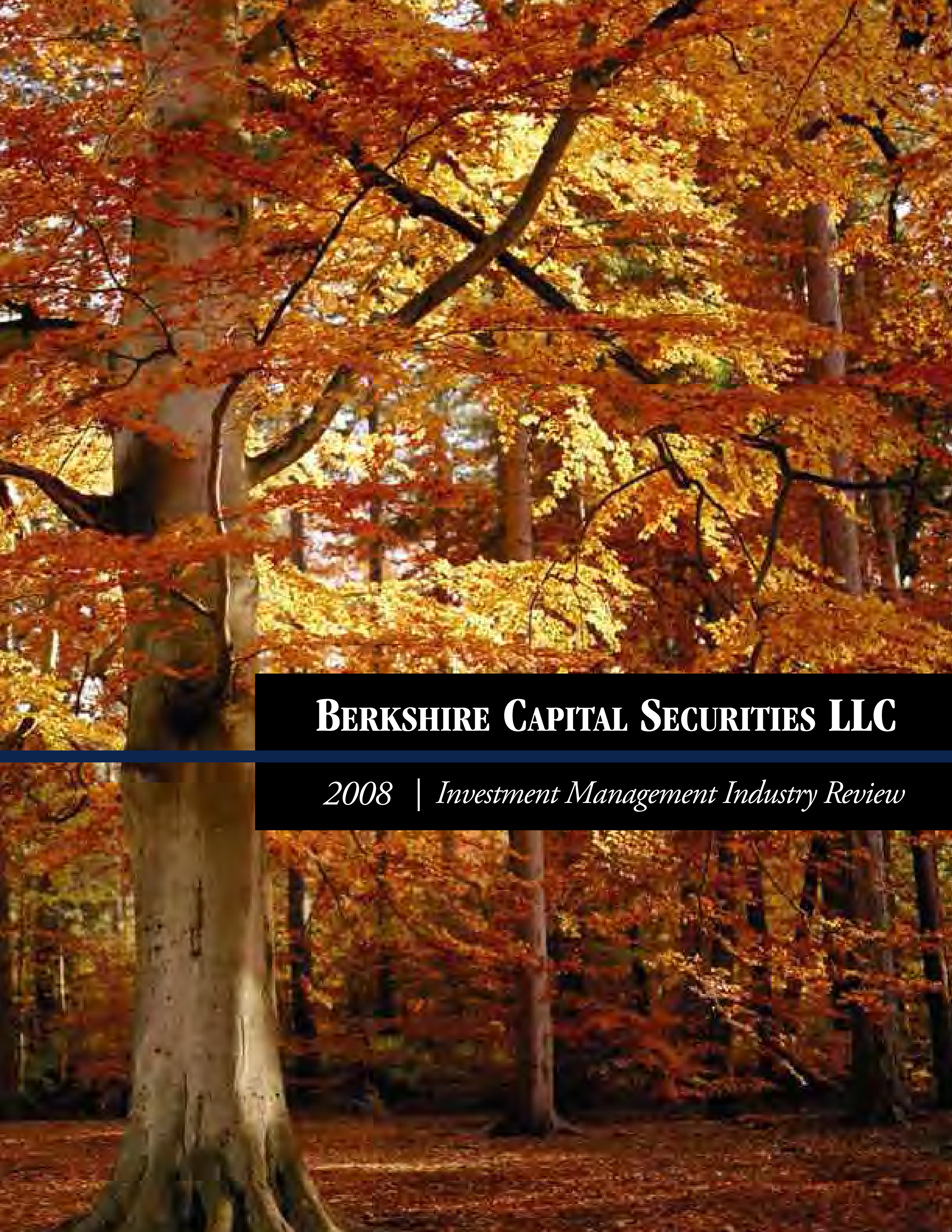

Berkshire Capital Securities LLC

2008 | *Investment Management Industry Review*

Mission Statement

Our mission is to advise clients on the initiation and execution of successful mergers, acquisitions, divestitures, joint ventures and other alliances in the financial services industry.

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Global Angst from the American Dream

Fueled by easy money and relaxed credit standards, in recent years a record 69% of households have been able to enjoy the American Dream of home ownership. At the same time, the bundling of mortgages into securities, an often-forgotten reform of President Franklin Roosevelt's New Deal, metamorphosed into a highly complex and massive financial industry with investors from New York to Tokyo, Arkansas to Iceland.

Then, as if from a plot in some dark novel, the riskiest borrowers began to falter and the world entered the latest in a series of global financial trials stretching back to the Latin American debt crisis of the early 1980s. Banks in London and Germany began to surprise the market with alarming losses, hedge funds collapsed, and the careers of the some of the most powerful executives in the financial services industry were dashed. By January 2008, banks had written down more than $100 billion worth of subprime-related securities, and the Organization for Economic Cooperation and Development (OECD) estimates that financial firms worldwide could ultimately end up taking a staggering $300 billion hit — twice the tab for the U.S. savings and loan crisis in the 1980s and 1990s.

In addition to hammering the profitability and capital base of banks, the subprime crisis again raised nagging concerns about the foundation of an American economy built on significant levels of indebtedness — and on the willingness of foreigners to continue underwriting the spending habits of American consumers and governments. In a reflection of the U.S. position, the dollar sank to new lows while powerful centers of influence entered the American investor's lexicon as they began to more visibly assert themselves: sovereign wealth funds.

The profile of these funds rose considerably last year as a result of several major investments from Asian and Middle Eastern SWFs that underlined just how much the center of gravity for the world's capital had shifted. SWFs, primarily from emerging markets, invested some $55 billion into financial services firms worldwide last year.

In the largest such investment in 2007, the Government of Singapore Investment Corp. rode to UBS' rescue during the subprime crisis with a $10.9 billion recapitalization investment, equivalent to a 9% shareholding — an investment that dovetails with the small republic's ambitions to become a private banking hub in Asia. The Abu Dhabi Investment Authority did the same for Citigroup, via an attractively structured $7.5 billion investment, and also sank $1.4 billion into Carlyle Group. Dubai International Capital took a 9.9% stake in Och-Ziff Capital Management when that hedge fund went public while Dubai International Financial Center Investments bought a 2.2% stake in Deutsche Bank.

China Investment Corp. made a $3 billion investment in another alternative investor, Blackstone Group, a high profile deal that led to a spate of media stories about the intentions of that new $200 billion state-run fund. By year-end, CIC pumped $5 billion into a battered Morgan Stanley grappling with a fourth-quarter subprime writedown of $9.4 billion and a loss of $3.6 billion.

Indeed, nearly three decades after the introduction of economic reforms, China made a major statement last year about its global ambitions. In addition to the U.S. deals noted above, Chinese state investment vehicles and financial services firms invested in Bear Stearns, Standard Bank of South Africa, Barclays and Fortis in Europe. Three of China's largest banks also approached Singapore's powerful state investment arm, Temasek, about purchasing its 17% stake in Standard Chartered, a major player in emerging markets. All this activity occurred as the country's economy continued to race along at an 11% growth clip and foreign exchange reserves topped $1.4 trillion, or about 50% of total GDP.

Meanwhile, the Abu Dhabi investments underlined the flood of greenbacks accruing to the Gulf states, with the Institute of International Finance estimating that six of those oil rich states hold $1.6 trillion in foreign assets. OPEC members as a whole are projected to have generated oil revenues of $658 billion in 2007, a number expected to reach $762 billion this year, according to the U.S. Energy Information Administration.

Slower Growth Ahead?

GDP Growth

	2006	2007*	2008*
U.S.	2.9%	2.2%	1.5%
Euro Area	2.8	2.6	1.6
U.K.	2.8	3.1	2.3
Japan	2.4	1.9	1.5
Developing Asia	9.6	9.6	8.6
China	11.1	11.4	10.0
Global	5.0	4.9	4.1
World Trade Volume (goods & services)	**+9.2%**	**+6.6%**	**+6.7%**

* Projected

Source: IMF, Revised World Economic Outlook, January 2008 (U.K., October 2007)

For asset managers, the rise of SWFs — which control some $2.5 trillion in assets — could spell tremendous opportunity. In a report released late last year, Merrill Lynch suggested the funds would make "extensive use of external asset managers" given the "high costs and difficulties associated with setting up internal portfolio management teams, together with the risk of protectionist backlash."

Noting that Norway's government pension fund relies on internal managers for just 39% of its $360 billion asset pool, Merrill projects that SWFs could shift $1.5 trillion to $3 trillion to global asset managers over the next five years, generating a windfall in fees of $4 billion to $8 billion. Merrill also expects SWFs to make direct investments in asset managers as part of the effort to enhance their internal capabilities. China Investment Corp. for one has spelled out its requirements for global equity asset managers, including minimum AUM of $5 billion and a six-year-long track record within one of the asset classes in which the fund will invest. Those classes include Asia (ex-Japan), emerging markets, global stocks, and developed markets other than the U.S.

While a *Wall Street Journal* columnist suggested that the "mergers-and-acquisition story of 2008 will be how these sovereign funds … direct their appetites," in 2007 the developing story became the diminished activities of private equity funds once the credit crunch hit. Beginning in August, private equity deal value fell off the cliff, reaching a low in the U.S. of just $5.5 billion in November, compared with the year's high of $114 billion in May, according to Thomson Financial. Through the end of October 2007, Dealogic tallied $200 billion in deals that private equity firms decided to cancel, twice the level of the year-earlier period. Worldwide, a record $4.5 trillion worth of deals were announced last year, compared with $3.6 trillion in 2006, according to Thomson Financial.

In the asset management industry, dealmakers coming off the record-breaking year of 2006 continued to set a torrid pace in 2007, with 198 deals valued at $38.6 billion. For the third straight year, there were several mega-deals and 13 billion-dollar-plus transactions valued at $26.4 billion. The year was also notable for the influence of private equity players in two major deals, as well as the large number of transactions designed to enhance the operations of European and American asset managers in Asia's emerging markets. In addition, investment banks and asset managers continued to scour the globe for hedge funds, with minority stakes remaining the investment choice for many.

For the first time in the asset management industry, the largest deal involved a private equity buyer, Madison Dearborn Partners, which acquired Nuveen Investments.

For the first time in the asset management industry, the largest deal involved a private equity buyer, Madison Dearborn Partners, which acquired Nuveen Investments (AUM: $170 billion) for $5.8 billion plus the assumption of $550 million of Nuveen's debt. MDP indicated it would remain on the prowl for tack-on acquisitions to enhance Nuveen's capabilities. Another private equity firm, TA Associates, was involved in the high profile management buyout of London's Jupiter Asset Management (AUM: $41 billion) from Commerzbank for $1.7 billion. TA also made investments in New York's Arnhold and S. Bleichroeder Holdings (AUM: $45 billion), manager of First Eagle Funds, and hedge fund K2 Advisors (AUM: $5.5 billion).

The second-largest deal last year involved a buyout by a notable player in the mutual fund industry, Thomas Marsico, who paid $2.7 billion to buy back his fast growing Marsico Capital Management (AUM: $94 billion) from Bank of America. The deal, driven in part by Marsico's desire to provide an equity incentive structure for employees, was aided by the low cost of borrowing. The pressure to hold onto core employees by creating equity incentives was also cited by Arnhold and S. Bleichroeder management in explaining the investment by TA Associates.

Mergers & Acquisitions

Number of Announced Deals	2006	2007
Worldwide	38,580	42,437 (+10%)
U.S.	10,679	11,219 (+5%)
Europe	12,523	13,684 (+9)
Value ($ billions)	**2006**	**2007**
Worldwide	$3,610	$4,482 (+24%)
U.S	$1,475	$1,614 (+9%)
Europe	$1,325	$1,804 (+36%)

Source: Thomson Financial

European firms took part in only a handful of deals involving American-based asset managers, their currency advantage notwithstanding. Moreover, the largest transaction — Standard Chartered's acquisition of Miami-based American Express Bank (AUM: $22.5 billion) — involved primarily an international business. In one of the more significant transactions, Aberdeen Asset Management of Scotland bought the $7 billion equity fund business of Nationwide Financial Services, in line with its strategy of "acquiring bolt-on businesses that enhance our product range and geographic reach." In 2005, Aberdeen established a U.S. presence when it acquired Deutsche Bank's global fixed income business.

