CAMBRIDGE INTERNATIONAL PARTNERS INC.

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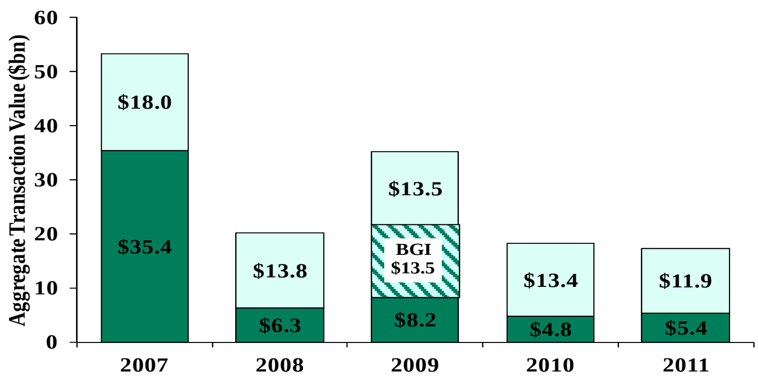
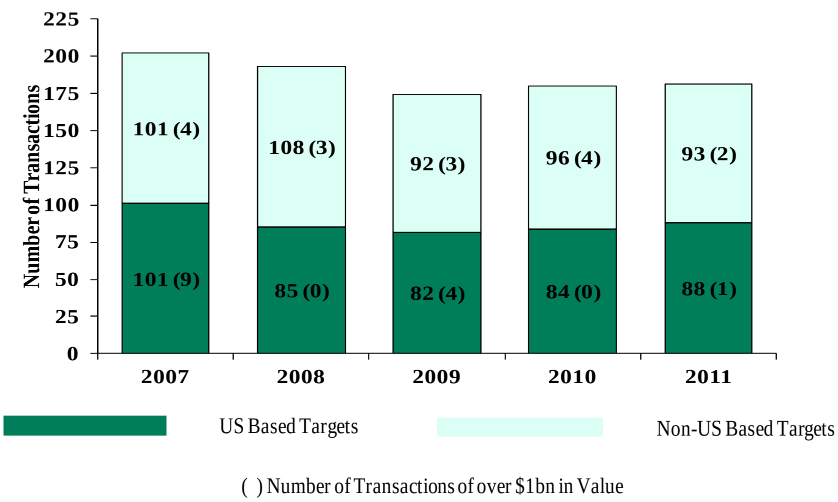
The Cambridge Commentary
A Review of Developments in the Investment Management Industry During 2011

Dear Friends:

The US economy may have continued its recovery in 2011, as evidenced by assets under management in the industry returning to 2007 peak levels, but it certainly did not *feel* as if good times had returned. In fact, the year could be better characterized as one of deep uncertainty, with unusually volatile markets held hostage by the messy and protracted political negotiation to solve the euro-zone debt crisis. As a result, despite an optimistic start, 2011 proved another challenging year in which to complete transactions. Jittery buyers and uncommitted sellers made a poor recipe for baking transactions, resulting in high failure rates and unusually long lead times. Nevertheless, the value and number of transactions in the industry for the year were substantially the same as in 2010, both in the US and globally.





**Excludes acquisitions of investment managers with less than $200 million under management or purchase of less than 10% of equity*

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Indeed, many of the themes for the year echoed those we identified in 2010:

- Non-US transaction value substantially exceeded US transaction value, with seven of the top ten transactions occurring outside the US. This was also true in 2010 when a remarkable nine of the top transactions were non-US and is in marked contrast to the boom years of 2006 and 2007 when these proportions were reversed. Of course, the financial crisis hit the US harder and earlier than the rest of the world – although that may now be changing given the continuing debt problems in Europe and economic slow-down in emerging markets.
- Five of the top ten transactions – in fact, the top five – were all divestitures from large financial institutions and three of these can be characterized as "forced sales" stemming from the financial crisis (KBC's sale of KBL European Private Bankers, the Lehman estate's sale of Neuberger Berman and ING's sale of its European and Asian real estate business). European financial institutions continue to focus on raising capital even as US institutions shift their attention to business rationalization and profit improvement.
- Regulatory uncertainty remained a significant theme with the implications of the Dodd-Frank Act and, in particular, the ban on proprietary trading by banks (the Volcker rule) still not fully understood by year end despite its imminent July implementation. From a transactional perspective, the Volcker rule is continuing to drive bank divestitures in the US and abroad, particularly of private equity, real estate and hedge fund managers, albeit at a slower rate than in 2010.
- Public companies underperformed the broader market for the second year in a row despite improvements in earnings. As a result, public company EBITDA multiples have hit lows not seen since the collapse of Lehman Brothers, presumably reflecting investor concerns over the industry's growth prospects.

