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EDITED TRANSCRIPT

AMG - Q2 2017 Affiliated Managers Group Inc Earnings Call

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OVERVIEW:

AMG reported 2Q17 aggregate revenue of $1.2b, economic net income of $188.7m and economic EPS of $3.33.

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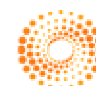

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PRESENTATION

Operator

Greetings, and welcome to the AMG Second Quarter 2017 Earnings Call. (Operator Instructions) As a reminder, this conference is being recorded.

I would now like to turn the conference over to your host, Ms. Selene Oh, Vice President, Investor Relations for AMG. Thank you. You may begin.

Selene Oh

Thank you for joining AMG to discuss our results for the second quarter of 2017. In this conference call, certain matters discussed will constitute forward-looking statements. Actual results could differ materially from those projected due to a number of factors, including, but not limited to, those referenced in the company's Form 10-K and other filings we make with the SEC from time to time. We assume no obligation to update any forward-looking statements made during the call.

AMG will provide, on the Investor Relations section of its website at www.amg.com, a replay of the call and a copy of our announcement of our results for the quarter, as well as a reconciliation of any non-GAAP financial measures to the most directly comparable GAAP financial measures, including a reconciliation of any estimates of the company's Economic earnings per share for future periods that are announced on this call.

With us on the line to discuss the company's results for the quarter are Sean Healey, Chairman and Chief Executive Officer; Nate Dalton, President and Chief Operating Officer; and Jay Horgen, Chief Financial Officer.

With that, I'll turn the call over to Sean Healey.

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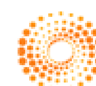

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Sean Michael Healey - *Affiliated Managers Group, Inc. - Chairman and CEO*

Thanks Selene, and good morning everyone. AMG reported strong results for the second quarter, including Economic earnings per share of $3.33, and record assets under management of $772 billion, a 19% increase over the year-ago quarter.

Our results reflect ongoing momentum across all aspects of our business, including the continued excellent investment performance of our Affiliates, positive organic growth from net flows, and the impact of new Affiliate partnerships.

During the quarter, our Affiliates generated positive net client cash flows of $1.8 billion, with strong new business momentum across a broad array of global equity and alternative strategies, partially offset by net outflows in U.S. equities.

Looking ahead, we see increasing demand for our global and emerging market equity products, as well as for our diverse set of alternative strategies. Our track record of positive organic growth for each of the past five years reflects the consistently strong investment performance generated by our Affiliates across a wide range of attractive alpha-oriented product areas.

Against the backdrop of rising global equity markets, our long-only equity Affiliates continue to generate excellent investment performance, especially in global and emerging markets equities. Given improving underlying fundamentals in many non-U.S. markets, we see ongoing opportunities for growth in these product areas. Separately, while the returns of most alternative strategies in the industry did not match the recent gains in the equity markets, as Nate will describe, across a broad set of alternative products, our Affiliates continue to generate strong performance in their respective strategies.

Focusing on alternatives for a moment, we believe that AMG's wide array of liquid and illiquid alternative strategies, many of which are uncorrelated with equity markets, both enhances the balance and stability of AMG's earnings stream while also positioning us ahead of strong and enduring client demand trends. Clients recognize the competitive advantages that focused boutique managers have in generating excess returns, especially in alternative strategies, but are also increasingly concentrating their alpha-oriented relationships with a more limited number of managers offering the highest-quality specialized products.

With one of the largest and most diverse sets of alternative products in the industry, managed by leading Affiliates such as AQR, ValueAct, BlueMountain, Winton, Capula, Pantheon, EIG, and Baring Private Equity Asia, AMG is well-positioned to continue to generate strong organic growth from our liquid and illiquid alternative products.

AMG's global distribution strategy provides global investors with access to best-in-class boutique firms in alpha-oriented product areas with attractive secular growth opportunities -- combined with the scale, resources, and risk management of a global asset management partner with in-market client service and a single point of contact. Our strategy allows us toleverage our scale on behalf of our Affiliates in areas where scale is a benefit, but importantly, AMG's partnership approach protects the unique investment culture of each individual Affiliate and the close alignment of client interests. We believe that this combination of scale and breadth of product, together with excellent alpha generation by focused specialist managers, offers unique advantages. Together with our Affiliates, we are increasingly building strategic relationships, spanning multiple Affiliates and asset classes, with the largest institutional clients and intermediaries around the world, and we believe this represents a tremendous opportunity for future growth.

Finally, given the growing scale of our business, our strong recurring free cash flow is an increasing source of shareholder value. We continue to have an outstanding opportunity to add excellent new Affiliates, further enhancing the diversity of our Affiliate group and product offering. With our unmatched competitive position and track record as the partner of choice to leading boutique firms over the past two-and-a-half decades, we are confident in our ability to execute on our substantial forward opportunity set and generate meaningful incremental earnings growth through accretive new Affiliate investments. In addition, we also remain committed to consistently returning capital to our shareholders through our quarterly cash dividend, which we initiated earlier in the year, as well as through share repurchases. Looking ahead, we are well-positioned to continue to enhance in scale, diversity, and earnings power of our business and build long-term shareholder value.

With that, I will turn it to Nate to discuss our Affiliates' results in more detail.

