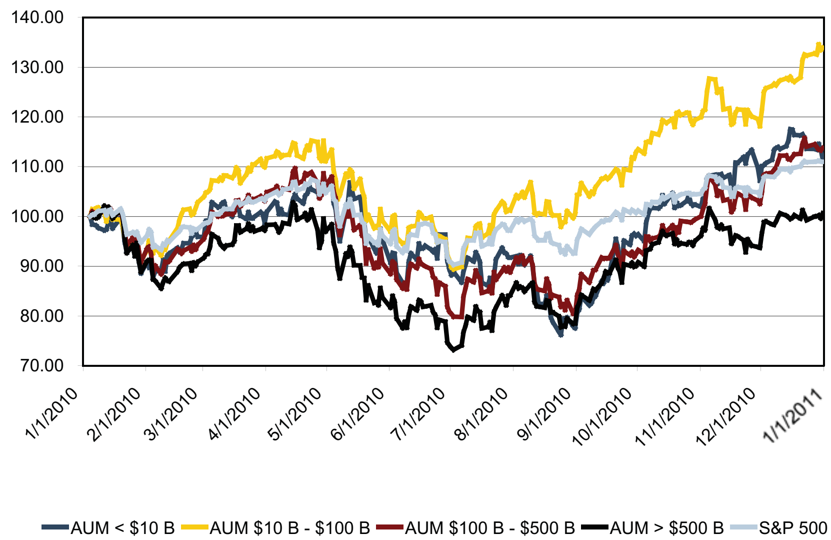
On the other end of the spectrum, Northern Trust was recently named "Best Private Bank in North America" and "Best Private Bank for Innovation" by two *Financial Times* publications. The judging panel applauded the company's overhaul of its asset allocation process since the crisis and the extension of its fiduciary model to minority groups and non-traditional families. Such innovation and appeal to a broader customer base may be needed to grow AUA as high net worth investors seek alternative asset classes for higher returns.

Famed bank analyst Dick Bove anticipates a wave of M&A activity among financial institutions in the near future with more stable trust banks like NTRS and State Street looking to grow through acquisition. Should these businesses face stagnant or declining AUA balances in future periods, they could turn to a more acquisitive growth strategy as many have resorted to in prior downturns.

Market Overview: 2010 Q4

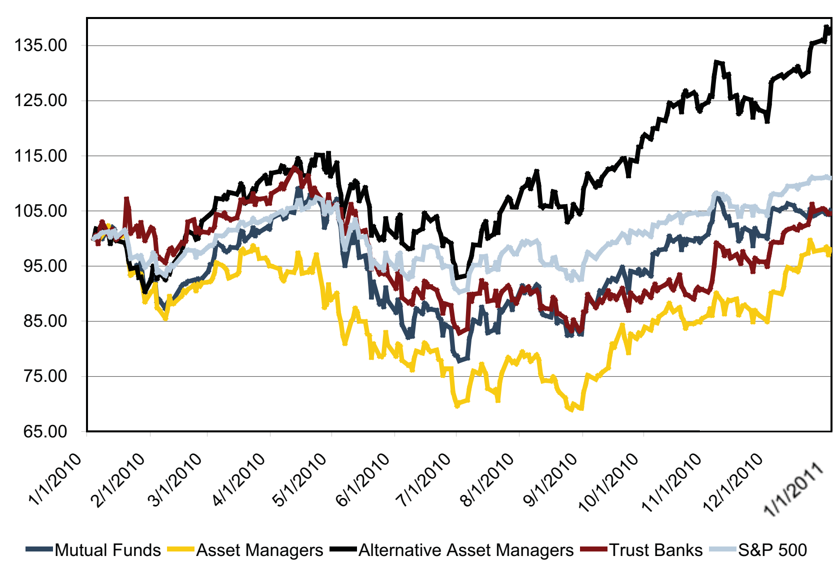
Still trying to regain their clients' trust following the financial crisis, most of the larger asset managers lagged the S&P in 2010. This is an unusual trend for these businesses which tend to thrive in bull markets when their top line advances with the market and operating leverage provides further momentum for gains in profitability. Indeed, the only class of asset managers (according to our size parameters in the adjacent chart) to underperform the broader indices was the very largest segment – firms with AUM balances exceeding $500 billion. The gradual flow of client assets from larger funds to smaller advisers and the general dissatisfaction with the behemoth asset managers and brokerage houses have been fairly consistent themes since the financial crisis, and many expect these trends to persist in the foreseeable future.

Asset Managers Index :: Breakdown by Size



The fourth quarter of 2010 witnessed the return of the retail investor and resurgence in risk tolerance, both of which are extremely bullish for alternative and traditional asset managers. Indeed these two segments both gained just over 16% for the quarter, outperforming the S&P and all other asset manager types for the period. Any continuation of this trend may have broader implications for the return of private equity (Blackstone up 14% for the quarter) and commercial real estate (Brookfield soared 59% in Q4) even as the housing market continues to show signs of strain.

Asset Managers Index :: Breakdown by Type



The outlook for asset managers in 2011 is generally positive and includes the continuation of many of the aforementioned trends from 2011, including the mobility of funds from larger managers to smaller advisers, and a growing willingness of retail investors to reenter a rising stock market that burned them in 2008 and early '09. Indeed as this newsletter goes to print, 2011 is off to a fast start for most asset managers in the Year of the Rabbit, according to the Chinese Zodiac. Still, 2010 marked the Year of the Tiger, and that didn't turn out to be entirely accurate.

