

# VALUE FOCUS

## Asset Management Industry



### SEGMENT FOCUS

## Trust Banks

## 2014

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Q1: Mutual Funds
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# Value Focus

## Asset Management Industry

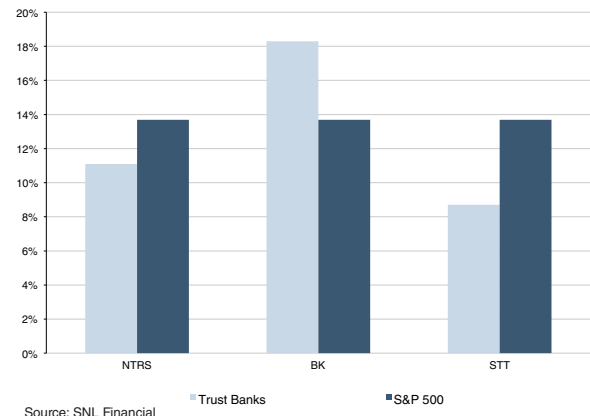
### Segment Focus

#### Trust Banks

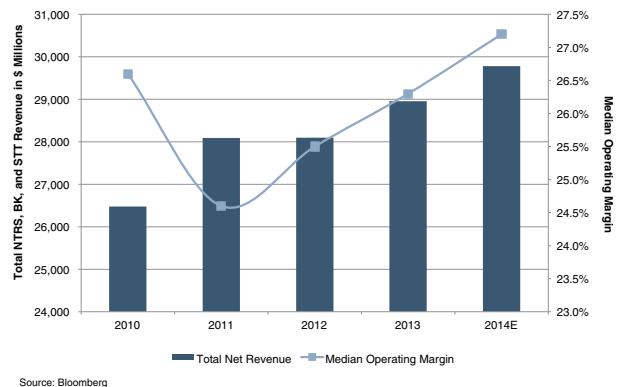
All three components of our trust bank index posted solid gains in 2014, continuing their upward trajectory from the prior two years but still lagging the broader indices since the financial crisis of 2008 and 2009. Placing this recent comeback in its historical context reveals the headwinds these banks have been facing in a low interest rate environment that has significantly compressed their money market fees and yields on fixed income investments. Their recent success may therefore be more indicative of a reversion to mean valuation levels following years of depressed performance rather than a sudden surge of investor optimism regarding their future prospects (See “Valuation Trends” on page 3 for additional perspective on historical asset manager multiples by sector).

Still, in recent quarters, most trust bank stocks have outperformed other classes of asset managers like mutual funds and alternative investors that endured a rocky 2014 as passive products and indexing strategies continued to gain ground on active management. Moving forward, continued market appreciation and any signs of yield curve steepening should lead to further gains in trust bank revenue, margins, and NIM spreads. A reversal of these trends, on the other hand, could send these stocks into correction territory given their recent gains and expectations for higher earnings in 2015.

Total Returns in 2014



Trust Bank Revenue and Operating Margins Since 2010



## Sector Analysis 2014 in Review

Only traditional asset managers and trust banks kept pace with the broader indices in 2014 as demand for passive strategies continues to trump the higher fees associated with alternative investments and mutual fund products. Alternative investment stocks were also anchored by CalPERS decision to abandon hedge fund and FOF strategies altogether and the market's fear that other major pension programs could follow suit.

More traditional RIAs also experienced some headwinds as nearly 80% of actively managed U.S. stock funds failed to beat their benchmarks in 2014, according to data from Morningstar. This trend is nothing new and is considered to be a major contributor to the rise in popularity of ETFs and other index strategies over the last decade. A closer glimpse at the variance in RIA stock performance in 2014 reveals that many of the outperformers during the year like BlackRock and Invesco offer ETF products that hedge against active strategies that tend to lag the market after fee consideration.

Also of note, smaller asset managers continue to outperform their larger counterparts in 2014, but this is likely more attributable to HNNA's (roughly two-thirds of the market-weighted index) outsized gain in market value rather than any indication of investor preference towards smaller advisory firms.