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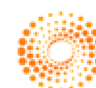

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Nathaniel Dalton - *Affiliated Managers Group, Inc. - President and COO*

Thanks, and good morning, everyone. As Sean said, we generated good organic growth in the second quarter and our Affiliates continue to extend their excellent investment performance and track records across a broad range of alternative and traditional active equity products, especially in global and emerging markets.

I'll cover performance in more detail in a moment, but first let me review a couple of themes in the quarter that we believe will continue to endure.

First, alternatives continue to experience very good demand and sales activity across most strategies and client types. Second, within traditional active equity categories, we see continued demand for global, international and emerging markets equity strategies, offset by ongoing weakness in U.S. equities. Obviously, these trends align very well with our overall strategic positioning and focus.

In general, we were pleased with our net client cash flows for the quarter, despite a handful of items I'll highlight in a bit that masked even better underlying flow trends. Looking ahead, we see the potential for significant future organic growth across our business given the combination of our strategic positioning and the strength of our Affiliates' track records in these areas.

Now, turning to the details for the quarter. As a reminder, our product categories include alternatives; global equities, including both developed and emerging markets; U.S. equities; and multi-asset and other strategies. In addition, we will continue to discuss our alternative products at the subcategory level to dimension underlying return and flow dynamics that are lost at the aggregate level.

Starting with our alternative strategies, which account for 38% of our business by assets. Within private equity and real assets, our Affiliates, including Baring Asia, EIG, and Pantheon, continue to maintain good long-term track records across their flagship offerings. As we enter a significant capital raising cycle starting in the third quarter, these historical investment returns, combined with very strong underlying demand for many of their strategies, will drive organic growth for these firms for the coming quarters. In addition, these firms are working to enhance and broaden their product set, which over time will produce additional significant growth opportunities.

In fixed income and equity-relative value, major indices posted positive returns in the quarter, as indicated by the HFRI Relative Value Index with a 0.5% return, the HFRI Equity Hedge Index with a 2.1% return, and the HFRI Event Driven Activist Index with a 2.6% return. Performance across our Affiliates was generally good on an absolute basis, but a bit more mixed on a relative basis. Our largest products in this area, including at AQR, BlueMountain, Capula and ValueAct, continue to maintain excellent longer-term relative performance records.

Within our multi-strategy and other category, most indices were slightly positive for the quarter, as indicated by the HFRI Fund Weighted Composite return of 1.1%. Against that backdrop, most of our Affiliates' strategies generated good, absolute and relative returns in the quarter. The majority of AQR's and all of First Quadrant's largest strategies in the category, including multi-asset style premia, tactical currency, and risk parity strategies, produced solid positive returns benefiting from continued broad portfolio positioning in the quarter.

In our systematic diversified category, the Soc Gen Trend Index fell by 5.0%, as mostly flat to positive performance across the industry turned negative for the quarter as trends reversed during the last week of June. Against that backdrop, each of our largest systematic diversified strategies outperformed the Index albeit posting negative absolute returns for the quarter. In addition, these Affiliates have a number of other diversifying strategies within the category that performed very well and are beginning to gain traction.

Turning to flows in our alternatives category in the quarter. We continued to produce good organic growth in this area with $4.8 billion of net inflows. This was supported by a pickup in institutional sales and continued solid retail sales.

Looking at the quarter on a sub-category basis, we saw good flows in both the fixed income and equity-relative value as well as the multi-strategy and other subcategories, notwithstanding the meaningful return of capital by ValueAct in the period. Net flows across our private equity and more illiquid product set were only slightly positive in the quarter, but as I mentioned earlier, we are entering a period of more meaningful fundraising across this product set starting in the third quarter of this year.

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Finally, we had a challenging net flow quarter in the systematic diversified sub-category as weak performance against strong traditional market betas in recent quarters resulted in some redemption activity. That said, sophisticated institutional and retail platform investors continue to believe these return streams represent an important, diversifying allocation in portfolios as they provide uncorrelated returns and they have the potential to perform very well in a strongly negative trending markets.

Moving to our global equities category, which accounts for approximately 35% of our business by assets. It was a strong quarter for global developed markets with the MSCI World Index returning 4.2%. Our Affiliates generated excellent results in the quarter as well, with the flagship strategies from AQR, Harding Loevner, TimesSquare, Trilogy, Tweedy, Browne, and Veritas all outperforming their benchmarks.

Emerging market indices also posted strong returns with the benchmark MSCI Emerging Markets Index up 6.4% in the quarter. Among our Affiliates, the flagship products at AQR, Harding Loevner, and Trilogy outpaced this index, while Genesis lagged for the quarter but still maintains a very good long-term track record.

Within global equities, we had $200 million in net inflows as sales activity improved across each of our client types. Looking ahead, AMG's largest Affiliates: AQR, Artemis, Genesis, Harding Loevner, Tweedy, Browne, and Veritas, all continue to maintain excellent long-term track records. In addition, a number of other Affiliates have been building their global investment capabilities with excellent products that are gaining traction.