Mergers & Acquisitions Review: 2010 Q4

Investment banking firm Freeman & Co. recently reported that the number of M&A deals among asset managers was up 27% in 2010 with alternative manager dealmaking surging 89%. According to *Pension & Investments*, the increase in alternative manager deals marks the first time the number of such deals outpaced those involving traditional managers. Eric Weber, managing director and COO of Freeman noted, "[2010] marked a return to normalcy with a decline in distressed deals, an increase in asset sales to new healthy buyers, and the return of growth-oriented financings and M&A. We expect 2011 to bring an acceleration of asset sales and a strong rebound in growth-driven deals."

Still, some of the recent impetus for dealmaking, particularly in the alternative manager space, is likely attributable to FinReg legislation and the Volcker Rule, which restricts banks from proprietary trading and places limits on their private equity and hedge fund investments. Weber acknowledges, "there is some real regulatory pressure that's causing transactions that you probable wouldn't see otherwise."

In spite of this assessment, Weber's general outlook for asset manager M&A in conjunction with Bove's expectations for trust bank transactions portends a more auspicious environment for overall dealmaking in the space for 2011. The continued recovery in AUM balances and asset manager valuations could entice prospective sellers previously sidelined by the financial crisis and Great Recession of 2008-09. In an interview with the *Houston Business Journal*, Dean Harman, owner and managing partner of The Woodlands-based Harman Wealth Management, noted that some firms may be looking to expand after shelving acquisition plans during the worst of the recession, and owners of some smaller firms are posturing for an exit now that M&A volume in the sector is beginning to pick up. "The big trend would be the recovery, and from that the people who said, 'hey, I can hang on for a couple of more years and get out," says Harman.

Market Multiples as of 12/31/10

	Ticker	Price / Trailing EPS	Price / Forward EPS	Total Capital / AUM	Total Capital / EBITDA
ASSET MANAGERS					
Affiliated Managers Group, Inc.	AMG	47.02	13.88	2.16%	13.12
BlackRock, Inc.	BLK	21.58	16.63	1.19%	14.07
Legg Mason, Inc.	LM	24.67	17.69	1.07%	12.86
Pzena Investment Management, Inc.	PZN	24.50	19.86	3.30%	12.41
W.P. Stewart & Co., Ltd.	WPSL	nm	nm	3.11%	nm
Westwood Holdings Group, Inc.	WHG	25.62	nm	2.80%	17.29
Group Median		*24.67*	*17.16*	*2.48%*	*13.12*
MUTUAL FUNDS					
AllianceBerstein Investments, Inc.	AB	15.45	12.41	nm	13.31
Calamos Asset Management, Inc.	CLMS	15.05	14.74	1.24%	2.56
Cohen & Steers, Inc.	CNS	24.86	19.77	3.56%	16.59
GAMCO Investors, Inc.	GBL	21.53	16.67	4.92%	12.97
Epoch Holding Corporation	EPHC	27.73	nm	2.77%	16.18
INVESCO Ltd.	IVZ	27.66	14.07	3.00%	17.56
Franklin Resources, Inc.	BEN	17.57	12.65	4.01%	11.00
Diamond Hill Investment Group, Inc.	DHIL	17.14	nm	2.85%	11.04
Eaton Vance Corp.	EV	21.59	14.06	2.20%	10.60
T. Rowe Price Group, Inc.	TROW	27.23	21.51	3.76%	15.34
U.S. Global Investors, Inc.	GROW	23.91	nm	4.76%	14.84
Waddell & Reed Financial, Inc.	WDR	21.01	16.49	4.22%	12.64
Federated Investors, Inc.	FII	14.79	14.54	0.91%	9.09
Janus Capital Group Inc.	JNS	18.01	15.26	1.98%	10.32
Group Median		*21.27*	*14.74*	*3.00%*	*12.81*
ALTERNATIVE ASSET MANAGERS					
Och-Ziff Capital Mgmt Group LLC	OZM	nm	11.21	23.9%	nm
Brookfield Asset Management, Inc.	BAM	48.96	32.32	43.9%	11.95
Blackstone Group L.P.	BX	nm	9.69	4.4%	nm
Fortress Investment Group LLC	FIG	nm	9.19	6.1%	nm
Group Median		*48.96*	*10.45*	*15.0%*	*11.95*
TRUST BANKS					
Wilmington Trust Corporation	WL	nm	nm	nm	nm
Northern Trust Corporation	NTRS	18.98	17.00	2.04%	9.52
Bank of New York Mellon Corporation	BK	14.11	11.84	3.29%	9.51
State Street Corporation	STT	11.76	12.49	1.22%	7.09
Group Median		*14.11*	*12.49*	*2.04%*	*9.51*
OVERALL MEDIAN		**21.58**	**14.64**	**3.06%**	**12.64**

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Segment Focus: Trust Banks

Fourth Quarter 2010 Market Overview

Fourth Quarter 2010 M&A Review

About Value Focus: Asset Management Industry

Mercer Capital's **Value Focus** is a quarterly publication providing perspective on valuation issues pertinent to asset managers, trust companies, and investment consultants. Each issue highlights a market segment: 1st quarter: Mutual Fund Companies, 2nd quarter: Traditional Asset Managers, 3rd quarter: Alternative Asset Managers, and 4th quarter: Trust Banks. To see past issues of **Value Focus**, visit www.mercercapital.com under the Knowledge Center section of our website.

About Mercer Capital

As one of the largest valuation firms in the United States, Mercer Capital provides asset managers, trust companies, and investment consultants with corporate valuation, financial reporting valuation, transaction advisory, portfolio valuation, and related services.

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