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IVZ - Q3 2012 Invesco Ltd. Earnings Conference Call

EVENT DATE/TIME: NOVEMBER 01, 2012 / 1:00PM GMT

OVERVIEW:

IVZ reported 3Q12 EPS of \$0.42.



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PRESENTATION

Unidentified Company Representative - Invesco Ltd

This presentation and comments made in the associated conference call today may include forward-looking statements. Forward-looking statements include information concerning future results or operations, expenses, earnings, liquidity, cash flow and capital expenditures, industry or market conditions, AUM, acquisitions, our ability to obtain additional financing or make payments. Regulatory developments, demand for and pricing of our products, and other aspects of our business or general economic conditions. In addition, words such as believes, expects, anticipates, intends, plans, estimates, projects, forecasts, and future or conditional verbs such as will, may, could, should, and would, as well as any other statement that necessarily depends on future events are intended to identify forward-looking statements. Forward-looking statements are not guarantees, and they involve risks, uncertainties and assumptions. There can be no assurance that actual results will not differ materially from our expectations. We caution investors not to rely unduly on any forward-looking statements, and urge you to carefully consider the risks described in our most recent Form 10-K and subsequent Forms 10-Q filed with the SEC. You may obtain these reports on the SEC website at www.SEC.gov. We expressly disclaim any obligation to update the information in any public disclosure if any forward-looking statement later turns out to be inaccurate.

Operator

Welcome to Invesco's first (sic - third) quarter results conference call. All participants will be in a listen-only mode until the question-and-answer session.

(Operator Instructions)



Today's conference is being recorded. If you have any objections, you may disconnect at this time. I would now like to turn the call over to the speakers for today, to Mr. Martin L. Flanagan, President and CEO of Invesco, and Mr. Loren Starr, Chief Financial Officer. Mr. Flanagan, you may now begin.

Martin Flanagan - Invesco Ltd - President & CEO

Thank you, and thank you for joining us today. And for those of you in the Northeast, I hope you and your families have made it safely through the storm. I would like to recognize and thank our employees in the Northeast for going above and beyond to deliver for our clients throughout this storm, and as always, our focus is on their safety, and it is the case, many of them had to work remotely because they couldn't get into the office, and they did work very diligently during the storm for the benefit of our clients. We appreciate that very much, and I'm sure that this appreciation was the same for all of you within your organizations, and I know it's been a difficult time. So on the call today with me is Loren, as was just mentioned, our CFO, and as is our practice, first of all the presentation is on the website if you're so inclined to follow it, I will review the business results for the quarter, Loren will go into greater detail on the financials, and as is always the case, Loren and I will answer any questions that people might have.

So I thought it might be helpful before getting into the numbers is to really provide a sense of the macro environment that we are operating in, and that we were operating in within the quarter. And although the markets in the quarter were generally positive, lately we've seen signs that investor confidence is under pressure again, and it is a variety of factors that are contributing to this. It's the deterioration of the economic environment in Europe, some continued softening in China, although it continues to be a very rapidly-growing part of the world, but here in the United States, uncertainty over the fiscal cliff, negative news that's coming in from abroad is really keeping investors on the sidelines, and again this week, the weather in the Northeast did not help any of that investor confidence.

In this uncertain market environment, what we've seen is advisors and consultants are focusing on managing risk as a major topic. We recently completed a survey with advisors in the United States, and 65 of them responded, saying that managing risk and wealth preservation were the predominant philosophies for managing client assets. Again, people are in a very cautious position still. And as you would expect, the emphasis on risk management for preservation of wealth is driving them into yield-oriented capabilities and multi-asset capabilities, many of which are continuing to see positive flows across the industry. Invesco's well-positioned ahead of this trend, and it is really the broad suite of income capabilities and multi-asset capabilities that we have for our clients that is responding well to these needs.

So moving on, let's take a look at the third quarter and some overview comments. Long-term investment performance was strong again across all time periods for the third quarter, and delivering strong investment performance to our clients contributed very solid operating results. And as we mentioned during the last quarter, we saw early signs of a turnaround in flows in July, and building on that early momentum, net flows grew to \$11.7 billion for the quarter, and this was amongst the strongest net flows in the history of the Company and most robust net flows we've experienced since the second quarter of 2010.

Invesco's quarterly dividend is now \$0.1725 per share representing a 41% increase over last year's dividend, and reflecting continued confidence in the fundamentals of our business. Returning capital to shareholders during the quarter totaled \$118 million. And during the third quarter, we did take advantage of a number of opportunities in the marketplace to further invest for the future of our business, and let me hit on a couple of those. And as many of you know, we currently have a presence in India through the enterprise support location in Hyderabad, and also with WL Ross & Company having a location there also. We plan to build on that presence, and it was really by acquiring a 49% stake in Religare Asset Management and creating a partnership in India for us. This move will enhance our presence in an important and growing market, and we will expand, again our comprehensive range of investment capabilities with these investment capabilities that Religare Asset Management bring to us.

During the third quarter, we continued to build out our market-leading multi-asset capabilities with the addition of a multi-asset team in the United Kingdom. In the next year, we look to introduce capabilities into that marketplace that, again, will very much expand and complement the multi-asset capabilities that we have across the organization globally. We continue to invest in the brand in the United States and where our awareness and brand equity score, now among financial intermediaries, has risen to 10, and just two years ago we didn't even show up in the results, and as we said, we do think it is very important for us to generate a level of awareness in brand equity in that marketplace. So good progress is being made there.



If we move on and take a look at the summary results, let me start there, and it's really driven by very strong net flows of \$11.7 billion during the quarter, assets under management grossed at \$683 billion during the quarter, up significantly from \$646 billion at the end of the prior quarter. Operating income was \$250 million versus \$249 million in the second quarter, and the operating margin was 34.1%. Earnings-per-share were \$0.42 per share versus \$0.41 in the prior quarter. A very key metric surrounding investment performance and distribution were among the strongest they've ever been for the organization. And as a result, employee compensation rose in the third quarter, driven by strong sustained investment performance and near record flows. And as we said for some time, a major focus for the firm, is to reinvest in the business and build on our strengths, and to further enhance our competitive position, which we think we've done during this quarter. We also took advantage during this quarter of opportunities in the market to continue to invest in our investment capabilities, our brand, global platform, and in our people in ways that we think again strengthen our business for the long-term.

Before I turn it over to Loren, let's take a look at investment performance, and as you know, we have an absolute commitment to investment excellence, and our efforts to build and maintain a strong investment culture has helped achieve solid investment performance in spite of a very volatile market, once again. And as you can see on slide 7, 63% of the assets were ahead of peers on a one-year basis, 67% of assets were ahead of peers on a three-year basis, and 78% of assets were ahead of peers on a five-year basis. Again, very, very strong. And again, we would like to call out during this past quarter, 79% of our US retail assets under management are currently rated four and five star by Morningstar and that is an all-time high for the firm. Again, good investment results.

Taking a look of flows during the quarter, as I mentioned earlier, net long-term flows totaled a near record \$9.4 billion during the quarter. We experienced solid growth in our active assets under management, with a strong broad flows across IBRA, high yield munis, alternative fixed-income and others. If you take a look at the pass of flows during the quarter, they again were very very strong for Invesco PowerShares excluding the QQQs. Flows are strong and broad across low volatility bank loans and other income-oriented ETFs, again, very consistent with what we're seeing from a macro point of view in the marketplace also. But as an example of that, this flows into additional Invesco PowerShares ETFs were \$2.1 billion and that represents an annual growth rate of 39%. So again, very very strong result for Invesco PowerShares.

