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Asset Management Focus
Freeman & Co. LLC

Reports of my Death were Greatly Exaggerated

The credit crisis has had a material impact on many parts of the asset management industry, but similar to Mark Twain's note about his life, the industry is not dead. Some products within the industry have died, such as CDOs and auction rate securities, but the industry will continue to grow, just as it did after the Internet bubble. We highlight a number of these promising areas. Lastly, M&A activity has been robust globally, and while slower in the US it is expected to increase as banks realign their businesses.

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Performance as of June 30, 2008

Index	Total Return 1H 2008	Total Return 1 Year	Total Return Annualized 3 Yr	Total Return Annualized 5 Yr
S&P 500	-11.9%	-13.1%	4.4%	7.6%
NASDAQ	-13.6%	-11.9%	3.7%	7.2%
FTSE 100	-10.8%	-11.6%	6.9%	10.7%
LBGC*	1.0%	7.2%	3.8%	3.6%
HFRI**	-1.0%	1.3%	9.6%	10.0%
FTSE Hedge***	-6.7%	-10.0%	1.8%	10.9%

Lehman Brothers Govt./Credit Index* * Hedge Fund Research Institute Fund Weighted Composite* ****in US$ terms*

Indices at 6/30/08:

DJIA	**11,350**
Nasdaq	**2,293**
S&P 500	**1,280**
FTSE 100	**5,626**
10 Year US Treasury Bond Yield	**3.98%**
USD per GBP	**$1.97**
USD per EUR	**$1.57**

Summary:

- **Deal Activity:** There were 119 acquisitions in 1H 2008, a 28% increase from 1H 2007. Reported deal AUM reached $906 billion compared with $1.35 trillion in full year 2007 and the highlight of 1H 2008 was Ping An Insurance Company of China's acquisition of a 50% stake of Fortis Investment Management ($381 billion AUM).
- While 1H 2008 activity on an annualized basis exceeds the levels of 2007, the sharp decrease in US buyer activity indicates that the credit crunch has had a greater impact on US companies than on those located abroad.
- **Credit Crisis:** The ongoing credit crisis has hit banks and other financial institutions hard, forcing some to divest asset managers and creating opportunity for aggressive buyers. We believe many banks will consider raising capital by divesting product manufacturing and keeping their distribution capabilities.
- **Emerging Markets:** Sustained GDP growth across many emerging economies coupled with increasing interest in local equity markets will benefit specialist asset managers. Already, specialist and regional money managers are seeing levels of funds grow, which we expect will soon be followed by an increase in M&A interest.
- **Retirement Products:** As economic uncertainty puts renewed pressure on retirement savings, new products such as life-cycle funds and managed payout funds have emerged to help investors insure that they will have adequate retirement income. In addition, products such as reverse mortgages and life settlements are gaining ground as a way for investors to raise funds for retirement.

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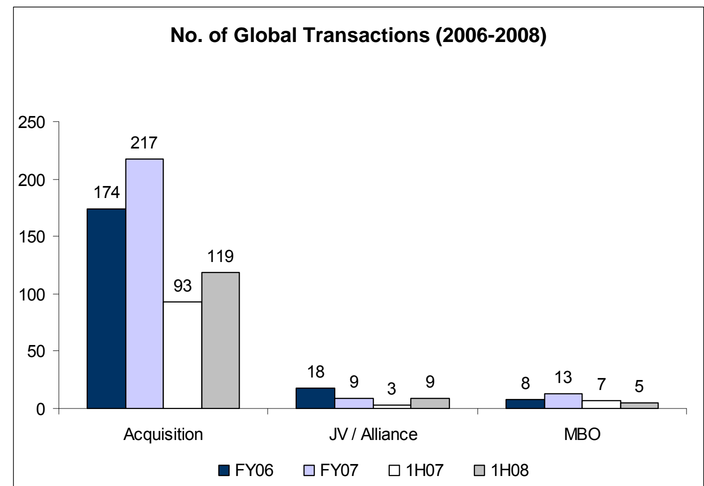
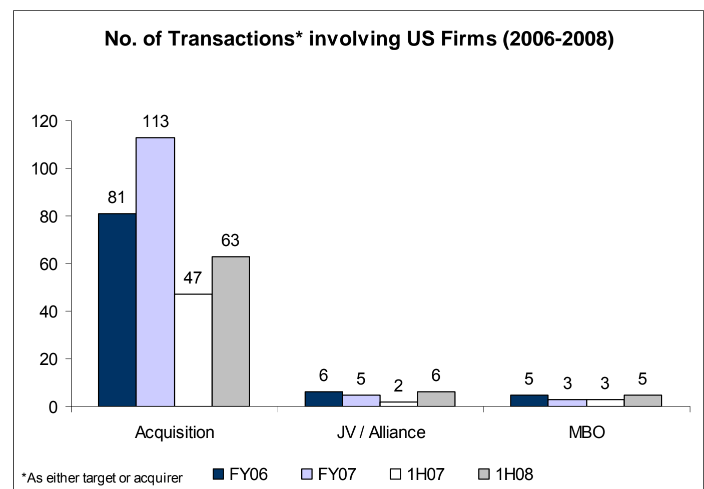
Deal Activity

While deal numbers declined significantly from last year in most industries, the asset management sector actually saw a slight increase in M&A activity. Through the first half of 2008 there were 119 acquisitions globally, 28% more than 1H 2007 and on pace to surpass the record 217 in full year 2007. The year's largest deals included Ping An's investment in Fortis Investment Management ($381 billion) and Royal Bank of Canada's purchase of Phillips, Hager & North ($69 billion).

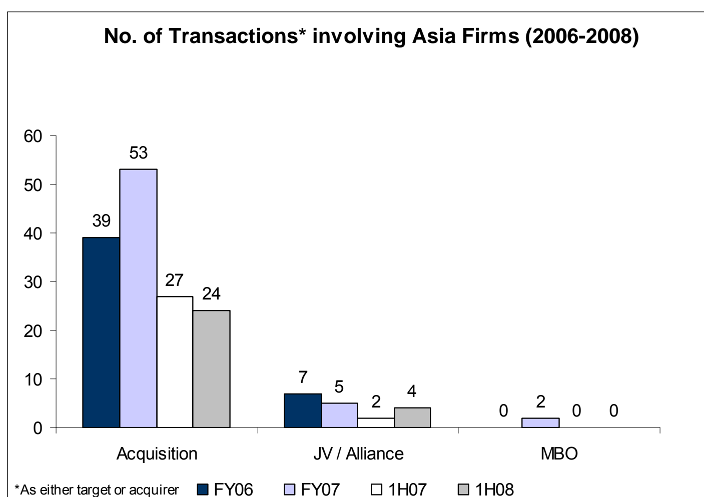


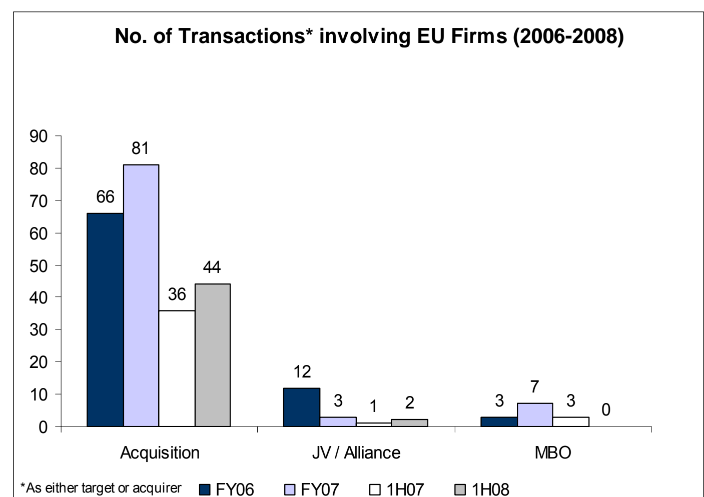
In the US, consolidation pushed the number of first half deals up 34% to 63 versus 47 in 1H 2007. In addition, deal-making in Europe also increased from 36 to 44 in 1H 2008, a 22% jump.

Strong M&A activity in emerging markets continues to underscore the growing demand for asset management services in the region. Asian firms (excluding Ping An's investment in Fortis Investment Management) acquired $43 billion in AUM in 1H 2008 compared with $35 billion during 1H 2007. While the number of deals decreased slightly from 1H 2007's 27 to 24, average deal size increased as larger players began to enter the market. The region's rapid economic growth and high levels of household savings should continue to provide attractive opportunities for asset managers.



While private equity buyers may seem down compared to past years, they are certainly not out. PE firms purchased over $110 billion in AUM in 1H 2008, highlighted by TPG Capital and Pharos Capital's acquisition of American Beacon Advisors ($65 billion) and Blackstone Group's acquisition of GSO Capital Partners ($10 billion). After a year of record fund-raising, look for private equity firms to continue investing in asset managers throughout the second half of the year.

