Value Focus

Asset Management Industry

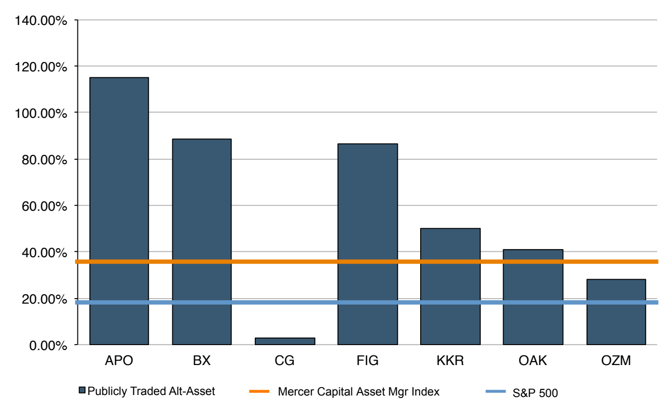
Segment Focus

Alternative Asset Managers

Apollo's shares have more than doubled over the last year as the New York based PE firm has exited several profitable holdings while accumulating capital on its latest flagship fund, Apollo Investment Fund VIII LP, which could total $20 billion before closing to new investors. This would mark the largest buyout fund since the US financial crisis, second all-time only to Blackstone's $21.7 billion raise in 2007. Larger buyout funds such as these tend to boost income from management fees but could squeeze out the potential for carried interest if their stature trumps viable investment opportunities.

Total Returns

for 12 Months Ended 9/30/2013



But the market doesn't seem to mind this trade-off as AUM fees represent a relatively stable source of income to complement unpredictable and often inconsistent returns from carried interest. Stocks of publicly traded PE firms have typically displayed more volatility than traditional money managers, and building larger funds with longer investment horizons may be one way to temper this disparity. Diversifying fund offerings beyond LBOs and into other asset classes such as hedge funds and real estate also helps. Sector analyst Marc Irizarry at Goldman Sachs notes, "All of these firms, including Apollo, have done a lot to diversify their businesses or to position themselves to grow assets on a more sustainable basis. The market is giving them some credit for that."

Much of the divergence in financial and investment performance within the alternative asset manager sector can be explained by timing. A recent article in *Financial Advisor* expounds, "buyout firms' earnings rarely follow a linear path because they are driven by the lumpy timing of exits as well as the "mark-to-market" valuations of fund holdings, which are vulnerable to market swings and required each quarter under accounting rules." The economic cycles and gyrations in the stock market since the financial crisis have compounded this volatility as many of the deals that were struck at the last buyout peak of 2005 to 2007 have taken longer to exit at profitable levels, so their shareholders have yet to witness a full fund cycle while these businesses have been publicly traded.

Irizarry elaborates, "[alternative asset managers] are still 'show-me' stories in the eyes of the market. There's some reluctance on the part of investors to ascribe higher valuations on these managers until they see how sustainable these businesses really are."

Market Review
Third Quarter 2013

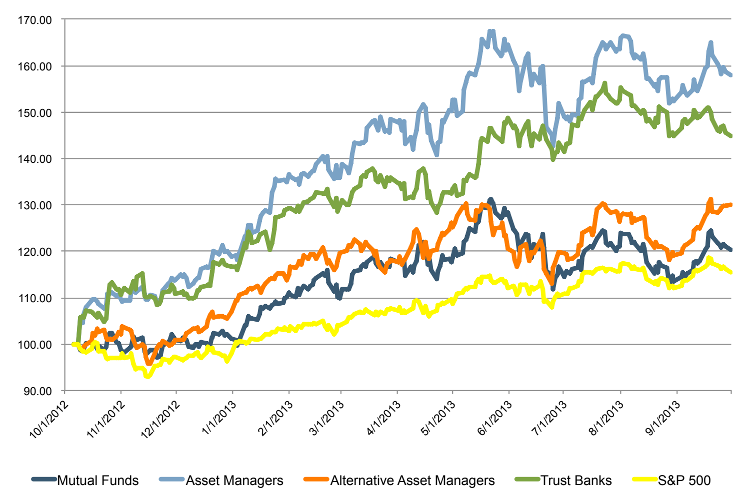
Most publicly traded asset managers continued riding the bull this quarter with many share prices and valuations hovering near all-time highs. A growing appetite for investment products and strong net inflows were additional tailwinds, according to a recent EY report titled, "The Asset Management Index – 3rd Quarter 2013." The report also notes that higher management fees from increases in AUM outpaced rising costs for most managers participating in the survey, leading to significant gains in profitability across the sector.