Taking a look on page 9, at flows again, as you recall, during the prior quarter, we mentioned the very robust institutional pipeline. During the third quarter, we saw good momentum in institutional flows, which totaled \$2.9 billion. And as a result, a good portion of the pipeline rolled off during the quarter with some sizable commitments funded, but in spite of these roll-offs, we continue to see solid momentum in our institutional business. Recently, that is rebuilding the pipeline to near-record levels. And if you take a look at how we've done on page 10, taking a look at flows, we're very strong again during the third quarter for the US retail business.

Net flows, excluding the PowerShares QQQs were nearly \$6 billion, up significantly from the prior quarter. Gross sales were up 17%, flows into the complex were strong across IBRA, munis, international growth, and again, a number of other capabilities. So very broad and deep improvements there. Redemption rates continue to be very, very favorable, relative to the industry. We have a redemption rate of 20% versus 28% for the industry as a whole. So again very good news.

Taking a look on page 11, globally, the multi-asset suite of capabilities is generating tremendous interest from clients who are attracted to the capability with the strong long-term performance that aims to provide a high level of protection in these very volatile markets. The Balanced Risk Allocation Mutual Fund in the United States did hit its three-year track record and a five-star Morningstar rating on a total return low weight basis earlier this year, and we are seeing a growing number of clients add this capability of putting it on their platform. As a result of this very strong performance of this capability, the multi-asset product suite flows have moved up quite nicely. Assets under management increased to \$20 billion, and flows in the third quarter were more than \$4 billion, up substantially from the second quarter.

So in spite of the mixed signals we saw in the market and the global economy during October, we do remain cautiously optimistic about the quarter ahead. We have a very robust culture that enables investment talent and delivers strong long-term investment performance to our clients. Our market-leading asset allocation capability is enormously popular and provides a powerful catalyst for future growth, and we offer a comprehensive depth and breadth of investment capabilities that enables us to provide solutions to meet clients needs in a variety of market environment, as we are proving. And as you might imagine, in this environment, we are seeing strong demand for income products, and Invesco is very well-positioned to meet these needs for clients seeking income, with strong performance in these capabilities. As a result, sales of income products, of our income



products in the US are up 76% year to date. So again, I think it positions us very well for the market that we are in. So with that, let me turn it over to Loren, and afterwards, we will come back to Q&A.

Loren Starr - Invesco Ltd - CFO

Thanks very much, Marty. Moving to the slide on asset roll-forward you will see that AUM increased \$36.4 billion quarter-over-quarter, that was 5.6% growth. It is a combination of the following elements, market and foreign exchange, that contributed \$26.4 billion of the increase, the long-term net inflows of \$9.4 billion, we have net inflows of money market products of \$2.3 billion, and these increases in AUM were slightly offset by dispositions of \$1.7 billion, as we sold off some of our European CLL management contracts in the quarter.

Average AUM for Q3 was up 2.6% to \$667 billion and our net revenue yield in Q3 came in at 44 basis points. This was an increase of 0.3 basis points quarter-over-quarter, and the increase was due to a combination of the following factors, the first is product mix and an extra day, as well as the expiration of fund mergers, related fee waivers and that added 1.1 basis points in aggregate. We also saw this offset, however, by lower performance fees in the quarter, that reduced our net revenue yield by 0.7 basis points, and also we saw lower other revenues, which had a negative impact of 0.1 basis points. I think the good news, however, is that our net revenue yield before performance fees was up substantially quarter-over-quarter, and that obviously sets us up nicely for Q4.

Moving to the next page, you will see that net revenues increased \$22.6 million or 3.2% quarter-over-quarter. That included a positive FX rate impact of \$3.2 million. Looking at this a little bit more closely, you'll see that investment management fees increased \$37.8 million or 4.7% to \$839.9 million. This increase was in line with our higher average AUM, but also in line with an expansion of revenue yield. FX increased our investment management fees by \$4.3 million. Service and distribution revenues were up by \$9 million or 4.8%, also in line with the increase in investment management fees and FX increased service and distribution revenues by \$0.4 million. Performance fees came in the quarter at \$3.4 million, represented a decrease of \$12.1 million versus Q2. Other revenues in the third quarter came in at \$24.4 million, that is down \$1.6 million off of Q2. The decrease was the result of a continued level of lower transaction fees from our real estate business, and again, obviously this was a little bit slower rate of transaction fee realization than we had previously hoped or anticipated.

Our third-party distribution service and advisory expense, which we net against gross revenues, increased by \$10.5 million or 3.3%. FX increased these expenses by \$1.7 million. So continuing on down the slide, you'll see that our adjusted operating expenses at \$484.3 million increased by \$21.2 million. That is 4.6% up relative to the second quarter, and foreign exchange had an impact of an increase of \$1.8 million on that line. Moving into the detail, you'll see that employee compensation probably was the biggest mover. That was at \$327.7 million. That also increased by \$21.2 million, and that was up 6.9%. The growth in compensation, as I mentioned, requires a little explaining, just given its magnitude. The increase in the third quarter reflected an \$8 million catch-up accrual for the first half of 2012, driven as Marty said, by the sustained strong long-term investment performance that our teams are delivering. As you know, there is also a certain amount of variability in performance in AUM in the first half, but given where we are year-to-date, we are able to forecast our full-year results with more confidence, and hence, that is why we took the adjustment now.

The impact of the first-half catch-up was roughly \$0.015 per share and approximately 100 basis points of operating margin. That was also a step up in the run rate of variable compensation in Q3 that reflected about \$4 million of the increase. In addition, given the significant increase in sales and net flows in the quarter, our commissions were up substantially, approximately \$4 million versus Q2. We also saw some other expenses, including medical insurance and relocation costs in the quarter, that accounted for about \$3 million of the increase versus Q2. And then finally, foreign exchange increased compensation expenses by \$1.5 million.

Moving off of compensation down to marketing, you'll see that that expense increased slightly, \$0.3 million, or up 1.1% to \$26.5 million. FX increased these expenses by \$0.1 million. Property, office and technology expense came in at \$69.3 million in the third quarter, and was an increase of \$1.5 million. The third quarter increase included effects of technology expenses associated with continued investment in portfolio trading and risk management systems across the firm. FX also increased these expenses by \$0.2 million. G&A expenses came in down, \$60.8 million. That was down \$1.2 million, or almost 2%.



So continuing on down the page, you will see that our non-operating income increased \$8.2 million compared to the second quarter, and that increase was due to the realized gains of certain of our CLL products in the quarter. The firm's effective tax rate on pretax adjusted net income in Q3 came in at 25.8%. The rate was slightly higher than the previous guidance, and that was a result of a one-off adjustments to our tax reserves. Going forward, we expect the effective tax rate to be back down between 24.5% to 25.5%, which brings us to the adjusted EPS at \$0.42, and our operating margin of 34.1%. I'm going to turn it back to Marty now.