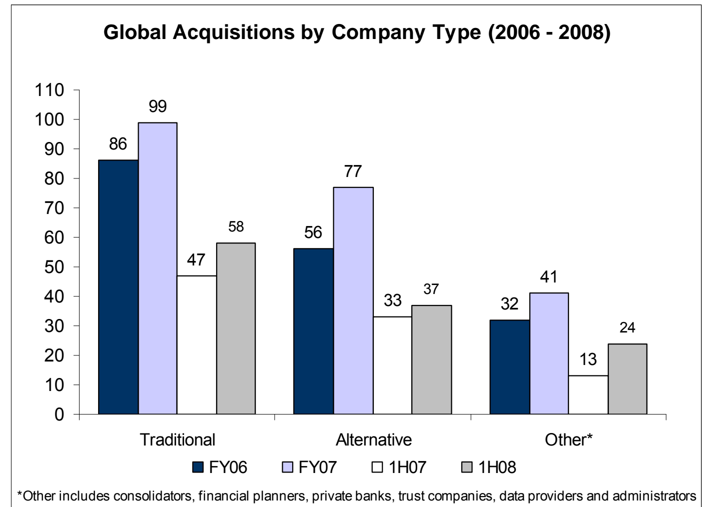




Source: Freeman & Co.

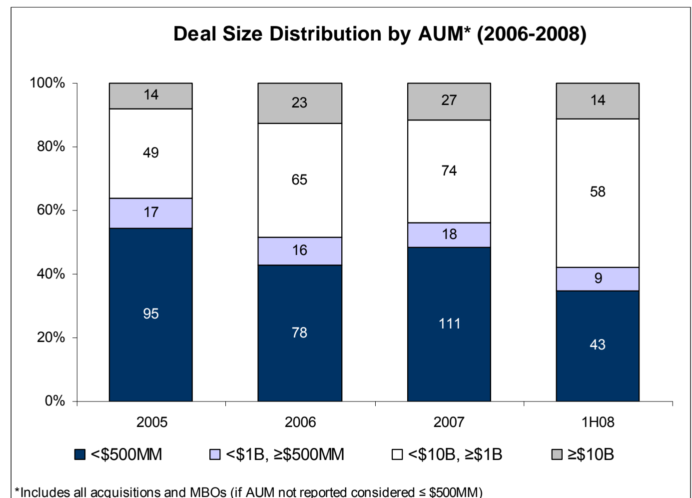
Transactions by Company Type

In the first half of 2008, traditional asset managers and "other" firms (including financial planners, trust companies, administrators and private banks) have seen the greatest increase in deal activity, increasing nearly 23% and 85% respectively from first half 2007. Together, traditional asset managers and "other" firms compose roughly 70% of global transactions for the first half of 2008. After a 37.5% rise in alternative asset manager acquisitions between 2006 to 2007, demand for alternative firms in the first half of 2008 grew from 33 to 37, a marginal increase compared to prior years. Activity in the alternatives sector continues to be driven by investor demand for sophisticated investment products.



Deal Size

With the exception of the Ping An / Fortis transaction ($381.0 billion) middle market and smaller firms dominated deal-making in 2008. The number of middle-market transactions between $1 and $10 billion surpassed the number of deals with AUM <$500 million and at 58 is on pace to surpass the 74 and 65 achieved in full year 2007 and 2006. Notable middle-market deals include Royal Bank of Canada's small stake in quantitative fund manager O'Shaughnessy Asset Management ($9.7 billion) and Blackrock's minority stake in DSP Merrill Lynch Fund Managers ($8.7 billion). Large transactions involving AUM over $10 billion remained relatively constant at 14 compared to 27 in full year 2007 and 23 in full year 2006.



Significant Deals in First Half 2008:

- Ping An Insurance Company of China purchase of a 50% stake in Fortis Investment Management ($381.0 billion)
- Royal Bank of Canada acquisition of Phillips, Hager & North Investment Management Ltd. ($69.0 billion)
- TPG Capital and Pharos Capital acquisition of American Beacon Advisors ($65.0 billion)
- Co-operators Group Ltd. purchase of Addenda Capital ($29.0 billion)
- Mitsubishi Corp minority investment in Aladdin Capital ($17.5 billion)
- CaLPERS minority investment in Silver Lake Group ($16.0 billion)
- AXA Investment Management purchase of a 50% stake in Kyobo Investment Trust Management Company ($15.0 billion)
- Aberdeen Asset Management purchase of Goodman Property Investors ($13.8 billion)
- La Caixa purchase of Morgan Stanley Private Bank-Spanish Operations ($13.3 billion)
- Adam Street Partners MBO of their outstanding 24.9% shares ($12.0 billion)
- BNP Investment Partners acquisition of IMS Group ($10.2 billion)
- Blackstone Group acquisition of GSO Capital Partners ($10.0 billion)
- TA Associates minority investment in Keeley Asset Management ($10.0 billion)

Source: Freeman & Co.

Assets Acquired by Seller Region

Assets Acquired* by Seller Region by Year ($MM)

Region	2004	2005	2006	2007	1H 2008
Africa	4,500	6,970	55,050	4,300	3,800
Asia/Middle East	22,765	52,211	77,832	115,819	45,273
Canada	5,506	32,156	8,045	67,905	103,120
Europe	110,476	488,649	225,341	265,157	498,875
South America	6,432	2,800	7,600	35,150	2,496
US	297,730	549,132	1,842,515	861,261	250,165
Total**	**$447,409**	**$1,131,917**	**$2,220,583**	**$1,349,592**	**$906,129**

	2004	2005	2006	2007	1H 2008
Acquisitions***	86	103	126	142	94
Average Size	5,202	10,989	17,624	9,504	9,640
Median Size***	1,615	1,470	2,600	2,950	2,750

*Assets acquired through acquisitions and MBOs

Source: Freeman & Co.

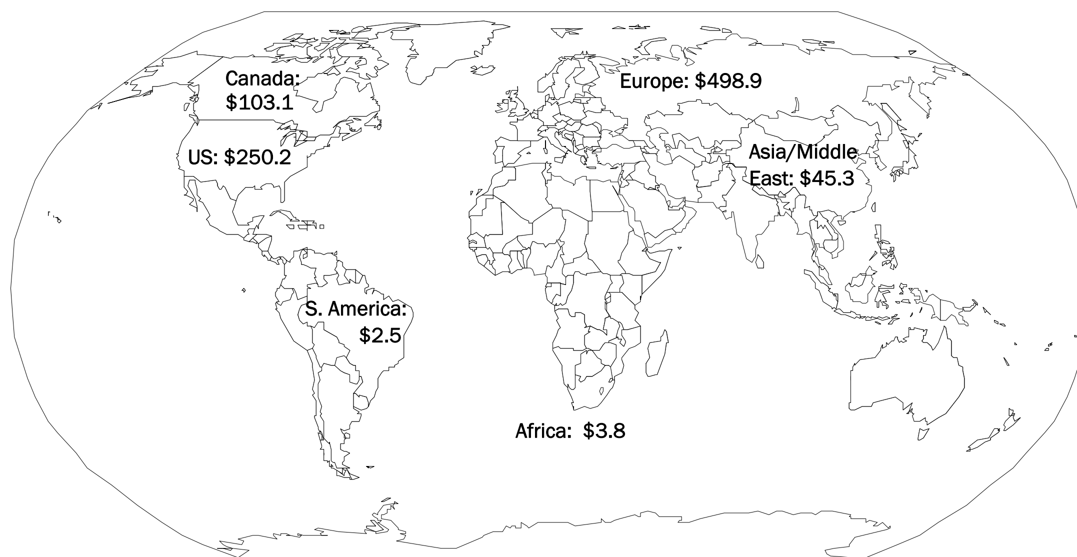
**Totals include assets acquired by Offshore Regions

***Acquisitions and Median deal size calculated using only deals with reported AUM

First half data shows 2008 to be outpacing 2007 in terms of the number of asset management deals. Moreover, 2008 has seen an increase in deal size, and more specifically transactions involving AUM between $1 and $10 billion. Median acquisition size for deals with reported AUM dropped slightly to $2.7 billion from last year's average of $3.0 billion.

The US saw a sell-side drop in assets acquired when annualized and compared against the previous three years. With $253 billion of assets changing hands in the first half of the year, the US is on pace to reach less than an annualized two-thirds of last year. This marks a considerable departure from the positive growth of the last few periods, although it remains to be seen whether we are experiencing a temporary pause or a more permanent downward deviation from the trend. Conversely, Canada has seen its share of sell-side assets acquired increase significantly from an average of $15 billion a year between 2004 and 2006 to $103 billion in the first half of 2008 alone. A noteworthy drop in assets sold occurred in Asia for the first half of the year, going from approximately $116 billion to $45 billion, a 61% decrease. Sell-side activity in Europe (excluding Ping An / Fortis) and Africa also decreased compared to a year prior.

Assets Acquired by Seller Region ($906 Billion)



Source: Freeman & Co. ($ in billions)

Assets Acquired by Buyer Region

Assets Acquired* by Buyer Region by Year ($MM)

Region	2004	2005	2006	2007	1H 2008
Africa	22,880	6,970	55,050	8,500	5,800
Asia/Middle East	985	39,589	79,932	177,283	424,323
Canada	2,006	74,356	8,375	260,200	119,331
Europe	50,635	425,321	252,711	229,998	148,560
South America	0	1,800	0	950	0
US	370,904	583,582	1,824,515	672,661	205,115
Total**	**$447,409**	**$1,131,917**	**$2,220,583**	**$1,349,592**	**$906,129**

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**Assets acquired through acquisitions and MBOs* Source: Freeman & Co.

