Invesco Ltd.

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Alexander Blostein: All right. So we're going to get started with our next session. Next, I'd like to welcome the management team from Invesco. With us today are the Company CEO, Marty Flanagan, and CFO, Loren Starr.

Following the acquisition of OppenheimerFunds, Invesco's now one of the largest global asset managers with over $1 trillion in assets under management across a wide range of products and capabilities. With the industry clearly undergoing lots of change, we look forward to getting an update from Marty and Loren on how Invesco's positioned to return to positive organic growth, hopefully over the next few years and, also importantly, getting your perspective on the evolution of the business broadly. As I mentioned, obviously there's a lot of changes happening in the asset management landscape. So, thank you guys both for being here.

So I guess it makes sense just to get started with an update on the integration. Obviously, you guys have taken a lot of costs out a little bit faster and a little bit larger amount than originally thought. So maybe give us kind of mark-to-market, so to speak, on where we are in the integration process, lessons learned so far and, more importantly, your kind of priorities for the Oppenheimer deal as you look out into 2020.

Marty Flanagan: So let me start with an update on where we are with the integration. So last quarter represented the first full quarter as a combined organization. Everything's gone largely to plan and let me -- you've seen the financials are coming through just exactly as we described, although the savings earlier and greater than anticipated. You would anticipate that would be the first thing that you would get through. Very importantly, the organization is in place. All the people are in place. Everybody's in their roles, moving forward. All those things have been done.

The premise of the transaction was multiple issues. One, bringing on a set of capabilities that -- largely around the international capabilities and the like that can go beyond the private wealth management channel around the world. So, they're now in market in Europe. The institutional pipeline is starting to build with some of the Oppenheimer historical capabilities. So early days, but that's important.

The other premise was being important within the largest wealth channel in the world, the US wealth management platform. That is in place. That has been the most disrupted, and we knew that going in, from the standpoint of if you look at that distribution organization in particular, it's now made up of half Invesco, half Oppenheimer. So that really has been - if you want to call it - a sales headwind, but we're at a stage where we look at January 1st back into sort of business as usual.

So what didn't go so well, the [transfer agency] conversion was the largest in the industry. That went very, very well. But what we didn't see, there was a service issue of a piece of software that didn't come over. So, our sales force was not in sales mode but in really service mode. That's all been taken care of. So we look at January 1st as the beginning of the combined organization business as usual and moving forward.

Alexander Blostein: That's helpful. So zoning in on that, I guess the last issue, if you look at Oppenheimer kind of legacy close -- and they have obviously a lot of mutual funds so people can really kind of track what's been going on there -- there's been about $2-ish billion on monthly outflows from like kind of legacy Oppenheimer's. Is that the issue? Because if you look at their performance, it's actually improved over the course of the year.

Marty Flanagan: Yeah.

Alexander Blostein: So do you kind of really think of that being a gross sales issue on the back of the legacy Oppenheimer structure as opposed to anything fundamental.

Marty Flanagan: Very much. And let me give the absolute color. People are people, right? So you literally had both sales forces wondering if they're going to have a job, right? And so that -- until that's clear--

Alexander Blostein: Right.

Marty Flanagan: It's very hard to move forward. And then the training that comes around the new product lineup. You also have the wirehouses in particular slowing down until there's clarity within the organization. Those things are all happening. So it's largely a gross sales issue, but there are a couple areas where there's been bank loans and one of the international products where there's been some underperformance. So I don't want to miss that. The international product, actually the performance is coming back very nicely.

Alexander Blostein: Right. On the equity side it's actually--

Marty Flanagan: That's right.

Alexander Blostein: Doing pretty good this year.

Marty Flanagan: Yeah. Exactly.

Loren Starr: Now something -- the other thing I'd say just in terms of the cost and the synergies, we were fortunate, as Marty said, to get a higher level of synergies earlier on than expected. We are still working through some of the other parts of the integration that will provide more savings through the course of 2020. There are probably some tens of millions of dollars to be had between technology, product rationalization, other things that are still to be done in 2020. Again, where we are right now, though, we're still looking at opportunities to invest relative to drop to the bottom line. And so the 501, which is a number that we've talked about, is still the one that we're providing guidance to, but we'll be in a position to give more thoughtful response as to how much might drop to the bottom line in 2020 as we get through this.