Turning next to U.S. equities, which accounts for 14% of our business by assets, market performance was positive and large cap and growth stocks continue to outpace small and value stocks. For the quarter, the S&P 500 returned 3.1%while the Russell 2000 Index returned 2.5%. Our performance was particularly strong in less efficient areas of the market, such as small caps, an area where several of our Affiliates, including GW&K, River Road, and TimesSquare, all outperformed. On the large-cap side, Yacktman's flagship had underperformed this last quarter, but has an outstanding long-term track record. Within U.S. equities, we saw $3.2 billion in net outflows, in-line with industry-wide trends, but overall, even including a significant one-off institutional redemption, we saw continued improvement relative to recent quarters. While there is a continued move towards formulaic exposures for the U.S. equity portion of portfolios, we believe true alpha-oriented U.S. equity managers will continue to produce excess return, which in turn will drive client demand, especially following the next period of significant volatility.

Finally, turning to our multi-asset and other category, which accounts for 13% of our business by assets and encompasses multi-asset and balanced mandates at our wealth management Affiliates as well as a number of specialty fixed income and multi-asset products. In the category, we produced net inflows of $55 million, and we continue to see good sales activity, especially for high-net-worth investors. Performance for most of the products in this category remains good versus our peers and the customized portfolios of our wealth management Affiliates continue to gain traction in a very diverse set of ultra-high-net-worth clients.

While the broader investment management landscape faces a number of challenges, we believe that the business we have built is very well positioned. Together with our Affiliates, we are one of the largest providers of alpha-oriented alternative and active global and emerging markets equities strategies in the world. The combination of focused excellence by our Affiliates and the scope and scale of a global asset manager provides us with a number of significant opportunities to continue to improve how we together meet the evolving needs of clients. As we do that, we will continue to both enhance our position as the partner of choice to the best boutiques in the world and drive significant organic growth across our Affiliate group.

And with that, let me turn it over to Jay to discuss our financials.

Jay C. Horgen - *Affiliated Managers Group, Inc. - CFO and Treasurer*

Thank you, Nate. As Sean discussed, our second quarter results reflect a substantial increase in the earnings power of our business as we ended the quarter with record assets under management of $772 billion, reflecting strong organic growth from positive net client cash flows and markets as well as the impact of our 2016 New Investments. As you saw in the release, we reported Economic earnings per share of $3.33 for the second quarter, which included net performance fees of $0.13. On a GAAP basis, we reported earnings per share of $2.22.

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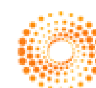

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Turning to our performance metrics. For the second quarter, Aggregate revenue, which is the sum of our GAAP revenue and our equity method revenue, grew 23% to $1.2 billion from a year ago, driven primarily by strong markets and organic growth in alternatives together with the full effect of our 2016 New Investments. The ratio of Aggregate revenue to average assets under management increased year-over-year from 62 basis points to 64 basis points, reflecting slightly higher performance fees. Excluding performance fees, we also saw a modest increase in our ratio as the mix shifted to higher-fee alternative products from net flows and the addition of New Investments. Adjusted EBITDA grew 16% to $254.8 million from a year ago, reflecting the mix between consolidated and equity method Affiliates. Economic net income grew 13% to $188.7 million from a year ago, reflecting strong growth in adjusted EBITDA, offset by a higher cash tax rate in the quarter. Finally, Economic earnings per share increased to $3.33 from $3.07 a year ago, which includes a modest increase in share count.

Turning to more specific modeling items. For the second quarter, the ratio of Adjusted EBITDA to average assets under management was 13.3 basis points, or 12.6 basis points excluding performance fees. In the third quarter, we expect this ratio to be approximately 12.7 basis points, reflecting a more modest level of performance fees in the range of $0.01 to $0.03 per share, which is typical in the third quarter.

With regard to our taxes, our effective GAAP tax rate was 32.5%, and our cash tax rate was 22.2% in the second quarter. Going forward, for modeling purposes, we expect our GAAP tax rate to be approximately 33% and our cash tax rate to be approximately 21%.

Intangible-related deferred taxes for the second quarter were $19.1 million. In the third quarter, we expect this number to increase to $21 million. Our share of reported amortization for the second quarter was $40.9 million, which includes $24 million of amortization from Affiliates accounted for under the equity method. For the third quarter, we expect our share of amortization to remain at approximately $41 million.

Our share of interest expense for the second quarter was $22.4 million. In the third quarter, we expect our share of interest expense to decrease to approximately $21 million, which reflects the retirement of our senior bond in August.

Other economic items for the second quarter were $2.4 million. For modeling purposes, we expect other economic items to be approximately $1 million per quarter.

Our adjusted weighted average share count for the quarter was 56.5 million, and we expect it to be approximately 56.4 million for the third quarter, reflecting the full impact of our Q2 share repurchases.

Finally, turning to our balance sheet. Reflecting the scale and diversity of our business, we were upgraded by S&P in June and are now rated A3/A-. In the second quarter, we also paid a cash dividend of $0.20 per share and repurchased $120 million in shares to bring our total to $200 million in the first half of 2017.

Looking forward to the second half of the year, we will retire our $200 million senior bond in August, which will be accretive to earnings given its relatively high cost, and also anticipate additional share repurchases of up to $100 million by year-end.

With record assets under management of $772 billion, together with the increased earnings power of our business of approximately $1.2 billion in run-rate EBITDA, we are well-positioned to generate substantial shareholder value through the execution of our growth strategy and the consistent return of capital to shareholders in the future.

Now we will be happy to answer your questions.

QUESTIONS AND ANSWERS

Operator

(Operator Instructions) Our first question comes from the line of Alex Blostein with Goldman Sachs.