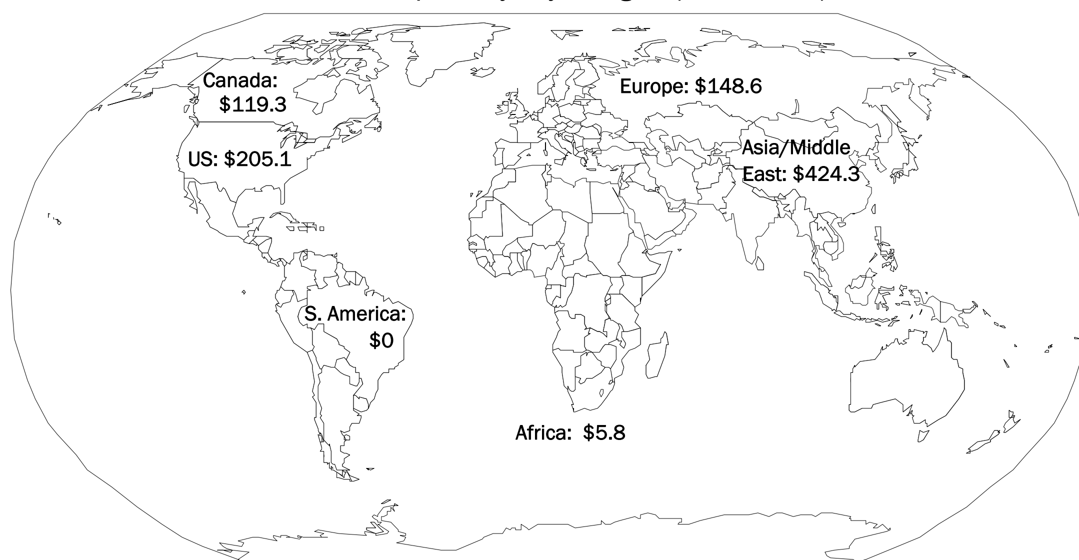
***Totals include assets acquired by Offshore Regions*

****Acquisitions and Median deal size calculated using only deals with reported AUM*

A buy-side analysis of assets acquired highlights some of the emerging developments in the asset management sphere. The most striking change is Asia's move from a net seller of AUM to a net acquirer. Ping An's purchase of 50% of Fortis Investment Management (**$381 billion**), accompanied by an increased stake in Fortis itself, expands an existing relationship and gives Ping An's access to new markets and additional know-how. It follows other high-profile investments by Asian companies in 2007 using cash from high growth in home markets to expand overseas, including the Industrial and Commercial Bank of China's **$5.6 billion** purchase of a 20% interest in Standard Bank of South Africa and the China Development Bank's **£1.6 billion** investment in Barclays. The trend toward aggressive pursuit of asset managers throughout the world has continued in 2008:

- Mitsubishi Corp. (Japan) acquired a minority stake in US credit manager Aladdin Capital (**$17.5 billion**)
- Australia's Macquarie Group purchased a majority of US FI manager Allegiance Investment Management (**$4.5 billion**)
- Istithmar World Capital (Dubai) acquired a majority of US credit manager Gulf Stream Asset Management (**$3.8 billion**)

Assets Acquired by Buyer Region ($906 Billion)



Source: Freeman & Co. ($ in billions)

Credit Crisis

Overview

When the dot-com bubble burst at the turn of the millennium, investors were left with steep losses and a new perspective on the hazards of letting "irrational exuberance" run wild. The latest crisis has already left investors with 2000-esque portfolio returns and promises to seriously alter the long-term dynamics of financial markets. The widespread and well publicized failures of commercial lenders, investment banks and hedge funds over the past twelve months have left many in the industry wondering if the carnage will ever come to an end. Indeed, few financial institutions have been spared by recent events, and while credit markets are showing signs that they might soon begin to unfreeze, firms are still vulnerable to additional systemic economic shocks. Asset managers have borne their fair share of the market's wrath, and while the ultimate extent of the damage to the space is still being appraised, it is clear that many firms will have to reevaluate key components of their businesses to survive in a post-credit crunch world. In this article, we discuss a few of the implications the crisis will have for asset managers as well as highlight a few ways in which prescient firms can take advantage of the opportunities it presents.

Credit Crisis Recap

As we discussed in more detail in our previous Asset Management Newsletter "The World is a Different Place" here is how we got into this mess:

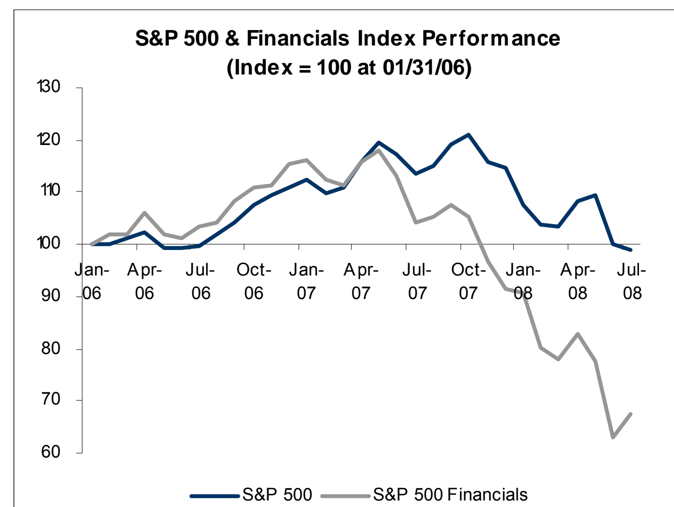
- Easy credit, soaring housing prices and relaxed lending standards led to demand for complex structured products with little transparency into the underlying assets.
- Credit risk priced far too low resulted in lenient lending conditions and dangerous amounts of leverage.

When the true value of the assets underpinning many of these complex instruments was finally recognized, banks were no longer able to sell them to investors resulting in the following events:

- Banks are left with $billions worth of distressed structured products whose illiquid nature makes them nearly impossible to value.
- Since July 31, 2007 investment banks have had write-down in excess of $364 billion and raised $279 billion in new capital.
- This, coupled with a significant increase in risk aversion by banks, squeezes liquidity across financial markets and severely curbs lending.

This leaves us with the current distressed conditions we see across the financial industry. However, possibilities do exist for well positioned firms to take advantage of dislocations in the market. We believe that moving forward, firms able to capitalize on the following three opportunities will enjoy a significant advantage over their peers:

1. Acquisition of quality asset management arms through divestitures by distressed banks.
2. Demand for new products by investors with evolving needs and risk appetites.
3. Investors flight to quality.



Source: Bloomberg

Write Downs & Capital Raises During the Credit Crisis (up to 8/27/08)

Firm	Write-Downs ($B)	Cap Raised ($B)	Market Cap ($B)
Citi	$55.10	$49.10	$97.15
Merrill Lynch	51.80	29.90	36.91
UBS	44.20	28.10	61.64
HSBC	27.40	3.90	185.33
Wachovia	22.70	11.00	30.31
Bank of America	21.20	20.70	132.33
Washington Mutual	14.80	12.10	6.12
Royal Bank of Scotland	14.40	23.60	66.01
Morgan Stanley	14.40	5.60	42.79
JPMorgan Chase	14.30	9.50	125.83
Deutsche Bank	10.60	3.20	43.38
Credit Suisse	10.40	2.70	52.64
Barclays	10.00	18.20	49.58
Lehman Brothers	8.20	13.90	9.95
Credit Agricole	7.90	8.70	43.04
Fortis	7.30	7.10	31.07
Societe Generale	6.70	9.60	54.33
CIBC	6.40	2.80	20.95
WestLB	4.70	7.40	N/A
E-Trade	3.60	2.40	1.58
Nomura Holdings	3.30	1.20	25.60
Natixis	3.20	6.60	10.59
Mitsubishi UFJ	1.60	1.60	81.57
Totals	**$364.20**	**$278.90**	

Source: Bloomberg & Freeman & Co. research

Divestitures by Distressed Banks

One outcome on the M&A front we expect to see from the credit crisis is increased interest by commercial banks in divesting in-house asset management platforms. Over time, a number of banks (from international money-center institutions to small regionals) have acquired or developed robust investment management platforms. This is generally a sensible strategy, as having their own platforms enables these banks to offer in-house investment product to their institutional and high net worth clients. Asset managers provide recurring fee income, offsetting declining net interest margins without burdening the bank's balance sheet.

Despite these benefits, distressed institutions desperate for capital will be forced to swallow hard and consider putting these platforms up for sale. Even "crown jewel" firms (like Lehman's Neuberger Berman unit) don't have immunity in this reality show. Successful platforms are to some degree victimized by their own success, as they become candidates for divestiture because their strong market position and recurring revenues enables them to command attractive valuations. Many are large enough to meaningfully impact their parent's financial condition. Weaker platforms are candidates too, as their owners decide they can replace them with products managed by third parties. There are multiple strategies for dealing with the transaction, including traditional sub-advisory agreements or using a TAMP/SMA provider to provide access to products managed by top-tier managers.

Although we haven't seen a run of divestitures of bank-owned platforms yet (it is still a strategy of last resort), there have been a few over time. The prospect for more arises when we examine banks with large, desirable platforms that have been hit hard by the credit crunch.

The need for banks to divest their asset management businesses creates opportunities for well-capitalized strategic buyers. Well-diversified bank platforms with marketable products, good performance and valuable clients can be a transformational addition to an existing asset management platform.