Europeans instead focused on emerging markets, joined by a number of large American firms. India, whose economy last year maintained the 8% growth rate it has averaged since 2002, was a center for joint ventures, while China continued to draw dealmakers from major financial services firms. AXA and Franklin Resources cut mutual fund deals in both markets, and were joined in India or China by international giants such as ING and Robeco. Bank of NY-Mellon set up a joint venture fund company in China and acquired a hedge fund in Brazil, while ING tapped the fast growing pension market in Latin America through the $1.3 billion acquisition of Santander's pension businesses in Mexico, Chile, Colombia and Uruguay. ING also cut deals in India and South Korea.

Europeans were busy in their own backyard, led by Generali's $1.6 billion purchase of Swiss Life private bank

Banca del Gottardo (AUM: $31 billion), which will be merged with the Italian insurer's Swiss private banking unit, BSI. The deal continues the consolidation trend in Switzerland's private banking industry. Another Swiss wealth manager, EFG International, acquired London hedge fund Marble Bar Asset Management (AUM: $4.4 billion) for an initial price of $517 million that could ultimately reach as much as $1.3 billion with performance incentives. EFG also acquired two wealth managers.

Other notable all-European deals included UBS' $650 million acquisition of French institutional and private client firm CCR Group (AUM: $25 billion), the largest European asset management deal UBS has made in recent years. The $100 billion purchase of ABN Amro included a significant asset management component for Fortis, one of the three European banks involved in buying and carving up the Dutch bank. Fortis scooped up ABN's asset management business (AUM: $480 billion) to create a global operation managing $800 billion.

A number of perennially active buyers were in the market again last year, including Federated Investors, which bought Rochdale Investment Management's international equity fund, Atlas Portfolio (AUM: $321 million). Federated has acquired seven equity or bond funds in the last three years as it seeks to expand beyond its core business of money market funds. Boston Private Financial Holdings made three investments in the wealth management sector, including two acquisitions that expanded its footprint, while aggressive newcomer Focus Financial Partners bought three more affiliates, bringing to nine the number of investments it has made since 2005. WealthTrust, an established dealmaker in the sector, acquired two more wealth management firms last year, bringing its affiliate total to 11.

Affiliated Managers Group, another U.S. firm with an established affiliate model, acquired stakes in two hedge fund companies as part of its strategic expansion in that sector, including credit specialist BlueMountain Capital Management (AUM: $4.8 billion). Citigroup paid an estimated $600 million for a year-old firm, Old Lane Partners (AUM: $4.5 billion), in large part to acquire the management talent of owner Vikram Pandit, who was subsequently named CEO following the resignation of Charles Prince.

There were two other deals of note last year designed to capitalize on the turmoil in the credit markets. Citigroup, hammered by its own subprime portfolio, acquired a small New York credit derivatives specialist, Carlton Hill Global Capital (AUM: $150 million). Perella Weinberg Partners also picked up a small credit specialist in distressed assets, Xerion Capital Partners (AUM: $400 million).

The hedge fund and fund of funds arena, flush with some $2 trillion in AUM, continued to draw an impressive list of buyers generally targeting larger and higher-profile firms. Lehman Brothers invested in two companies, including a 20% stake in established hedge fund D.E. Shaw (AUM: $30 billion). BNP Paribas, Goldman Sachs, Merrill Lynch, Morgan Stanley and Swiss Re were among the other major firms investing in hedge funds.

* * *

Over the past 25 years, there has been a steady succession of financial crises — from the Latin American debt crisis to the savings and loan debacle to the Long-Term Capital Management collapse and the dot-com implosion. The addition of the subprime crisis to this active boom-and-bust list underlines the explosion in global capital and the linkages among markets, as well as the higher level of risk investors and financial firms are willing to assume to achieve higher returns and profitability. Separately, it also raises questions regarding just how vigorously many investment professionals are going about the business of due diligence.

Last year, bankers and investors paid an enormous price for their aggressive posture. The list of casualties included such prominent global banking chief executives as Stanley O'Neal of Merrill Lynch, Charles Prince of Citigroup and Peter Wuffli of UBS. In the fourth quarter, Citigroup announced a loss of nearly $10 billion and subprime-related write downs of more than $18 billion, while Merrill's fourth-quarter results were the worst in its history, with losses of nearly $10 billion and $15 billion in write-downs.

But few firms were spared, it seemed, and the pain extended worldwide, with November bringing announcements from Zurich's Swiss Re and Tokyo's Mizuho Financial Group of subprime-related losses of $1.1 billion and $630 million, respectively. This came on top of bank collapses in the U.K (Northern Rock) and Germany (IKB), and the hits taken by many European-based hedge funds. Moreover, even as firms attempted to put the bad news behind them,

Mid-Year Market Stall

Major Stock Indices

	2007 Final Index	07 Midyear Index (6/29)	2H07 Performance
DJIA	13,265	13,409	-1.1%
S&P 500	1,468	1,503	-2.3
Nasdaq	2,652	2,603	+1.9
DJ Stoxx 50 (Europe)	3,684	3,947	-6.7
FTSE 100 (UK)	6,457	6,608	-2.3
DAX	8,067	8,007	+0.7
DJ Asia-Pacific	158	159	-0.6
Nikkei 225	15,308	18,138	-15.6
DJ World Index	301	303	-0.7

Investment Management Transactions

	2003	2004	2005	2006	2007
Majority Equity	116	119	124	150	164
Minority Equity	10	8	9	12	24
Management Buyout	9	6	6	5	10
Total	135	133	139	167	198
Total Transaction Value ($B)	$9.3	$10.7	$19.3	$47.2	$38.6
Total AUM Changing Hands ($B)	$375	$720	$1,202	$2,340	$1,282

Source: Berkshire Capital Securities LLC

the hemorrhaging continued into the new year, with few observers surfacing to identify a light at the end of the tunnel and many raising red flags in areas such as credit card debt.

The impact on shareholders of financial stocks was severe. At Citigroup, a virtual poster boy for the crisis, shareholders watched more than $100 billion of market capitalization disappear during 2007 as the valuation of Citi sank to just eight times trailing earnings by mid-December. The sanctity of Citi's dividend was also called into question, along with the value of maintaining its financial "supermarket" structure. (In January 2008, Citigroup announced a 40% cut in its dividend.)

For banks within the Dow Jones U.S. Index, shares declined 27% for the year through mid-December, making banking one of the index's worst industry performers, while net income for the industry dropped 27% in the third quarter. In the fourth quarter, Thomson Financial projected a 45% decline in profits for banks and brokerages as a whole. The nonstop bad news and beaten down share prices led at least one notable investor, Legg Mason chief investment officer Bill Miller, to put the buy sign out for financial stocks late in the year. Quoting Roman poet Horace by way of legendary value investor Ben Graham, he wrote: "Many shall be restored that now are fallen and many shall fall that are in honor."

Although the fallen included many hedge funds betting the wrong way on housing, asset managers appeared to be weathering the storm fairly well. The collective earnings of the asset managers in the Dow Jones U.S. Index dropped 13% in the third quarter, but share prices for the group rose 21% in the year through mid-December. Many individual asset managers delivered strong results. T. Rowe Price saw its third-quarter net income climb 37%, Franklin Resources recorded a 14% gain in net income in its fiscal fourth-quarter, and State Street registered a 39% rise in third-quarter earnings per share (excluding certain merger and integration costs related to its acquisition of Investors Financial Services Corp.).

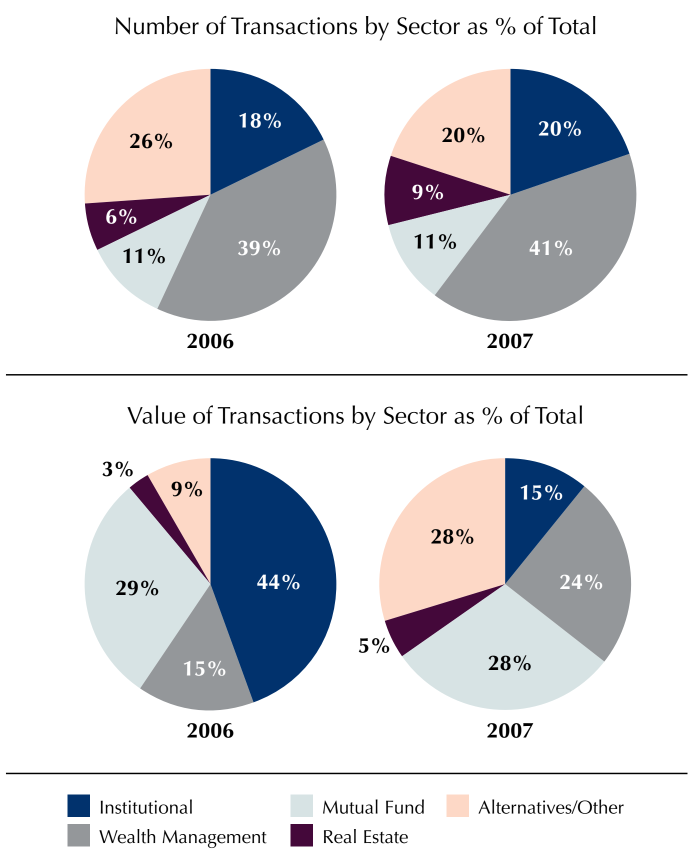
One of the best performing asset management stocks was London-based GLG Partners, which last year became the first pure hedge fund to trade on the New York Stock Exchange (NYSE). Taken public initially through a reverse takeover by a special purpose acquisition vehicle, Freedom Acquisition,

GLG chose a listing in New York as part of an effort to raise its profile among U.S. investors. The firm, whose third-quarter results included a 160% jump in net income to $29 million and a 49% increase in AUM to $20.5 billion, saw its share price climb nearly 50% by mid-December.

Private equity giant Blackstone Group, private equity and hedge fund manager Fortress Group, and hedge fund Och-Ziff Capital Management also began trading on the NYSE last year, with all three suffering negative returns through mid-December. In Europe, fund of hedge funds manager Gottex Fund Management began trading on the Swiss Exchange and was joined on other exchanges by at least seven individual hedge funds, including the $1.1 billion BH Macro fund run by London's Brevan Howard. In Asia-Pacific, Sydney-based hedge fund Platinum Asset Management began trading on the Australian Securities Exchange.

As entrepreneurial money managers gravitate toward the

Who's Selling



Source: Berkshire Capital Securities LLC

Who's Buying

	2003	2004	2005	2006	2007
Bank	32	43	35	39	43
Wealth Manager	12	18	16	24	37
Financial	3	8	6	18	21
Institutional	13	19	19	20	20
Securities Firm	11	7	9	14	15
Real Estate Manager	2	1	4	6	14
MBO	9	6	6	5	10
Mutual Fund	20	7	13	11	8
Insurance Company	9	4	7	13	7
Trust Company	9	3	8	6	4
Other	15	17	16	11	19
Total	135	133	139	167	198

Source: Berkshire Capital Securities LLC

presumed wide-open spaces of the hedge fund industry, they are discovering this sector is more akin to other parts of the asset management industry. Morgan Stanley figures the top 100 hedge funds accounted for 67% of hedge fund AUM in 2006, up 18 points from 2003.