Alexander Blostein: Got it. You jumped ahead a little bit on my--

Loren Starr: I'm sorry.

Alexander Blostein: Next question, but we'll get there.

Loren Starr: Okay.

Alexander Blostein: Why don't we kind of go back there I guess for a second. So as you think about the areas of incremental savings, can you spend a little bit of time of kind of where could they come from? How do you guys ensure that that doesn't actually disrupt any of the revenue targets there or any revenue improvements that you're trying to go after? And if you were to take a guess in terms of how much of that could drop down to the bottom line versus get reinvested in the business, any sort of framework to help us think about that would be helpful.

Marty Flanagan: Yeah. Let me give -- so every firm has some language, so our language is this is day two. So day two is basically technology platform opportunities. And I'd say some of the developments of the service providers are very positive because you can now have more holistic solutions on your platform. That's a day two for us and that will take us probably into 2021. I mean it's -- those are big undertakings.

My point is it's more operational efficiency effectiveness, driving down per unit cost of production on a permanent basis, but also taking out money. So it's not a disruptor to the revenue side. It's not looking at client-facing people or teams. So it'll be much less disruptive than anything that we've gone through over the last 12 months here.

Alexander Blostein: Yeah. One of the key points when you guys announced the acquisition was potential linkage between MassMutual and the distribution force that they have which is over 8,000 financial advisory, I think 8,500 or something like that. So can you maybe update us on where we stand in you trying to pursue that channel a little bit more aggressively? Any kind of updates on timing? And really, which products do you think could gain the most traction through that channel?

Marty Flanagan: Yeah. Let me make a couple comments and Loren will also. So the first part, the partnership's gone very well. I'm committed to it. Roger Crandall, the CEO of MassMutual, is 100%. The top leadership of both organizations are focused on this and that continues.

There's the obvious 8,500 wealth team here in the United States. Multiple efforts are -- product extensions onto platforms, models of course, what can we do with some of the solutions engagement. So that's all happening right now. It's probably a 2020 event before you start to see things kick in. Opportunities around the general account. Asian real estate is actually an area that's being looked at right now. But it's more holistically looking at things that we can do together. So it's -- I feel quite confident about it.

Alexander Blostein: Shifting gears a little bit, I want to touch on the US intermediary landscape in terms of distribution capabilities. Obviously, it feels like lots of change in that part of the model over the last couple of years as the distribution partners continue to sort of demand more from the manufacturers that they partner with, and whether it's really expansive product set and capabilities, model portfolio, separate accounts, etc. Give us a bit of an overview. What are you guys -- where are you guys positioned right now with Oppenheimer in US intermediary? And any sort of shifting in economics we should be mindful of which would potentially accrue to the distributors from the manufacturers?

Marty Flanagan: Yeah. Look, I think you're understating the change in that landscape. We start with basic fundamentals. It continues to be the largest pool of assets in the world. It is the most competitive pool of assets in the world. And every distribution partner is on the path to continue to work with fewer money managers.

And what you're talking about, managing money is not enough. You need to be able to build models. You need to be able to be a solutions provider. You need to do thought leadership. You need to have the wherewithal to help their sales forces be more effective. You're literally partnering with them. You need to have the ability to invest in digital to be effective in those channels. And so what that really is doing is just by -- you have to have the breadth and capability and resources to pull that off.

So, if you don't have scale and the range of these capabilities, you're not going to be successful and I think that's what you're seeing. I think -- so if you are not a fully resourced organization, you're just not going to be competitive and that's what you're seeing right now. And again, that was fundamental to one of the reasons why Oppenheimer was so important to us. We're now the sixth largest money manager within those platforms and we have all the range of capabilities that you just outlined there and that's a difference maker going forward.