Select Banks with Asset Management Arms

Bank	Market Cap ($B)	Stock Price 6/30/07 - 6/30/08	Name of Main AM Unit	AUM ($B)
National City	$3.9	(86%)	Allegiant Asset Management	$29
Fifth Third Bancorp	7.9	(74%)	Fifth Third Asset Management	33
Lehman Brothers	12.8	(74%)	Neuberger Berman	277
Wachovia	39.3	(70%)	Evergreen Investments	245
Key Corp.	6.2	(68%)	Victory Capital Management	80
SunTrust	16.4	(58%)	Trusco	137
Wells Fargo	104.6	(32%)	Wells Fargo Investments	256
US Bancorp	55.6	(15%)	FAF Advisors	158

Source: Company Filings and Freeman & Co. research

Financial buyers with access to capital will join the party too. With their dependable cash flow, some bank-owned asset managers may be attractive LBO targets. And where banks need capital but are not prepared to divest their asset management units completely, private equity firms and other financial buyers can enter as buyers of minority stakes.

Of course, just because the "for sale" sign is out does not always mean you should buy. Bank-owned asset managers are notoriously uneven in quality. Care must be taken to avoid too much "plain vanilla" product. It will not be differentiating for the buyer, and it may be a challenge to integrate with the buyer's operation. Even if the product set is desirable, care still must be taken to make sure that the firm has the necessary track record and depth of investment talent to attract and retain investors.

Even if the manufacturing operation is running on all cylinders there still may be a problem with distribution and the client base. If the AUM flow is overly dependent on the bank parent, there may not be much worth buying. And the *non*-bank distribution must be examined to insure that it is sufficiently robust.

Previous Asset Management Spin-Outs

Bank	AM Unit	Acquirer	Year	Deal Value ($MM)	AUM ($B)
Fortis	Fortis Investment Management	Ping An Insurance Co.	2008	3,359(1)	381
National Bank of Canada	Asset Management Finance (AMF)	Credit Suisse	2008	384(2)	50
SunTrust	**Lighthouse Partners**	HFA Holdings	2007	624(3)	9
Bank of America	Marsico Capital	MBO	2007	2,700	94
Commerzbank	Caisse Centrale de Reescompte	UBS	2007	366	24
PNC	Blackrock	Merril Lynch	2006	9,500(4)	539
Washington Mutual	WM Advisors	Principal Global Investors	2006	740	26
Comerica	Munder Capital Management	MBO / Crestview Partners	2006	302	25
AM South (now Regions)	AM South Mutual Fund Business	Pioneer Investments	2005	n/a	5
PNC	Blackrock	MBO	1999	126(5)	165

(1) Purchase of 50% stake

Bold denotes client represented by Freeman & Co.

(2) AMF holds passive, non-voting revenue share interests in 12 asset managers with combined AUM of $50 billion

(3) Purchase of SunTrust's 25% stake

(4) PNC reduced its holdings in Blackrock from 70% to 35%

(5) Purchase of 30% stake

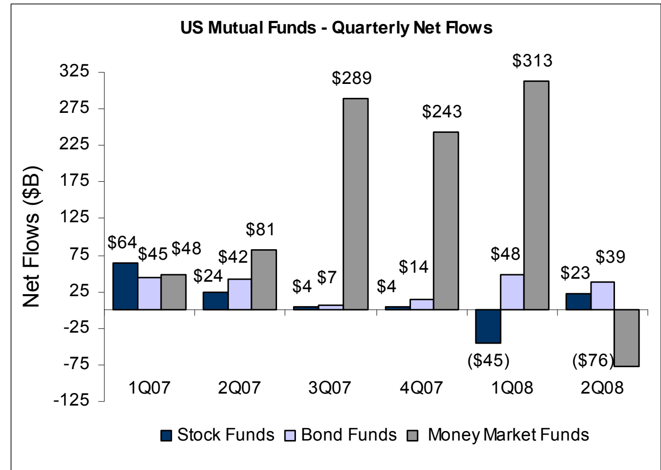
Source: Company Filings and Freeman & Co. research

Product Challenges

In this challenging environment, what can an investor do?

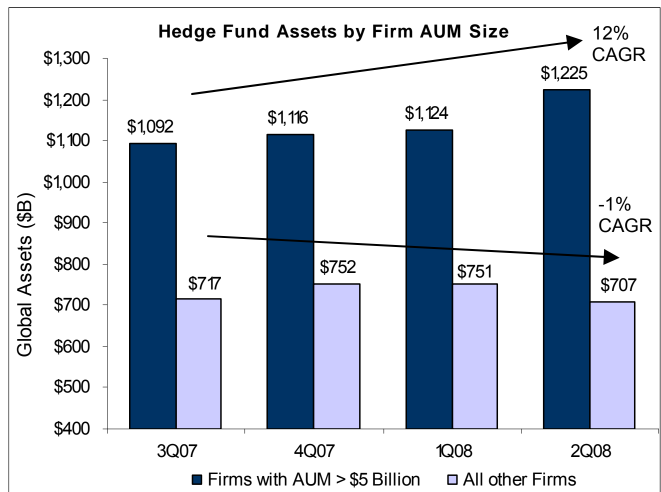
- **Equities:** The S&P was down nearly 12% YTD at June 30, with recovery still uncertain; Nasdaq was even worse.
- **Bonds:** Total return for the LBGC was only 1% YTD.
- **Cash:** Investors have been seeking shelter here as seen by flows leading up to the 2nd quarter of 2008, yields do not keep up with inflation.
- **Credit derivatives, CDOs, MBS and other exotic products:** Not for most investors now as distressed buyers circle.

Investors are faced with losses, poor prospective returns, low cash yields and rising inflation. Any negative period also creates opportunity for product manufacturers and investors:



Source: ICI

Problem	Solution / Example
Correlated risk amplifies volatility	Uncorrelated risk products - Mortality risk (life settlements, etc.), real estate
Liquidity, market problems have overly impacted some credits	Disciplined investment in distressed credit - Distressed debt funds
Concern over insufficient retirement income	Retirement products - Life cycle, reverse mortgage
Absolute return with downside protection	Principal protected notes and similar products

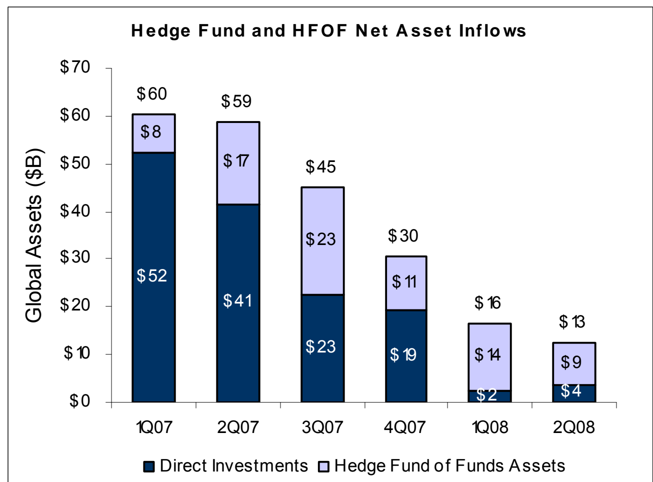


Source: Hedge Fund Research Institute

Flight to Quality

The credit crisis has caused investors to shift from taking all kinds of risk for no premium to taking no risks regardless of the premium offered, as one of our past clients indicated. This risk shift is having an impact on asset management business models, too. There is an aversion to smaller firms and to non-diversified products. We expect investors will favor products from larger firms with greater resources and infrastructure, which will continue to increase the competitive pressures on firms below "critical mass" levels of AUM.

Preferred	Less Preferred	Reason
Large, established managers with well-established processes and deep teams	"One man bands" and small, less seasoned firms	Process will be more important than "talent"
Firms with transparent processes and products (such as SMAs)	Black boxes	Much more scrutiny of risk management issues
HFOFs	Single strategy hedge funds	Investors increasingly find it "worth it" to pay HFOF fees to insure that the due diligence and risk analysis has been done



Source: Hedge Fund Research Institute

History of Valuations – Stock Prices

Over the past 2 ½ years public asset managers and the overall market experienced growth (albeit at different levels) to mid-2007 and then as credit issues arose and the overall economic conditions worsened, their stock levels fell off.

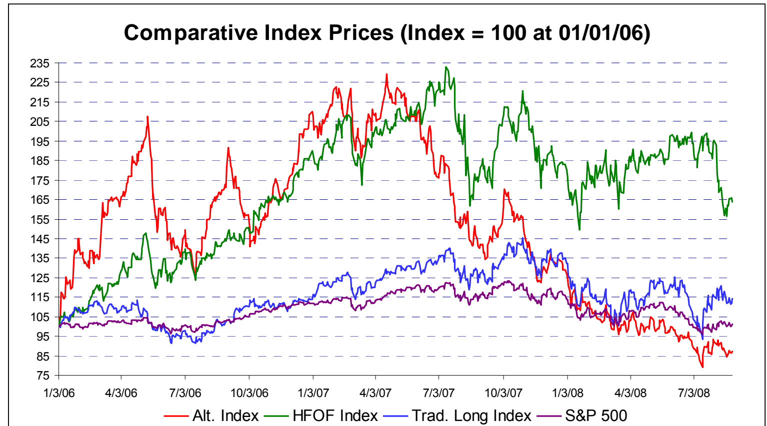
- Stocks of **alternative managers** experienced immense levels of growth supported by strong historical performance and the exuberance of the Fortress and Blackstone IPOs. Stock prices reached as high as 230% of 01/01/06 levels on 04/20/07. However as performance and market conditions have weakened the exuberance has worn off and prices have fallen sharply to 87% of 01/01/06 levels.
- **HFOF managers** (Man Group and Partners Group) rose sharply like the other alternative managers, achieving 233% of their 01/01/06 levels on 07/13/07. However, unlike the other alternative managers, HFOFs have fended off a sharp decline and still trade at 164% of their 01/01/06 levels. The resilience is in part due to their being less dependent on incentive fee revenues than hedge fund or private equity firms.
- Stocks of **traditional managers**, historically having a beta not much more than 1.0, have slightly outperformed the S&P 500, peaking on 10/30/07 at 145% of 01/01/06 levels. Traditional managers currently trade at 114% of 01/01/06 levels as compared to the S&P 500 which is about where it was at the beginning of 2006.