As in the mutual fund industry, where the big three of American Funds, Fidelity Investments and Vanguard Group accounted for 38% of all U.S. fund assets last year, the concentration trend — driven in part by the institutional preference for larger hedge fund firms — is expected to place pressure on many smaller firms to partner up. In an interview with FT.com, Peter Clarke, chief executive of Man Group, predicted that in the volatile year of 2007, 10% of all hedge funds wouldn't last long enough to celebrate the new year, let alone life with a new investor.

Here are some other trends we see playing out in 2008:

- For years in these reports and our newsletters, we have kept an eye on the gradual liberalization of China's financial services industry and the opportunities that would ensue for international financial firms, but India's acceptance of freer markets and the resulting dynamism of its economy are also attracting attention. As these two Asian giants continue to grow and develop more sophisticated investment infrastructures, the drive for joint ventures between domestic and international firms will remain strong.
- As alternative asset classes continue the maturation process, they are assuming the trappings of more traditional asset managers. We expect these characteristics — increasing transparency and compliance efforts; fee compression; a multitude of products; and more competition for seed capital — to further the institutionalization of the sector.
- Although the financial services "supermarket" model has lost much of its allure, some insurers in particular are committed to expanding their asset management units and will remain on the lookout for companies that can provide targeted investment expertise.
- The first wave of baby boomer retirements in the U.S. is finally occurring, and asset managers, particularly mutual fund companies, will continue to refine their products to accommodate the changing life circumstances of a generation that has more money and will live longer than any preceding generation.
- The evolution of international retirement markets will increasingly mirror the U.S. paradigm, with funded plans becoming the norm and individuals increasingly responsible for their own portable retirement assets. Emerging markets, having limited-to-nonexistent experience with traditional retirement schemes, are nearly certain to pursue the defined contribution model.
- Europeans are in a fix regarding the U.S. market. On the one hand, subprime-related angst has caused financial institutions to step back from acquisitions of U.S. asset managers. On the other, the depreciation of the greenback has made such investments an extremely attractive long-term bet. We'll wrap up by deferring a wager on the outcome of this internal debate while counting it among the more intriguing potential trends in the year ahead.

Wealth Management

Wealth management has been one of the hottest areas of asset management over the past decade and, if the sentiments of industry executives are any indication, that's not likely to change any time soon. A 2007 survey by PricewaterhouseCoopers reveals what the consulting firm describes as "staggeringly optimistic" views of future gains. One key indicator: expectations that industry AUM will jump 23% on average annually over the next three years, with chief executives citing 30% growth for their own firms. Moreover, insider projections are bullish for both mature and emerging markets.

With millionaires being minted each year in large numbers, there's good reason for optimism. The latest World Wealth Report from Capgemini and Merrill Lynch estimates that in 2006 the number of people worldwide with more than $1 million in investible assets rose 8.3% while their wealth grew 11.4% to a staggering $37.2 trillion, a total the report projects will top $51 trillion by 2011. The ranks of the wealthiest individuals — those with more than $30 million to invest — are growing at an even faster clip (up 11.3% in 2006), along with their assets (up 16.8%).

Not surprisingly, acquisitions represent part of the growth plan for wealth managers, with 90% of industry executives expecting "some, if not significant, consolidation," according to the PwC survey. But that strategy isn't just limited to buy side. Most sellers have determined that their best shot at growth involves joining a similar sized or larger firm that can help it then tackle challenges ranging from recruitment to technology to compliance. "The ability of CEOs to develop the brand, transform [information technology], and to both attract and retain quality client relationship managers is seen as the key critical success factor," writes PwC.

In 2007, buyers and sellers again cut deals in significant numbers to meet those challenges, with the sector registering a record 82 transactions valued at $9.1 billion. Although there was no blockbuster deal along the lines of Bank of America's 2006 acquisition of U.S. Trust, the list of buyers included many familiar and high profile players seeking to enhance existing operations, such as Convergent Capital Management, Merrill Lynch and Wilmington Trust, as well as newcomers like AmeriServe Financial gaining entry.

The largest transaction last year spanned the Atlantic and included a new dealmaker in the sector, Standard Chartered, which acquired Miami-based American Express Bank (AUM: $22.5 billion), the private banking and dollar clearing arm of the credit card giant. The agreement calls for StanChart to pay an amount equal to the net asset value of the business at closing, plus $300 million, a total expected to range between approximately $860 million and $1.1 billion. Using the lower end of the price range as its reference point, StanChart said it paid 14 times net profits, based on annualized 2007 first half results.

Peter Sands, group chief executive of StanChart, said the deal "turbo-charges the growth of our newly launched private bank, and both deepens and extends our distribution reach." Standard Chartered Private Bank was launched in the first half of 2007 and, like its parent bank, has focused on Asian and other developing markets, including India, Indonesia, Hong Kong and Singapore.

AEB has a presence in 47 countries and more than 10,000 customers, with 60% of AUM in markets where StanChart already operates. Pointing to AEB's nine branches in India and Taiwan as examples of the infrastructure StanChart is gaining, Sands said, "That may not sound like a lot, but these are key markets for us where regulatory restrictions make getting more branches very difficult." StanChart said it also expects to generate $100 million in cost savings from the combination by 2009. For Amex, the deal is in line with a strategic focus on its core card business and follows the 2005 spinoff of asset manager Ameriprise Financial.

Within the U.S., there were several notable deals, including those of three buyers that follow an affiliate model. Convergent Capital Management, the asset management arm of City National Corporation, acquired a fast growing ultra high net worth firm, Lydian Wealth Management of Maryland. Launched as a single family office in 1994, Lydian's clients on average have $40 million in AUM with the firm, which adds $7.3 billion in AUM to CCM's previous total of $28 billion. Following the closing, Lydian, the 10th affiliate in Convergent's portfolio of companies, changed its name to Convergent Wealth Advisors. City National said the two firms "will be uniquely positioned to expand their reach" into the key wealth markets of California and Nevada, both states in which CYN has banking operations.

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WealthTrust of Nashville brought to 11 its portfolio of affiliated asset managers, as it concluded two deals last year. The larger of the two firms, Cleveland-based Fairport Asset Management, has $1 billion in AUM and was formed in 2001 from the merger of two companies. Fairport said the link with WealthTrust provides the benefits of scale and "facilitates succession planning that ensures we can service our clients without disruption for generations to come." The second deal was for Axiom Asset Management (AUM: $600 million), a 4-year-old Pennsylvania firm. With the two acquisitions, WealthTrust has about $8 billion in AUM.

Boston Private Financial Holdings tapped the market for three acquisitions designed to enhance its wealth management business, including increasing its stake in Bingham, Osborn & Scarborough from 50% to 60%. Boston Private made an initial investment in the San Francisco wealth manager in 2004 and has raised it each year since. Founded in 1985, BOS has $2 billion in AUM, up from $150 million in 1993, and was an early advocate of the use of ETFs in its clients' portfolios. In its 2006 annual report, Boston Private touted BOS as its fastest growing wealth advisory firm.

A second deal, the $72 million purchase of Charter Financial Corp. of Washington state, extends Boston Private's footprint along the West Coast to Seattle's Puget Sound. Charter Financial is the bank holding company for Charter Bank, a commercial bank formed in 1998 that provides services to professionals and family-owned businesses. On the East Coast, the acquisition of Davidson Capital (AUM: $1 billion) provides Boston Private with entry to the "Main Line" area of greater Philadelphia. Boston Private took a 70% stake in the firm, with Davidson management retaining the remainder. James Davidson, founder and chairman of the firm, cited the "opportunities provided by being part of a larger, publicly traded organization." Over the past 10 years, Boston

Private's AUM has grown from $700 million to $30 billion, with the majority of that growth coming via acquisitions. The firm's goal is to have a presence in 15 of the top 30 "newly affluent geographic regions" in the U.S.; it is also considering international expansion.

Newcomer Focus Financial Partners bought three more affiliates that tripled its client assets to $15 billion. The major deal involved Buckingham Family of Financial Services, a 13-year-old St. Louis firm with $7.7 billion in assets under management or administration that also owns a turnkey asset management provider, Buckingham Asset Management Advisor Services — a business that can enhance the operations of Focus' other affiliates. For the past eight years, Buckingham has been among the 25 fastest growing private businesses in St. Louis, as ranked by the *St. Louis Business Journal*. Mont Levy, chief operating officer of BAM Advisor Services, said the affiliation provides his firm with the "opportunity to share best practices with the other highly successful Focus partners," thereby enabling all the firms "to better serve their clients."

Wilmington Trust stepped back into the market to acquire Boston-based Bingham Legg Advisers.

Focus has quickly taken stakes in nine wealth managers throughout the country and plans to boost that number to 50 in the years ahead, targeting companies with a minimum of $300 million in AUM. As with other companies pursuing an affiliate model, Focus' strategy is to take a stake that may range from 40% to 60% and then leave local management in place while providing the benefits of scale. Its founder, "Rudy" Adolf, formerly worked at American Express and McKinsey & Co., and the firm has backing from Summit Partners, a Boston-based private equity firm.

Among some larger U.S. players, Merrill Lynch was involved in two high profile deals with a wealth management component, including the $1.8 billion acquisition of First Republic Bank. The San Francisco-based commercial bank, which will retain its identity, has $16.4 billion in assets under management or administration. Merrill paid a significant premium (44%) over the bank's prevailing stock price, or 24 times 2007 earnings. Merrill also took a non-controlling stake in Sterling Stamos Capital Management (AUM: $4 billion), a 5-year-old firm that invests in alternative and traditional assets and whose other investors include realtor and New York Mets owner Fred Wilpon. The two firms touted the deal as a merger of scale and investment expertise. "We believe this partnership uniquely positions us in the industry by bringing together Merrill Lynch's global infrastructure and resources with our experience in the alternative investment space," said Peter Stamos, chairman and CEO of Sterling Stamos.

Wilmington Trust stepped back into the market to acquire Boston-based Bingham Legg Advisers (AUM: $1.5 billion), a specialist in tax-sensitive investment strategies. The deal provides Wilmington with a presence in the fifth-largest high net worth market in the U.S. and gives it blanket coverage of the Northeast corridor. Wilmington said that while the firm has been serving New England clients for many years it had "been seeking the right opportunity to expand our physical presence in the region."

In California, Kochis Fitz of San Francisco and Quintile Wealth Management of Los Angeles agreed to a merger creating the state's largest independent wealth manager, with $5 billion in total AUM (newly named Kochis Fitz/Quintile). Tim Kochis, co-founder and CEO of Kochis Fitz, said the deal "creates a solid platform for sustainable long-term growth" and "permits us to sustain our independence indefinitely." Both firms have been averaging around 25% annual growth in AUM, with multifamily office Quintile sporting a particularly well heeled clientele that on average has $50 million in assets with the firm. The two firms said their longer-term goal is to build a national presence.

In another deal involving an ultra high net worth firm, Microsoft co-founder Paul Allen bought a 30% stake in Silvercrest Asset Management Group through his diversified private investment holding, Vulcan Capital. Most of the shares were purchased from a fund run by private equity firm Rosemont Investment Partners. Founded in 2002 and based in New York, Silvercrest has $8 billion in AUM, having added $2 billion since 2005. In a 2006 survey of advisory firms by *Wealth Manager*, Silvercrest ranked ninth for average client AUM ($33 million per client). In explaining its investment, Vulcan cited the rapid growth expected in the ultra HNW market and the "limited supply of sophisticated managers that focus exclusively on this sector." For its part, Silvercrest welcomed the "deep resources and relationships, long-term perspective and financial acumen" offered by its "new strategic partner."

