

THE INTERNATIONAL NEWSPAPER OF MONEY MANAGEMENT

Investing

Market optimism reigns in outlook for new year

Many predict rebound for S&P 500, though 1 says recession is likely

By **Barry B. Burr**

Many institutional investment strategists believe the S&P 500 generally will return more than 10% in 2012, even though they expect the U.S. economic growth rate to be slow

and unemployment to remain high.

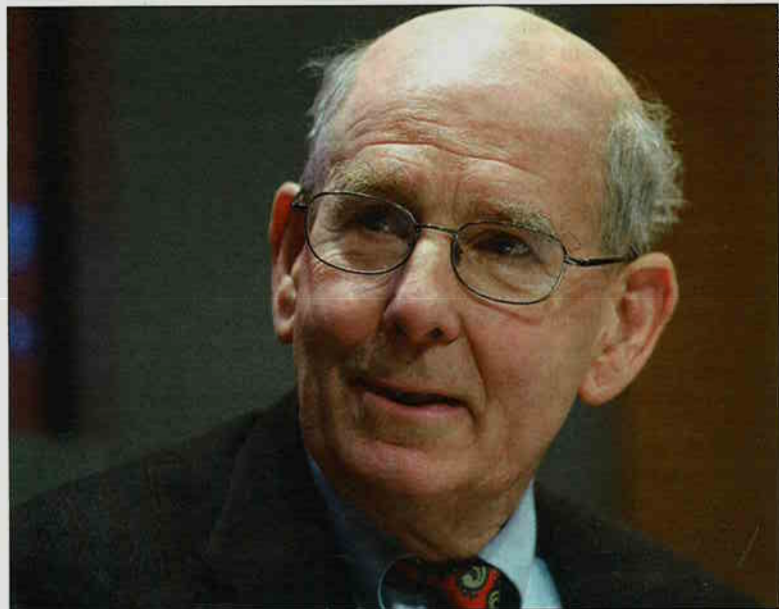
At least one strategist sees a recession coming, while two others predict an increase up to 20% for the benchmark index.

"Fundamentals will overtake fear" in 2012, predicted James W. Paulsen, chief investment strategist, Wells Capital Management Inc., Minneapolis. Mr. Paulsen sees a strong performance for U.S. equities, though "the irony is we could have a pretty bloody bond market."

A. Gary Shilling, president and economist of an eponymous economic consulting and investment advisory firm based in Springfield, N.J., forecasts a "mild to moderate" U.S. recession for the year. He is bearish on stock and bullish on Treasury bonds.

Globally, the strategists were generally optimistic about Asia and emerging markets equities, but see Europe's prospects as weak.

{ See **OUTLOOK** on page 24 }



FALLING: A. Gary Shilling sees a 'mild to moderate' recession for the U.S. economy.

At Deadline

2 announce contributions

Two corporations — Avery Dennison Corp. and Sutter Health — announced contributions to their pension funds.

Avery Dennison officials will use some of the proceeds of the \$550 million cash sale of its office and consumer products business to 3M Co. to make additional contributions to its defined benefit pension plan, confirmed spokesman David Frail.

Mr. Frail said additional information on the contributions is expected to be announced upon the release of the firm's fourth-quarter earnings statement on Feb. 2.

The firm reported assets of \$540 million in its U.S. pension plan and \$744.8 million in projected benefit obligations as of Dec. 31, 2010, according to its latest 10-K filing.

Sutter Health contributed \$400 million to the company's defined benefit pension plan, according to a news release. The company made the contribution last month.

The fair value of assets in the Sutter Health Retirement Plan was \$1.98 billion, with a funded status of 109.4% as of Dec. 31, 2010, the most recent data available.

Shell to close U.K. plan

Royal Dutch Shell will close its £12.4 billion (\$19.3 billion) U.K. defined benefit pension plan to new

Continued on page 22



Private Equity

The undead live, and they're draining investors' purses

By **Arleen Jacobius**

Deep inside most private equity portfolios lurk funds that have little hope of turning a profit, yet they still feed on the resources of institutional investors — and there's not much investors can do about it. They're called "zombie funds"

and they're a dirty little secret of private equity investors and consultants, dwelling in the bottom quartile of private equity portfolios.

In a recent survey by Collier Capital Inc., London, a private equity firm that invests in the secondary market, two-thirds of investors worldwide indicated they have

zombie funds, the informal term used for funds that are practically dead but still charging fees until their lives expire. These funds have little hope of making money, or have made money but still have one or two holdings that can't be sold.