However, there were also some significant differences from 2010, of which the most notable were:

- Three of the top ten transactions were unsponsored management buyouts, an unusual occurrence as support of MBOs by private equity sponsors has historically been needed for large transactions. The ability of these management teams – Neuberger Berman, Mondrian Investment Partners and BlueCrest Capital Management – to raise the debt needed is testament to improvement in the lending environment that has occurred since the credit crunch.
- The number of outward cross-border transactions, i.e. purchases of non-US based managers by US buyers, doubled in 2011 with Principal Financial Group being particularly active, making three such purchases. Inward cross-border activity did not change versus 2010, with CIBC's purchase of J.P. Morgan's 41% stake in American Century being the most significant.
- US banks bought as many managers as they sold, in marked contrast to 2010 when three times more managers were sold than acquired.
- Private wealth management transactions bounced back after a couple of down years. Not only did the sector account for two of the three largest transactions of the year but the number of US wealth manager transactions more than doubled to 34 as AUM recovery encouraged sellers to test the market.

Ten Largest Investment Management Transactions in 2011

(All amounts in US$) **Target**	**AUM ($bn)**	**% Acq'd**	**Purchaser**	**Amount Paid ($MM)**	**Strategic Rationale**
KBL European Private Bankers *Luxembourg*	62.8	100%	Precision Capital	1,440	Belgian bank, KBC Group, tries again to sell its private bank as mandated by the European Commission -- this time to a Qatari investor. A previously agreed sale to Hinduja Group at a 20% higher price was shot down by regulators earlier in the year
Neuberger Berman *New York, NY*	183.0	48%	Management	1,190	Neuberger management comes full circle by buying out the Lehman estate's $813 million of preferred stock at par and its 48% equity stake in tranches over five to seven years. Neuberger expects to issue $720 million in new debt to finance the purchase
Bank Sarasin *Basel, Switzerland*	110.5	46%	Safra Group	1,130	Safra Group takes over Rabobank's voting control position in this publicly-traded Swiss private bank, extending its reach in Europe, the Middle East and Asia and doubling its assets under management
ING Real Estate Investment Management *Amsterdam, Netherlands*	59.8	100%	CB Richard Ellis Group	940	To raise capital, ING sold the European and Asian operations of ING REIM to CBRE, creating the world's largest commercial real estate fund manager, separately selling the US component to management and Lightyear Capital
American Century Investments *Kansas City, MO*	112.0	41%	CIBC	850	By contrast to KBC and ING above, Canadian bank CIBC demonstrates its capital strength by stepping into JP Morgan's shoes in this American Century-initiated divorce after 13 years of often-frosty marriage
Hedging-Griffo *São Paulo, Brazil*	27.3	50%	Credit Suisse	800	After five years of partial ownership, Credit Suisse gets full control of one of Brazil's most important investment managers including Verde, Brazil's largest and most successful hedge fund
Mondrian Investment Partners *London, UK*	70.0	27%	Management	600e	Hellman & Friedman more than quadruples its money as it sells back to management its investment in this premier UK-based international manager that spun out from Delaware Investments in 2004
Apollo Global Management *New York, NY*	67.6	8%	Initial Public Offering	570	In the only significant industry IPO in 2011, Apollo forsakes the GSTrUE private exchange for a full listing on the NYSE alongside its private equity competitors, Blackstone, Fortress and KKR
BlueCrest Capital Management *Guernsey, UK*	25.0	26%	Management	560	Reassessing its earlier strategy of taking minority stakes in hedge fund managers after its acquisition of GLG, Man Group takes profits as it sells its ownership back to management
Gartmore Group *London, UK*	25.7	100%	Henderson Global Investors	520	Weakened by withdrawals after losing two top hedge fund managers, this recently public Hellman-backed UK manager is swallowed whole by Henderson

e = Cambridge estimate

The Other Shoe Drops in Europe

The gradual healing of financial institutions seen in 2010 was interrupted this past year with the European sovereign-debt crisis renewing capital concerns at financial institutions, especially in the euro zone. Dexia became the first victim, being rescued for the second time in three years, resulting in both its asset management and its private banking businesses being put up for sale. By the end of the year, Precision Capital, which represents a Qatari investor, had announced its purchase of 90% of Dexia's private bank following up its earlier agreement to purchase KBL European Private Bankers, a $1.4 billion transaction that was the largest in the industry in 2011. KBL's owner, the Belgian bank KBC Group, had agreed to sell the business as part of a settlement with the European Commission under the terms of government support it had received during the financial crisis. ABN Amro, which had also been rescued, sold its Swiss private bank to Union Bancaire Privée which is struggling to rebuild assets and credibility after its fund of hedge fund business, once the largest in the world, invested with Madoff.