Alexander Blostein: Yeah. Another pretty important change in the US retail space, obviously, has been the pending merger between Schwab and Ameritrade. So I want to get your thoughts on how important is the kind of Schwab/Ameritrade distribution channel for Invesco/Oppenheimer combined, and really more broadly speaking, implications from that merger on the ecosystem?

Marty Flanagan: Yeah. It's a very, very important relationship for us. It has been historically and will continue going forward. It's probably the second largest relationship that we have if you look at assets under management on their platform. For us, it's materially -- it's dominated by ETFs for us. We have historically been the largest ETF provider on the Schwab platform. And this change where -- I think for ETFs -- and I think it's become sort of a common thought right now -- it's good news if you're an ETF provider.

But what I'd also say, I would take it to another level. It just upped the bar on the ability to be competitive as an ETF provider. I think if you don't have scale in ETFs and a breadth of capabilities right now, it's going to make it just that much harder to be an ETF provider going forward, because of the demands on such a large organization and what they're trying to accomplish with the [RAAs].

Alexander Blostein: Yeah. Maybe pivot a little bit onto non-US distribution. When I look at your footprint in UK and EMEA, it's been a bit of a perfect storm in many ways for Invesco over the last couple of years there.

Marty Flanagan: Yeah.

Alexander Blostein: Help us frame I guess the opportunity maybe you see in that part of the market as we get closer to Brexit and they get some sort of resolution. Any kind of intel you're getting from some of the distribution channels in terms of money on the sidelines that could eventually make its way back into the products and how you guys are positioned?

Marty Flanagan: Again, you framed that very, very well. Historically, the UK or the EMEA business for us has been the strongest part of the organization historically. When Brexit first got announced, it really -- it was a lot of news, but really didn't start to impact business so much. The last 18 months, in particular last year specifically, have been very difficult as Brexit became quite real.

If you look at gross sales in the UK and on the Continent, using products as a proxy, they just literally dried up and so you just saw a risk-off mentality take hold. And if you take it to the next extent within the United Kingdom, it was our largest, most successful market which turned into an incredible headwind. And we happened to be the largest in the UK equity asset category, which became an asset category no one wanted anymore.

Alexander Blostein: Right.

Marty Flanagan: And then you have some relative underperforms with the value bias. You end up with a very different situation than what we had in sort of the decade before that. So we look at this vote Thursday as very, very important. If Boris Johnson gets the votes that he needs, that's an incredibly positive outcome I think for the UK, for the UK market, and for our business. And look, everybody's been wrong every step of the way, but it does look like at the moment that's a likely outcome.

So what do you do in the meantime, as that change? If you look at the ETF business for us, it's grown dramatically over the last 12, 18 months. So the source deal has been very positive and about $13 billion inflows, is that right?

Loren Starr: For Europe, it was something around 10, yeah.

Marty Flanagan: Ten this year and growing. So the source combination is coming in very, very strongly.

The other very important development for us was buying Intelliflo, the digital platform there, and that's in response to the regulatory change in the market. Owning a platform is very, very important. And so those are, as we look to the future, very important developments for us.

Alexander Blostein: Yeah. Another important market for you guys, at least thematically, has been China. And you're one of the few asset managers that actually has a footprint there. There's been a few sizeable wins, particularly in the money market fund space. So maybe talk a little bit about the opportunities that you see in China and the growth prospects there for Invesco. And what are some of the other areas outside of money market funds where you could see potential inflows?

Marty Flanagan: China today is our single largest opportunity and it's beyond thematic. It's actually real. We were the first joint venture in China in 2003, called Invesco Great Wall. We're the only firm that leads with our name, which actually is important. It is a very high-performing joint venture. Right now it's sort of -- we own 49%. We're heading towards a majority. But what's important and very differentiated, we've had management control from the beginning. So we operate in China through our joint venture and our -- the Invesco traditional business as one organization.