Martin Flanagan - *Invesco Ltd - President & CEO*

So why don't we open it up to any questions people might have.

QUESTIONS AND ANSWERS

Operator

(Operator Instructions)

Our first question does come from Ken Worthington of JPMorgan. Your line is open.

Ken Worthington - *JPMorgan Chase & Co. - Analyst*

I wanted to start with the sales question. You had particularly strong sales into Fixed Income, maybe you can talk about why Fixed Income is slowing so well, and if you could mention Perpetual, those products seem to be performing particularly well. How are Perpetual sales in particular for the quarter? Perpetual Fixed Income sales for the quarter?

Loren Starr - *Invesco Ltd - CFO*

So, can, the fact that our Fixed Income is doing well is probably consistent with what you're seeing in the industry. It is nothing necessarily unique to Invesco. I think we are very well-positioned, particularly around some of the alternative Fixed Income offerings that we have, whether it is mortgage products or our bank loan capability, Stable Value continues to do very well. The High Yield product is and High Yield Muni product is doing very well. So we are benefiting from the interest in those types of products, and we have very good performance of those types of products as well, and that is a trend that we see continuing into Q4.

And then in terms of Invesco Perpetual product, we are seeing really good strength in sales in some of the fixed-income products, particularly as they are selling, not just within the UK but also across Continental Europe. And then the traditional equity income products again are sort of mainstay, in terms of what people are looking for in the UK, are doing very well, and the performance is extremely strong as you mentioned. So I think from a competitive position, we are feeling good about where we are in the UK, in particular. We are also looking at, as Marty mentioned, some of the multi-asset capabilities and so we think there is an opportunity to continue to expand offerings within the Invesco Perpetual sort of footprint. And so that is work in progress, that it is still too early to say how that's going to go, but that's pretty exciting.

Martin Flanagan - *Invesco Ltd - President & CEO*

I think I would add to it, if you look at some of these macro factors, as people are, as I said, it is a cautious environment, still, but as they move more towards credit type products, we do very well, and the same thing with equity income oriented capabilities. Again, we do very well with that, and if you just use the US as a barometer and look at a lot of where do the Fixed Income flows go in the United States, it was in intermediate bond categories. We are still -- that is not playing to our strength, right, and these results, I would say, are really strong when you consider that the world is just starting to move to really where our strengths are.



Ken Worthington - *JPMorgan Chase & Co. - Analyst*

Okay, thank you. And then management fees rose bunch this quarter, both on the active side and the passive side. I know there is a million things that influence it, but as we look forward, based on what you know, what is the outlook on both the active and passive side? And, obviously, you don't know what the markets are going to do or how the mix is going to affect it, but there's a lot of other things that you do have insight into, so what is the near to intermediate term outlook if you can share that?

Martin Flanagan - *Invesco Ltd - President & CEO*

So, again, I think if you agree with the macro observation that people -- if they do start to move more towards this broad category of income capabilities, and to me, that's equity income capabilities but also more credit-type capabilities, we do very well in that and our effective fee rates are higher in those products. You move into, if there is a continued appetite for multi-asset strategies which we think is not a short-term trend but a long-term movement in the market, we do very well in that area, and again the effective fee rate is higher there. And even within PowerShares, where you have seen the movement, where people were first starting to get exposure to the equity markets, really using the QQQ capability, which is a very good capability. As you know, it is, for us it is really an expense reimbursement type situation where we had tremendous growth and our traditional PowerShares capabilities that set up 39% [yield], with again much greater effective fee rates. So, if you agree with the macro theme, we should do reasonably well in the quarters ahead.

Ken Worthington - *JPMorgan Chase & Co. - Analyst*

Great, and just a little one. Loren, on the tax rate, usually 3Q is the best quarter of the year for the tax rate being low. It actually perked up a little bit. I think if my calculation is correct, it was the highest we have seen this year. What influenced the tax rate this quarter, and again, what is the outlook going forward?

Loren Starr - *Invesco Ltd - CFO*

Yes, so, the historic benefit we've seen in the third quarter were really statute of limitations on certain tax reserves, and those got released. And so that wound down and there wasn't anything else left. So wasn't something seasonally happening, it was really specific to certain tax positions that we've had. This, in particular went the other way, so this was an increase in the reserve that we took related to Canada. Nothing specific to point out, but it was a one-off reserve adjustment. So, we would say it's easy to -- it's always hard to predict where the tax rate ultimately comes out, but right now, we believe the guidance we gave at 24.5% to 25.5% is good for Q4 and going forward.

Martin Flanagan - *Invesco Ltd - President & CEO*

And Ken, as I think about your question some more, I think it is also very important for everybody to understand. So, this is a more short-term intermediate movement towards income, we think that's going to be here for a long time, but also importantly, if you believe the world is getting stronger, we are, again our strengths are our equity capability and if you look at the performance of our international capabilities and merchant market capabilities and our domestic equity capabilities, they are very strong, and that again should bode very well for the organization.

Ken Worthington - *JPMorgan Chase & Co. - Analyst*

Thank you very much.

Operator

Our next question does come from Michael Kim of Sandler O'Neill. Your line is open.



Michael Kim - *Sandler O'Neill & Partners - Analyst*

First, Marty, to follow up on some of your comments on risk management. One of the reasons behind the strong demand for the IBRA products has been assays increasingly looking to outsource asset allocation services. So, just wondering if the markets remain constructive, and maybe retail risk appetite starts to rebuild the bit, could you see somewhat of a reversal in that trend as advisors maybe get more comfortable picking their own strategies again?

Martin Flanagan - *Invesco Ltd - President & CEO*

I find that not likely, but I think what is more likely, I do believe, these multi-asset strategies are here for the long haul, and I'd say were, still very early on, what ultimately where they will go. That said, you could see the flows be less dramatic than what you have seen, and movement much more into again, as I was just mentioning, the international capabilities, domestic equity capabilities, and again I think that's fine. I think that is good for the clients, that's good news, and by the way, we happen to match up very well against that.

Michael Kim - *Sandler O'Neill & Partners - Analyst*

Got it, okay, and then you mentioned earlier the institutional pipeline rebuilding. Can you just give us some color in terms of where you are seeing the demand? Is it still mostly centered in bank loans and stable value and maybe real estate, or have you seen any signs that US or non-US investors are maybe getting a bit more willing to take on some more risk?

Martin Flanagan - *Invesco Ltd - President & CEO*

What we're seeing globally, it is still largely alternatives to multi-asset strategies, Fixed Income. It is broad categories, and as you say, some of the [naturals under], there are real estate bank loans and it is more preservation of capital income type things. That said, we are starting to see and it depends on where in the world global equities within -- EMEA is actually getting quite a bit of attention, I think, which is a good thing. But there is still an income appetite really around the world.

Loren Starr - *Invesco Ltd - CFO*

I would just say, we won a \$1 billion mandate in Germany, the [Quantum] mandate. It is really very interesting to see that happen, since Quantum had been largely ruled out as a category for a long time and so clearly that is an equity exposure. Japanese equity is still of interest. We are seeing wins there, and maybe not institutional, but Canada by the way, has just won a \$330 million mandate which is across equity products, which would include Canadian equity, small Canadian stocks, global endeavors as a broader equity mandate. And then international growth.