However, the biggest European seller of investment management businesses was ING, which sold its European and Asian real estate investment management business to CBRE; its US real estate business, Clarion Partners, to management and Lightyear Capital; and its Australian investment manager to UBS. While ING's sales record may be eclipsed in 2012 by Deutsche Bank, which has put Deutsche Asset Management (excluding DWS, the German retail arm) on the block with a reported asking price of €2 billion, successful sales of bank-integrated asset management arms cannot be taken for granted given, in varying degrees, issues of product mediocrity, uncertain post-transaction distribution and nationalist political pressures. These issues were evident earlier in the year when UniCredit abandoned its year-long quest to sell Pioneer Investments.

Globalization Continues Unabated

It should come as no surprise that transactional activity acts as a lagging indicator of investor interest. A good example in 2011 was the increase in purchases of emerging market equity managers after an astonishing 100% rise in emerging market equities over the prior two years. The biggest such transaction was Credit Suisse's purchase for $796 million of the remaining 50% of Brazil's Hedging-Griffo that it did not already own. Hedging-Griffo has become the largest manager of private client assets in Brazil on the back of a 33% 14-year annualized return on its $8 billion Verde fund. Ashmore's purchase of 63% of Virginia-based Emerging Markets Management for $126 million of cash and stock and an earn-out of up to $120 million was next on the list, with Ashmore gaining diversification from its core emerging market bond franchise into equities. Another significant transaction, BMO Financial's purchase of Hong Kong-based Lloyd George Management for $87 million and an expected earn-out of $13 million, is intended to repeat the success of BMO's 2008 acquisition of London-based international equities manager, Pyrford International, whose products have since sold well in Canadian retail and private client channels. The Lloyd George transaction also marked the end of a 16-year minority investment by Eaton Vance that never lived up to expectations.

Minority transactions in emerging markets announced during the year included the sale of CITIC Securities' 51% stake in China Asset Management Co., the country's largest asset manager, in four 10-11% stakes to state-owned enterprises and one 10% stake to Power Corp of Canada, contributing $1.3 billion in aggregate value to the year's transactional activity. In the US, the principal minority investment was the purchase by private equity investor, Lovell Minnick Partners, of Bill Hambrecht's stake in Matthews International, a successful Asian specialist based in San Francisco with $19 billion under management.

Even as investor interest for emerging market equities abated during the year, asset flows were strong in global equities, global and emerging market bonds, commodities and global asset allocation funds. This has triggered buyer interest but not many transactions, mostly because there are few specialist independent managers offering these products. That said, Principal Financial Group did acquire two such businesses, both based in London: 51% of Finisterre Capital, an emerging market bond manager, and 74% of Origin Asset Management, a global and international equity manager. Another global manager, Altrinsic Global Advisors, sold a minority stake to nabInvest, the investment management arm of National Australia Bank. Connecticut-based Altrinsic, which has a 25% profit-sharing and distribution arrangement with CI Funds of Canada, already manages one-quarter of its assets for Australian clients.

Australia has been one of the fastest growing markets over the last few years, underpinned by a government-mandated retirement scheme funded at 9% of salary rising to 12% by the end of the decade. This has triggered an increasing number of transactions as foreign investment managers position themselves to take advantage of the opportunity. In 2011, both Franklin Templeton and UBS made significant Australian acquisitions, acquiring Balanced Equity Management with $11 billion under management and ING's Australian investment management subsidiary with $36 billion under management, respectively. With an eye toward gaining access to Australian investments for its Japanese clients seeking offshore investments, Mitsubishi UFJ purchased a 15% stake in the fund management subsidiary of AMP Ltd. for $436 million.