So the joint venture continues to grow incredibly rapidly. We also are very successful with the institutional business there. And we see opportunities in further partnerships, digital type platforms and also other opportunities with some of the banks there. So the growth for Greater China has been organic growth of 15% this year. If you look at Mainland China, I think it is north of 30%. And as we look into the pipeline of opportunities, we just look at that as continuing to grow quite rapidly.

With regard to the expansion beyond the money funds on the platform, again, we are the only non-Chinese money manager on the platform and they're now starting to put our other capabilities onto that platform. And right now, if you look at various digital platforms in China, half of our flows this past year has been on digital platforms, so it is also a very important market to study to see what's possible emerging around the world.

Loren Starr: No, I would just say I think the biggest opportunity with the partners is we're actually having banks and others approach us to work with them. And these are huge opportunities; really tens of billions of dollars of flow potential that are sort of presenting themselves to us. So again, early to say whether any one of these things are going to really materialize but, if any one of them do, I think it's a game changer for us in the region.

Alexander Blostein: Yeah. Shifting gears a little bit, prior to the Oppenheimer acquisition you guys talked a lot about Jemstep, and Intelliflo you just mentioned, Marty, as well. Obviously, if we look at the wealth management landscape, sort of digitization of capabilities on the wealth advisor side is also a pretty important theme. And those are kind of the tools that you talked about enhancing your presence in that part of the market. So maybe give us an update on the assets that are on both of those platforms right now, so as we think about the addressable market for Invesco there, and what are you doing to penetrate more of those assets with your products?

Marty Flanagan: Do you want to start?

Loren Starr: Yeah. So we have really two stories. Jemstep, they're focused in the US and they're now really working with one of the largest banks who's testing their capability with their employees. And they're going to launch it nationally in the first quarter is what we've been told. So there's hundreds of billions of dollars of opportunity in this space, ultimately, that could be made available as assets under administration where we can penetrate with our models. And this particular client has said that they are definitely using our models with our product in the model. So, that's a flow potential for 2020 that we'll begin to see build. And certainly once we get through this US opportunity, there are ways for us to think about things globally.

Intelliflo has been sort of focused in the UK predominantly. It's about $500 billion of assets under administration that they currently have in their system. We just launched our model portfolios into that system in the third quarter. And so still early days, but the take up and the interest levels have been significantly higher than we thought and so it is one where we would expect to see build in these products and our flows will come into the products that are in these models, and we're looking to sort of use this platform in other countries. So this opportunity about really assets under administration and being able to have -- I want to say captive assets is really I think one that we're actively pursuing.

Marty Flanagan: And the way to think about it, too, is the digital platforms for an organization like us, what it does, it literally extends our reach to clients. And so if you look in the United States, if you're successful with a wealth management platform, you have 3%, 4%, 5% market share.

Alexander Blostein: Right.

Marty Flanagan: When we look at these digital platforms, it ranges anywhere from 15% to 25% market share. So it's a very dramatic change in what you can do even with these open platforms, and you don't see many opportunities like that. And again, they're slow on the uptake as we've been talking about, but 2020, we're starting to see some things really come together.

So the other point I'd come back to, and you hit it in another way, and it just sort of represents what does a money manager look like going forward. To be successful, yes, it's the digital platform, but you have to be able to build models, you have to have the range of capability to build the models, and that's from active to passive and into alternatives depending on the area, along with a distribution sale force that's capable. So again, it's really puzzle pieces that come together that create the opportunity.

Alexander Blostein: Yeah. Bringing this maybe on level deeper, I want to talk about some of the mix shift dynamics in pricing we generally see in the industry. So when you guys look out at the opportunity set for Invesco over the next couple of years, with the near term you kind of have a sense of the pipeline. You mentioned a couple of things on the institutional front. And you think about sort of the assets that are coming in versus the assets that are coming out and the incremental difference in the fee rate. What's sort of your expectations for the evolution or the kind of blended management fee rate over the next couple of years; again, kind of holding markets steady, which I know is ultimately likely to swing around quite a bit. But in that construct, what should we think about?

Loren Starr: Yeah. I think, again, expecting that we're going to continue to see interest in lower-fee products, I mean that's not a theme that's going to go away, we would expect to see continued downward movement on management fee, really just through mix.