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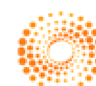

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Alexander Blostein - *Goldman Sachs Group Inc., Research Division - Lead Capital Markets Analyst*

Great. So Jay, maybe a couple of questions around the P&L dynamics this quarter. I guess, if we look at the operating income for your consolidated Affiliates, you guys are putting up revenues up slightly, but expenses are essentially flat. A little, I guess, inconsistent with what we've seen previously. So maybe some color on what's going on there would be helpful.

Jay C. Horgen - *Affiliated Managers Group, Inc. - CFO and Treasurer*

Yes. Well, obviously, Alex, quite a bit of our operating income comes from equity method, so that will not be included in the revenue line. But when you look at it on an aggregate basis, both GAAP revenue and equity method revenue, you'll see the increase is about 23%. About 3% comes from GAAP, and something much higher than that comes from equity method. That mix is 23%, translating into an EBITDA growth rate of about 16%. As it relates to operating expenses, most of those operating expenses are for the account of our Affiliates. You'll see a slight decrease in the SG&A line, mainly because of FX at our non-U.S. Affiliates. Again, that's for their account. We've done a pretty good job here, at the holding company, holding our expenses constant year-over-year. So really we're experiencing some margin, albeit small, as it relates to AMG. And so when you look at it on an EBITDA basis, which is really our top line, you see quite a bit of growth.

Operator

Our next question comes from the line of Mike Carrier with Bank of America Merrill Lynch.

Michael Roger Carrier - *BofA Merrill Lynch, Research Division - Director*

Just wanted to get an update, just given that you've been active on the buyback front and then you're paying down some of the debt, just on the opportunity for additional managers out there and maybe just the environment, what you're seeing, given maybe where market levels are, but kind of some of the shifting in the trends in the industry, increasing regulation, how do you see that outlook playing out over the next couple of years?

Sean Michael Healey - *Affiliated Managers Group, Inc. - Chairman and CEO*

Sure. Well, we continue to have an excellent pipeline, as we indicated. I would say that given the phenomenon, which continues, I think driven as much by uncertainty in the macroeconomic and geopolitical environment, of the highest-quality boutiques being relatively less active. And so if you think about that in the short term, it means that our deal activity this year is going to be more back-end loaded and even into next year. Over the medium to long term, our opportunity to build and diversify our business through investments in additional Affiliates is just tremendous. Even in a period which is, I should say a matter of months at this point, where we are announcing fewer transactions, we're continuing to build relationships with some amazing firms. And given the inevitability of demographics, it's just a question of when, not if, we proceed with investments in the set of outstanding boutique firms with whom we've built relationships. And our competitive position is better than ever as scale, stability, especially permanence relative to private equity vehicles, and the real strategic capabilities we offer become even more important. So we remain extraordinarily optimistic about the contribution from New Investments.

Operator

Our next question comes from the line of Robert Lee with KBW.

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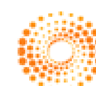

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Robert Andrew Lee - *Keefe, Bruyette, & Woods, Inc., Research Division - MD and Analyst*

Maybe a question for Nate. Could you -- is it possible to -- with the fundraising cycle, I guess, you're entering this quarter with a bunch of your Affiliates, is it possible to kind of scale that in the aggregate? And kind of what your current thoughts are about fundraising. And then should we think of this as an 18-month cycle? And then maybe on the flip side, were realizations in some of these noticeable in your flows this quarter, or maybe year-to-date?

Nathaniel Dalton - *Affiliated Managers Group, Inc. - President and COO*

Okay. Yes. So let me take that inreverse order. As it relates specifically to this quarter, I don't think there was anything I'd sort of call out from either specifically a fundraising or realization standpoint on what we thought about as sort of the illiquid book. And so then moving to the bulk of your question -- and what I'll do is, I'll answer it in terms of the overall, including the illiquids, and I think that's an important way to think about it, and you'll understand it as I get through this. So if you think about the pipeline overall, we feel really good about the activity levels. And it's mostly consistent with the underlying trends we've talked about in alts and global, and there's a little bit of overlap in the way I'm describing that between the illiquids, which I'll come back to, but even outside of the illiquids, the number of searches, RFPs, is kind of consistent with history and all that. But the thing that's really interesting about the pipeline right now is the magnitude of some of the pieces of business -in the late stage of that pipeline. It's not really just one thing. It's sort of a couple of handfuls of things across Affiliates, across geographies, across client types. And so while we always talk about the kind of the inherent lumpiness of the institutional business, there's some very large pieces of business in the pipeline, and some of that speaks to the scale and breadth of the largest Affiliates' and our capabilities. Some of that speaks a little bit to some of the strategic conversations that you heard Sean reference in the prepared remarks. And it also supports and points to, this idea that people are kind of consolidating relationships. So some of these may include illiquid and liquid alts, for example, or illiquid and the global equities piece. It's really some of that kind of good broadening out that we've been talking about. Now specifically on the illiquid side, as we started mentioning a couple of quarters ago, in the third quarter, we're entering what we've talked about, this significant cycle of fundraising at a number of flagship products as well as, honestly, some newer products, seem to be coming to market at roughly the same time. And then in terms of dimensioning it, what I'd say is, we feel really good about it and delivering on it -- yes, we sort of kind of talked about a kind of $10 billion net number over this next kind of 12+ months here. But I would say, if anything, it's feeling good about that and maybe a little of upward bias to it. But then the reason I'm sort of pushing on this idea of whether we should talk about it as a cycle or not -- it's feeling that way going into it, but we're also starting to get visibility beyond that end that we pointed to when we were saying 12 to 18 months. Both as products are building and then people are building capabilities and as people are building their separately managed account capabilities, it's in some cases into these broader relationships we're talking about. It kind of feels like a cycle going in, but we don't think that's really the right way to think about it in terms of the back end of it. We think it will continue.