I don't think equity is a dead category. It is still not where it should be and where it can be, but it is certainly still making headway. And in generally around the institutional pipeline, it has been strengthening relative to the second quarter, I think about, more than 20%, and then versus a year ago I think it is up substantially. I think closer to, just to get the number, I think it is 30% off of last year. So, good growth in the pipeline.

Michael Kim - *Sandler O'Neill & Partners - Analyst*

Got it, and just one final one to follow up with Loren. How does the step up in the bonus accruals this quarter potentially impact performance fees, looking into the fourth quarter and into next year? And then also any guidance in terms of how we should be thinking about the other revenue line going forward as well?



Loren Starr - *Invesco Ltd - CFO*

Well the bonus accrual was really reflective of where we are today in terms of its performance through the full-year and where we think we are going to end up, but it doesn't include any magic assumptions of performance fees coming in. So it is a pretty conservative view when we forecast forward. It is really reflective more of where we are from an average asset perspective. Generally, in terms of performance fees, though, we do see in the fourth quarter, and we have seen in the past, good performance fees related to our high net worth business, where I think people are familiar that they have an MLP product, which as a category is doing very well and our MLP product is doing even better than the category. So that could be of a similar magnitude that you have seen in prior years.

I think the transaction and other revenues, that one is harder to predict. We thought it would step up this quarter, it obviously did not. We do see a higher level of transactions in the pipeline for Q4, which should mean maybe there is some pickup off of that line item, but again I think it is really hard because the timing of these things are very difficult to predict and so, again, the run rate of transaction fees and other revenues probably face -- it would be safer to take where we are today and assume there is a small pick up, \$2 million off of that benefit into Q4, but that is about as much as I can offer up.

Michael Kim - *Sandler O'Neill & Partners - Analyst*

Okay, that is helpful. Thanks for taking my questions.

Operator

Our next question does come from Dan Fannon of Jefferies. Your line is open.

Daniel Fannon - *Jefferies & Company - Analyst*

Loren, just to clarify in the comp, is the \$8 million accrual step up, is that the starting point we should think about for 4Q, or should that be backed out as a run rate?

Loren Starr - *Invesco Ltd - CFO*

Yes, so take our current comp, obviously there is \$4 million of sales commissions as well, so hopefully we continue to -- that might continue, that would be good. I think the \$8 million you should back out, that was definitely a catch-up for the first half and should not be seen as recurring cost going into Q4. So, take the number or take the number and subtract out the \$8 million, and you should sort of figure out how that might increment up or down based on performance fees coming in, or average assets up off of where we were off of Q3. But again the normal operating margin -- operating leverage would be existing at that point, so you would begin to see margin increasing into Q4, if we stay where we are today in terms of asset size.

Daniel Fannon - *Jefferies & Company - Analyst*

That's helpful, and just a clarification as to why we didn't see that in Q2, just in terms of the timing issue, the way you think about comp?

Loren Starr - *Invesco Ltd - CFO*

Yes, I think it is just because of the volatility of performance. I mean as you know, we have risk-on risk-off and then actually has an impact on some of our teams in terms of how they are positioned from a performance perspective, and obviously assets were rather volatile through the second quarter. So, again, it's hard to really figure out went to make the move and then we saw such a large pickup in assets into Q3. We felt it was obviously pretty evident to make it in Q3. So, again, it's part of the difficulty of forecasting to know when to ease that in.



Daniel Fannon - *Jefferies & Company - Analyst*

Understood, and I guess just thinking about the environment we are in, and your focus on margins, in an environment where your sales are strong, is it hard to think about margin expansion? Given kind of the payouts and the way that works with regard to compensation?

Loren Starr - *Invesco Ltd - CFO*

I don't think sales, the big -- obviously the big factor was the catch-up in the quarter. If you back that out, you would be back at 35.1% margin, so you would be back in the 35%, and then you see step off into Q4 with higher margins. So, again, I think the sales was an element, but it is not one that should depress margins normally. It is just that was one element within the picture, but not the biggest one.

Daniel Fannon - *Jefferies & Company - Analyst*

Okay, thank you.

Operator

Our next question does come from Bill Katz of Citigroup. Your line is open.

William Katz - *Citigroup - Analyst*

Going back to the margin discussion for a second, if I did my math right, and I haven't adjusted for anything other than the \$8 million catch-up, looks like you have a 60% incremental margin, it seems pretty robust in the construct of spending on that brand equity as well as the variable compensation related to sales. Is that the right way to be thinking about the incremental margin on a go-forward basis or are there any other operating efficiencies globally to be anticipating?

Loren Starr - *Invesco Ltd - CFO*

So, yes, we've talked about incremental margins which again, we don't manage quarter-to-quarter it is more of a result as opposed to something we manage to. And again, but generally the concept is you will see a lower incremental margin, if the market is not helping us, you will see a higher incremental margin, if the market is helping us, because it's increasing assets without having to do a lot of marketing and sales activity and new product development, so it really will depend on what sort of market we are going into, going forward. I think the range of 50% to 60% is still probably a decent one for people to think about, and we are still investing in the business, and we have intentions to continue to invest in the business. But again, we are hoping to be able to offset some of those expenses by those efficiencies that you suggested we are doing, and it's a continued theme for us to look for those across the firm and position our operations in the best location, that gives us the best unit cost, so to speak, of production.

And that's an ongoing dialogue. We have been talking about outsourcing our transfer agency in Europe and the UK and that is going along. That project is actually probably going to spill into Q1 of next year as opposed to ending this year, just because of the magnitude of it. That has some nice run rate savings that we would expect \$10 million to \$15 million, in that range, coming off of that. So, all of those things are factoring into our thinking to try to develop and deliver margins that will expand even if the markets are flat.

William Katz - *Citigroup - Analyst*

That's very helpful, and then Marty a quick question for you. I'm curious, you had of a couple of things of why you are gaining some share in the United States, but the conversation on the multi-asset being here for a bit of time, just tell me where that is coming from in terms of what's shifting

within the retail distribution? Is it just a shift from product sales, is it a specific asset class, is it share gains, what's your sense of what is driving that unit growth?

Martin Flanagan - *Invesco Ltd - President & CEO*

Yes, so it is really very broad, Bill, were seeing it from retail to institutional and really around the world, and I think really what it is doing is -- and again it's going to be different in different parts of the world, why we're doing it, but much of it is bringing the capability that across different asset classes, which is not necessarily inherent, I'd say. I'd say it's also the repositioning of really the advisors in the channel where they are much more taking on a broader role and a very constructive role of broader advice and asset allocation, and these really work within it. And as we've been doing some of the capability extensions into income elements around it, and there is elements of commodities capabilities within it, so you're really getting some asset class exposure and some constructions that meet the investment needs of the different clients. So, it seems it's going to be here for quite a while.

William Katz - *Citigroup - Analyst*

Okay thanks and just last one. Curious are there any update or thoughts on money market reform? I guess there's been some movement to a selective redemption gate at the core level. Any thoughts of what you're hearing in the regulatory discussions?

Martin Flanagan - *Invesco Ltd - President & CEO*

Not -- really not so much at this time. I mean I think there are -- there has continued to be ongoing conversations within the industry as have been for the last four years, and again, I think it is just a very constructive set of dialogues. And we will just have to see what the ultimate outcomes are, but again, I feel that the money fund vehicle is a very good one, and it's going to remain one. But it will continue to play out I think over the next months, quarters, and well into next year.