Alexander Blostein: Right.

Loren Starr: I mean people -- ourselves, we're not cutting fees. It's really where the demand is. So for us, as we see that, that's why scale and growth is critical for the asset management of the future, that you need to have enough scale. You need to have the ability to grow in regions and be able to take product across the globe in different locations to really offset that type of dynamic. And that's really what we've tried to position with the Oppenheimer deal. But certainly with the ETFs models, all those digital platforms, we think that we're going to be able to sort of grow faster to offset that dynamic.

Marty Flanagan: I think the other thing that's not really been fully realized, don't draw a straight line to lower fees and lower profitability.

Alexander Blostein: Right.

Loren Starr: Yeah.

Marty Flanagan: The profitability of our ETF platforms, or even the money fund platform, it's north of our traditional profitability. I think what you're -- what is the pace of this change in asset mix. And you hit on a topic earlier. What we've seen as an organization, a little bit of this perfect storm of what's happened in the UK, the Continent in particular, and then sort of the noise -- not noise, but the dislocation going through a transaction here in the United States at the same time. So we look for that to start to slow down as we look into next year.

Alexander Blostein: Yeah. Another growth topic I want to hit on is obviously ETFs for you guys. We talked a little bit about that throughout this conversation, but kind of specifically zoning in on PowerShares and thinking about their competitive position today after having done a couple of deals. And again, taking into account the changes that occurred on the distribution side of things with commissions for ETF trading going to zero, consolidation of Schwab/Ameritrade, right? That enabled you to perhaps redirect some of the marketing dollars in a way, maybe do some of the other platforms, LPL being one of them. There's obviously a recent announcement with them. So if you think about the kind of financial advisory market that you have not focused as much on in the past or you weren't able to penetrate as much in the past, how big of a deal do you think that's going to be kind of zoning in on the LPLs of the world?

Loren Starr: Yeah. I mean I think it's an enormous opportunity for us. It's one that I think through this Oppenheimer deal has become even a bigger one for us to be able to address. So it's probably a number one, number two priority for us in the US.

Alexander Blostein: Yep.

Marty Flanagan: Yeah. And look, it is the combination, as you said. So we've historically been strong at Schwab, Oppenheimer, stronger at LPL, stronger at Fidelity and continuing. And look, we're all seeing the rise in the RAA market and the range of capabilities that we have. It's a natural -- be a natural match for that marketplace.

Alexander Blostein: Yeah. Makes sense. Why don't we pause here and see if there are any questions from the room. And if not, I have a few things I want to -- I would like to hit on. So if you have a question, just raise your hand. All right.

Marty Flanagan: I think there's one right there.

Alexander Blostein: There's one. You were behind the podium so I couldn't see you.

Unidentified Audience Member: Hi. So you have a -- your stock yields over 7% and your PE is around 7 to 8 times. I mean, I'm just curious how you think about that. I mean, obviously, that's very cheap. You've suffered from outflows for a couple of years. You've done this deal which generated a lot of synergy, but how do you feel in the defensibility of your dividend and how do you evaluate sort of like dividend versus buyback here? And what do you think the market's missing when it ascribes such a high yield to your franchise?

Marty Flanagan: Yeah. Why don't I start with the perception topic and then, Loren, why don't you pick up on the capital allocation.

I would say it was a handful of things. The Oppenheimer transaction, I've never seen a market go to a show me like we just did, especially when you look at our historical transactions. No one believed that we could pull off what we've done with Oppenheimer, in particular on the synergies. It literally took to last quarter where it was actually done and dusted before anybody believed it was going to happen. It is then this next stage of showing the stronger organization. So that has been, really, I'd say the biggest headwind with regard to that.

I'd say at the same time, if you're looking at buying a money manager and if you look at our historical strength in the UK and the Continent and you see Brexit, that's a risk -- people look at it as a risk and not an asset. Same thing with our strength in China and the trade wars. You look at it as a risk, not as an asset. So it's a whole lot easier to go somewhere else where you're not dependent upon a couple geopolitical factors along with the risk of completing a combination.