Wealth Management Transactions

	2003	2004	2005	2006	2007
Number of Transactions	51	64	59	65	82
Combined Value ($B)	$6.3	$2.1	$6.2	$7.2	$9.1
Total Seller AUM ($B)	$189	$94	$119	$284	$189
Average Deal Size ($M)	$124	$33	$106	$111	$111
Average Seller AUM ($B)	$3.7	$1.5	$2.0	$4.4	$2.3

Source: Berkshire Capital Securities LLC

Compass Bancshares, acquired in 2006 by BBVA of Spain for $9.6 billion, enhanced its wealth management business with the purchase of Capital Investment Counsel, a 17-year-old Denver-based firm with $1.3 billion in AUM and an additional office in Phoenix. D. Paul Jones, Compass chairman and CEO, said the purchase "is consistent with our business plan aimed at increasing fee-based revenues." Compass said the addition allows it to enhance services in Arizona and Colorado, where it already has banking offices.

Smaller retail banks are also sniffing around the market. In two all-Pennsylvania deals, AmeriServe Financial purchased West Chester Capital Advisors (AUM: $215 million) and Susquehanna Bancshares acquired Widmann, Siff & Co. (AUM: $300 million). In Georgia, Savannah Bancorp acquired Minis & Co. (AUM: $500 million), an investment adviser for individuals and families that has been in business since 1932. Savannah said the purchase would complement its existing trust business.

In a deal between two Toronto-based companies, asset management giant CI Financial Income Fund paid $230 million plus the assumption of $18 million in debt for asset manager and broker Rockwater Capital Corp. (AUM: $4 billion), whose wealth management division has 180 investment advisors across Canada and $9.4 billion in assets under administration. Rockwater's board reportedly put the company up for sale following disappointment over its lagging share price and results. In its latest annual report, CI Financial CEO William Holland said the Rockwater acquisition "reflects our commitment to achieving growth through acquisition" and promised that CI "will continue to seek acquisitions that offer strategic benefits … as we believe that size is a prerequisite to compete effectively and profitably in our industry." In a bid to enhance shareholder returns and improve management of its cash flow, CI converted in 2006 to an "income trust" structure that provides corporate tax benefits for the distribution of larger dividends.

Switzerland, an active market for dealmakers in recent years, played host to another major transaction in the sector, involving the exercise by Rabobank of an existing agreement to buy all the outstanding class "A" shares of Sarasin, the venerable Swiss private bank. The $550 million transaction allowed Rabobank to assume a majority stake in Sarasin, which has $75 billion in AUM. Rabobank acquired a minority stake in 2002, the same year Sarasin shifted from a limited partnership to a joint-stock corporate structure. The transaction followed the appointment of the former head of Credit Suisse's private banking business, Joachim Straehle, as chief executive of Sarasin, a move that foreshadowed more aggressive expansion plans, particularly in Asia.

Straehle said the "stronger cooperation" with Rabobank will help Sarasin reach its "ambitious targets" and noted that the company is looking for "selected acquisitions and opportunities for cooperation." Sarasin also tightened its focus by selling off its Luxembourg bank and brokerage operation. The company, which retained its operational independence and listing on the Swiss Stock Exchange, absorbed Rabobank's international private banking operations in Hong Kong and Singapore.

Another Swiss private bank, fast-growing EFG International, made two more acquisitions last year, on top of the three it completed in 2006, with both extending its global presence.

Another Swiss private bank, fast growing EFG International, made two more acquisitions last year, on top of the three it completed in 2006, with both extending its global presence. The first involved Canada's Bull Wealth Management Group, a 7-year-old firm with $1.3 billion in AUM that provides EFG with "an established presence in Toronto, as well as a solid platform for its ambitious expansion plans in the Canadian wealth management market." Bull Wealth said the deal enables it "to further expand its business, and to offer a broader range of solutions to clients." In the second deal, EFG targeted the U.K. for the third straight year, buying Ashby London Financial Services (AUM: $300 million) as it sought to strengthen its existing business in England's Midlands region. EFG, which became a publicly traded company in 2005, saw its AUM jump 46% to $73 billion in the first half of 2007, while net profit rose 57% to $133 million.

Julius Baer acquired Capital Invest (Monaco) as part of a drive to expand into key markets. Founded by Deutsche Bank in 1998, Capital Invest (AUM: $360 million) was bought out by management in 2003; it will be rebranded under the Julius Baer name. Nearly 40% of Julius Baer's total AUM of $360 billion resides in its private banking unit.

Institutional

For years, sovereign wealth funds (SWFs) have been significant but generally low profile players in the institutional marketplace. An explosion in investible assets, particularly among emerging nations, has brought that anonymity to an end. The McKinsey Global Institute figures Asian central banks and the sovereign wealth funds of oil producing states have some $5.3 trillion in assets, and with growth racing along recently at a 20% average annual clip that number could grow by a few trillion more in the next several years.

The Abu Dhabi Investment Authority alone has $875 billion in assets, including a recent $1.4 billion investment in Carlyle Group. The newly formed China Investment Corp., armed with $200 billion of China's $1.4 trillion in reserves, made headlines worldwide when it sank $3 billion in Blackstone Group, while the nation's National Council for Social Security Fund has held talks with Carlyle and Kohlberg Kravis Roberts involving equity shares. Dubai International Capital agreed to take a minority stake in Och-Ziff Capital Management when that hedge fund went public. The $300 billion Government Pension Fund of Norway plans to boost its equity allocation by 20 percentage points to 60%.

The metamorphosis of SWFs underlines the dynamic nature of the global economy while highlighting the enormous and growing piles of institutional money in search of homes.

Although increasing amounts of the capital held by government entities are being invested directly into companies or financial instruments, there's plenty to go around, and much of it will continue to find its way into the hands of institutional money managers. Indeed, a *Financial Times* columnist suggested that a safe political path for the international investments of the newly aggressive SWFs would involve employing indexed products or "external, long-only diversified investment managers," as opposed to direct share purchases.

The metamorphosis of SWFs underlines the dynamic nature of the global economy while highlighting the enormous and growing piles of institutional money in search of homes. *Pensions & Investments* estimates that the 500 largest institutional asset managers worldwide had assets of $25 trillion in 2006, up 14.3% from 2005 and a stunning 2 1/2 times the amount in 1998.

In search of their share of that mouth watering pie, asset managers continued to scoop up attractive institutional managers last year, cutting 39 deals valued at $5.8 billion. While the number of deals increased in 2007, value dropped significantly from the robust year of 2006 and reverted to levels recorded in 2004-05. Dealmaking in the hedge fund sector remained a vibrant if distinct part of the institutional marketplace, with Goldman Sachs, Lehman Brothers and Threadneedle Asset Management among the numerous financial services companies acquiring stakes in hedge funds last year *(see Hedge Funds section)*.

Within the traditional equity and fixed income areas, there were a number of significant cross border deals, and for the second year in a row a major European deal involving an American private equity player, as TA Associates backed the management buyout at Jupiter Asset Management, the prominent London-based firm owned by Commerzbank. The $1.3 billion deal saw management take a 60% stake, with TA claiming the remainder. Commerzbank, which divested three asset managers last year as part of a strategic refocus on its home market of Germany, acquired the 22-year-old fund manager in two stages in 1995 and 2000.

Calling the buyout "the best way to incentivize and retain senior management, including fund managers," Jupiter said the new structure "provides considerable stability and continuity for employees and clients." Since 2000, Jupiter's AUM has climbed from $25 billion to $41 billion. TA holds investments in 11 asset managers, including Affiliated Managers Group, Arnhold and S. Bleichroeder Holdings, AIM Management Group, and K2 Advisors.

In a second transatlantic deal involving an American investor, Wachovia's Evergreen Investments division tapped the institutional marketplace for the second consecutive year to acquire a majority interest in European Credit Management, a privately held fixed income manager based in London that counted Wachovia among its major clients. ECM was started up by three former Merrill Lynch employees in 1999 just after the introduction of the euro to capitalize on the fledgling bond market in that currency; it now manages $30 billion in assets. Evergreen said the deal enhances its "expertise in asset management" and "global distribution platform" while providing ECM with access to the U.S. market. Fixed income products account for around 40% of Evergreen's AUM of $253 billion.

In a Latin American transaction between two European firms, ING bought the pension businesses of Santander in Mexico, Chile, Colombia and Uruguay, with combined AUM of $20 billion. (Separately, ING was negotiating for the purchase of Santander's Argentine pension business.) The $1.3 billion deal, priced at 15 times trailing earnings, made the Dutch insurer Latin America's second-largest pension fund manager, with $51 billion in AUM. The acquisition also strengthened ING's position in two key markets where it already had pension businesses, Chile and Mexico. In those two countries, as elsewhere in the region, pension assets — bolstered by the introduction of mandatory savings plans — have been growing at solid double digit annual rates. ING projects its pension assets in the region will double between 2008 and 2011.

ING, which also has insurance businesses in several Latin American markets, said the deal underlined its commitment to "strengthening our wealth accumulation business in developing markets." ING is the largest life and pension insurer in Central Europe and the second-largest international life insurer and international asset manager in Asia-Pacific (ex-Japan), where it also cut two asset management transactions last year (see *Cross Border*). For its part, Santander is focusing its Latin American business around its retail and wholesale banking businesses.

In another cross border deal between two European firms outside the Continent, Aberdeen Asset Management purchased parts of Deutsche Bank's Australian asset management business, accounting for around $12 billion in AUM, for as much as $120 million. It marked the second institutional business Aberdeen has acquired from Deutsche Bank in three years, and was driven in part by the

Scottish firm's desire to reunite the Australian fixed income investment team with the Deutsche businesses it acquired in 2005 in Philadelphia and London.

The deal also "significantly enhanced" Aberdeen's presence in the attractive Australian market, including its lineup of local products. By contrast, Deutsche's divestiture is in line with its effort to "migrate from primarily a domestic manufacturing platform to a distribution platform with some specialist investment capabilities." Deutsche retained three-quarters of its AUM in Australia, including commodity and property assets. Bolstered by that 2005 acquisition, AUM at Aberdeen has nearly tripled in the years since to $168 billion, while its fixed income business as a proportion of AUM rose from 17% to 48% by March 2007.

Institutional Advisor Transactions

	2003	2004	2005	2006	2007
Number of Transactions	27	36	37	30	39
Combined Value ($B)	$1.4	$4.9	$5.8	$20.9	$5.8
Total Seller AUM ($B)	$118	$550	$642	$1,168	$496
Average Deal Size ($M)	$54	$136	$158	$695	$150
Average Seller AUM ($B)	$4.4	$15.3	$17.4	$38.9	$12.7

Source: Berkshire Capital Securities LLC

In a European cross border deal, Intesa Sanpaolo paid $1.1 billion for the 65% interest held by Credit Agricole in their short-lived Italian asset management joint venture, CAAM SGR (AUM: $132 billion). The venture, created in 2005 with Banca Intesa, was slated for dissolution by the Italian Competition Authority following the 2006 mega-merger between Banca Intesa and Sanpaolo IMI, the nation's second- and third-largest banks. At the time of the original deal with Credit Agricole, Banca Intesa's asset management unit was the second-largest in Italy.

Canadian firms were buyers, bolstered by a currency that reached parity with the U.S. dollar for the first time since the early 1970s, with Toronto-Dominion Bank's $8.5 billion acquisition of Commerce Bancorp of New Jersey the headline banking deal. Within the institutional sector, there were two transactions of note involving Canadian buyers on both sides of the Atlantic. In the U.S., RBC Capital Markets acquired Ohio's Seasongood Asset Management as part of a larger deal for parent Seasongood & Mayer. SAM manages $1.5 billion in assets for government pension funds. (RBC also acquired Alabama National Bancorp and RBTT Financial Group of the Caribbean.) As part of an effort to "expand our internal investment management capabilities outside of North America," BMO Financial Group acquired Pyrford International, a London-based value and "low absolute volatility" investor with $3 billion in AUM.