William Katz - *Citigroup - Analyst*

Okay, thanks for taking all of my questions.

Operator

Our next question does come Matt Kelley of Morgan Stanley. Your line is open.

Matthew Kelley - *Morgan Stanley - Analyst*

Just wanted to come back to the margin, sorry for beating a dead horse here, but looking at your operating margin versus the overall industry, and arguably you are at as strong of a point you have been in the recent past for flows in performance. Do you think your margin relative to peers could substantially grind higher? If we are thinking about 35% now, is 40% out of the realm of possibility, and how do you think about yourselves versus the industry-wide margin?

Loren Starr - *Invesco Ltd - CFO*

So, Matt, we definitely would not view 35% as sort of the only margin that we aspire to or where we are forced to be at. We would absolutely expect to see our operating margins increase over time as our assets grow, and as our net revenue yield hopefully begin to continue to increase and trend forward. So, it's been, if you go back and try to figure out what happened to Invesco, why margins are where they are, and we have seen our net revenue yield decline substantially over the last several years. Despite that, we kept assets growing and so margins have probably been stayed

roughly flattish, and that has been the real situation. For us to be able to see our net revenue yield increase over time will require obviously the continuation of some of these new products with higher fees that are in very significant demand, and we are seeing that, now, which is a very positive trend for us, and we also believe that if you do continue to see equity markets stabilize, and maybe improve from here, we will begin to see the net revenue yields increase. Our basis plan is obviously a huge topic, right? It is \$65 million in the year. If we can continue to see that trend on top of good organic growth, margins will expand and will see them into the 40% and above.

Martin Flanagan - *Invesco Ltd - President & CEO*

Yes, I agree with that, and I would also add to it if you do look during this period that Loren talked about, go back to 2005 and look at operating expenses as a percentage of average assets under management, and I don't have the numbers in front of me, you'd think I have them indelibly in my brain, they have dropped quite dramatically during that period, I mean substantially. And as Bill was asking earlier and others, we continue to be very focused on always being more efficient, more effective all the time, and we do that. But we are not going to have that magnitude level of efficiency gains that we created over the past five, six years.

But again, at the same time you just do the math and watch the effective fee rate during that period, it dropped dramatically, and if we had not been as strong of operators as we were, it would have really been a really bad outcome. But to Loren's point, we think there is no reason that we shouldn't start to see the effective fee rate increase, based on the capabilities we have and where we think investors are starting to move -- make their asset allocation decisions, and where they think they're going to go, going forward and you get any wind at your back, and it could be quite a good story for the margin.

Matthew Kelley - *Morgan Stanley - Analyst*

Okay, and then I wanted to ask you guys about the team you hired from Standard Life GARS in the UK. I've seen the press releases about how much they were managing over there, what are your plans for folding them into your multi-asset platform? Is it going to be more of a new fund, or are they going to dovetail off of the balance risk platform? How do you think about that?

Martin Flanagan - *Invesco Ltd - President & CEO*

I don't know if I got the question in total, Matt, but I think you said what are the plans ultimately. So obviously they have a tremendous reputation and it's going to be some time before we are in the market with a capability in the United Kingdom. It will be into next year just for all sorts of various reasons. Initially, the focus is going to be a suite around the existing Invesco Perpetual capabilities, which again, are very highly regarded as you know, from your background in the United Kingdom.

And we think that is a very strong complement to the existing multi-asset capabilities that we have, and that is how are looking at this really around the world, what can be global, and how do we meet some of the local needs. And we think this is going to be a very powerful one in the United Kingdom, and from there we will just see where it goes. Again they have a great reputation. We think it is extremely complementary and a part of what we have, and again, as part of the overall plan that we're trying to accomplish.

Matthew Kelley - *Morgan Stanley - Analyst*

Okay, and just one quick last one from me. Just on the PowerShares platform, be curious to get your thoughts for future expansion there? Do you think you're pretty well set up with your current product line-up or any products you think you would be interested in adding or potentially subtracting from your existing platform as well? And how much associated operating leverage do think you can get from that platform as well?



Martin Flanagan - *Invesco Ltd - President & CEO*

Well, if you look at the line up over the last couple of years, I think the team has done a very good job in sharpening it, both from strategically introducing capabilities, and quite frankly, winding down some that we didn't think made sense anymore. So that is from a US perspective. And there will continue to be natural product development over time, but it probably will not be as robust as activity as you saw over the past few years in the United States.

What you have seen has been an extension into different markets, into Canada, that has been very successful. We have some reasonably good plans into the greater China area, in particular, we think we are positioned very well there. Europe continues to be an area that we are looking at, it's an area that we have been there for some period of time, and we have not made the inroads that we would have hoped, but again, it is a very tremendously changing environment, as you know, in that part of the world. But we think we are still early days on where we are going to go with our ETF capabilities globally.

Matthew Kelley - *Morgan Stanley - Analyst*

Great, thanks.

Operator

Roger Freeman of Barclays, your line is open.

Roger Freeman - *Barclays Capital - Analyst*

First on the IBRA products, I think you said they were 43% of long-term flow this quarter, 25% last quarter. I think you just hit the three-year performance benchmarks right before your earnings call in July. I'm just wondering if this is a run rate reflective of that, or still in a ramp process? It probably still is, right?

Loren Starr - *Invesco Ltd - CFO*

It's always fun to see exponential growth extrapolated. We definitely view -- there's very definitely continued demand for the product, and it's hard to say whether it stays at the same pace. Sometimes we saw it takes a breather and then it comes back, and so there is probably some degree of seasonality in terms of even how the platforms take on these products, in terms of their selection. And I think October is -- there may be times when they start thinking about these things. So, it is certainly something that we think is going to continue to grow, and even globally we think it has got huge opportunity, not just within the US. So, I'm not going to pour too much cold water on the trend other than, I can say fourth quarter is going to be exactly as strong as the third quarter, because that was certainly a very exceptionally strong quarter.

Roger Freeman - *Barclays Capital - Analyst*

Okay, and then Marty, you had mentioned earlier that you've gotten up to number 10 on brand recognition. I think you had said that is where you were back on the 4Q call in January, and you also said the hardest part is going up from 10 and working your way up that ladder. I'm just wondering where you are in pursuing that, and maybe you haven't been an updated market survey, if you have moved up since then, but just your thoughts around that?

Martin Flanagan - *Invesco Ltd - President & CEO*

Yes, so, again, we've made great progress from, frankly no recognition. And our view is that we don't aspire to be number one, we think that would just be -- we don't think you need to be, and we don't want to spend the money to be. We don't think you get that benefit. 10 is an important place

mark, quite frankly if we were -- we would probably think if we were somewhere 4 to 7, that is a pretty fine place to be so we are going to continue to work very hard to build our reputation. But again we think your reputation largely gets built by generating very good investment performance, and it's really the recognized leadership through investment performance, and we're going to do it, but don't worry, we are not hell bent on -- we are an investment management organization driving investment results, and we're not hell bent on becoming Coca-Cola.