Operator

Our next question comes from the line of Craig Siegenthaler with Credit Suisse.

Craig William Siegenthaler - *Credit Suisse AG, Research Division - Global Research Product Head for the Asset Management Industry*

So in 2Q results, for a lot of your peers, we learned that a lot of them were forced to spend more, really invest in areas like technology. How is AMG impacted by this trend as a lot of the raised costs at your Affiliates may not be passed back to AMG due to the revenue share structure? But is AMG also working on some centralized initiatives at the holding company that it can actually scale across the Affiliates?

Sean Michael Healey - *Affiliated Managers Group, Inc. - Chairman and CEO*

Well, we've made material investments in global distribution and compliance, really since the financial crisis, and that continues, but not in a way that I would say is fundamentally different now. Indeed, we believe that our scale in both these areas is a strength. At this point, Nate and I both have mentioned the increasing opportunities we see with the largest global institutional clients and intermediaries and the way in which we're building relationships and are increasingly seeing traction from those relationships. Across the industry, there are obviously areas which are more process-oriented, which are more impacted by these issues. We have a predominantly institutional business where the clear distinguishing,

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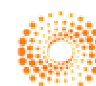

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competitive advantage is around alpha generation in these specialized strategies, and that's the clear focus. So we, of course, continue as our Affiliates do to invest in the business, but the focus is on leveraging outstanding alpha generation across specialized products and leading with that, as opposed to some of the considerations that perhaps peer companies are talking about.

Operator

Our next question comes from the line of Dan Fannon with Jefferies.

Daniel Thomas Fannon - *Jefferies LLC, Research Division - Senior Equity Research Analyst*

I guess, Jay, if you could kind of update us on your outlook, and kind of midway through the year, I know that you are only doing guidance annually, but maybe talk about some of the broader assumptions versus the actuals through the first half of the year and then think about performance fees at this point of the year and looking towards, obviously, the fourth quarter being the big component of that.

Jay C. Horgen - *Affiliated Managers Group, Inc. - CFO and Treasurer*

Yes. Thanks, Dan. So I guess, first, just starting from the press release, you can see we began the third quarter at $772 billion, and that was a record. We actually kind of had momentum all the way through to the end. Our average AUM for the quarter was only $764 billion. So we were already spot rate up about 1% as we ended the quarter, which is a carry forward. And then since that time, so far in the third quarter, we're up another 1.5%, so bringing our year-to-date market blend to a little over 8%. So in addition to that carry-forward in the quarter and another 1.5%, and as you know, our model convention is 2% per quarter, so we're experiencing higher market levels through July than our convention. I think most people are tracking that. The other two main assumptions that impact 2017's Economic earnings per share are performance fees and capital deployment. And as you had mentioned, the majority of our performance fees crystallize in the fourth quarter, just noting that year-to-date, we had $0.31 of performance fees, but the majority still crystallized in the fourth quarter. It's still early, I think. It's still only July.But you can see from our AUM table under market changes for alternative managers that, in total, the combined mix of our alternative products have posted kind of more modest returns year-to-date. But when you look at it more granularly, which Nate did, most of our alternative categories are experiencing positive performance with just the systematic diversified category being down. So that's kind of a mix issue. And as you also heard from Nate, we continue to see strong performance across a number of our products, especially in the relative value and multi-strat categories. Again, just still early to predict. On capital deployment, consistent with our expectations for the first half of the year, we did repurchase $200 million. As we've told people, we are going to retire $200 million of senior bonds. That will be accretive $0.05 this year. It's more of a $0.14 run-rate accretion for next year. We anticipate repurchasing another $100 million, as you heard me say in the prepared remarks, by year-end. Given that timing, it will only have a modest impact on 2017, but it's probably worth a couple pennies.

Operator

Our next question comes from the line of Bill Katz with Citigroup.

William R Katz - *Citigroup Inc, Research Division - MD*

So coming back to capital management for a moment. I guess I'm a little surprised not to see more of a buyback given what sounds like a bit of a pushout on deal activity. And then within the deal activity, I was sort of curious, Sean. A number of your peers are talking about the fact that companies in the $10 billion to $30 billion of size are losing traction in a post-DOL world, a little more consolidated world. Does that shift your focus from an acquisition strategy a little bit more tilted toward alts? Sort of curious on your latest thinking on that.