EBTIDA Multiples

As in the post dot-com era where the average EBTIDA multiple of traditional managers dropped approximately 6x from 13x to 7x, the current market environment has created a similar plunge. Since year-end 2007, the average EBITDA multiple has come down roughly 30% from 14x to 10x.

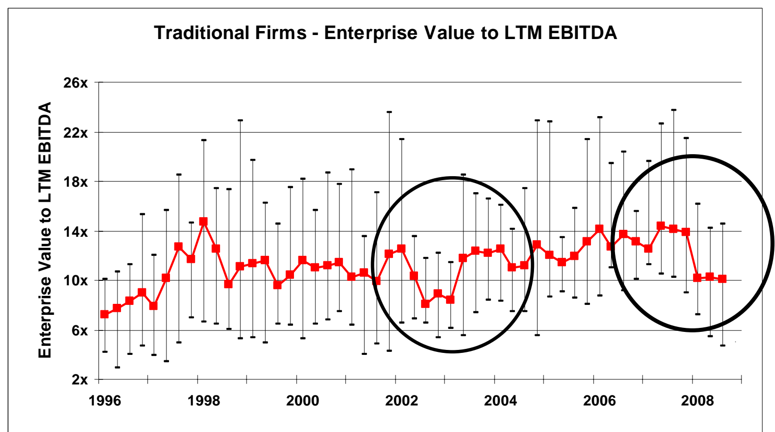
Will the rebound be similar to that experienced 4-6 quarters after the post dot-com trough? There is reason to think so, as traditional asset managers as a business have relatively steady revenue streams and little to no balance sheet risk.

Alternative managers that have recently entered the public market (e.g.. Fortress Group, Blackstone, Polar Capital, GLG Partners, Och-Ziff) have experienced a challenging start with valuations down as much as 60% off of initial IPO levels. Lower performance and tightened lending conditions have played key roles in this decline.



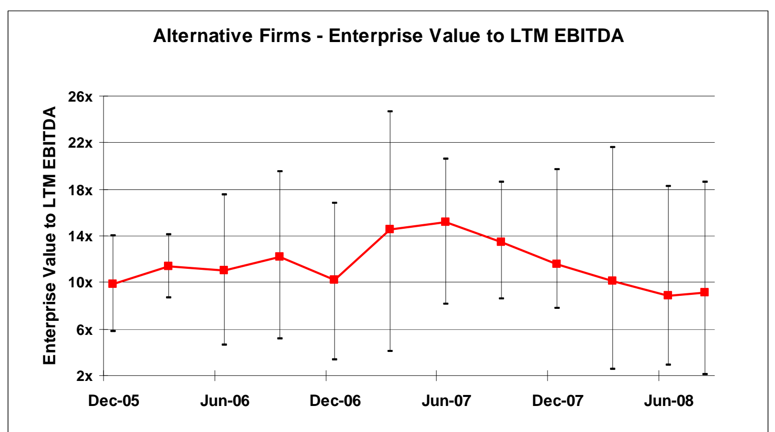
Traditional Long Index: Blackrock, Eaton Vance, Federated Investors, Franklin Resources, INVESCO, Janus Capital, Legg Mason, Schroders, T Rowe Price
HFOF Index: Man Group, Partners Group
Alternative Index: Absolute Capital, Blackstone, BlueBay, Charlemagne, Fortress, GLG Partners, Och-Ziff, RAB Capital
Note: The above are all equally weighted indexes

Source: Capital IQ



Traditional Firms: Blackrock, Cohen & Steers, Eaton Vance, Federated Investors, Franklin Resources, Gamco, INVESCO, Janus Capital, Legg Mason, SEI investments, T Rowe Price, Waddell & Reed

Source: Publicly available SEC filings, Capital IQ, Freeman & Co.



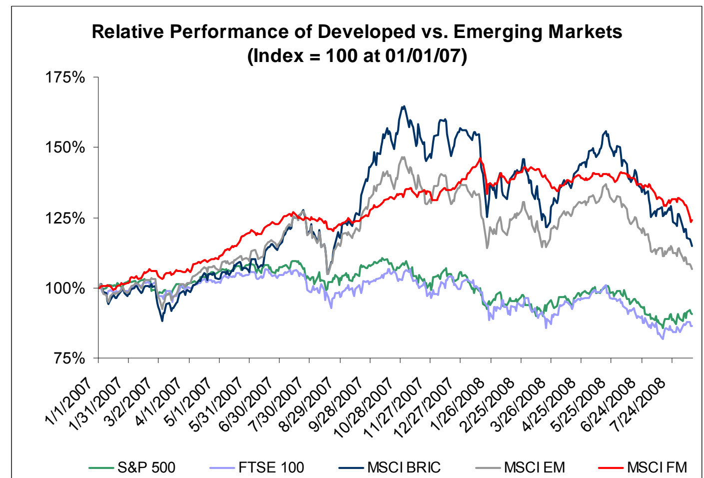
Alternative Firms: Ashmore, Blackstone, BlueBay, Charlemagne Capital, Fortress, GLG Partners, Man Group, Och-Ziff, Partners Group, Rab Capital

Source: Publicly available SEC filings, Capital IQ, Freeman & Co.

The Future of Emerging Markets Asset Management

Introduction

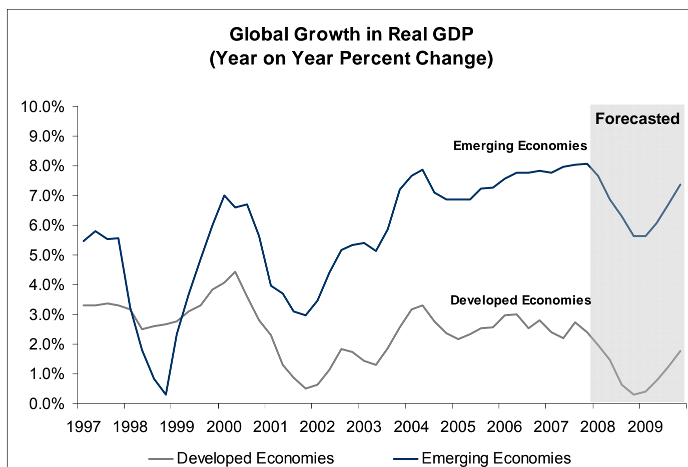
Over the past fifteen years emerging markets have captured the attention of investors and asset management executives alike. The former have been looking to ride the 'demographic' and 'emerging middle class' themes and tap the potential for uncorrelated returns. The latter have been enticed by the possibilities of greater business diversification and the potential to access increasing allocations from both local and domestic funds. Notwithstanding short term volatility, we see emerging market firms gaining in relative size and importance in the years to come from all perspectives: allocator, investor and corporate acquirer. Moreover, whilst many of the large global asset managers have a deep history and meaningful presence in emerging markets we are also witnessing a significant growth in independent firms both from existing Western bases and, increasingly, locally within the emerging markets themselves.



Source: Bloomberg

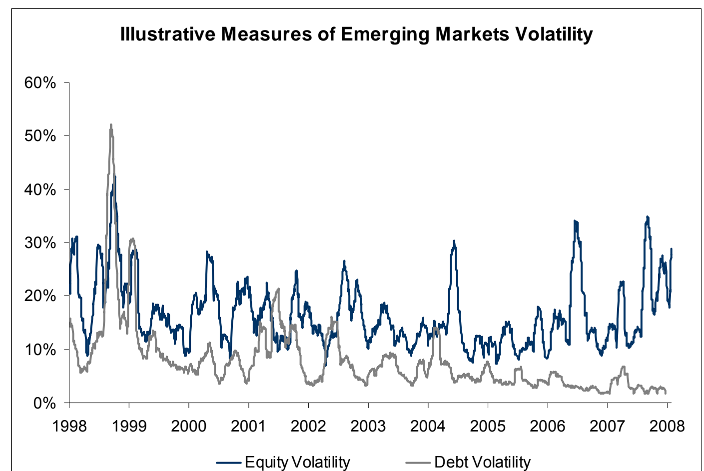
A Long Term Play

When considering the future of emerging markets it is important not to over-analyze the weekly ups and downs of the indices but instead evaluate the long-term fundamentals. At their most basic levels, emerging markets present a long-term growth play that provides investors the opportunity to capitalize on the surging population growth and economic development of second and third world nations that have adopted market-oriented economic policies. In line with higher expected returns are higher risks, both in the forms of country/region specific risks (i.e. political risk, currency risk, inflation, etc.) as well as differing standards of corporate transparency and potential liquidity issues. Still, growth prospects continue to be strong. According to World Bank data, the combined GDP of the four largest emerging markets – Brazil, Russia, India and China (collectively referred to as BRIC) – has grown at a CAGR of 6.1% from 2000 to 2007, representing 13% of global GDP in 2007 and is currently expected to exceed 15% by 2008. Whilst economists predict that emerging economies with populations over 20 million will continue to face volatility in coming years, their combined GDP is expected to double over the next ten years and increase five-fold within twenty years. In contrast, the combined GDP of OECD countries is not expected to exceed a 50% increase in ten years and less than double in twenty.