Not surprisingly, asset managers of all shapes and sizes have, as a whole, outperformed the broader indices in a market environment so conducive to building AUM and generating returns for clients. Specifically, SNL's index of US-based asset managers returned just over 40% in the last year compared to 19% for the S&P. A steady market tailwind helps client retention and net asset flows for most money managers, and the past year has been no exception. The one laggard (on a relative basis) is the mutual fund sector, which is struggling to compete with the increasing popularity and specialization of ETF products.

Still, with AUM balances at or close to peak levels for most equity managers, ongoing management fees and profitability have never been higher, so valuations have risen accordingly. Barring any sort of pending market correction or shift in asset flows back to fixed income, the sector's future appears bright, and buyers are starting to take notice.

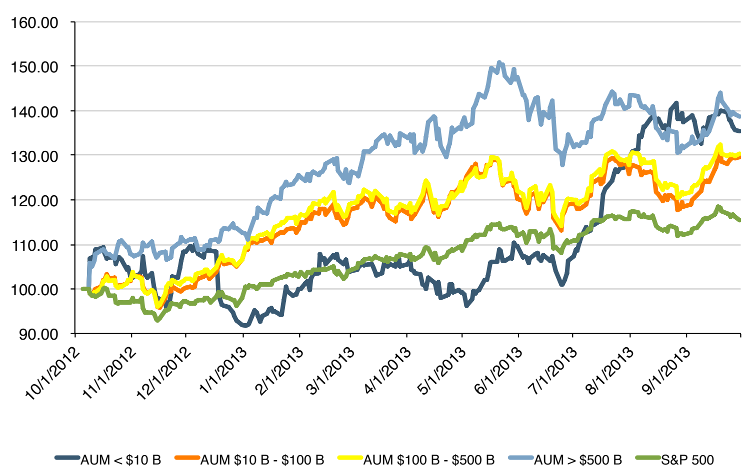
Asset Managers Index

Breakdown by Type



Asset Managers Index

Breakdown by Size



M&A Review
Third Quarter 2013

After a relatively sluggish Q2, asset manager transaction activity picked up again last quarter, driven primarily by acquisitions of private client groups, which represent almost half of the 44 deals that took place, according to Sandler O'Neill's *Transaction Review* for the quarter. The report noted that many of the acquisitions were made by aggregators and roll-ups as United Capital, Banyan Partners, Focus Financial, and Fiera Capital each made at least two transactions in the quarter.

Still, transaction size continues to drift lower with median disclosed deal value falling below $100 million, according to the investment banking firm. This trend could be indicative of buyer's becoming more focused and interested in smaller niche RIAs with private client investors. Divestitures and acquisitions of alternative asset managers remained en vogue during the third quarter as well. The most notable recent transactions include:

- Virtus Investment Partners announced its partnership with $70 billion AUM alternative manager Cliffwater, LLC on October 28, 2013;
- Deutsche Bank's announced sale of its $22 billion AUM Stable Value business to Goldman Sachs;
- Focus Financial Partners's sale of an undisclosed interest to $62 billion manager Centerbridge Partners;
- Dexia SA's sale of Dexia Asset Management to New York Life Investments, which has $100 billion under management;
- Ares Management sold a minority stake to Alleghany Corporation, which manages $66 billion;
- ING's sale of ING Investment Management to Macquarie Group Limited ($22 billion in AUM)

The outlook for asset manager M&A seems relatively positive in light of recent market dynamics. With so many AUM and profit levels near all-time highs, sellers may finally be able to recover the value drained by the financial crisis. The sector's recent growth and prospect for continued asset flows into equities may entice prospective acquirers. The lack of an impending tax deadline may portend lower year-over-year transactions next quarter, but the long-term outlook remains robust.