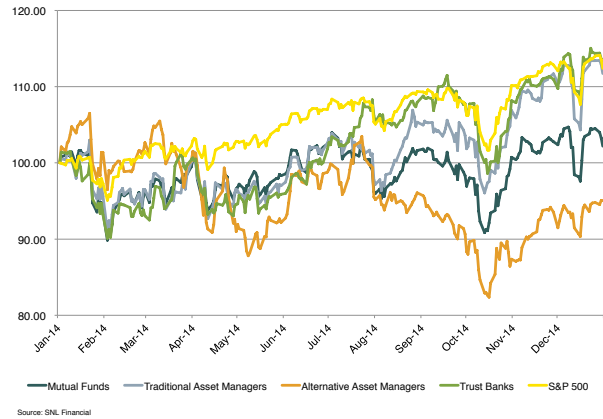
With AUM balances close to peak levels for most asset managers, ongoing management fees and profitability have never been higher, so valuations have risen accordingly in spite of modest multiple contraction over the last year.

## Valuation Trends

Prior to last year, RIA multiples have generally trended upward since 2011 on rising stock prices and the anticipation of higher earnings associated with emergent AUM balances. In 2014, multiples pulled back a bit on slower growth and expectations for continued asset flows out of active equity funds. Despite the multiple contraction, most publicly traded asset managers are more valuable now than ever as earnings growth outpaced the recent rise in cap rates.

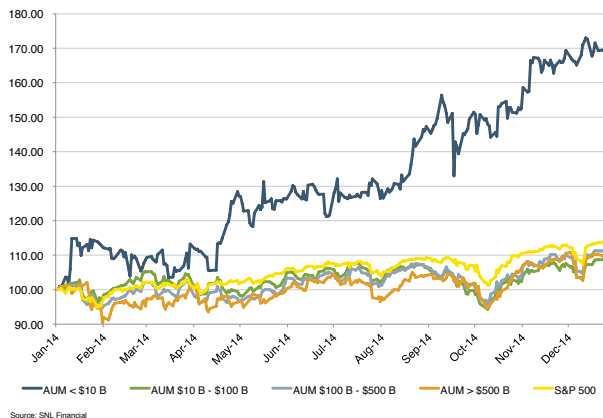
### Asset Managers Index

#### Breakdown by Type

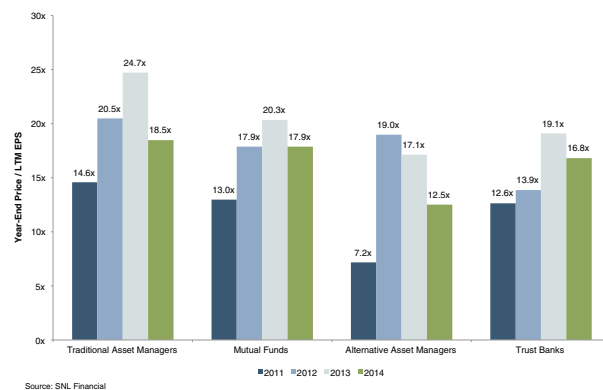


### Asset Managers Index

#### Breakdown by Size



### Historical Median Price / LTM EPS by Sector



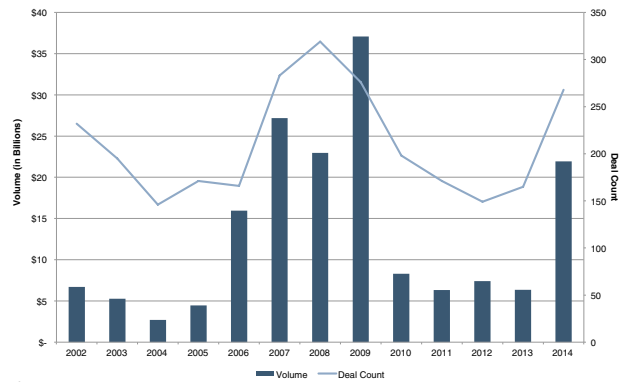
# M&A Review

## Fourth Quarter 2014

Some notable deals in the asset manager space during the fourth quarter include:

- Leading financial services provider TIAA-CREF completed its acquisition of \$230B manager Nuveen Investments on October 1st for \$6.25 billion or 2.7% of AUM. This deal marks the largest asset manager transaction since BlackRock purchased Barclays Global Investors for \$13.5 billion in June of 2009, which was the largest asset manager acquisition since Madison Dearborn bought Nuveen in 2007 for roughly the same amount. Interestingly, the PE firm paid roughly 16x EBITDA on the entry price but only 12x on the exit despite growing AUM from \$166 billion to \$230 billion over the holding period.
- UK-based Henderson Group (holding company of Henderson Global Investors) bought US growth equity manager Geneva Capital Management on October 1, 2014, for initial consideration of \$130 million or 2.4% of its \$5.4 billion in AUM with deferred consideration and potential earn-out payments totaling another \$70 million if certain performance targets are met.
- Affiliated Managers Group (ticker: AMG) completed its acquisition of \$17 billion manager Veritas Asset Management on October 31, 2014. AMG has been the most active acquirer of asset managers in recent months, having already purchased majority interests in SouthernSun and River Road earlier in the year. Collectively, AMG has acquired asset managers with over \$100 billion in AUM in aggregate since the financial crisis of 2008 and 2009.
- Legg Mason (ticker: LM) purchased international equity specialist Martin Currie Limited (\$10.1 billion in AUM) on October 1st after buying NY based QS investors earlier in the year. LM has also been an active acquirer in the space, having added Fauchier Partners in early 2013.

Asset Manager M&A Since 2002



Source: Bloomberg

- The following day Boston Private Financial Holdings completed its acquisition of \$4.5B manager Banyan Partners for a total up front payment of \$65 million with additional earn-out consideration of \$15 to \$20 million based on achieving certain profitability measures. Please see our 2014 Q2 newsletter for a more thorough discussion of deal pricing and terms – <http://mer.cr/1yqzi5s>
- London Stock Exchange Group completed its acquisition of \$275B manager Russell Investments from Northwestern Mutual on December 3, 2014, for \$2.7 billion or 1.0% of AUM.

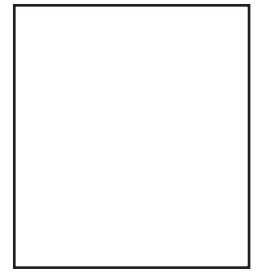
The recent momentum in asset manager M&A could continue well into 2015 and beyond if markets stabilize and valuations remain in a reasonable range. The recent dip in multiples may be enough to entice the more price conscious buyers while sellers can still expect to receive top dollar for their growing businesses. Absent a market correction or sustained period of volatility, 2015 could be another banner year for sector M&A.