Source: IMF

Note: Developed Economies include Australia, Canada, Denmark, Euro area, Japan, New Zealand, Norway, Switzerland, Sweden, UK and USA



Source: EMPEA

Note: Equity volatility demonstrated by MSCI Emerging Markets Index; Debt volatility demonstrated by EMBI Global Index

Recent market movements in the world's largest emerging markets, however, might make the above seem a little out of date. Since January 2008 China's Shanghai Composite index has fallen 52%, Russia's stock market has fallen by 27%, India's by 37% and Brazil's by 5%. Yet all that this short term volatility reinforces is the point that successful investing in emerging markets requires a long term time horizon. Investors may be more selective and risk-conscious going forward but they have not completely lost their taste for emerging markets investing. Middle Eastern and African markets, for example, have remained popular and experienced positive net asset inflows that have continued to grow. East Asian markets too are gradually recovering from their steep drops in 1H 2008 and in the wake of the continuing level of global exposure it is possible that the region will see asset net inflows again turn positive. Moreover, should the US dollar continue to strengthen, global trade with dollar-linked emerging markets will likely improve and help promote growth and momentum in the medium-term.

Current Key Players and Products

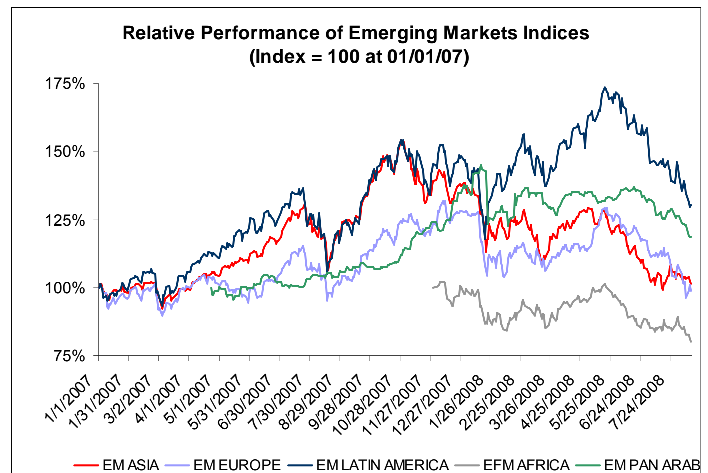
Historically, the lion's share of emerging markets public equity, both retail and institutional, has been invested in Global and Regional Emerging Markets products offered by the largest, best known names in asset management: firms such as Oppenheimer, Templeton, Fidelity, Schroders, Threadneedle and Legg Mason to list a few. In addition to these giants are a handful of independent global Emerging Markets specialists which have grown rapidly in recent years. At present, the list of players in the US and Europe with a firmly established presence in the space is substantial but hardly exhaustive when compared to the related market potential. If allocations to emerging markets continue to grow, and we believe they will, those underweight in emerging markets products or expertise will likely look to buy or build enhanced positions.

From a product perspective, existing Global and Regional funds will continue to offer a highly diversified geographical coverage of emerging market countries around the world. By investing in all of the major regions/companies in a specific region, these funds necessarily restrict their investment universe to the companies with the largest market capitalizations in the largest countries. As such, many are as proportionately shallow as they are broad. Whilst all segments are likely to grow, we think there will increasingly be product innovation and specialization led by locally managed specialist firms across the emerging markets.

An Alternate Paradigm: Be Specialized, Be Local

Recent years have witnessed the emergence of a new breed of emerging markets asset managers whose mantra is 'be specialized and be local (or multi-local)'. Many such firms are headquartered in the regions in which they operate. Because of it, instead of offering a generic CEE or pan-African equity fund, these firms launch much more specialized regional or country-specific funds that place a greater emphasis on local alpha rather than regional beta. Additionally, many of these firms currently market their funds domestically as well as to the developed markets and have been greeted with enthusiasm by local investors who are eager to invest in their own futures. This trend both reinforces these firms' dedication to the region and provides them with an additional, generally stickier investor base.

In addition to covering each region in greater detail, emerging markets specialists have also significantly improved investors' access to a large number of frontier markets too small to be covered by many GEM funds. In 2007 African stock markets boasted eye-catching returns of 56% and in recent months the MSCI Frontier Markets index overtook its Emerging Markets peer while demonstrating significantly less volatility. Indeed, frontier markets have become increasingly popular with investors and asset managers alike precisely because



Source: Bloomberg

Country Constituents of Relevant Indices:
MSCI EM Asia: China, India, Indonesia, Korea, Malaysia, Pakistan, Philippines, Taiwan
MSCI EM Europe: Czech Republic, Hungary, Poland, Russia, Turkey
MSCI EM Latin America: Argentina, Brazil, Chile, Columbia, Mexico, Peru
MSCI EFM Africa: Egypt, Kenya, Mauritius, Morocco, Nigeria, South Africa, Tunisia
S&P/IFC Pan Arab: Bahrain, Egypt, Jordan, Kuwait, Lebanon, Morocco, Oman, Qatar, Saudi Arabia, Tunisia, U.A.E.Saudi Arabia, Tunisia, U.A.E.

they are largely uncorrelated with global markets, with other emerging markets, and with each other. The downsides, however, are their limited size, liquidity, and access. Further, they pose the same macro risks as emerging markets, also magnified by the fact that frontier markets are generally less mature than those dubbed “emerging”.

Whether independent or asset management subsidiaries of larger regional financial institutions, specialized firms are the new trend setters for the emerging markets asset class and we expect to see their business models replicated elsewhere. Below, we have set out an illustrative sample of specialist emerging markets managers which have caught our attention in recent times (please note that this list is not exhaustive).

Illustrative Sampling of Specialist Emerging Markets Managers

Asset Manager Company	Headquarters	Year Founded	Ownership	Product Focus	AUM ($mm)
Diversified					
Ashmore Asset Management	London, UK	1992	Publicly Listed	Diversified	37,500
Emerging Markets Management	Arlington, USA	1987	Independent	Diversified	17,500
Actis Partners	London, UK	1948	Independent	Private Equity	6,800
Charlemagne Capital Ltd.	London, UK	1995	Publicly Listed	Diversified	5,000
EM Capital Management	San Francisco, USA	2000	Independent	Hedge Funds	1,300
Asia					
SPARX Asset Management	Tokyo, Japan	1989	Independent	Diversified	8,100
Value Partners	Hong Kong, China	1993	Independent	Value	6,400
Arisaig Partners	Singapore	1996	Independent	Diversified	4,200
Artradis Fund Management	Singapore	2001	Independent	Hedge Funds	4,000
ADM Capital	Hong Kong, China	1998	Independent	Distressed Debt	2,400
Ward Ferry Management	Hong Kong, China	2000	Independent	Hedge Funds	2,000
Apex Capital Management	Hong Kong / New York	2004	Independent	Hedge Funds	1,300
Central & Eastern Europe					
East Capital	Stockholm, Sweden	1997	Independent	Diversified	6,700
UFG Asset Management	Moscow, Russia	1996	Independent	Diversified	675
Latin America					
Gavea Investimentos	Rio de Janeiro, Brazil	2003	Independent	Hedge Funds	6,500
Fir Capital	Belo Horizonte, Brazil	1999	<50% DFJ	Venture Capital	5,500
GP Investments	Hamilton, Bermuda	1993	Publicly Listed	Private Equity	3,000
GAP Asset Management	Rio de Janeiro, Brazil	1996	Independent	Hedge Funds	2,800
Moneda Asset Management	Santiago, Chile	1993	Independent	Diversified	2,300
Middle East & Africa					
Citadel Capital	Cairo, Egypt	2004	Independent	Private Equity	7,000
Allan Gray	Cape Town, South Africa	1974	Independent	Diversified	5,800
Blakeney Management	London, UK	1990	Independent	Value	2,300
Frater Asset Management	Cape Town, South Africa	1998	Independent	Diversified	1,100
Algebra Capital	Dubai, UAE	2006	25% Franklin Temp.	Diversified	1,000

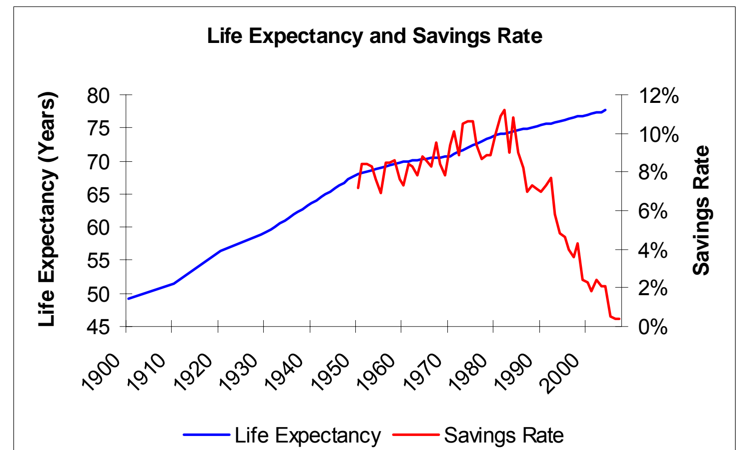
Source: Freeman & Co. & Company websites

Paralleling current M&A trends in the HFOF and Private Equity segments, two firms in the above list of specialist emerging market managers, Fir Capital and Algebra Capital, have sold minority stakes in their businesses to high-powered buyers looking to expand their experience and expertise in a new market. In both cases the financial partnerships have the potential to offer strategic cross-marketing opportunities for both buyer and seller: Fir Capital and Algebra Capital should benefit from the global relationships and fundraising capabilities of their minority stakeholders, while Silicon Valley-based venture capital giant Draper Fisher Jurvetson and Franklin Templeton should in turn gain a bigger slice of the emerging markets pie along with access to the regional expertise and local contacts of each specialist manager. If this model proves successful, and we believe it will, we expect to see an increased number of private placements and minority transactions in addition to outright acquisitions.