Roger Freeman - *Barclays Capital - Analyst*

Certainly to tie to that, lastly in retail as you point out the redemption rates came down a lot. They did for the industry as well over a number of quarters. Over the past year you have widened the gap, and otherwise redemption rates have been lowered by a greater degree sequentially, they were again this quarter. Just wondering if the moves are more industry related with a number of firms are pointing this out, or are you are seeing any incremental benefits of that Van Kampen combination in terms of some of the older funds that were underperforming, seeing those redemption rates come off as people move into stronger products or anything along those lines?

Martin Flanagan - *Invesco Ltd - President & CEO*

Yes, so, I sure hope it's an industry trend for decreasing redemption rates. I just think it's the exact right thing for clients, personally, so that is the first place I would start. We have been very fortunate to have our redemption rate be quite low. It is a combination of, again, starts with a very strong investment performance across the complex. There is no question the Van Kampen combination has been a very important one for us, bringing investment talent into the organization and other talent generally, so that has been a positive, also. And at the same time, when you are growing, and you have capabilities that are of interest to clients and they're investing in them, those all three add up to a relatively lower redemption rate than that of the industry. But I would come back to, I sure hope there is an industry trend down, because I think that is really good for investors ultimately.

Roger Freeman - *Barclays Capital - Analyst*

Okay, all right, thank you.

Operator

Glenn Schorr of Nomura, your line is open.

Glenn Schorr - *Nomura Asset Management - Analyst*

Loren, are the Van Kampen fee waiver roll-offs fully in the run rate now? I just don't remember where we are at in that process?

Loren Starr - *Invesco Ltd - CFO*

Yes, Glenn, they are. So that is \$7.5 million per quarter is in there, so that is part of the [24] basis points, I think is what that translates to an annualized basis. So that is some of the benefit going from -- on our yield before performance fees increase.

Glenn Schorr - *Nomura Asset Management - Analyst*

Okay, cool. You noted it before, but there seems to be a real divide between real strong performance in US equity and then other outside the US. I'm curious, A, I expect that flows treat the same, in other words you just have a little bit better flows going on inside the US versus out and more importantly, is there a common thread on the investment theme across the non-US geographies that is leading to the underperformance?



Loren Starr - *Invesco Ltd - CFO*

You're looking at some of the charts that show some underperformance in some of our regions, is that from regional equity?

Glenn Schorr - *Nomura Asset Management - Analyst*

Correct, slide 20, I think is the best one.

Loren Starr - *Invesco Ltd - CFO*

Yes, I don't think -- it's hard to say there is one basic theme that captures what is going on there. I think when you look -- I mean we have some spots of underperformance, but they are not connected or related. The Asian equity bit, maybe some of our Chinese equity, China has been depressed and probably the impact has been worse there than people anticipated with our investment teams, as one example. But there isn't any theme, and Marty, jump in.

Martin Flanagan - *Invesco Ltd - President & CEO*

Is if there is one area in particular, that we have a very good Japanese investment team that frankly came over from Morgan Stanley during that combination. They have a very good long-term track record, very good investors, and a lot of their investment focus has been an export-oriented theme and its relative performance has been hurt over the last 12, 18 months with some of the challenges in Japan in particular. But again it is a very strong team and they are the ones that are feeling the relative underperformance at the moment.

Loren Starr - *Invesco Ltd - CFO*

I would also say Canada, which is another example, it is a great turnaround story. You don't really see it in that chart, but their five year performance is going to increase as we get towards the end of the year. Their whole performance profile is really dramatically improved, so the one and the three year numbers look fantastic and five years are going to follow. So again, these probably give equal prominence to it, and if you did on the asset weighted basis clearly it's not as equal.

Glenn Schorr - *Nomura Asset Management - Analyst*

No, it is a single digit percentage AUM, that's why asked the question on if it's a heavier percentage on the flows. Anyway last question, a lot of people dance around the margin issue. I guess if you decompose it, this really comes down to comp ratio, where you stand out towards the high end versus a bunch of peers, and I just don't know if it's something related to payout either A, on the Van Kampen deal, or B, just more broadly on how comp is structured. When you comp yourself relative to the peers, are there a few things that would tend you to be on the high end on the comp ratio side, and as this continues to boost, the way you did this quarter, does that bait over time as you grow into your strong performance?

Loren Starr - *Invesco Ltd - CFO*

So, what I would say is the vast majority of our compensation is driven by investment teams, they are at the heart of it. In the Company, in terms of what they are ultimately delivering and I think we have a common philosophy that may be more unique to Invesco than some of our peers, in that we pay more on investment performance than we do on a revenue share concept. And so people who pay on revenue share or have a higher percentage of their comp directly tied to revenue have a different philosophy around how they want to pay their investment teams. And we think ultimately it is the right thing for our clients to provide incentives that are linked to what the clients want, as opposed to something dropping out due to where the markets are going today.



And that I think is maybe some elements of what is unique, and perhaps the other element, which is again a strength of the firm and one that we feel really good about is that we have many different capabilities across the globe that ultimately give us a better diversified offering to our clients than many of our peers. And so, we should be able to grow more effectively. We should be able to provide solutions to our clients in a better way as a result of that, but that is a more expensive proposition than just having one thing, which again, I don't say our peers have one thing, but we probably have more of capabilities than some of our peers.

Glenn Schorr - *Nomura Asset Management - Analyst*

All right. Thanks, Loren.

Operator

Our next question does come from Cynthia Mayer of Bank of America. Your line is open.

Cynthia Mayer - *BofA Merrill Lynch - Analyst*

Briefly on RDR, I think we are in the final quarter before it goes into effect, and I'm wondering if you expect any impact of this quarter, maybe front-loading of sales? And then when it does go into effect, would you expect, what kind of impact are you expecting at this point, in terms of sales and redemptions? If the share class, for instance is grandfathered, would you expect lower redemptions ahead? Thanks.

Loren Starr - *Invesco Ltd - CFO*

Yes, those are really good questions, Cynthia. We obviously have set up share classes that respond to the requirements to only have a management fee associated with the products that will be flowing. So all the new flows coming in off of January 1, 2013 will be in this new share class, but you are right, existing assets and products with clients are grandfathered. So, I think the real question will be to see what the advisors, the IFAs do in that context, and in some cases they may rather just transfer everyone into the new share class as opposed to having the two share classes, but we don't know yet, really, how that's going to work. It doesn't have an impact on our business from a profitability perspective one way or another, we are still netting the same management fee under both scenarios.

It could create some activity in terms of people switching and exchanging, but that should not do anything really in terms of ultimately the bottom line, we don't think. So, were watching it carefully. We are still -- hard to predict exactly what happens, but I don't think it's going to happen in a dramatic way, I think it's going to be -- people are going to take some time to think about how it's going to go.

Cynthia Mayer - *BofA Merrill Lynch - Analyst*

Great, thanks. And then maybe just in terms of the revenue yield. When you look at your near record pipeline and you look at the mix of that, is the mix of that any different from your current revenue yield?

Loren Starr - *Invesco Ltd - CFO*

It is better. It is improving. So, we are very pleased by the net revenue yield coming in at a higher rate. And certainly and also to be [similar to] redemptions, those are at a lower rate. So we are seeing lower fee product going out and higher fee product going in, and a lot of these alternative products, and certainly the balanced risk types of products are at a fee rate that is at or higher than our current rate.