There were a number of notable mid-size deals among U.S. buyers and sellers, including Principal Financial Group's $75 million acquisition of Morley Financial, a "stable-value" asset manager with $14 billion in AUM. The deal marked Principal's fourth tack-on acquisition of a specialist asset manager since 2001. Jim McCaughan, CEO of Principal Global Investors, said Morley strengthens "our portfolio of offerings suitable for retirement investing and other long-term investment strategies." Stable-value funds, accounting for around 10% of 401(k) assets, are fixed income instruments that guarantee principal as well as accumulated interest. Founded in 1982, Morley had been owned by Nationwide Mutual Insurance since 1998. Principal said Morley would retain its autonomy while benefiting from the parent's infrastructure, a "multi-boutique approach" the company said has "greatly contributed" to the rapid growth in AUM (to $214 billion) in recent years.

As part of a growth and diversification strategy that includes building an asset management arm, investment bank and securities firm Piper Jaffray acquired Fiduciary Asset Management, a 13-year-old St. Louis firm with $8.3 billion in AUM in a variety of separately managed accounts and closed end funds. Piper Jaffray will pay as much as $66 million for Fiduciary, the first in what chairman and CEO Andrew Duff plans as a series of small asset management acquisitions. In 2006, Piper Jaffray sold its retail brokerage business to UBS, a deal netting $750 million that the company is using for share buybacks and acquisitions. Privately held Philadelphia asset manager Logan Circle Partners, a joint venture between employees and Guggenheim Partners, acquired a team of fixed income managers, traders and marketers as well as $13 billion in AUM from Delaware Investments.

Affiliated Managers Group took a 70% stake in Cooke & Bieler (AUM: $9 billion), a "high quality, low risk" equity manager that has registered 35% average annual growth in AUM since 2002. Based in Philadelphia and founded in 1949, C&B manages separate accounts for institutional and high net worth clients and acts as subadvisor to two Wells Fargo mutual funds, a deal cut in 2004. In explaining the sale, Kermit Eck, a member of C&B's management committee, cited the benefits of AMG's resources combined with its "entrepreneurial" approach toward affiliates. C&B was owned by United Asset Management for 15 years until management led a 100% buyout in 2001, following Old Mutual's acquisition of UAM.

There were several small management buyouts in the U.S. involving institutional firms. Executives at Johnson Asset Management bought out their firm from Johnson Financial Group, through the newly formed Optique Capital Management. An investor in domestic and international equities, JAM had $1.6 billion in AUM. JFG is the financial holding company for the heirs to SC Johnson Wax company. Management at Froley, Revy Investment acquired their firm from First Republic. A specialist in convertible securities founded in 1975, Froley, Revy suffered a big drop last year in AUM to $800 million after losing two key clients, Oregon Investment Council and Nuveen Investments. In a cross border deal, management at Tamro Capital (AUM: $750 million), a small cap asset manager based in Virginia, bought out ABN Amro's interest, backed by private equity firm Northern Lights Ventures. The two companies plan to continue a subadvisory and distribution relationship.

Mutual Funds

While investor and media attention has centered on the dynamic private equity and hedge fund industries in recent years, the old fashioned mutual fund sector has been showing that it knows how to generate news, too. The innovative and lucrative "130/30" funds, which mix traditional long strategies with short selling, now hold $75 billion in assets and Merrill Lynch suggests that total could reach $1 trillion in the next five years. Just last year, Rydex Investments launched a managed futures fund that retail investors can purchase with a minimum investment of $2,500.

Target-date or "life-cycle" funds, providing baskets of funds and varying levels of risk tied to expected retirement dates, are growing rapidly, with assets more than doubling between 2004 and 2006 to $300 billion, according to the Investment Company Institute (ICI). Importantly, mutual fund providers are broadening the appeal of these investments to capture 20-somethings by offering target dates 40 years down the road.

Fidelity Investments has added a new item to the retirement menu with its "Income Replacement" product, which guarantees payments for a fixed period of time but with lower costs than fixed annuities. TD Ameritrade introduced the first target-date exchange traded funds, aimed at those retiring between 2010 and 2040. The broader ETF market continued its ascent, with assets growing another 46% in the U.S. in the year through August 2007, to $507 billion, according to ICI.

Amid that change and transformation, mutual fund dealmakers remained exceptionally busy for the second year in a row, as the industry recorded 21 deals valued at $10.9 billion. Although transaction value dropped from the recordbreaking year of 2006, it was more than double the total recorded between 2003 and 2005. The numbers included a couple of major billion-dollar-plus deals in the U.S., one involving a private equity firm and the other a management buyout.

In the first, Madison Dearborn Partners acquired Nuveen Investments for $5.8 billion, by far the largest asset management deal ever involving a private equity firm and another indicator of that industry's growing interest in asset managers. In addition, MDP, which was joined by several major investors, assumed $550 million of Nuveen's debt. (The investors include Citigroup, Deutsche Bank, Merrill Lynch, Morgan Stanley and Wachovia.) MDP paid more than 17 times pretax earnings, or 3.5% of AUM. While MDP owns a number of financial services firms, Nuveen represents its first investment in an asset manager.

For Nuveen, the deal ends its brief sojourn as an independent company: in a secondary public offering in April 2005, St. Paul Travelers Cos. divested its majority shareholding in the Chicago-based fund manager, which has $170 billion in AUM (one-third in closed end funds). Nuveen had been publicly traded since 1992. The $65-per-share price paid by MDP was nearly twice the 2005 secondary offering price and a 20% premium on the share price at the time of the announcement. Nuveen said the transaction, which is expected to incorporate an equity interest for management, provides it with "the opportunity to accelerate [the] development of new investment capabilities, products and distribution channels, and helps us attract and retain top industry talent." MDP indicated it would seek bolt-on acquisitions to add new products to Nuveen's portfolio.

The second major deal involved the $2.7 billion management buyout of Marsico from Bank of America, which had acquired the firm for a total of $1.1 billion in two stages in 1999 and 2000. In the years since, Marsico's AUM has jumped from $15 billion to $94 billion. Thomas Marsico founded his firm in 1997 after an impressive career at Janus, where Morningstar named him "Fund Manager of the Year," and he will be sole owner following completion of the deal.

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In explaining the move to repurchase, Thomas Marsico acknowledged BoA's contribution to his company's expansion but said Marsico's continued growth and competitiveness required an incentive structure with equity stakes for employees — a recurring theme in several of the fund deals last year and indicative of the competition for talent within the industry. Marsico said low interest rates allowed him to make the offer. BoA will continue to distribute Marsico's funds, while Marsico maintains its role as subadvisor to the bank's Columbia fund line.

Prior to the Marsico deal, Bank of America sold seven closed end, fixed income Colonial Funds with total AUM of $1.2 billion. The buyer, MFS Investment Management, ran six closed end funds with $2.8 billion in AUM prior to the acquisition. For BoA, the sale marks its exit from the closed end fund market: in 2006, the bank sold its closed end Liberty All Star equity funds to ALPS Advisers of Denver. For a brief period in 2006, MFS was itself on the sale block before parent Sun Life Financial of Canada pulled back, saying it remained committed to asset management in the U.S.

In a second transaction involving a private equity firm, TA Associates took a minority stake in Arnhold and S. Bleichroeder Holdings (AUM: $45 billion), the New York-based manager of First Eagle Funds (accounting for 80% of AUM), as well as hedge funds and separately managed accounts for institutions and high net worth clients. The mutual funds are overseen by Jean-Marie Eveillard, a noted value investor and longtime portfolio manager for Eagle who came out of a two-year retirement last year to again head up investment strategy. "My first responsibility is to avoid losing money, at least over the long term," he recently told *Fortune Advisor*. "Unlike hedge funds, mutual funds are dealing with the savings of middle class people. If I lose money, it could make life more difficult for retirees and other people who need the money."

Majority ownership of ASB will remain with the founding family shareholders, who said the new structure allows them to provide equity incentives to employees. TA Associates has 11 investments in asset managers, including two others announced last year: hedge fund K2 Advisors and U.K. institutional firm Jupiter Asset Management (see *Alternative* and *Institutional* sections, respectively, for more information).

In a significant acquisition involving two similarly sized, privately held firms, Security Benefit Corporation (AUM: $20 billion) acquired Maryland-based Rydex Investments (AUM: $15 billion), a specialist in creating institutional style products for the retail market, including alternative investments and currency-based ETFs. Security Benefit, founded in 1892, left the life insurance business 10 years ago to concentrate on variable annuities and expand its asset management business; AUM has tripled during that time. The two firms had a long prior relationship, with Rydex funds offered as part of Security's variable annuity products.

Kris Robbins, Security Benefit chairman, president and CEO, said the combination "will benefit from a more robust and broader platform of investment products and capabilities" and from their ability to "leverage award-winning technology platforms." The two companies also merge relationships with 40,000 financial advisors. Strategically, Security Benefit and Rydex intend to focus on the retirement needs of baby boomers — what Rydex CEO Carl Verboncoeur calls the "largest single asset management opportunity in the next 10 to 20 years" — and provide more innovative products, including ETFs. The sale follows four years after the death of Rydex founder A.P. "Skip" Viragh and the subsequent desire of the family to diversify its holdings and create a "long-term ownership solution."

In a continuation of the tack-on acquisition strategy aimed at expanding its menu of non-money market funds, Federated Investors bought Rochdale Investment Management's Atlas Portfolio, a $321 million international equity fund. Since 2005, Federated has made seven acquisitions of equity or bond funds. Federated transferred the assets to a new Federated InterContinental Fund, which will continue to be run by the former Atlas management team. As part of the deal, Federated agreed to acquire the proprietary quantitative investment model Rochdale uses to manage the fund. Rochdale is a wealth manager based in New York.

Although bond and equity funds accounted for just 25% of Federated's $237 billion in AUM in 2006, they represented more than half of revenues, with equities comprising 39%. Money market funds accounted for 73% of Federated's AUM in 2006, down two points from the previous year. Since 2002, Federated's equity assets have more than doubled to $41 billion and have also accounted for more than half the growth in total AUM.

Mutual Fund Transactions

	2003	2004	2005	2006	2007
Number of Transactions	28	14	19	19	21
Combined Value ($B)	$0.7	$0.9	$2.0	$13.8	$10.9
Total Seller AUM ($B)	$21	$43	$194	$752	$370
Average Deal Size ($M)	$24	$64	$106	$728	$520
Average Seller AUM ($B)	$0.8	$3.1	$10.2	$39.6	$17.6

Source: Berkshire Capital Securities LLC

In a deal unique for both the location of the participants and the assets involved, Sentinel Investments of Vermont acquired New Hampshire's Citizens Funds, a 25-year-old "socially responsible" mutual fund group with $800 million in AUM. Sentinel, part of the National Life Group of Vermont, plans to wrap Citizens' eight funds into existing or new Sentinel funds. Sentinel has been an active buyer of late, acquiring New York's Bramwell Capital Management in 2005 and the mutual funds run by Synovus of Georgia in 2006, adding a total of $744 million in AUM in the process. Sentinel manages $18 billion in mutual funds and institutional accounts.

Outside the U.S., Asia was a hotspot for a large number of cross border deals. The attention asset managers are paying to India is particularly noteworthy: Franklin Resources, Morgan Stanley and Robeco all made investments in that nation's fledgling mutual fund industry.

China and South Korea also drew the attention of international financial firms. ING purchased Morgan Stanley's South Korean asset manager, Landmark Investment Management (AUM: $6 billion), and several European insurers took stakes in Chinese asset management joint ventures, including Aegon of the Netherlands, Aviva of the U.K., and Eurizon Financial Group of Italy. (See *Cross Border* section for more information on deals in Asia.)

Within the U.K., management acquired Premier Asset Management (AUM: $3.6 billion) through a newly created buyout vehicle, Harvard Bidco. The $90 million transaction was backed by London private equity firm Electra Partners, which targets the mid-size European buyout market and has $1.8 billion in funds under management. The companies said the privatization would allow Premier to strengthen the business through reinvestment of profits and by providing equity incentives "to attract, incentivise and retain highly talented individuals."