Industry experts estimate as much as \$100 billion of the roughly

\$2.4 trillion in private equity could be invested in zombie funds.

And these funds are multiplying. Already, a number of venture capital funds raised in 1999 and 2000, especially those formed to invest in Internet-related companies, can be classified as zombie funds. And in

{ See **ZOMBIE** on page 22 }

SPECIAL REPORT MONEY MANAGER M&A

Spurned suitors the norm in 2011

Economic zigzags make year a poor one for deals

By **Randy Diamond**

Merger-and-acquisition activity in the money management industry last year was more about broken engagements than successful marriages.

Volatile financial markets hampered deal-making in the industry, leading to another year of depressed activity.

Freeman & Co. LLC, the New York based M&A advisory and strategic management consulting firm, dubbed its annual report on asset management industry deals, "The Year that Wasn't."

Worldwide, 181 money

{ See **BROKEN** on page 11 }

INSIDE

» 2

UBS' FRANCOIS PELLERIN: Pension funding volatility is "the equivalent of going to Las Vegas and playing roulette — one month you're lucky and one month you're not."



Now on POnline.com/features

Engaging participants:

Proactive strategies can boost 401(k) participation of non-native English speakers. Employers have found success with automatic enrollment and culturally sensitive communications as a means to increasing their participation rates among employees who speak English as a second language.

Era of dissonance:

Financial markets entered an "era of dissonance" that will stand in sharp contrast to the harmony and economic expansion of the last half of the 20th century, writes Bluford H. Putnam, CME chief economist.

Ask the Expert: Dave Eager offers advice to a manager thinking of re-



sponding to an RFP from a former client, who terminated his firm.

Chart Central:

- Among the charts at pionline.com/charts:
- S&P 500 index forecast to increase an average of 6% in 2012
- Dividend increases rise 89% in 2011
- DoubleLine's flagship bond fund returns more than double TCW's in 2011

MONEY MANAGER M&A

Broken

Continued from page 1

manager M&A deals were announced in 2011, with a total transaction value of \$17.3 billion. That's one more deal than in 2010 but less than that year's \$18.2 billion total transaction value, according to a report by New York-based investment bank Cambridge International Partners Inc.

The problem: a less-than-rosy economic environment meant buyers weren't willing to meet the price demands of sellers, said Eric Weber, a managing director at Freeman & Co.

"Buyers were being stingy," Mr. Weber said.

Whether 2012 will be a better year largely will depend on whether the economy stabilizes and spurs new transactions, according to M&A specialists.

One continuing trend that could create new activity, even without economic improvement, they noted, is banks being forced to divest money management units to raise cash and meet tighter regulatory constraints. In fact, one potential deal in 2012 could be bigger than any of the transactions in 2011 in terms of deal value. Deutsche Bank Group is shopping its Deutsche Asset Management unit, with \$730 billion in assets under management, and has set a price tag of around \$2 billion.

2011 started out with markets per-

forming well, fueling hopes that it would be a strong year for M&A activity.

It didn't turn out that way.

Up slightly

U.S. deals and transaction totals in 2011 were up slightly from the previous year, but international activity was down, according to the Cambridge report.

The report found 88 announced deals involving the acquisition of U.S.-based money managers in 2011, with an aggregate transactional value of \$5.4 billion. That compared with 84 deals and \$4.8 billion in 2010. Deals involving the acquisition of non-U.S. asset managers in 2011 totaled 93 compared with 96 in 2010. The transactional value of those deals amounted to \$11.9 billion in 2011, down from \$13.4 billion a year earlier. (The Cambridge report includes only transactions in which money management operations account for more than 50% of an acquired firm's revenue.)

Seven of the top 10 money manager transactions in 2011 were outside the U.S., the Cambridge report noted.

It was also the second year in a row Cambridge noted that the aggregate transactional value of non-U.S. deals was more than double those of U.S. transactions.

The market turmoil for the last six months of 2011 was a dominant theme, as behind-the-scenes negotiations to build deals fell apart before they got to the announcement stage, said John Temple, a Cambridge managing direc-



"Jittery buyers and uncommitted sellers made a poor recipe for baking transactions."

CAMBRIDGE INTERNATIONAL PARTNERS' JOHN TEMPLE

tor in New York.

"The failure rate was high," he said.

The "messy and protracted political negotiations to solve the eurozone debt crisis" dragged on for the second

half of 2011, making dealmakers wary, he added.

"Jittery buyers and uncommitted sellers made a poor recipe for baking transactions," Mr. Temple said.