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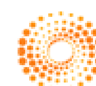

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Sean Michael Healey - *Affiliated Managers Group, Inc. - Chairman and CEO*

Well, start with the second part of your question, which is -- and I'm not sure what context you're referring to. I think we see outstanding boutique firms, certainly in the alternative category, but also more broadly across long-only equity categories, especially global and emerging market equities. For us, it's really all about finding complete firms with outstanding track records of alpha generation. And we absolutely believe in, and we see, and happily have partnered with, a number of firms in the size range you described, which have enduring opportunity to generate organic growth and create additional franchise value. So we feel very good about that. The very short-term opportunity set and the cycles around that, I think, is something we've seen before and says really nothing about the tremendous medium- to long-term opportunity. And with respect to capital deployment, as we have said, we see all elements, given our scale today, coming into play. And you've seen that if you look over any rolling period over the last 5 years, really, you see substantial New Investment activity, return of capital through share repurchases, and now a dividend. And obviously, to the extent we have additional opportunities, as Jay described, to pay down expensive debt, then we'll reduce leverage and build capacity for further future deployment.

Operator

Our next question comes from the line of Brian Bedell with Deutsche Bank.

Brian Bertram Bedell - *Deutsche Bank AG, Research Division - Director in Equity Research*

All right. Nate, maybe just to circle back on some of the flow commentary. I appreciate the $10 billion in net new investment. When you say net new capital raising, are you including realizations in that number? And then if not, if you could just comment on your view of realizations in the private equity firms. And then you mentioned a return of capital from ValueAct. If you could size that and the large redemption within institutional U.S. equities?

Nathaniel Dalton - *Affiliated Managers Group, Inc. - President and COO*

Okay. So let me start with the ValueAct. Unfortunately, I think we're not going to be able to give you the precise amount. I think that the 2 redemptions we talked about in the prepared remarks, both the ValueAct one and the other specific U.S. equity one, look, these definitely impacted it. But there's not much more we're going to say beyond that. I think moving to the $10 billion, that was a net number. So when we gave it, and still today, the color that I gave around feeling that there's actually kind of upside to it, that was in that number. But I do want to reinforce the point, which is, it's really interesting how that number -- how we're seeing really large opportunities, again, some of which actually incorporate what was in that $10 billion number plus other things. But it's, yes, the base business excluding that, if you were going to look at it that way, we feel good about the pipeline and see really some significant opportunities in the near end of the pipeline. And then, yes, that $10 billion was a net number. And then, as I said before, if anything, kind of an upward bias to that. And then also, the back end of it, -it may feel like a cycle going into it, but at the back end of it seems like it's really extending as the number of the firms that have these types of products have also continued to extend their investment capabilities as well -- as well as not just investment capabilities, but also operational and distribution capabilities into new channels and into new product packages, including separately managed accounts that will be more like Evergreen.

Operator

Our next question comes from the line of Chris Shutler with William Blair.

Christopher Charles Shutler - *William Blair & Company L.L.C., Research Division - Research Analyst*

I was intrigued by the comments from both Sean and Nate around the broader strategic relationships and AMG helping their Affiliates. Maybe just dive into that a little bit more and talk about how AMG is assisting in those efforts for some of these broader mandates?

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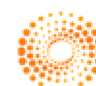

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Sean Michael Healey - *Affiliated Managers Group, Inc. - Chairman and CEO*

Well, I'll start and then Nate will add further context. I can't give you, for obvious reasons, specific examples, but already, and then as you heard us say, on an increasing basis going forward, we're seeing the benefits of large, sophisticated global institutional clients who are wanting to have stronger relationships, a narrower set of relationships, while simultaneously appreciating the benefit for the alpha portion of their product allocation, the benefit of access to a broad range of specialty products, both long-only as well as alternative. And within alternative, of course, the more diverse, the better, including liquid and illiquid. And that, I think, is an enduring trend and one that plays very much to the strength of our product set and the scale and diversity of our business. You want to add something to that, Nate?

Nathaniel Dalton - *Affiliated Managers Group, Inc. - President and COO*

I agree with all of that. I think if you sort of step back a little bit, and you've heard both of us talk about it before, we are a place where you have a combination of many great asset managers, boutique asset managers -- we talked a little bit in the prepared remarks about kind of focused excellence -- who are very, very good at a set of things. And then you combine that with -- and many firms are excellent in packaging, distribution into one or more channels. And that's fantastic. But you package that, you combine that with the opportunity to partner with us, if they want, in accessing additional markets and additional channels. And then on the other side, the opportunity to go into channel partners, whether it's intermediaries, as Sean said, or whether it's large, sophisticated end clients, institutional or retail, many of whom have global reach themselves, and to be able to have conversations which allow them to see how they can access all of that, or much of that, or some of that, depending on their needs of that capability, easily, and then partner with us on the other side in terms of how they make sure they can get all those return streams into what it is they're trying to achieve, either for themselves for their clients, and then hopefully our shared clients. You put those together and then, the only thing I'd add is we do have a somewhat unique additional -- increasingly recognized from the client's perspective and the intermediary's perspective -- product development capability, which is our continuing to add additional new Affiliates. And you've heard us talk about this in other settings as kind of, that virtuous circle. So looking at bringing all of that to bear. And look, these are all very long conversations and almost partner-like conversations with the channel and with the end-users. And again, we've been engaged in that for a while and it's good to see some of those really gaining some traction.

Operator

Our next question comes from the line of Robert Lee with KBW.

Robert Andrew Lee - *Keefe, Bruyette, & Woods, Inc., Research Division - MD and Analyst*

Couple of questions on the high-net-worth business. I mean, the channel has been a pretty consistent sources of inflows. I'm just curious if you can maybe break that down a little bit more. How much of that is being driven by your RIA Affiliates versus maybe how much of that is a reflection of demand for SMAs in bigger distribution channels? Just trying to get a little more of a feel for that and how you think about its sustainability.