In a second U.K. fund deal, London-based Syndicate Asset Management paid as much as $11 million for Insight Guernsey (AUM: $1 billion), a fixed income specialist based in the Channel Islands. SAM said the deal expands its offshore presence and its product line, while providing for synergistic savings. The Guernsey-based business was part of the larger Insight Investment Management group, which said the subsidiary "did not form part of the plan for Insight's expansion into continental Europe." Formed in 2002 by Edinburgh-based financial services giant HBOS, Insight Investment has $180 billion in AUM. SAM (AUM: $12 billion) has made eight acquisitions since going public in 2005, including a second deal last year for EPIC Investment Partners (AUM: $5 billion), an institutional fixed income manager, also based in the Channel Islands.

Cross Border

Since the formation of the single European market, observers have looked for signs that the protectionist walls stifling banking mergers on the Continent had finally crumbled. Last year's $100 billion purchase by a consortium of European banks of ABN Amro, a Dutch institution whose history dates to 1824, may well have represented the collapse. It marked the third major European cross border deal in four years, the largest banking transaction in history, and took place amid talk of other major European banks reviewing cross border tie-ups, including Unicredit and Societe Generale.

The ABN deal also opened the door to team approaches to acquiring large, diversified financial firms whose parts may be more valuable to buyers than their sums. ABN Amro is being split three ways: Fortis will take the asset management and Dutch banking operations; Santander, the Brazilian and Italian operations (Santander promptly made plans to sell Antonveneta, the Italian bank it acquired); and Royal Bank of Scotland, the U.S., Latin American (minus Brazil) and investment banking businesses.

ABN Amro led a robust and interesting year for cross border deals in financial services, with notable investments worldwide by sovereign wealth funds and Chinese financial firms *(see Summary)*. Within the asset management industry,

The ABN deal also opened the door to team approaches to acquiring large, diversified financial firms whose parts may be more valuable to buyers than their sums.

dealmakers were particularly active cutting cross border transactions in China and India, the European wealth management sector, and the hedge fund industry *(see Hedge Funds/Private Equity)*. In 2007, there were 61 cross border asset management deals with a value of $11.8 billion.

Fortis' acquisition of ABN Amro's asset management arm, including the private banking business, involved the largest transfer of AUM ($480 billion) of any cross border deal. (In total, Fortis paid $35 billion for its piece of ABN Amro, including the Dutch banking business, or nearly 10 times 2007 earnings.) The combined firm, with $800 billion in AUM, will become a far more formidable asset manager, and includes Europe's third-largest private bank (AUM: $315 billion). The group will remain focused in Europe (80% of AUM), with considerable strength in the attractive Benelux markets, where it will be either No. 1 or 2 in private banking and mutual funds. Benelux accounts for more than half of the combined firm's private banking AUM and 40% of total AUM.

But both firms boast operations throughout the world, including more than two dozen markets outside Benelux where their businesses do not overlap. In the coveted developing markets of Asia — which in 2006 generated 28% of Fortis' global private banking net inflows — ABN Amro says the combination will create a top-10 private bank, with $30 billion in AUM. Fortis also projects $440 million in cost savings by 2010 as a result of the merger. "The combination of ABN Amro's and Fortis' asset management businesses will create an organization of real scale and a top tier asset manager in Europe," said Jean-Paul Votron, CEO of Fortis.

The wealth management business drew numerous European dealmakers to the negotiating table, with Swiss buyers and sellers particularly busy. Dutch financial services firm Rabobank exercised its option to acquire a majority stake in Swiss private bank Sarasin (AUM: $53 billion), at a cost of $550 million. EFG International, an aggressive publicly traded Swiss firm, acquired Ashby London Financial Services (as well as Canada's Bull Wealth Management Group), for its sixth European acquisition in three years. Clariden Leu, formed last year via the merger of four Credit Suisse private banks and the firm's securities dealer, took a 10% stake in a German bank serving private clients, Nordaktienbank. Clariden, with $115 billion in AUM and offices in 21 markets, also acquired the Asian private banking business (AUM: $750 million) of South Africa's Standard Bank.

Milan-based Banca Profilo crossed the border to buy a majority stake in a Geneva-based private bank, Societe Bancaire Privee. The publicly traded investment bank said the acquisition is part of the effort "to internationalize" its private banking business. Elsewhere, BNP Paribas of France strengthened its wealth business in the Netherlands through the acquisition of Kas Bank's private bank, a deal adding $1 billion to the $2.4 billion BNP already managed there. ABN Amro divested its London-based private banking business (AUM: $2 billion), with buyer Societe Generale Private Banking calling the deal "a rare opportunity" to expand its U.K. business "through external growth." (See *Wealth Management* for more information on some of the deals noted above.)

Aviva, the U.K. insurer and asset manager, went trawling in the developing markets of Eastern Europe to acquire a Romanian asset manager, Certinvest (AUM: $35 million), jointly owned by management and the Romanian-American Enterprise Fund. Aviva, which in 2000 established a local life insurance business, said the deal "confirms our clear ambitions for growth in Romania and more broadly in Central and Eastern Europe." Commerzbank continued to divest its international asset management business, selling Jupiter Asset Management of the U.K. to management and TA Associates of the U.S. (see *Institutional*); CCR Group of France to UBS; and Commerzbank International Capital Management (Japan), its Japanese asset manager, to Fortis.

The $650 million acquisition of CCR Group (AUM: $25 billion) marked the largest asset management deal UBS has made in Europe in recent years and strengthens the company's relatively small operation in France. CCR offers a mix of fixed income, equity and alternative products for institutions and also includes a private client unit. UBS launched a wealth management business in France in 1999 and four years later acquired Lloyds TSB's local wealth manager.

Although the euro reached new highs against the greenback, that did not translate into an aggressive move by Europeans into the U.S. asset management industry. Standard Chartered's acquisition of Miami-based American Express Bank (AUM: $22.5 billion) for as much as $1.1 billion was the largest such deal. AEB, the private banking and dollar clearing arm of the credit card giant, is domiciled in the U.S. but has an extensive international presence, particularly in the developing markets that make up the bulk of StanChart's business (see *Wealth Management* for more information).

Cross Border Transactions

U.S. - International	2003	2004	2005	2006	2007
Number of Deals	12	15	13	24	18
Value ($B)	$1.1	$3.4	$1.7	$8.3	$5.7
Two International Firms	**2003**	**2004**	**2005**	**2006**	**2007**
Number of Deals	16	15	23	24	43
Value ($B)	$0.5	$0.9	$7.8	$1.4	$6.2
Total	**2003**	**2004**	**2005**	**2006**	**2007**
Number of Deals	28	30	36	48	61
Value ($B)	$1.6	$4.2	$9.5	$9.7	$11.8

Source: Berkshire Capital Securities LLC

Scotland's Aberdeen Asset Management also crossed the Atlantic to acquire Nationwide Financial Services' equity fund business, with $7 billion in AUM. Martin Gilbert, chief executive of Aberdeen, said the transaction "broadens Aberdeen's U.S. operations with the addition of a highly regarded equities team" and "continues our strategy of acquiring bolt-on businesses that enhance our product range and geographic reach." In 2005, Aberdeen acquired Deutsche Bank's global fixed income operation, which included a significant U.S. business. The publicly traded company has enjoyed average annual growth of nearly 50% in AUM in the five years through March 2007, to $180 billion. (In 2007, the company also acquired Deutsche Bank's Australian asset manager. See *Institutional* section.)

European financial services firms were far more active in Asia, a reflection both of the region's coming of age and the ongoing liberalization of its financial markets. Cerulli Associates figures the mutual fund industry in Asia (excluding Japan) grew 27% in 2006, to $652 billion, and expects growth to average 19% annually over the next five years. Among emerging Asian markets, China has been the focal point for investments by financial services firms in recent years, including within the mutual fund industry. After growing 80% to $109 billion in 2006, the nation's fund assets doubled again by mid-2007, placing China second behind South Korea (AUM: $278 billion) among Asian markets, excluding Japan.

But India has been attracting interest as well, and last year the country played host to numerous deals. Estimates of assets in India's mutual fund industry in 2006 range between $75 billion and $90 billion, with projections of near-term annual average growth as high as 30%; more than 30 money managers operate within the industry. European insurance companies led dealmakers in India and China, with several building upon existing operations in those countries. Two firms cut fund deals in both markets: AXA and Franklin Resources.

Within India, two Dutch firms were active, including Robeco (the asset management unit of Rabobank), which paid $26 million for a 49% stake in Canara Bank's asset management arm, subsequently named Canara Robeco (AUM: $480 million). B. Sukumaran, managing director of Canbank Investment Management Services, said the joint venture combines Canara Bank's branch network "with the international product and fund management expertise and global network of Robeco." In a bid to energize its existing Indian mutual fund operation, ING sold a 39% stake to Hathway Investments, controlled by Indian conglomerate Rajan Raheja Group. ING, which retained a 43% stake, already had a successful insurance joint venture with Rajan. (ING also acquired a South Korean asset manager last year, in line with plans to expand its financial services business in developing markets via small-to-mid-size acquisitions.)

Cross Border Transactions by Domicile and Type

2007	Buyer: U.S. Seller: International	Buyer: International Seller: U.S.	Buyer: International Seller: International	Total
Wealth Management	0	3	16	19
Institutional	3	2	5	10
Mutual Fund	0	1	6	7
Other	6	3	16	25
Total	**9**	**9**	**43**	**61**
2006	**Buyer: U.S. Seller: International**	**Buyer: International Seller: U.S.**	**Buyer: International Seller: International**	**Total**
Wealth Management	2	2	6	10
Institutional	2	1	2	5
Mutual Fund	1	2	2	5
Other	2	12	14	28
Total	**7**	**17**	**24**	**48**

Source: Berkshire Capital Securities LLC

In an extension of a relationship that began two years ago with an insurance joint venture, AXA and diversified conglomerate Bharti Enterprises formed a joint venture asset manager touted as a merger of the French company's "globally recognized investment expertise" and Bharti's "enviable brand reputation" and "unique understanding and insights on the Indian retail market." AXA assumed a 75% shareholding. Dominique Carrel-Billiard, chief executive of AXA Investment Managers, said the deal, combined with investments elsewhere in Asia, demonstrates the firm's "ambitions for the region, and is further proof of our continued global expansion."

American companies joined the dealmakers from Europe. Pioneer Investments of Boston, majority owned by Italy's Unicredit, re-entered India through a 51% stake in a joint venture with Bank of Baroda, Baroda Pioneer Asset Management. Pioneer quit the market in 2002 after a failed joint venture. Pioneer called the investment an important part of its commitment to "rapid growth" while Bank of Baroda said it "demonstrates the bank's commitment to providing its customers with a complete range of financial solutions." The bank has 2,700 branches in India.

Subsequent to the ING-Hathway deal, Franklin Resources bought out Hathway's 25% interest in their joint venture for $90 million, a plan Franklin had announced in 2006. Operating under the Franklin Templeton name, the venture has $5.5 billion in AUM, making it one of the fund manager's top 10 international markets (Franklin entered India in 1995). Meanwhile, Schroders was reportedly in talks with several companies regarding a fund joint venture, while AIG entered the market through a wholly owned local subsidiary. Morgan Stanley filed papers to introduce two new funds in India, 13 years after the launch of its first fund, Morgan Stanley Growth.

For most of 2007, UBS held the distinction of having cut the largest deal in India, the proposed $120 million purchase of Standard Chartered's local mutual fund business. But by year's end the nation's central bank nixed the transaction, first announced in January 2007. StanChart, ranked No. 9 in the market with $3.2 billion in AUM, was reportedly in talks with other major financial firms regarding a sale of that business. As was the case with many of the European companies doing deals, UBS was seeking to build upon an existing business in India, where it is already one of the top securities brokers for international investors. Separately, UBS and StanChart said they plan to form a strategic alliance for fund distribution in Asia, the Middle East and Africa.