Cynthia Mayer - BofA Merrill Lynch - Analyst

Great, and then just maybe finally I think you mentioned, sorry if you mentioned this already, but G&A stepped down a little bit, is that G&A a sustainable level for 4Q?

Loren Starr - Invesco Ltd - CFO

We think it is. We are seeing some investment of Minerva, I'm sorry, that's the code name, forgive me. It is the outsourcing of our transfer agency business, forgive me for using code names. That is -- we are beginning to see some of the benefit of that fall into our G&A line item. We would expect to see more, we said it is something that is going to move into the first quarter, so the ultimate positive impact of run rate savings will be achieved as we get into 2013, but we're going to begin to see -- we're beginning to see some of it in this quarter, and some of it in the fourth quarter as well. So I think that G&A numbers should stay now. The only offset to that is, and we talked about it last quarter, regulatory requirements and legal and all these things associated with positioning ourselves in the geographies we are in is becoming more and more expensive. And so that is a counter-theme to some of the savings that we are expecting to get from this outsourcing activity.

Cynthia Mayer - BofA Merrill Lynch - Analyst

Great, all right, thanks a lot.

Operator

Jeff Hopson of Stifel, your line is open.

Jeffrey Hopson - Stifel Nicolaus - Analyst

Thank you. The balanced risk product, I'm not sure if you gave us any sense of the geographic breakdown, US versus non-US and any change in the momentum of some of those products in Europe and the UK?

Loren Starr - Invesco Ltd - CFO

Good question. So, they're going to be mostly US-based at this point. So as of the third quarter, 75% is US-domiciled. We've got 12% in Canada and about 13% in the offshore in the UK. So, again, a growing piece outside, but it is still the minority, and that is why we think this opportunity is pretty large, that we could obviously do what we did in the US in these other regions, it will be truly amazing. And yes, just back in the fourth quarter of 2009, it was all US. So, that just gives you a sense of it beginning to grow.

Jeffrey Hopson - Stifel Nicolaus - Analyst

Okay and so is it an issue of track records in those regions, or just how long the product has been really focused on, or what are the issues as far as why it isn't bigger over there and why it could be bigger in the next quarter or years?

Loren Starr - Invesco Ltd - CFO

So, let's say for Canada for example obviously the market is only so large, but the take on it has been huge. I think it is one of the fastest growing capabilities in that space, that we're doing very well there in terms of cash and really good flow. Outside of the US, it is doing well in Europe, so I think that is one that is getting fully sized. The UK, it is a pretty new concept and so there is still a fair amount of education, which was the same as it was in the US, and that takes probably a year at least and it was only launched I think at the beginning -- yes February or sometime. So, there's



definitely time that needs to go by for ultimate results to take hold, but we have good hope that it will, and certainly some of the new hires that we have there will also help expand our presence in UK in terms of all the offerings in the multi-asset sector.

Jeffrey Hopson - *Stifel Nicolaus - Analyst*

Okay. And you mentioned about the institutional pipeline, but any other sense of what has happened here in October, in terms of flows across the regions? What are investors doing any different in October versus the previous few months?

Loren Starr - *Invesco Ltd - CFO*

Yes, I think it's a little hard to drill down in a particular month, probably much better to look at it within the quarter, only because what happens in any particular month has a lot to do with just noise on timing and things of that nature. So, I'm just going to defer on that one if that's okay, Jeff, to avoid making a statement on a trend that doesn't really exist.

Jeffrey Hopson - *Stifel Nicolaus - Analyst*

Okay, but have you seen any change in behavior, I guess, of investors, generally, would you say?

Loren Starr - *Invesco Ltd - CFO*

I don't know, I mean, obviously, there's the macro theme of coming up to election and people being a little bit skittish about where to put their money because they don't understand what the fiscal cliff is going to mean to the markets. And so, yes, I think there are some sense of a little bit of risk off relative to what we might have seen a little bit earlier, but again, I don't know what is going to happen after the election. Maybe it will be something else.

Jeffrey Hopson - *Stifel Nicolaus - Analyst*

Sure, okay, great. Thank you.

Operator

Our next question does come from Eric Berg of RBC Capital. Your line is open.

Eric Berg - *RBC Capital Markets - Analyst*

You've talked at length about, repeatedly and in detail, about the growth of the asset allocation product and the rise of your international business, but it is also the case that the domestic business, at least for the industry, US equities, has been an outflow for the industry for many months. Indeed, if you look back for 10 years, it appears that this outflow phenomenon from domestic equity funds is really not new, it even predated the financial crisis. So my question is, what is really the thinking on what is going to take to reinvigorate US domestic funds, or maybe this is a permanent trend away from them that we are seeing? I'd like to get your thoughts. Thank you.

Martin Flanagan - *Invesco Ltd - President & CEO*

Good question, I wouldn't bet on that it is a permanent trend, and I think what you ask, and again, I think it's easy to come to that conclusion. I think what you would do though if you look at flows into equities in total, and in total meaning active and passive, you get a different outcome. I



think an awful lot of people are extrapolating that to say active US equity investing in the United States is dead. And I think it is a misread. I think it is movement into passive is really a first step onto risk-on, but I think the more relevant fact if you look at what is happened in the marketplace post the crisis, and if you look at the correlation of returns to market events as opposed to stock-taking events, it is very high.

And I'm going to forget, it is basically a 90% correlation of returns coming from macro events as opposed to stock-specific events. That is probably 25 percentage points higher than historical. That is the same phenomena that you saw at the end of the 80s, post the '87 crash into the 90s, and when you get these correlation period you don't get paid for -- active investors have a hard time generating alpha. So I personally think that is the thing to pay attention to, and we would go to a -- I think as you look forward and if probably the United States is probably further ahead on healing itself economically, and if that is the case, I think active equity investors are going to generate alpha again and you will see -- more broadly they will -- you will see money flow back into active US equity capabilities. So that is my perspective, and I think it is important and something to take a look at, the correlations of returns.

Eric Berg - *RBC Capital Markets - Analyst*

Thank you.

Operator

Our next question does come from Robert Lee, of KBW. Your line is open.

Robert Lee - *Keefe, Bruyette & Woods - Analyst*

Most of my questions were asked, but I did have one question. On their call a couple of weeks ago Blackrock talked about merging their iShares sales force with their US retail sales force. Could you update us on and remind us how you integrate the PowerShares products into your retail distribution, or if there's any need to change how it works now?

Martin Flanagan - *Invesco Ltd - President & CEO*

We've been doing that for years, so that is not a new thing for us. When we bought the idea of ETFs, we had made the observation in 2005, 2006, that we thought the advisors were moving much more to a holistic approach, and advising their clients, and that it would be first and foremost, it's meeting the investment objectives, and then they would look at the different vehicles that did that, and naturally asset allocations and meeting those needs for a combination of vehicles. So, we've been doing that for really almost from the beginning of the combination with PowerShares. So, we say that is a good idea.

Robert Lee - *Keefe, Bruyette & Woods - Analyst*

That was it, thanks for taking my question.

Operator

The next question does come from Christopher Schultzer of William Blair. Your line is open.



Christopher Schulter - *William Blair & Company - Analyst*

One quick one, it looks like the performance in the US and foreign growth remains challenged on both a one-year and three-year basis, so I certainly recognize it takes time to rebuild those capabilities, and those categories certainly aren't in favor today but just one get your thoughts on performance there, and how you're feeling about the teams and products we have in place?