Success of the Independents

Independent investment managers have been major beneficiaries of the turmoil of the last few years. McKinsey has reported that independents' AUM share among the top 50 asset managers has grown from 28% in 2002 to 54% in 2011. Their success has been driven by faster organic growth and, more particularly, by transactional activity – both divestitures by institutions and acquisitions by independents. Affiliated Managers Group, Ameriprise Financial, BlackRock and Invesco had been at the forefront of the latter activity in 2009-2010 and, although none announced acquisitions in 2011, Ameriprise and Invesco were reported at year end to be participating in the Deutsche Asset Management sale process. The largest acquisitions by independents in 2011 were CBRE's acquisition of ING's European and Asian real estate investment management businesses and Henderson Global Investors' absorption of Gartmore Group for stock after publicly-traded Gartmore put itself up for sale following the disastrous loss of two top fund managers and the assets that they managed. Initial indications were that Henderson was able to retain 90% of the assets with just 40% of Gartmore's employees, resulting in incremental operating margins north of 50%.

Contributing to growth of the independents has been an increasing number of management buyouts, sometimes sponsored by private equity and sometimes not. Almost 20% of all transactions in the industry globally were buyouts by management, private equity or a combination of both including, as we have previously mentioned, three of the top ten. One of these was the sale back to the company by Hellman & Friedman of its 27% stake in Mondrian Investment Partners which had resulted from sponsorship of management's 2004 buyout of Delaware Investments' London-based international manager. By all accounts, this was a very profitable investment for Hellman & Friedman which has developed a well-earned reputation in the industry. Even its Gartmore investment could be considered successful as the equity that Hellman had provided to management for the 2006 buyout from Nationwide was repaid from the IPO proceeds, leaving the 4.6% of Henderson that it retains as profit.

Mixed Reviews for Alternatives

Acquisition interest in alternative managers remained relatively strong in 2011, continuing a multi-year positive trend as investment managers look for ways to broaden their product suite. Given the perceived future growth opportunities for alternative managers from increased institutional allocations as well as enhanced distribution opportunities in Europe and Asia through UCITS III offerings, we expect strategic interest in this category to continue despite redemptions by high net worth investors disappointed by lackluster returns.

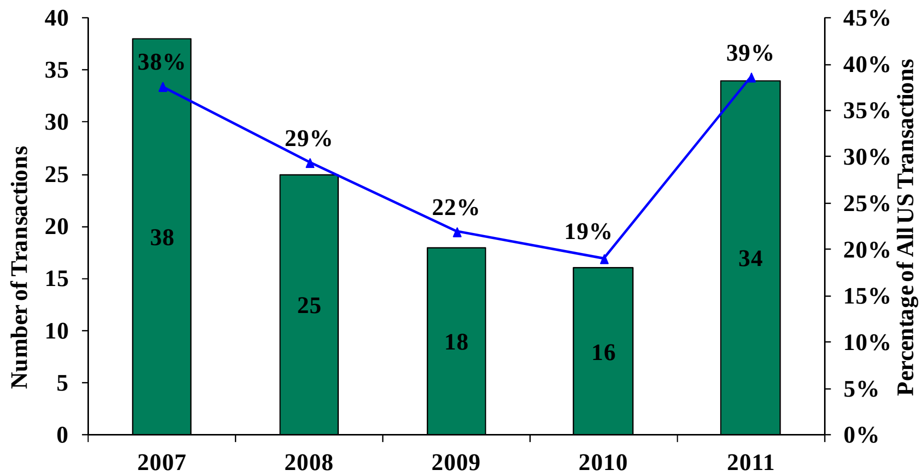
Even so, the overall number of transactions in this segment of the market declined to 56 from 80 in the prior year, primarily due to a spike in the number of Dodd-Frank driven bank divestitures during 2010. From a strategic perspective, competition between private equity groups to consolidate overcapacity of CLO/CDO managers remained an important theme with Blackstone, Apollo and Carlyle all making additional acquisitions. Carlyle was a particularly aggressive acquirer generally and, excluding fund-level investments, purchased three investment management businesses during the year including AlpInvest, a global fund of private equity funds manager, and Emerging Sovereign Group, a hedge fund manager focused on emerging markets and macroeconomic strategies. Carlyle has filed with the SEC for its initial public offering and product diversification is an important part of its selling proposition. Oaktree Capital Management also filed with the SEC, but neither group has priced its IPO in what has been a very challenging public market for investment managers. As a group, publicly traded alternative managers were down 16% in 2011, slightly worse than their more traditional peers. The only alternative manager to go public in 2011, Apollo, suffered a share price decline of 35% from its March 29th IPO date.