## Asset Manager Multiples by Sector

	Ticker	12/31/14 Stock Price	% of 52 Week High	Pricing as of December 31, 2014			
				Price / Trailing EPS	Price / Forward EPS	Total Capital / AUM	Total Capital / EBITDA
<b>TRADITIONAL ASSET MANAGERS</b>							
Affiliated Managers Group, Inc.	AMG	\$212.24	96.74%	27.21x	15.91x	2.09%	9.93x
BlackRock, Inc.	BLK	357.56	96.99%	18.48x	17.42x	1.52%	13.79x
Legg Mason, Inc.	LM	53.37	93.39%	18.48x	16.03x	1.01%	13.79x
Pzena Investment Management, Inc.	PZN	9.46	74.34%	17.85x	15.51x	2.33%	10.14x
Westwood Holdings Group, Inc.	WHG	61.82	27.20%	17.32x	nm	2.59%	11.86x
<b>Group Median</b>			<b>93.39%</b>	<b>18.48x</b>	<b>15.97x</b>	<b>2.09%</b>	<b>11.86x</b>
<b>MUTUAL FUNDS</b>							
AllianceBernstein Investments, Inc.	AB	\$25.83	91.66%	13.67x	12.85x	nm	12.38x
Calamos Asset Management, Inc.	CLMS	13.32	92.24%	13.32x	23.37x	1.16%	nm
Cohen & Steers, Inc.	CNS	42.08	93.47%	24.05x	20.53x	3.79%	14.44x
GAMCO Investors, Inc.	GBL	88.94	98.55%	20.03x	17.44x	5.15%	13.10x
INVESCO Ltd.	IVZ	39.52	95.21%	18.38x	14.22x	2.95%	13.79x
Franklin Resources, Inc.	BEN	55.37	93.17%	14.61x	13.04x	4.08%	10.32x
Diamond Hill Investment Group, Inc.	DHIL	138.04	95.23%	17.39x	nm	3.16%	11.09x
Eaton Vance Corp.	EV	40.93	87.55%	16.77x	13.83x	1.87%	9.72x
Hennessy Advisors, Inc.	HNNA	21.94	87.94%	16.88x	nm	2.88%	11.04x
Manning & Napier, Inc.	MN	13.82	73.24%	nm	11.06x	0.37%	nm
T. Rowe Price Group, Inc.	TROW	85.86	96.86%	19.38x	17.70x	3.06%	12.48x
U.S. Global Investors, Inc.	GROW	3.10	76.54%	nm	nm	4.55%	nm
Waddell & Reed Financial, Inc.	WDR	49.82	65.16%	13.57x	13.72x	3.40%	8.57x
Federated Investors, Inc.	FII	32.93	96.97%	22.87x	19.15x	1.05%	14.02x
Virtus Investment Partners, Inc.	VRTS	170.49	75.01%	20.68x	nm	4.55%	11.31x
Janus Capital Group Inc.	JNS	16.13	97.11%	20.68x	18.35x	1.98%	nm
<b>Group Median</b>			<b>92.71%</b>	<b>17.88x</b>	<b>15.83x</b>	<b>3.06%</b>	<b>11.84x</b>
<b>ALTERNATIVE ASSET MANAGERS</b>							
Apollo Global Management, LLC	APO	\$23.58	64.59%	15.41x	10.67x	11.52%	12.07x
Brookfield Asset Management, Inc.	BAM.A	NA	nm	14.00x	31.09x	46.25%	9.55x
Blackstone Group L.P.	BX	33.83	93.76%	12.35x	9.22x	7.04%	nm
Carlye Group, L.P.	CG	27.50	69.83%	12.50x	9.79x	0.91%	6.25x
Fortress Investment Group LLC	FIG	8.02	87.55%	12.53x	8.91x	3.90%	5.73x
Kohlberg Kravis Roberts & Co.	KKR	23.21	87.58%	10.70x	8.79x	20.96%	nm
Oaktree Capital Group, LLC	OAK	51.83	83.19%	12.52x	14.36x	15.10%	3.43x
Och-Ziff Capital Mgmt Group LLC	OZM	11.68	73.00%	8.28x	7.66x	23.58%	8.49x
<b>Group Median</b>			<b>83.19%</b>	<b>12.51x</b>	<b>9.50x</b>	<b>13.31%</b>	<b>7.37x</b>
<b>TRUST BANKS</b>							
Northern Trust Corporation	NTRS	\$67.40	95.14%	22.17x	18.27x	nm	nm
Bank of New York Mellon Corporation	BK	40.57	97.08%	16.76x	15.19x	nm	nm
State Street Corporation	STT	78.50	97.01%	16.81x	14.67x	nm	nm
<b>Group Median</b>			<b>97.01%</b>	<b>16.81x</b>	<b>15.19x</b>	<b>nm</b>	<b>nm</b>
<b>OVERALL MEDIAN</b>			<b>92.24%</b>	<b>16.84x</b>	<b>14.67x</b>	<b>3.11%</b>	<b>11.09x</b>



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## Mercer Capital

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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](http://www.mercercapital.com).

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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## What We're Reading

### **Jeffrey Gundlach's Surprising Forecast**

*Barron's Market Week: Johnathan R. Laing*

<http://mer.cr/1tTyBG>

(subscription required)

### **2014 Investment Company Fact Book**

*Investment Company Institute*

<http://mer.cr/1x4s3ey>

### **Money-Management Blues**

*Barron's Market Week: Lawrence C. Strauss*

<http://mer.cr/1Dtmizm>

(subscription required)

### **The Worst Case Scenario For Bond Bears According To JPM: Rising Stock Prices**

*Zero Hedge*

<http://mer.cr/1AxdLaV>