Nathaniel Dalton - *Affiliated Managers Group, Inc. - President and COO*

Okay. I think you understand the channel exactly right, and I think it's been pretty consistent contributions from both. So if you sort of -- and as you saw, we had kind of $800 million or so in net inflows, $4.3 billion of gross sales, $3.5 billion of redemptions. A little bit underlying your question, I think this is now 14 straight positive quarters in a row for this channel. And in the quarter, it was both wealth management Affiliates generating positive net flows. And second quarter is not a traditionally especially strong quarter there, but it was a fine quarter for us and there is -- again, to be clear, there is a little bit of seasonality there in the second quarter. And then SMA flows were also positive. And for us, that's coming through, particularly in global equities and municipal bonds. And looking ahead, we think we have good momentum on both sides. I do think we see a good, you call it a sort of a tailwind or something, a good tailwind in the separately managed account market on major platforms. And there should be opportunity for us to continue sort of both driving sort of the global and international equities as well as muni bonds, and then also maybe broadening that out, I would say, kind of as a medium-term thing, especially if we can figure out ways to bring some of the more specialty, including

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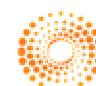

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alternative products, into some of the platforms. Obviously, the muni bond market has its own very specific dynamic and we're participating well there. So I think that's what I would say. So, it has been a strong, stable kind of contributor and we see that continuing.

Operator

Our next question comes from the line of Brian Bedell with Deutsche Bank.

Brian Bertram Bedell - *Deutsche Bank AG, Research Division - Director in Equity Research*

Just can you describe the specific $3.4 billion reduction in the high-net-worth channel that you covered in footnote F, -that's the the transfer of assets from the Forbes Family Trust to Wealth Partners Capital Group? Could you describe exactly what's going on there?

Sean Michael Healey - *Affiliated Managers Group, Inc. - Chairman and CEO*

Sure. In the quarter, we restructured our wealth management business in the following way: First, the $40 billion of scaled boutique wealth management Affiliates remains with absolutely no change, but the team that was focused on building that business, some of which stayed with, but some went to start a new business that is focused on smaller wealth management firms with an underlying aggregation strategy. And I think there's every chance of success for that business. And by contributing our Forbes interest, we took back a minority interest in this new entity. But the new entity, to be clear, is independent and really doing things that are less of a fit with AMG's core business. I think, over time, we will absolutely make incremental investments in scaled boutique wealth management firms, but at the moment, the pricing and the M&A environment strikes us as uneconomic, and in many cases, driven by an influx of new competitors. And for the moment, we'll be happy to continue to work with our existing Affiliates and benefit from, as Nate said, their ongoing organic growth.

Jay C. Horgen - *Affiliated Managers Group, Inc. - CFO and Treasurer*

I just wanted to address the financial impact. So obviously, it ran through our other AUM, because we contributed it. It's no longer an Affiliate. As it relates to the P&L, it had no material impact. In fact, the restructuring will add benefit to us in EBITDA over the next 12 months of kind of $4 million just as we save some money and contribute to the business. So the net effect is actually positive to us.

Operator

Our next follow-up comes from the line of Bill Katz with Citigroup.

William R Katz - *Citigroup Inc, Research Division - MD*

Okay. A number of your peers in the publicly-traded alternative manager space are also talking about this consolidation of strategic relationships among the bigger players, which I think is a theme you've been mentioning as well, Sean. They also mentioned that it is coming at a bit lower fee rate, potentially longer duration in terms of the opportunity set. Can you talk about the net economic impact to AMG among these relationships versus more stand-alone type of opportunity?

Sean Michael Healey - *Affiliated Managers Group, Inc. - Chairman and CEO*

Well, I'm sure it runs the gamut as I think about the forward opportunity set. It is absolutely net positive. These are in the main high-fee products with, certainly for the broad illiquid category, locked-up vehicles, in many cases, and so the overall contribution to our business is very positive. As Nate described, we see this as a long-term opportunity and not one of short-term cyclicality. And that's based on the breadth of our business and

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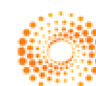

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our exposure across illiquid alternatives as well as the continuing product development and innovation across the various Affiliates who manage these products. Would you add anything?

Nathaniel Dalton - *Affiliated Managers Group, Inc. - President and COO*

The only thing I'd add, and this may be something that others are talking about as well, but these relationships can be quite helpful. They can be true partnerships and quite helpful in working with us and Affiliates to extend their capabilities even further, right? So there's sort of a second derivative, which is it may be that duration and fees and use of capacity and all those things have to be part of the analysis, as does the derivative, which is okay. If you're going to be building things in the context of the relationship, what else can you do with the things that you're building? So, if the firm is a private equity firm and a relationship allows them to extend into infrastructure, real assets, or something else, then that can become something that you go do other things with. The relationships can evolve into somewhat partnership-like, where you can work together to continue to drive.

Sean Michael Healey - *Affiliated Managers Group, Inc. - Chairman and CEO*

Yes. And one other point, which may be not clear from your question, the universe of "alternative firms" in the industry, of course, includes a range of firms with a range of capabilities. But I think if you step back and look at the breadth and depth and diversity of our overall product set, more than 550 products, even within the alternative category, is a very large number of products, -in liquid and illiquid capabilities, which we would put against literally anybody in the industry in terms of the quality and breadth of our alternative product set.