Fund of funds transactions represented about 20% of alternative activity as financial institutions and investment firms sought out this expertise in response to product demand from their clients. Evercore's acquisition of a significant minority stake in ABS Investment Management, a $3.5 billion specialist global equity fund of hedge fund manager, was driven by precisely this objective. The search for scale prompted a number of other deals as size has become an increasingly important determinant of success in gathering new assets, as exemplified by Nexar's acquisition of London-based Ermitage less than a year after its acquisition of Allianz's fund of hedge fund business in Paris.

US Wealth Management Transactions Bounce Back

Private wealth managers returned to the forefront in 2011, accounting for 39% of all US investment management transactions. After three years in decline, interest picked up dramatically in 2011 with 34 wealth management deals – in line with the 2007 peak. Much of the rebound in activity can be attributed to the return of independent RIA assets under management to 2007 levels. With pressure to sell proportionate to retirement proximity, improvements in revenue and profitability in 2009 and 2010 have raised valuations and opened an exit window for founders despite market multiples that remain lower than in 2007.

US Wealth Management Transactions*



**RIAs serving high net worth clients, excluding brokers and investment consultants*

The uptick can be partly explained by the return of the bank buyer. Banks and trust companies as a group acquired nine managers during the year compared to just three in 2010. M&T, which sold Zirkin-Cutler to United Capital, and Boston Private, which sold its stake in Coldstream Capital to management, both continue to rationalize their wealth management businesses while SunTrust and BNY Mellon both expanded through niche acquisitions. SunTrust acquired CSI Capital Management, with $1.5 billion under management, providing meaningful scale to its Sports and Entertainment Specialty Group with three new wealth management offices. Meanwhile, BNY Mellon, after several years of searching, found a beachhead from which to challenge Northern Trust's dominance in Chicago, acquiring Talon Asset Management's wealth management business.

The combination of returning sellers and lower multiples proved a boon for financial holding companies whose access to capital has improved significantly in the last two years. Private equity-backed Focus Financial Partners was the most active group, claiming eight lift-outs and/or acquisitions of financial planners, brokers and RIAs during the year. These acquisitions increased assets under management to $45 billion, a remarkable total considering the firm made its first acquisition just two years before the 2008 financial crisis. No doubt an IPO can be expected here as soon as the public markets become more receptive. Perhaps this success accounts in part for the announcement by Affiliated Managers Group that, after years of reluctance, it will now actively participate in this segment of the market by forming AMG Wealth Partners, although no transactions have yet been announced.

Outlook for 2012

With the euro-zone debt crisis continuing to play out in slow motion, possibly for months to come, and with ominous rumblings of a slowing economy in China and emerging markets, the question for the US is whether these developments will undermine a recovery that is looking stronger now than it has for many months. The 11% rise in the S&P 500 in the last three months of the year suggests optimism that the US can decouple itself from problems in the rest of the world but the level of uncertainty remains very high. This is not helped by the US political impasse on deficit reduction and attempts to legislate reform of financial services. Until this uncertainty abates, managers' business focus will remain short term – and acquisitions, an activity requiring a much longer time horizon, will remain on the back burner.

Nevertheless, areas of strength are emerging, particularly in the US. Groups with global aspirations will continue to pursue product and distribution expansion. Consolidation and margin improvement will remain an important focus for mutual funds and wealth management, marrying divestitures of sub-scale and non-core businesses with serial acquisitions by surviving independents. Private wealth management, a highly fragmented marketplace, also has a natural rate of transactional activity stemming from the aging of founders interested in an exit. While this rate may have been depressed for a few years by the financial crisis, 2011 proved that this was activity deferred, not cancelled. Meanwhile, in Europe, the pace of divestitures looks set to continue or even accelerate as financial institutions struggle to raise capital by selling non-core assets.

Against this backdrop, we at Cambridge are approaching 2012 with cautious optimism. A steadily improving US economy has the potential to bring back a much needed sense of confidence to buyers and sellers which in turn will be reflected in more and larger transactions and in firming valuations.

In a milestone for us, Paul Holt, who founded Cambridge 23 years ago, has retired from day-to-day involvement in client assignments while retaining his position as Chairman. We are confident that many of you, who have benefited from his thoughtful advice and friendship over the years, will join us in wishing Paul and his wife, Linda, every happiness in retirement.

Sincerely,

John H. Temple | David W. Abbott | Richard H. Haywood, Jr.