Life-Cycle Funds and Life-Settlements Create Value for Baby Boomers

Maximizing the Value of your Assets with Protective Features

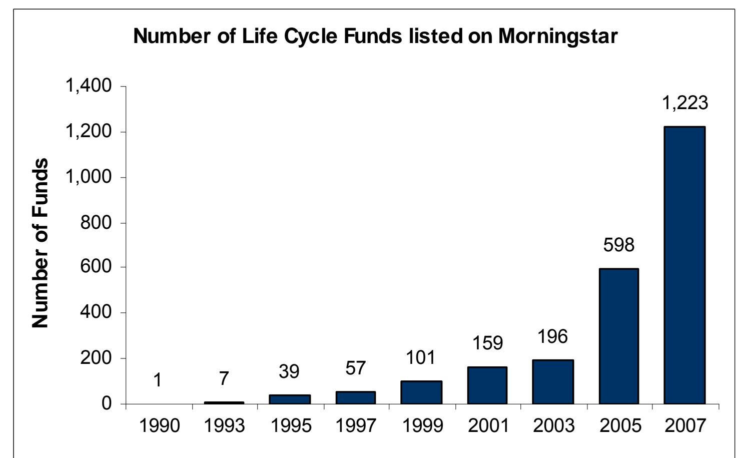
At a time when the very foundations of our financial markets are shaken, concerns about the adequacy of retirement assets loom large. In particular, the trend from DB to DC plans has shifted retirement funding risks to the individual from the corporation. As such, retirement planning has become more complex including investment risks as well as other factors to consider: increasing life expectancies, lower savings rates, rising healthcare costs and greater personal leverage.



Source: CDC, US Census Bureau, Bureau of Economic Analysis

The result has been the introduction of retirement funding products including: (1) lifecycle funds, (2) managed payout funds, (3) reverse mortgages and (4) life settlement products.

Life-cycle funds were the first of these products introduced and have had much success. A life-cycle (often called lifestyle) fund is a portfolio of stocks, bonds, and money market accounts that is managed based on a preset level of return/risk, the fund then automatically decreases the risk of the portfolio as the person ages (funds are often called Target 2040, for the year you will need the funds).



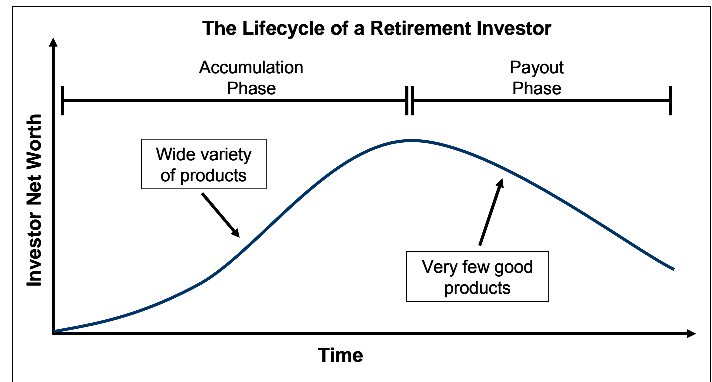
Source: Manning & Napier, Morningstar

A popular application of life-cycle funds within 401(k) portfolios led to the creation of the "target date" fund, a product that has grown rapidly in popularity over the last few years. The premise behind such funds is that there are many retail investors who either (1) lack financial sophistication, (2) do not wish to put in the effort of managing an asset allocation, or (3) prefer the security of handing the allocation decision to an expert. Fund companies have therefore put together products where, in addition to their traditional role of choosing individual investments, they select an appropriate asset allocation based on the client's expected retirement date. These products are then structured as a series of mutual funds, each with a different target retirement date, and each holding a different asset allocation, which is adjusted towards more conservative investments as the target date draws nearer. The products have a simple appeal (e.g. Target Date 2040), and may have a positive impact on overall retirement savings by simplifying what can be an overwhelming process for many people (and hence one to be avoided).

Now on Sale: Post-retirement Products

A secondary approach, one addressing the needs of individuals' post-retirement, was slower in coming. Recently, Vanguard launched a series of three "Managed Payout Funds" that target distributions of 3%, 5% and 7% respectively. The idea behind these funds is that Vanguard will choose asset allocations using the company's existing products and then package those products into funds that pay out a fixed percentage over time. The funds will all seek to preserve and grow invested capital. The target audience for these products is similar to that of the target date funds above: those without the sophistication or willingness to manage their own asset allocations. Thus, a retiree could put his or her entire savings into such a fund and have a well diversified asset allocation managed by mutual fund firms across a number of products with similar goals of the Target Date funds above – that you can withdraw 3-7% per year to live and expect to spend all the money by a set date (e.g. 30 years from now).

However, it remains to be seen whether firms offering these products will be successful at maintaining a high 7% payout level, given the number of studies that advocate a 4-5% payout rate (adjusted for inflation) as the only reasonably sure way to avoid running out of cash in old age. Fidelity has taken the concept a step further with "Income Replacement Funds" that have specific horizon dates ranging from 2016 to 2042. Over time the funds expect to distribute income and principal in such a way that assets are completely depleted as near to the horizon date as possible. These products are designed by building an asset allocation strategy that is appropriate for an investor with a given time horizon. The difference between these funds and other target date funds is that the process works in reverse: instead of accumulating assets for the ultimate goal of retirement on a certain date, the funds pay out returns until the projected date of the investor's death, however the individual stills has the "longevity risk" of outliving their money.

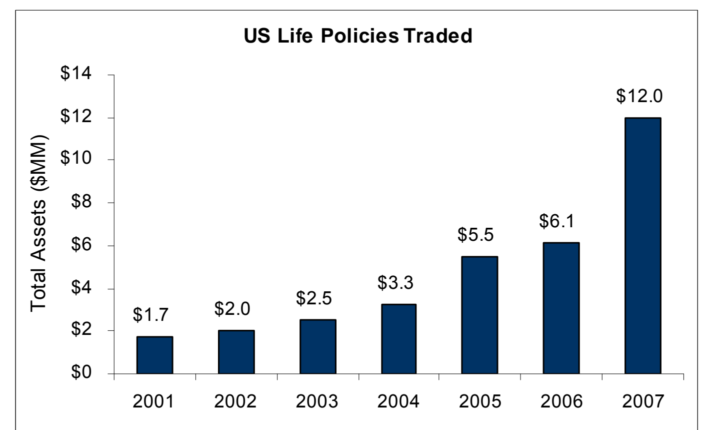


Source: Freeman & Co.

Reverse Mortgages and Life Settlements Squeeze Liquidity out of Illiquid Assets

A third approach to retirement funding is reverse mortgage products which give pending retirees another way to access equity capital without selling their homes. The origination of reverse mortgages is now sponsored by the Federal Housing Administration (FHA) and the annual number originated has quickly grown from less than 10,000 in 2000 to more than 100,000 in 2007. Given the need for individual retirement funding and government sponsoring of the products, the market should continue to grow, but only after housing prices stabilize.

The last product innovation to support retirement funding for individuals is life settlement. Since 1999 consumers have had the opportunity to sell existing life insurance policies into the secondary market for an amount greater than the cash surrender value. Depending on their health, the actuarial value of their life insurance policy may be much greater than the surrender value. Consumers can tap this asset to pay for their health care, retirement needs or to fund the educational costs of children or grandchildren. According to industry estimates the value of face amounts transferred in life settlements was $12 billion in 2007. Reports also predict that by 2016 a conservative estimate of the potential size of the US life settlement market could range from $90 to $140 billion in policy face amount per year. While there is a fair amount of friction between insurance brokers, life settlement providers, and investment banks attempting to control multiple segments of the life settlements value chain, we expect this to change. We believe firms will be force to specialize in a segment of the business (origination, underwriting, portfolio management) to compete with the number of new entrants.



Source: Conning, BVZL

Conclusions

The shift from DB to DC plans, combined with increasing investment risks and the loss of home equity for individuals, has increased the opportunity for firms to address individuals' retirement funding needs with new and creative solutions. Unfortunately we continue to see the erosion of the three-legged retirement stool of government, corporate and individual savings. Gen X and Gen Y will be forced to rely predominately on individual savings, but at least they will have time to prepare and the use of life cycle and income payout funds will help simplify the process for them. For many Baby Boomers, time may not allow them to save enough for their retirement funding needs. In these cases, reverse mortgages and life settlement products will offer older individuals the ability to fund their retirement needs in their golden years.