It's hard to value a money manager when the markets swing so suddenly and so dramatically, he said.

"There is a lack of confidence in the marketplace," he said. "Buyers and sellers don't know if the markets will rise 10% or plunge 10%."

Sam Yildirim, M&A lead partner for PricewaterhouseCoopers LLP New York, said the desire for M&A remained high globally for 2011 because achieving organic growth has been difficult for money management firms due to increased competition for assets, volatile asset values, investor pressure for lower fees and higher compliance costs.

But despite that demand, many deals were not completed because of valuation disagreements, Ms. Yildirim said.

Before the financial crisis, she said, asset manager sales ranged from a low of 10 to 11 times earnings before interest, taxes, depreciation and amortization to a high of 15 EBIDTA. More recently, sales have been around seven to eight times EBIDTA, a reality that some sellers have not been willing to accept, she said.

"There is a huge gap between buyers and sellers," Ms. Yildirim said.

Still, deals announced in 2011 were bigger in terms of assets under management than in 2010. Freeman estimates

{ See **BROKEN** on page 12 }

The largest investment management transactions in 2011

All amounts are in U.S. millions.

Acquired	Acquired assets	% acquired	Acquirer	Transaction value	Strategic rationale
KBL European Private Bankers	\$62,800	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	\$183,000	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	\$110,500	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	\$59,800	100%	CBRE 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 U.S. component to management and Lightyear Capital.
American Century Investments	\$112,000	41%	CIBC	\$850	By contrast to KBC and ING above, Canadian bank CIBC demonstrates its capital strength by stepping into J.P. Morgan Chase's shoes in this American Century-initiated divorce after 13 years of often-frosty marriage.
Hedging-Griffo	\$27,300	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	\$70,000	27%	Management	\$600*	Hellman & Friedman more than quadruples its money as it sells back to management its investment in this premier U.K.-based international manager that spun out from Delaware Investments in 2004.
Apollo Global Management	\$67,600	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	\$25,000	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	\$25,700	100%	Henderson Global Investors	\$520	Weakened by withdrawals after losing two top hedge fund managers, this recently public Hellman & Friedman-backed U.K. manager is swallowed whole by Henderson.

*Estimate. Source: Cambridge International Partners Inc.

MONEY MANAGER M&A

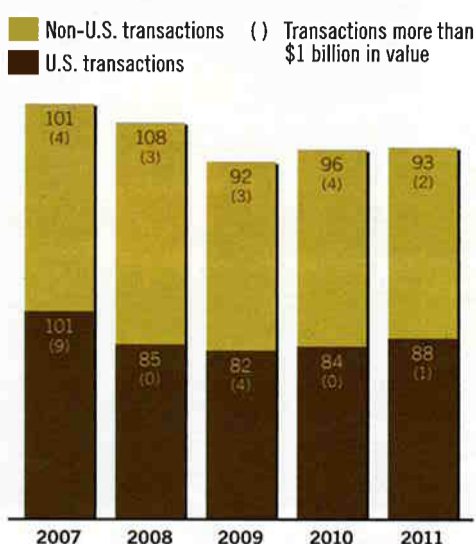
Global investment management M&A scorecard

Excludes acquisitions of investment managers with less than \$200 million under management or purchases of less than 10% of equity. Dollar amounts are in U.S. billions.

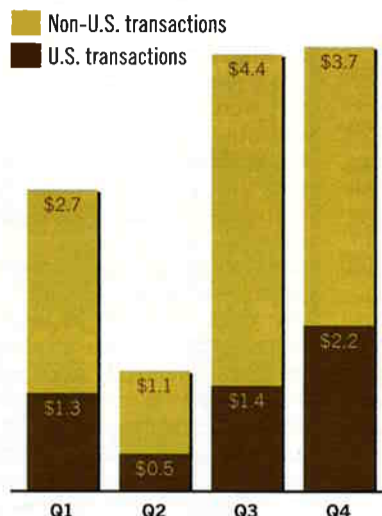
Transaction value by year



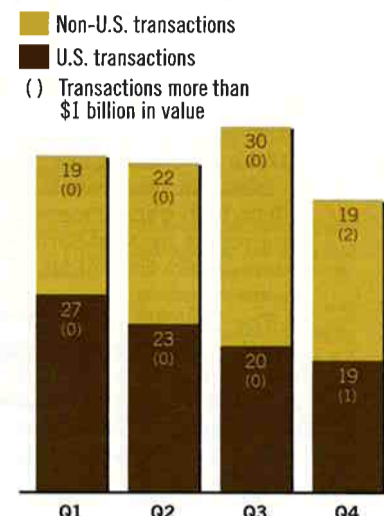
Number of transactions by year



Transaction value by quarter in 2011



Number of transactions by quarter in 2011



Source: Cambridge International Partners Inc.