So, those have been the largest perception elements. And it's just a market that says -- everybody in this room -- show me that you can do it and we're knocking them off one at a time. And I think that's -- and it would be -- organic growth would be the next one. After being in net flows for nine years, as you say, the last two years, really a year-and-a-half, it's been quite a change. We've not seen that for a long time.

And as we -- as we look at next year right now, I don't know what the market's going to do, but our baseline as we look at the organization, from what we perceive, will be -- the baseline is flat to slightly positive next year for organic growth. It's not two years. We see it next year right now with what we see in the pipeline and a number of these developments that we've been just talking about today.

Do you want to--?

Loren Starr: Yeah. In terms of sustaining the dividend, I mean there's no question in our mind that we have ample cash flow to sustain the common dividend. In fact, we've been buying back stock and paying out the dividend at a rate that's probably -- that probably is not sustainable, the rate in which we've been doing the buyback. So we bought back 960 million in roughly a year. We're moving to a somewhat more modest and normal kind of rate. Think about 240 million which is left on our commitment of the 1.2 billion which will be taking place through 2020, early 2021.

We'll build up a little bit more cash on our balance sheet to really take care of -- or give us more financial flexibility around some of the debt retirements that are happening in 2022. We have some forward purchase payments that we need to make in April of 2021. But in terms of the cash flow that's generated from the combined business -- I mean the Oppenheimer business, a little money came through with the synergies as well, in excess of $500 million -- we can cover that dividend very, very handily. So to us, it's more of a stock price topic than it is a dividend topic.

Alexander Blostein: Yeah. Just building on the capital point, I guess, where does deleveraging sit in the priority list for you guys in terms of use of cash?

Loren Starr: Yeah. So we've been very I guess focused and aggressive on the buyback as I mentioned. We're not looking to, per se, deliver because we have very little on our credit facility to begin with. But we are looking to build some more cash. And depending on where markets are and how the firm is sitting in 2022, we can decide whether it makes sense to retire the debt, almost $600 million that's coming due that year or not. But ultimately, if we continue along the path that we're going, gaining the scale and starting positive organic growth, it'll be come less of an issue around delevering.

Alexander Blostein: Great. Time maybe for one more. Yep. One in the back there.

Unidentified Audience Member: Thanks. Good morning. I appreciate you guys have built a global diverse company with passive and active exposure, but it just -- from my seat, it feels like the whole world is absolutely capitulating on active; retail investors and now institutions. And it almost feels like the more the world capitulates on active, the harder it is for active to outperform. What do you think resets this structural balance? Is there something that can reset the structural balance over time? Because it just feels like every single incremental dollar into -- at least stocks -- equities is passive and every dollar out is active.

Marty Flanagan: Yeah. It's a great question, but I think you also put the right color on it of sort of where attitudes are right now. And I think what's happened in this market, for active to be successful, you actually have to be a very good active manager. And I think what's being blown out in particular are active managers that are closer to index huggers. And that has -- that gives you -- paying active fees, that creates not a very positive overlay to all of active management and there are a number of active managers that continue to perform quite well. You're right on what's happening right now, and I think it's really the risk appetite and what people are trying to do. Frankly, a bear market or a very sharp rotation out of FANG would be something that would start to change that dialogue.

I also think what's happening very much is that the way that active is being used and the way that clients are -- and I don't care of it's institution or within the retail platforms, there's a much greater focus on the totality of outcomes and using component parts, active being a part of it, in building these models or these solutions for clients. So just the way that it's happening is very, very different. But I think much of what you're talking about is where we are in the market cycle and it's been so prolonged. I look at this as still a post-financial crisis phenomena that's really hit people right between the eyes.

Alexander Blostein: Great. Well, I think we'll leave it there. Marty and Loren, thank you guys very much.

Marty Flanagan: Good. Thank you.

Loren Starr: Thank you very much.

Alexander Blostein: Thank you for being here.

Marty Flanagan: Thank you.