Asset Manager Multiples

Pricing as of 9/30/13

	Ticker	Price / Trailing EPS	Price / Forward EPS	Total Capital / AUM	Total Capital / EBITDA
TRADITIONAL ASSET MANAGERS					
Affiliated Managers Group, Inc.	AMG	38.96	17.13	2.38%	10.92
BlackRock, Inc.	BLK	17.62	15.48	1.38%	12.60
Legg Mason, Inc.	LM	17.62	13.34	0.85%	12.60
Pzena Investment Mgmt Inc.	PZN	18.22	15.26	2.08%	10.90
Westwood Holdings Group, Inc.	WHG	26.18	nm	2.52%	17.03
Group Median		**18.22**	**15.37**	**2.08%**	**12.60**
MUTUAL FUNDS					
AllianceBerstein Investments, Inc.	AB	24.19	11.29	0.47%	21.02
Calamos Asset Management, Inc.	CLMS	14.20	17.14	1.08%	nm
Cohen & Steers, Inc.	CNS	24.55	17.10	3.18%	15.32
GAMCO Investors, Inc.	GBL	20.70	15.66	4.70%	12.72
INVESCO Ltd.	IVZ	19.26	13.51	2.81%	15.64
Franklin Resources, Inc.	BEN	15.28	13.93	4.27%	10.70
Diamond Hill Inv. Group, Inc.	DHIL	17.79	nm	3.32%	11.52
Eaton Vance Corp.	EV	25.60	15.34	2.07%	12.39
Hennessy Advisors, Inc,	HNNA	15.48	nm	2.06%	11.10
Manning & Napier, Inc.	MN	nm	13.18	0.49%	nm
T. Rowe Price Group, Inc.	TROW	19.72	17.49	3.05%	12.33
U.S. Global Investors, Inc.	GROW	nm	nm	3.66%	nm
Waddell & Reed Financial, Inc.	WDR	21.32	16.92	4.49%	13.19
Federated Investors, Inc.	FII	15.07	15.24	0.85%	9.29
Virtus Investment Partners, Inc.	VRTS	nm	nm	3.66%	nm
Janus Capital Group Inc.	JNS	16.15	12.64	1.37%	8.60
Group Median		**19.26**	**15.29**	**2.93%**	**12.36**
ALTERNATIVE ASSET MANAGERS					
Apollo Global Management, LLC	APO	8.32	9.76	13.95%	8.31
Brookfield Asset Mgmt, Inc.	BAM.A	19.39	nm	nm	9.12
Blackstone Group L.P.	BX	23.47	8.99	6.24%	nm
Carlye Group, L.P,	CG	20.81	7.82	0.66%	6.86
Fortress Investment Group LLC	FIG	33.33	10.00	5.30%	8.38
Kohlberg Kravis Roberts & Co.	KKR	13.30	8.92	9.08%	nm
Oaktree Capital Group, LLC	OAK	9.28	11.29	nm	nm
Och-Ziff Capital Mgmt Group LLC	OZM	nm	8.35	nm	14.88
Group Median		**19.39**	**8.99**	**6.24%**	**8.38**
TRUST BANKS					
Northern Trust Corporation	NTRS	18.70	15.35	nm	nm
Bank of New York Mellon Corp.	BK	18.80	12.08	nm	nm
State Street Corporation	STT	14.40	12.56	nm	nm
Group Median		**18.70**	**12.56**	**nm**	**nm**
OVERALL MEDIAN		**18.75**	**13.43**	**2.66%**	**11.92**

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Value Focus Asset Management Industry

Segment Focus: Alternative Asset Managers

Third Quarter 2013 Market Overview

Third Quarter 2013 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. View past issues at www.mercercapital.com.

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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