Broken

Continued from page 11

total AUM value of 2011 deals will

be around \$829 billion, up 20% from 2010's \$691 billion.

Those numbers are still far below \$4.7 trillion in 2009, the year BlackRock Inc. acquired Barclays Global Investors, or even 2008, when the total AUM involved in

M&A was \$1.673 trillion.

5 largest transactions

The five largest announced transactions in terms of deal value according to Cambridge, were all divestitures from large financial

institutions:

- the \$1.4 billion purchase by Precision Capital of KBL European Private Bankers SA, the private banking arm of KBC Group;

- the \$1.19 billion management buyout of the Neuberger Berman Group from Lehman Brothers Holdings;

- Safra Group's \$1 billion acquisition of the controlling stake in Bank Sarasin & Co. Ltd. from Rabobank Group;

- CBRE Group Inc.'s \$940 million purchase of ING Real Estate Investment Management; and

- Canadian Imperial Bank of Commerce's \$850 million purchase of a 41% interest in American Century Investments from J.P. Morgan Chase & Co.

Three of the five — KBL, Neuberger Berman and ING Real Estate — also could be characterized as forced sales stemming from the financial crisis, Mr. Temple said.

Belgian bank KBC Group had been trying to sell KBL European Private Bankers for two years as part

of a restructuring plan mandated by the European Commission in exchange for government aid to shore up its assets. A deal announced in 2010 to sell the unit to Mumbai, India-based Hinduja Group fell apart in March 2011 when it did not receive regulatory approval.

The sale of Neuberger Berman stems from the Lehman Brothers bankruptcy in September 2008 and ING Group sold its global real estate businesses, including ING Real Estate, as part of the firm's broader restructuring plan following a Dutch government bailout during the financial crisis of 2008.

Mr. Temple said one significant difference in 2011 from the previous year was that three of the top 10 deals involved management buyouts, but without funding from private equity partners.

He said the ability of the management teams to raise debt to complete the three deals — Neuberger Berman; London-based Mondrian Investments Partners Ltd.'s \$775.9 million buyback of a 27% stake held by private equity firm Hellman & Friedman; and London-based Blue-Crest Capital Management LLP's buyback of Man Group PLC's 26% interest in the firm for \$633 million — was indicative of an improvement in the lending environment since the credit crunch.

Whether 2012 will be different from 2011 is unclear.

Freeman's Mr. Weber said more activity could occur if European banks remain under pressure to raise capital. One example is Paris-based Societe Generale SA, and its subsidiaries TCW Group Inc. and Lyxor Asset Management.

Another possible deal, he said, involves Dexia SA, the French-Belgian banking group, which is seeking buyers for some of its operations — including its Dexia Asset Management unit — after government bailouts.

Cambridge's Mr. Temple said that ultimately, more confidence is needed in the economic outlook for the stock market to rise on a longer-term basis, creating the foundation for more M&A activity.

While the U.S. economy has shown some resilience, Europe's sovereign debt crisis still remains a problem as well as slower growth in China and other emerging markets.

"The question is how it all balances out," he said.



"OK, OK. We'll get the P&I Daily license."

Give your people a P&I Daily License and help everyone at your firm keep up with the pulse of the industry.

For one low annual fee, you get:

P&I Daily, the industry's best newsletter. It gives you the breaking news of the money management business, including up to the minute search and hire activity.

Written by the same team that writes and edits *Pensions & Investments*, it brings you reporting that is timely, accurate and impactful. And it brings it right to your desktop or PDA at 4:30 p.m. ET, Monday - Friday.

You also get access to the *Pensions & Investments* website which includes:

- P&I and P&I Daily current and back issue content
- *Pensions & Investments* and P&I Daily searchable article archives
- Latest news articles

A P&I Daily License will provide you, and all of your colleagues, with the industry's most sought after competitive intelligence. Untie yourself and contact Paul Margolis at 212-210-0244 or pmargolis@pionline.com

Pensions&Investments
www.pionline.com

Reprints

- 2-color, 4-color
- Glossy, matte
- 500-1,000,000
- One-sided, two-sided booklet

It's your choice.

Contact Laura Picariello
(732) 723-0569
lpicariello@crain.com

Pensions&Investments