China continued to draw financial firms to its fast growing asset management industry. A recent McKinsey & Co. report forecasts ninefold growth in AUM to $1.4 trillion in the ten years through 2016, or 24% average annual growth. Although McKinsey notes that high churn rates and competitive fees can crimp profitability, the fact that only 3% of household financial assets are in mutual funds — combined with official efforts to build the financial services industry and pension vehicles — bode well for the industry. (Despite the huge run-up in the Shanghai Stock Exchange, 79% of all personal financial assets remain in bank accounts.)

The nation's growing and bloated foreign exchange reserves — $1.4 trillion by the middle of 2007 — have also placed pressure on Beijing to ease rules on capital outflow, providing another avenue of opportunity for international asset managers. That came last year in the form of the state-sanctioned Qualified Domestic Institutional Investor II program, allowing retail customers to purchase mutual funds owning international assets.

BNY Mellon Asset Management received regulatory approval to provide QDII subadvisory services for China

Southern Fund Management, while Deutsche Bank's long established Harvest Fund Management joint venture became the first such firm approved for participation. (Separately, BNY Mellon set up a joint venture fund management company with Western Securities, in which it took the maximum allowable 49% stake.) The government set a QDII investment quota of $15 billion for 2007, a number that JP Morgan Chase says could reach $90 billion in 2008. In another reform, Beijing also lifted limits on Chinese insurers' overseas assets from 5% to 15%.

European life insurers were notable participants in the market last year, including AXA, which took a 39% stake in a joint venture with Shanghai Pudong Development Bank. The joint venture planned to raise $1.3 billion by the end of 2007 for its first fund. Dutch insurer Aegon took a 49% stake in Industrial Fund Management Co. (AUM: $2.3 billion), owned by Industrial Securities, one of the nation's largest securities firms. The companies said Aegon's "longstanding and broad-based expertise in pensions, innovative product development and risk management" will support IFMC's ambitions in China's pension market.

Nikko Asset Management became the first Japanese asset manager to enter the market, via its 40% purchase of Rongtong Fund Management.

Italian insurer and asset manager Eurizon Financial Group paid some $75 million for a 49% share in Penghua Fund Management, soon after purchasing a 20% stake in Union Life of China. Founded in 1998, Penghua has $3.5 billion in AUM, having recorded 120% growth in assets in 2006. Prudential of the U.K. raised its stake from 33% to 49% in Citic Prudential (AUM: $1.1 billion), the joint venture it formed in 2005 with Citic Group, the powerful state-owned investment company. Prudential has life insurance operations in 12 Asian markets and mutual fund businesses in India and China. Barclays received regulatory approval to invest in New China Trust & Investment, a deal that would make the British bank the first non-Chinese firm with a stake in a local trust company.

In a deal concluded with China's largest life insurer, China Life Group, Franklin Resources acquired 26% of China Life Franklin Asset Management. Citing the relaxation of investment restrictions on Chinese banks, Franklin said the joint venture would leverage "Franklin Templeton's global investment expertise to manage China's growing pool of overseas assets." China Life Insurance (Overseas), a China Life subsidiary, also has a stake in the venture. Franklin has had a representative office in the nation since 1997. Morgan Stanley paid $8.6 million for a 35% stake in Jutian Fund Management, equal to the shareholding of the other major partner, Jutian Securities.

Nikko Asset Management became the first Japanese asset manager to enter the market, via its 40% purchase of Rongtong Fund Management (AUM: $3.1 billion). The deal cemented a 6-year relationship involving research services by Nikko. The company reportedly paid more than $12 million for its initial stake of 20% in March 2007, an investment it increased several months later. The two firms touted the venture as a merger of Nikko's "best practices" and Rongtong's "unparalleled understanding of the Chinese market." In 2007, Citigroup acquired securities broker Nikko Cordial, majority shareholder of Nikko AM.

South Korea recorded several deals in 2007, having accounted for the largest transaction in Asia in 2006 — UBS' $158 million investment in Daehan Investment Management Trust. ING acquired 100% of Landmark Investment Management from several shareholders, including majority owner Morgan Stanley, merging the firm with its ING Investment Management Korea unit to form a top-10 Korean asset manager (AUM: $13 billion). The company, which aims to triple AUM by 2010, said the deal is in line with its "organic growth strategy of pursuing carefully selected add-on acquisitions to strengthen our position in Asia-Pacific." ING has a second investment in Korea's KB Asset Management and also runs the fourth-largest insurance company in the market, as well as wholesale bank and real estate businesses. (ING also acquired a pension business in Latin America. See *Institutional* section.)

Goldman Sachs entered the Korean market through the acquisition of Macquarie-IMM Investment Management (AUM: $11 billion), in the process touting the deal as part of its effort to become "one of the leading asset managers in the Asia region." Goldman also has a 9% shareholding in Hana Financial, one of the country's largest financial services firms. Macquarie Bank of Australia has a larger asset management joint venture with Shinhan Financial Group, Macquarie Shinhan. JP Morgan also entered the market through a wholly owned asset manager.

Elsewhere in the world, financial services firm Oman National Investment Corp. Holding acquired 20% of Canadian fund manager FrontierAlt Investment Management. The deal represented Oman National's first investment outside the Middle East. In 2006, Toronto-based FrontierAlt created a subsidiary catering to Islamic clients and also launched two "Islamic" funds with investment principles based on Shariah law. In another sign of the burgeoning financial relationships between the oil rich Gulf states and the West, Franklin Resources took a 25% stake in Algebra Capital, a Dubai-based fund manager. Algebra estimates that mutual fund AUM in the Middle East/North Africa region will triple over the next five years to $200 billion. Referring to that "tremendous opportunity," Franklin president and CEO Greg Johnson said, "Algebra's experienced team in the regional markets make it a solid strategic investment for our organization." Franklin said it would build off the acquisition to create a "Shariah-compliant fund."

Alternatives

Real Estate

Although the woes of investors in U.S. subprime securities came to dominate the attention of the world in 2007, the year was also notable for the continuing interest displayed by investors in international property markets. Morgan Stanley took in $8 billion for a global real estate fund and made a $3.9 billion acquisition of Australia's largest office property owner, Investa Property Group, while Goldman Sachs' Developing Markets Real Estate fund raised $2.1 billion, mainly for investment in Asia.

The California Public Employees' Retirement System (Calpers) committed $500 million to a new Asian property fund from ARA Asset Management, owned by leading Hong Kong real estate firm Cheung Kong Group, noting the "large investment opportunity universe outside the U.S. in which we intend to increasingly participate." Private U.S. real estate investment firm Beacon Capital Partners closed the largest ever global office fund, with $4 billion in capital, targeting select "knowledge-based" markets "with constraints on size" in both the U.S. and Europe. It was joined by a $2 billion closed end global property fund from Alpine Woods Capital Investors that floated on the New York Stock Exchange and a global real estate fund from Charles Schwab, the first such proprietary fund the discount broker has introduced.

Within the real estate advisory sector, there were two cross border deals with European targets that illustrate the efforts of firms to extend their portfolios internationally. One involved Australia's second-largest property trust, Stockland Corp., which entered the European market via the $335 million acquisition of Halladale Group (AUM: $1.6 billion), a publicly traded U.K. property development and investment company. Matthew Quinn, managing director for Stockland, called the deal "the first step in our U.K. expansion strategy" and touted "the potential for Stockland to develop a significant and successful international business in the long term." Stockland's acquisition is part of a broader trend of European investments by Australian property funds, driven by capital from the nation's large superannuation plans.

The property fund manager of Scotland's Aberdeen Asset Management enhanced its presence in Germany with the $160 million acquisition of Dresdner Bank's real estate advisory arm, DEGI. The deal adds $9 billion in AUM to the $20 billion Aberdeen previously managed. Rickard Backlund, CEO of Aberdeen Property Investors, said DEGI's "established position with institutional and private investors and the highly complementary nature of our product ranges and investment regions make DEGI the ideal partner for Aberdeen."

Germany is the largest property fund market in Europe and Aberdeen one of the leading such managers in Europe, with 13 national and regional funds as well as fund of property funds. Aberdeen Asset Management set up its real estate asset management division in 2000 with two acquisitions and the business has enjoyed rapid growth, with AUM more than doubling since 2004. Aberdeen was an active buyer outside the U.K. last year, acquiring Nationwide Financial Services' U.S. equity fund business and parts of Deutsche Bank's Australian asset manager (see *Cross Border* and *Institutional* sections, respectively).

Real Estate Transactions

	2003	2004	2005	2006	2007
Number of Transactions	4	3	6	10	17
Combined Value ($M)	$361	$51	$221	$1,536	$2,044
Total Seller AUM ($B)	$21.4	$3.8	$3.7	$31.1	$53.6
Average Deal Size ($M)	$90	$17	$37	$154	$120
Average Seller AUM ($B)	$5.4	$1.3	$0.6	$3.1	$3.2

Source: Berkshire Capital Securities LLC

Hedge Funds/Private Equity

The subprime mortgage blow-up had an immediate but perhaps short lived impact on the hedge fund industry, as net inflows of $45 billion in the third quarter remained healthy in the face of the turmoil, if lower than the first two quarters, according to Hedge Fund Research. The $164 billion net inflow total in the first three quarters easily passed the full-year record of $126 billion set in 2006, while total hedge fund AUM worldwide topped $1.8 trillion, approaching the size of the U.K. economy.

Nevertheless, the subprime crisis served as a reminder that the sector carries risks. Numerous high profile quantitative funds were particularly hard hit as their computer-reliant models failed to account for the meltdown. Goldman Sachs' $5.5 billion Global Equity Opportunities fund lost a third of it of its value in one week in August, while two of Bear

Stearns' funds folded altogether. The $3 billion in hedge funds run by Sowood Capital lost more than half their value (with some of the assets being scooped up by Citadel Investment Group, the hedge fund company owned by Chicago billionaire Kenneth Griffin).

Institutions are increasingly willing to live with those risks as they come to view an investment strategy overly reliant on traditional stocks and bonds as even riskier. In a more radical example of this trend, the $100-billion Teacher Retirement System of Texas said it would increase its target portfolio allocation for alternatives (including real estate and private equity) from 4% to 29% over the next three years. Citing the five years it took the pension fund to recover from stock market losses suffered in 2001-02, TRS Chairman Jarvis Hollingsworth said the transition toward alternatives "will guard against the downturns of the markets" and provide the "opportunity for more robust returns."

As institutions gravitate toward these investments, the industry itself continues to assume the characteristics of a more mature industry, including greater transparency and public ownership. Last year, several additional hedge fund companies went public or announced plans to do so, including GLG Partners and Och-Ziff Capital Management in the U.S.; Gottex Fund Management in Switzerland; and Platinum Asset Management in Australia. In Europe, numerous individual hedge funds floated on stock exchanges. The industry is also becoming more concentrated, with the top 100 hedge funds accounting for 67% of AUM in 2006, up 18 points from 2003, according to Morgan Stanley. *Alpha* magazine figures the top 100 also increased AUM by 39% in 2006.

For dealmakers, 2007 was by far the most active year to date, with a record $8.4 billion in transactions that easily eclipsed the total from the previous five years. The roster of buyers was also impressive, with investment bankers — accustomed to and comfortable with risk — continuing to dominate the action, joined by a small number of pure asset managers.

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Among the many prominent investment banks entering the market last year was Lehman Brothers, which added to its pre-existing portfolio of three hedge fund investments with one U.S. and one European deal. Lehman also held firm to its strategy of buying minority shareholdings. In the largest hedge fund transaction last year based on AUM, Lehman bought 20% of D.E. Shaw, one of the top-five hedge fund managers in the world with more than $30 billion in AUM. Lehman called the deal "consistent with our pioneering program of minority positions in world class investment platforms."