Operator

Our next follow-up comes from the line of Dan Fannon with Jefferies.

Daniel Thomas Fannon - *Jefferies LLC, Research Division - Senior Equity Research Analyst*

Just a follow-up on the potential redemption trends within the systematic bucket of alternatives. We've seen the underperformance in this year, as you kind of talked about, Nate, and it seems like it was a little more magnified toward the back half of 2Q. I guess as you of think about looking ahead, how are you thinking about the redemption trends within that sub-bucket?

Nathaniel Dalton - *Affiliated Managers Group, Inc. - President and COO*

Okay. So maybe just to step back, and again, I was reporting on the quarter. But look, when you look at the space, it has absolutely has been a challenging space lately. But there's very long-term data series supporting the strength of trend-following strategies, and included in that are periods of drawdown as well. But as we said on other calls, I mean, look, they play a very important part in investor portfolios, very high quality, uncorrelated returns, in many cases lower realized volatility when included within that portfolio context. And so sophisticated investors obviously -- sort of obviously understand that. And they also are strategies we continue to like because they have really significant scalable capacity because they can invest in almost -- or you think about them as investing in all tradeable asset classes. So the opportunity to continue to develop new products as well has lots of long-term promise. And in fact, I think we said this in our prepared remarks, you are actually seeing many of the firms with these capabilities among our Affiliates continuing to do product development, many of which are getting some traction. And we saw some of that a little bit in the last quarter, and we have already seen some of that this quarter so far. And so I think, while no question it has been challenging space, we feel like these are excellent firms. We have invested in some fantastic firms. Great people running them, lots of opportunity to continue to take those uncorrelated return streams into both the existing sets of clients that they work with today, but also many, many other, both geographies and channels. Combine that with their product development capabilities, and we feel good about the space.

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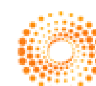

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Operator

Our next question comes from the line of Alex Blostein with Goldman Sachs.

Alexander Blostein - *Goldman Sachs Group Inc., Research Division - Lead Capital Markets Analyst*

Again, sorry, nitpicky follow-up. If you look at the retail channel, surprisingly weak given the positive data we've been able to see through some of the public channels, on both on the U.S. and the non-U.S. side of the mutual fund domain. Any particular outliers that kind of drove the decline in the quarter, either by kind of channel, geography or Affiliate level, that drove the gap between the observable flows in the quarter versus the $0.4 billion of outflows you reported?

Nathaniel Dalton - *Affiliated Managers Group, Inc. - President and COO*

Yes. So let me take that. Again, you understand it exactly right. So we did have net outflows. Gross sales about $11.4 billion and redemptions about $11.9 billion. Despite the overall negative number, I think you're right,overall retail trendsfor us were pretty stable. The way I would describe the underlying trends would be strong, good alternative trends, good global equity trends, and offset by continued weakness in U.S. equities. In terms of the quarter, in particular -- and apologies if this didn't come through as we did the description at a product level, but this is actually where some of those -- there was a lumpy sub-advisory outflow here. And then also in addition to that, this is the reason it's probably not footing exactly to the publicly available stuff. There were outflows within subadvisory offset by good non-U.S., if you're looking at the U.S. retail only. So U.S. retail is negative sub-advisory offset by good non-U.S. And within subadvisory, there was actually some breadth to it, it tended to be U.S. equity and probably some of it was platform rebalancing. And when you turn to July, obviously now focusing on the things that are publicly visible, if you look at July flows in the U.S., it's looking pretty good. I think it was $400 million or something and change in the visible U.S. and then probably another $200 million and change in the visible non-U.S., so it is ahead of where we were last quarter. So again, just going by the stuff that's visible, quarter's shaping up well and ahead of where we were last quarter.

Operator

Our next question comes from the line of Craig Siegenthaler with Credit Suisse.

Craig William Siegenthaler - *Credit Suisse AG, Research Division - Global Research Product Head for the Asset Management Industry*

So just one follow-up modeling question here for Jay. The guidance is $21 million interest expense for 3Q. Does this include or exclude the imputed interest expense? And also what type of range of imputed interest expense are you guys looking for, for 3Q?

Jay C. Horgen - *Affiliated Managers Group, Inc. - CFO and Treasurer*

So. Yes, on imputed interest expense, it's only in the neighborhood of $1.5 million now, because it's just on a recurring basis related to our convertible. It is on contingent payments that can come through, but we don't have any really expected contingent payments in the future. So really it's just that $1.5 million. The $21 million is the interest expense for the cash basis. And we do see it coming down because of the high-cost bond that we're retiring.

Operator

Ladies and gentlemen, we have come to the end of our time allowed for questions. I'll turn the floor back to Mr. Healey for any final remarks.

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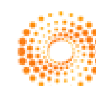

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Sean Michael Healey - *Affiliated Managers Group, Inc. - Chairman and CEO*

Thank you, again, for joining us this morning. We are pleased with our results for the quarter and we are confident in our ability to continue to create shareholder value through the organic growth of our existing Affiliates, accretive investments in new Affiliates, and consistent capital return to investors. We look forward to speaking with you again in October. Thank you.

Operator

Thank you. This concludes today's teleconference. You may disconnect your lines at this time. Thank you for your participation.

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