Public US Money Managers – Valuations

(All figures in millions, except for per share data or unless otherwise noted)

Company Name	End AUM ($ bils)	Stock Price 9/4/2008	Equity Value	Enterprise Value [a]	LTM (6/30/2008) Revenue	LTM (6/30/2008) EBITDA [b]	LTM (6/30/2008) EPS	Enterprise Value as a Multiple of LTM Revenue	Enterprise Value as a Multiple of LTM EBITDA	PE Ratio LTM	Equity Value % AUM
Diversified [c]											
Blackrock	$ 1,427.5	$ 210.91	$ 25,344.8	$ 25,163.8	$ 5,429.4	$ 1,889.8	$ 8.23	4.6x	13.3x	25.6x	1.8%
Eaton Vance	159.1	35.00	4,299.3	4,499.2	1,144.0	402.4	1.82	3.9x	11.2x	19.2x	2.7%
Federated Investors	333.5	34.63	3,511.1	3,414.9	1,202.7	401.4	2.18	2.8x	8.5x	15.9x	1.1%
Franklin Resources	580.2	101.56	24,318.0	21,567.6	6,340.1	2,416.5	7.32	3.4x	8.9x	13.9x	4.2%
Gamco	28.3	50.46	1,413.1	1,286.5	289.5	107.3	2.34	4.4x	12.0x	21.6x	5.0%
SEI Investments	178.2	22.96	4,488.8	4,209.9	1,366.5	455.9	1.12	3.1x	9.2x	20.6x	2.5%
Janus Capital	191.8	26.10	4,229.8	5,081.9	1,136.1	388.4	1.26	4.5x	13.1x	20.7x	2.2%
T Rowe Price	387.7	57.08	15,558.3	14,877.1	2,314.4	1,086.4	2.46	6.4x	13.7x	23.2x	4.0%
Waddell & Reed	70.1	28.34	2,447.0	2,444.7	933.6	216.2	1.56	2.6x	11.3x	18.2x	3.5%
Calamos Investments	41.2	22.38	435.4	754.7	465.9	62.5	0.83	1.6x	12.1x	26.9x	1.1%
Legg Mason	922.8	42.60	6,069.2	7,159.3	3,800.8	1,276.4	4.57	1.9x	5.6x	9.3x	0.7%
Cohen & Steers	27.0	27.40	1,138.5	1,028.6	245.2	93.2	1.44	4.2x	11.0x	19.0x	4.2%
TOTAL	**$ 4,347.5**		**$ 93,253.3**	**$ 91,488.2**			**AVERAGE**	**3.6x**	**10.8x**	**19.5x**	**2.7%**
							MEDIAN	**3.7x**	**11.2x**	**19.9x**	**2.6%**
Alternatives											
Fortress	$ 35.1	$ 9.63	$ 3,916.3	$ 4,461.2	$ 757.0	$ 350.4	$ 0.48	5.9x	12.7x	20.2x	11.2%
Blackstone	99.7	16.74	18,296.9	18,457.3	1,320.4	433.1	0.28	14.0x	NM	NM	18.3%
GLG	23.7	8.11	1,992.3	1,924.6	869.3	304.7	0.71	2.2x	6.3x	11.4x	8.4%
Och-Ziff	33.6	16.34	5,786.5	5,629.5	1,205.6	881.7	1.67	4.7x	6.4x	9.8x	17.2%
TOTAL	**$ 192.1**		**$ 29,992.0**	**$ 30,472.5**			**AVERAGE**	**6.7x**	**8.5x**	**13.8x**	**13.8%**
Holding Companies											
Affiliated Managers	$ 241.8	$ 92.04	$ 3,983.1	$ 5,241.1	$ 1,372.6	$ 312.2	$ 4.61	3.8x	16.8x	20.0x	1.6%
Alliance Capital	716.6	51.79	13,554.0	13,368.5	4,414.9	1,451.5	4.48	3.0x	9.2x	11.6x	1.9%
TOTAL	**$ 958.4**		**$ 17,537.1**	**$ 18,609.5**			**AVERAGE**	**3.4x**	**13.0x**	**15.8x**	**1.8%**
Bank / Trust Companies [d]											
Boston Private Finl	$ 37.0	$ 8.56	$ 489.5	$ 489.5	$ 377.8	$ 105.0	$ (2.73)	1.3x	4.7x	NM	1.3%
Wilmington Trust	50.8	23.85	1,606.0	1,606.0	704.4	268.2	1.65	2.3x	6.0x	14.5x	3.2%
TOTAL	**$ 87.8**		**$ 2,095.4**	**$ 2,095.4**			**AVERAGE**	**1.8x**	**5.3x**	**14.5x**	**2.2%**
Overall TOTAL	**$ 5,585.7**		**$ 142,877.9**	**$ 142,665.6**							
							HIGH	14.0x	16.8x	26.9x	18.3%
							AVERAGE	4.0x	10.1x	17.9x	4.8%
							MEDIAN	3.6x	11.0x	19.1x	2.9%
							LOW	1.3x	4.7x	9.3x	0.7%

Source: Publicly available SEC filings, Bloomberg and IBES estimates.
Note: All figures have been adjusted for extraordinary and non-recurring items.
(a) Enterprise Value calculated as Equity Value plus Net Debt (Total Debt less Cash & Cash Equivalents).
(b) EBITDA is shown net of minority interest.
(c) EV, BEN and LM fiscal year end of October, September and March have been calendarized.
(d) Enterprise Value calculated as equal to Equity Value

Public European Money Managers – Valuations

(All figures in millions, except for per share data or unless otherwise noted)

Company Name	End AUM (£ bils)	Stock Price 9/4/2008	Equity Value	Enterprise Value [b]	LTM (6/30/2008) [a] Revenue	LTM (6/30/2008) [a] EBITDA [c]	LTM (6/30/2008) [a] EPS	Enterprise Value as a Multiple of LTM Revenue	Enterprise Value as a Multiple of LTM EBITDA	PE Ratio LTM	Equity Value % AUM
Traditional											
Schroders	£130.2	£9.72	£2,716.2	£1,929.2	£933.9	£301.8	£0.91	2.1x	6.4x	10.7x	2.1%
F&C Asset Management	£96.5	£0.94	£481.2	£530.0	£263.2	£77.9	£0.04	2.0x	6.8x	23.8x	0.5%
Henderson Group	£52.6	£1.32	£961.6	£977.0	£327.9	£176.1	£0.15	3.0x	5.5x	8.6x	1.8%
Azimut Holding Spa	£11.0	EUR 5.82	EUR 822.4	EUR 1,270.3	EUR 303.8	EUR 245.2	EUR 0.66	4.2x	5.2x	8.8x	5.5%
New Star Asset Management	£23.1	£1.04	£242.4	£480.4	£173.3	£100.5	£0.19	2.8x	4.8x	5.5x	1.0%
Liontrust Asset Management	£5.2	£2.54	£85.6	£76.5	£40.8	£15.6	£0.36	1.9x	4.9x	7.1x	1.6%
Aberdeen Asset Management	£107.3	£1.36	£855.4	£861.6	£387.2	£96.6	£0.11	2.2x	8.9x	12.5x	0.8%
TOTAL	**£425.9**										
							AVERAGE	2.6x	6.1x	11.0x	1.9%
							MEDIAN	2.2x	5.5x	8.8x	1.6%
Alternatives											
RAB Capital	£3.0	£0.37	£201.2	£157.9	£121.2	£50.4	£0.06	1.3x	3.1x	6.3x	6.8%
MAN Group	£37.6	£5.05	£8,629.5	£7,239.5	£1,598.5	£1,044.0	£0.45	4.5x	6.9x	11.1x	22.9%
Ashmore Group	£18.4	£2.66	£1,784.4	£1,563.4	£211.4	£158.3	£0.17	7.4x	9.9x	15.8x	9.7%
Charlemagne Capital Limited	£3.3	£0.32	£90.9	£57.7	£67.6	£35.9	£0.10	0.9x	1.6x	3.1x	2.8%
BlueBay Asset Management	£8.3	£2.83	£542.1	£480.3	£114.6	£51.5	£0.18	4.2x	9.3x	15.5x	6.5%
Polar Capital Holdings	£1.6	£1.01	£74.2	£42.9	£47.4	£16.0	£0.12	0.9x	2.7x	8.2x	4.7%
Partners Group	£10.9	CHF 152.50	CHF 3,797.3	CHF 3,716.6	CHF 305.8	CHF 226.6	CHF 9.42	12.2x	16.4x	16.2x	15.6%
HFA Holdings Limited (d)	£4.5	AUD 1.16	AUD 537.7	AUD 640.6	AUD 76.3	AUD 50.2	AUD 0.10	8.4x	12.8x	11.5x	5.7%
TOTAL	**£89.2**										
							AVERAGE	4.4x	7.0x	9.8x	8.3%
							MEDIAN	4.2x	6.9x	11.1x	6.5%
Overall TOTAL	**£515.1**										
							HIGH	12.2x	16.4x	23.8x	22.9%
							AVERAGE	3.6x	6.6x	10.3x	5.5%
							MEDIAN	2.5x	6.0x	9.8x	3.8%
							LOW	0.9x	1.6x	3.1x	0.5%

Source: Publicly available company filings, Bloomberg and IBES estimates.
Note: All figures have been adjusted for extraordinary and non-recurring items.
(a) Polar, Liontrust, Aberdeen and Man Group reflect LTM financials as of 3/31/2008; Azimut, Ashmore, BlueBay, Charlemagne and Partners Group reflect LTM figures as of 12/31/2007
(b) Enterprise Value calculated as Equity Value plus Net Debt (Total Debt less Cash & Cash Equivalents).
(c) EBITDA is shown net of minority interest.
(d) Trades on Australian Stock Exchange

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