Founded in 1988 by a Columbia University computer science professor, David Shaw, the group has departed slightly from its stock-in-trade as a market neutral quant firm to mix in traditional long-only strategies and a private equity arm that last year acquired insurance company James River Group. In its second deal, Lehman acquired a 20% share of Spinnaker Capital, a London hedge fund with $5 billion in AUM. Founded in 1999 by former Credit Agricole employees, Spinnaker specializes in emerging market bonds. Lehman aims to hike its shareholding to 25%.

Citigroup also went to market twice in a bid to strengthen its large alternative investment arm, including purchasing fledgling hedge fund Old Lane Partners (AUM: $4.5 billion), a deal designed more to capture owner and Wall Street heavyweight Vikram Pandit and his team than financial assets. Pandit, a native of India and former Morgan Stanley executive whose firm followed a global multi-strategy approach, was subsequently named head of Citi Alternative Investments (AUM: $49 billion), which had been operating without a chief executive since 2006. (Following the resignation of Citigroup chairman and CEO Charles Prince in November, Pandit was named CEO.)

Pricing on the deal was generally estimated to be in the $600 million range. The second acquisition, occurring amid Citi's subprime and leadership crises, involved Carlton Hill Global Capital, a New York credit derivatives specialist with $150 million in AUM. Carlton, which will be wrapped into the fixed income arm of Citi Alternative Investments, was started in 2006 by two veterans of Morgan Stanley's fixed income group.

Perella Weinberg Partners also picked up a small credit specialist during the subprime meltdown, Xerion Capital Partners (AUM: $400 million), a 5-year-old company that focuses on distressed assets. Perella, a corporate advisory and asset management firm formed in 2006 with more than

$1 billion in capital, also pledged to pump $100 million into Xerion investments. Perella said the acquisition brings the company "a highly regarded team with a strong record of accomplishment investing in distressed and special situations just as the credit markets are presenting very dynamic opportunities."

Goldman Sachs, one of the top two hedge fund managers in the world, added to its capabilities by taking a 10% stake in one of London's largest hedge funds, Winton Capital Management. The investment was made via a new Goldman private equity fund that plans to raise some $500 million to invest in hedge funds. A 10-year-old managed futures investor, Winton's AUM has skyrocketed to $10 billion from $400 million in 2003. The firm was founded by David Harding, who sold the AHL commodity trading system to Man Group in 1989.

Two other New York financial giants, Merrill Lynch and Morgan Stanley, cut hedge fund deals for the second straight year, with Merrill acquiring nearly 20% of GSO Partners (AUM: $8 billion), a 2-year-old hedge fund and private equity hybrid. As part of the deal, Merrill said it "will invest capital in a number of GSO's strategies." In 2006, GSO teamed up with Merrill and other investors to take Reader's Digest Association private. Morgan Stanley, which made a dramatic entry into the hedge fund sector in 2006 with four investments in the U.S. and U.K., added two more last year.

In the first, Morgan Stanley turned its attention to Asia, where it acquired a "significant" minority investment in Hong Kong start-up Abax Global Capital. Run by former executives from Citadel Investment Group and Merrill Lynch, Abax focuses on special situations in China, Hong Kong and Taiwan. In the second deal, the company took 20% of Traxis Partners (AUM: $1.5 billion), started up by Barton Biggs, the prominent former chief strategist for Morgan Stanley. Traxis, which has had a relationship with Morgan Stanley since its founding in 2003, pursues a global, multi-asset strategy. Biggs worked for Morgan Stanley for 30 years before embarking on his latest venture as he approached the age of 70. "I was spending more time going to meetings and less time being an investor," he told National Public Radio in 2006, in explaining his move.

Bank of New York Mellon also tapped an emerging market in acquiring ARX Capital Management (AUM: $2.6 billion), a 6-year-old Brazilian manager of both hedge funds and traditional equity funds. Brazil's asset management industry has been growing by an average of 27% annually in the last five years. BNY Mellon, which has $26 billion in assets under management or administration in its Brazilian subsidiary, had been acting as administrator for ARX funds prior to the deal. Ronald O' Hanley, president and CEO of BNY Mellon Asset Management, said the deal met a "strategic objective of broadening our capabilities in the world's most important emerging markets."

European financial services firms that were buyers last year included BNP Paribas and Swiss Re. BNP Paribas, which temporarily suspended trading in three of its hedge funds during the subprime crisis, early in 2007 acquired a minority stake in Finaltis (AUM: $450 million), a Parisian hedge fund that offers multi-strategy and single strategy funds. The 6-year-old firm began as a partnership with Robeco, but management bought out the Dutch company's 25% stake in 2003. BNP Paribas also took a stake in National Bank of Canada subsidiary Innocap Investment Management, a hedge fund managed account specialist that advises more than $2 billion in mandates.

Hedge Fund Transactions

	2003	2004	2005	2006	2007
Number of Transactions	10	5	10	29	29
Combined Value ($M)	$198	$1,067	$1,390	$1,570	$8,399
Total Seller AUM ($B)	$4.2	$19.8	$36.4	$57.6	$133.0
Average Deal Size ($M)	$20	$213	$139	$54	$290
Average Seller AUM ($M)	$421	$3,960	$3,640	$1,985	$4,587

Source: Berkshire Capital Securities LLC

Amid the investment banks and asset managers, the insurance sector was represented by Swiss Re, which bought a 15% stake in one of Europe's largest hedge funds, Brevan Howard (AUM: $17 billion). Founded in 2002, the London-based firm is a global macro investor that last March floated the first individual hedge fund on the London Stock Exchange, BH Macro, a feeder fund for its $15 billion flagship global macro fund. Although the fund raised $1.1 billion, it did fall short of a $1.4 billion goal. A second flotation in October raised an additional $130 million. In 2006, two insurers, American International Group and London's Aviva made hedge fund investments.

In a teaming of two fund of hedge funds managers that follow absolute-return strategies, HFA Holdings of Australia acquired Florida's Lighthouse Partners, creating a firm with $8 billion in AUM. The $640 million cash-and-share deal (11 times 2008 EBITDA) builds upon an advisory relationship between the two companies that began in 1998 and merges HFA's retail and Lighthouse's institutional bases.

Lighthouse has recorded 20% average annual growth in AUM in recent years, and more than one-third of its assets are sourced from HFA, which had $2.7 billion in AUM. As part of the deal, Lighthouse agreed to reinvest 50% of the after-tax deal cash proceeds into its products. HFA, which began trading on the Australian Securities Exchange in 2006, touted the transaction as creating "a truly international provider and manager of absolute-return products." Lighthouse had been 25%-owned by SunTrust Banks of Atlanta.

In a second and larger fund of funds deal, BlackRock acquired Quellos Group (AUM: $20 billion) for a cash-and-stock payment of $750 million and up to $970 million in additional contingency payments through 2010, for a potential total of $1.7 billion. The combination makes BlackRock a top-10 fund of funds manager with more than $25 billion in AUM, including some private equity assets, and meets the company's goal of expanding beyond its fixed income base. Referring to the demand for "a wider array of investments and strategies," BlackRock chairman and CEO Larry Fink said the "combined expertise of BlackRock and Quellos will enhance our ability to deliver innovative solutions to our clients worldwide." Quellos, formed in 1994 and based in Seattle, will invest a "substantial portion" of the after-tax cash proceeds into BlackRock's fund of funds products.

Affiliated Managers Group, which in 2004 took a stake in noted quant firm AQR Capital Management, returned to the hedge fund sector last year to invest in ValueAct Capital, a private equity-hedge fund hybrid focusing on undervalued companies. Ordinarily, AMG acquires majority stakes in its affiliates, leaving minority ownership with managers as an incentive, but in both the AQR and ValueAct deals the company took minority stakes. Sean Healey, CEO of AMG, said ValueAct "has extremely strong new business momentum and very compelling future prospects." ValueAct has doubled its AUM to $6 billion in the last two years, while its flagship fund has returned 22% annually since 2000. The San Francisco firm has generated that performance in part by focusing on healthy companies whose stocks suffered when they failed to file financial statements on time.

Several U.K. firms made acquisitions designed to strengthen capabilities in emerging markets, which have generated some of the strongest hedge funds returns in recent years. These included British hedge fund RAB Capital, which purchased Hong Kong-based Pi Investment Management (AUM: $220 million) for as much as $26 million in cash and shares and wrapped the firm into its newly formed Hong Kong subsidiary. Founded in 2002, Pi runs long-short and absolute-return funds centered in the Asia region. In a second Asian deal, RAB took a 20% stake in its Japanese distributor, Prestige Asset Management, as part of a bid to expand in that market. RAB has cut four deals since going public in 2004, including the 2006 acquisition of Northwest Investment Management, a London-based specialist in Asian-focused absolute-return funds. In the third quarter of 2007, RAB had $7.1 billion in AUM, up 75% over the same period in 2006. Investors in the company include Lakshmi Mittal, one of the world's wealthiest individuals with holdings that include Arcelor-Mittal, the world's largest steel company.

In other deals involving U.K. firms, Threadneedle Asset Management acquired Convivo Capital Management (AUM: $480 million), an absolute-return fund specializing in emerging market debt and currencies; and Crosby Capital Partners acquired the fund of funds business of Forsyth Partners (AUM: $1.2 billion) in a distress sale. Forsyth, which had been aggressively expanding its international operations, had its license withdrawn in its home base of Dubai, due to insufficient capital. Crosby acquired 39 funds from Forsyth across a range of strategies.

As anticipated, private equity firms picked up their activity in the asset management industry, taking part in several significant deals in 2007, with TA Associates a participant in three of them.

Swiss-based wealth manager EFG International acquired PRS Group, a Miami firm with $2.5 billion in AUM in proprietary fund of funds. Geneva-based Banque Piguet & Cie held a 25% interest in PRS, which was founded in 1981 and served wealthy clients, as well as institutions. In 2006, EFG acquired hedge fund manager Capital Management Advisors of Bermuda. Another Swiss wealth manager, Julius Baer, sold a 90% stake in its U.K.-based hedge fund business to management, which subsequently changed the firm's name to Augustus Asset Management (AUM: $10 billion). Management at AAM will pay for the acquisition out of company profits. In explaining the sale, Julius Baer said AAM did not fit with its GAM alternative asset management business in the U.K., acquired in 2005. Julius Baer did retain a 10% share in AAM and a subadvisory relationship.

As anticipated, private equity firms picked up their activity in the asset management industry, taking part in several significant deals in 2007, with TA Associates a participant in three of them, including an investment in fund of hedge funds manager K2 Advisors (AUM: $5.5 billion). TA said it had been searching for an "institutional-quality fund of hedge funds to invest in for a long time" and described K2 as a "recognized pioneer in portfolio transparency and risk analytics." K2, founded in 1994 and based in Connecticut, said it will invest $100 million of the proceeds into existing and new funds.

TA also took minority stakes in London's Jupiter Investments (AUM: $41 billion) as part of the management buyout of that firm from Commerzbank, and in New York fund manager Arnhold and S. Bleichroeder Holdings (AUM: $45 billion). In the largest asset management deal ever involving a private equity firm, Madison Dearborn Partners' paid $5.8 billion for Nuveen Investments and assumed an additional $550 million in Nuveen debt (see *Mutual Funds* and *Institutional* for more information on these deals).

In Germany, there were two acquisitions of private equity firms: Sal Oppenheim's purchase of a majority stake in VCM Capital Management, (AUM: $2.7 billion), a fund of funds private equity investor in Europe; and Deutsche Bank's purchase of a minority shareholding in Aldus Equity (AUM: $3 billion). Deutsche said it planned to develop with Aldus private equity fund of funds products for institutions and private clients.

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