Martin Flanagan - *Invesco Ltd - President & CEO*

Let's see, two things, and it is backed almost the question before, two questions ago. If you want to see where the bulk of the outflow is coming in the US, it is large cap US growth as a category. For us specifically, the team running large-cap, mid-cap has been with the organization about two years, we think they are really very talented people, and have good investment capability. And this gets back to a little bit of my answer earlier where a lot of their investment philosophy is driven by stock picking, and it has been challenged in this environment. So, that said, we think the team is very good, and they have had a history prior to being with us as having very good results, and we think they will generate them in time. This has not been the environment for their investment philosophy. That said, if you look at the small cap growth capability, it is very strong, and continues to be.

Christopher Schulter - *William Blair & Company - Analyst*

Okay, thanks a lot.

Operator

The next question does come from Marc Irizarry of Goldman Sachs. Your line is open.

Marc Irizarry - *Goldman Sachs - Analyst*

Marty, can you talk a little bit about the alternative business for you? How you think about building out strategies there? What is weighing on flows? Where are you seeing some success? And how do you think about building versus buying in that business?

Martin Flanagan - *Invesco Ltd - President & CEO*

So, again, I think you have to go asset class by asset class and some of it would be repetitive, but very good with real estate, feel very good with private equity. Feel very good in bank loans. Feel very good about some of these extensions that we have through our multi-asset suite and our asset allocation capabilities, whether it be commodities or some other areas there. So, we just continue to look at it and look at where demand is, and if we are capable of meeting client needs, we will respond.

In fact, one of the trends that people have talked about, and I wouldn't get too excited about it, but there are alternative capabilities that are appropriate and growing quite dramatically in the retail channel, and we've seen that ourselves and we are continuing to develop that. We just introduced in the last couple of months, another really alternative capability into the retail channel. It is directed toward high net worth individuals, qualified investors. So, just being very appropriate. And so I think we will continue to see those things, but we think we are positioned really quite well to do strongly throughout the alternative capability as a firm, and we would just continue to respond where necessary.

Marc Irizarry - *Goldman Sachs - Analyst*

Okay, great. Thanks.



Operator

Our next question does come from Gregory Warren of Morningstar. Your line is open.

Gregg Warren - Morningstar - Analyst

I'm glad you guys touched on the issue with US stock flows, because it's an opportunity or a situation where people tend to focus on the headlines, on just the active side. If you really hold up the passive of flows and strip out American funds, which has a heavy influence on that active side, the flows don't look as dire as the picture that gets painted with the headlines. So, I'm glad you pointed that out, and I guess my question follows on where we are with the flows.

How do you from a longer-term perspective think about allocating resources, given what is going on now? It's easy to throw money at Fixed Income or multi-asset class products or structured products in an environment where those things are selling. How do you think about allocating capital to equities? Because we have seen a few of your competitors year after year come out and do marketing campaigns or other programs to say, equities are still here?

Martin Flanagan - Invesco Ltd - President & CEO

Yes, so, let me see if I can answer that in two ways. One, we just start from a position of what are we trying to do for our clients? And our view is that we are committed to having a broad and deep capability across asset classes, equities through Fixed Income. We are very strong in equities in particular and to your point, even as you were more articulate than I was as describing the US equity picture, we have very good, strong teams. We are committed to the strong teams, and we just know asset classes go in and out of cycle. And so, we are absolutely committed to them through the cycles, and we want them dedicated to delivering against the investment philosophy that they are known for and that they delivered.

So, to your final point, so what we do about it? And if you look at, again, how are we -- and I'll answer more from a retail channel point, but it's not limited to that -- if you look for the last two years, what have we been communicating with our investors, with our clients, is that we have been showing them the benefit, making very clear the benefit of a combination of capabilities, whether it be a US equity capability, a US income capability, an international equity capability, so we've been doing that for more than two years. And we think it's -- we want to be very thoughtful and appropriate in making sure that you are giving investment guidance that makes sense for clients over the longer-term, and not be responsive to where flows go, because we think that gets you in trouble.

Gregg Warren - Morningstar - Analyst

Okay, okay. And I guess thinking about equities overall, when I was looking through the flow data third quarter, you saw outflows pretty much on par what we saw last year in the third quarter. And a huge difference in performance in the markets, and yes, with the fiscal cliff coming, there is the elections, but I don't think it was as dire of a situation. So when I start looking at the performance numbers overall for active funds, it seemed to be that on a relative basis, pretty much every category was underperforming this year, like it was last year. And I'm wondering, do you think it's a matter of performance getting better? If you start having active managers outperform the markets, that sort of is the catalyst to get people back in?

Martin Flanagan - Invesco Ltd - President & CEO

Yes, so, I think that relative performance, active versus passive, is back to the comment I made earlier. I think it's really the market environment we are in is the 90% correlation to macro events and to your point that you were appropriately pointing out earlier, and I talked about the point of, it is much better if we are giving -- the advice channel is encouraging people to be invested for the longer-term, if you take a three to five-year time horizon, I really want to be investing in US equities. I think it is going to be one of those things you're going to look back three years from now and say, why didn't I have greater exposure to US equities? That said, I would be going to the managers that again, you all from what you do are committed to very good teams, very good long track records, very thoughtful investment philosophies and processes, and you're going to do very



well, and I think the reason why the money is not going into active equities is more, it feels like a bigger commitment on an investors' part, and I think you cannot underestimate still how nervous investors are to invest for the long-term in the environment that we are in.

Gregg Warren - *Morningstar - Analyst*

Yes, that is the same thing we're hearing across the board. Well, thanks for taking my questions.

Operator

Matt Kelley, Morgan Stanley. Your line is open.

Matthew Kelley - *Morgan Stanley - Analyst*

One quick follow-up from me on the capital management side. You have a pretty sizable amount of debt coming due in late February, and I just wanted to touch on it, because I don't think we've discussed it this quarter. What are your thoughts there in terms of extend or retire or some of both, or how are you thinking about it at this point? Thanks.

Loren Starr - *Invesco Ltd - CFO*

Matt, it is a good question. I think we are looking at it, obviously it is a unique opportunity in terms of, you could issue debt and replace it at a very low cost or you could let it expire and just put it on the credit facility. They both can make a lot of sense. So, I would just say it's something we are looking at. We haven't committed to one way or another as to where we are going to go on this one, but we are -- definitely we've been looking at it quarter by quarter, and we will continue to pay a lot of attention to that opportunity. But overall, we are committed to keeping the debt levels flat or declining over time, as we want to continue to deleverage and show continued financial strength, and certainly build up some more cash on the balance sheet. So that is still part of our objectives on the capital side, combined with, of course, continued and dedicated return of capital through dividends and buybacks as you have seen us do and as you will continue to see us do.

Matthew Kelley - *Morgan Stanley - Analyst*

Great, thanks, Loren.

Operator

At this time, I show no further questions.

Martin Flanagan - *Invesco Ltd - President & CEO*

Thank you very much everybody, for the engagement and the dialogue in particular, and I will be speaking with you next quarter. Have a good rest of the day.

Operator

Thank you. Today's conference has ended. All participants may disconnect at this time.



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