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Asset Management Focus

Freeman & Co. LLC

The World is a Different Place

Wouldn't it be keen if we could click our ruby red slippers and go back to Kansas as Dorothy did in *The Wonderful Wizard of Oz*? Instead we are currently stuck battling the Wicked Witch (aka sub-prime) and the Winged Monkeys (delinquent borrowers), while looking for Glenda the Good Witch (Ben Bernake, perhaps?) to lead our way through the broader troubles of today: lack of transparency (who is the wizard behind the curtain?), lack of liquidity, poor balance sheets, structured product complexity, etc.

The result has been a change in opportunities. We see firms re-focusing on their core areas, divesting non-core assets, and looking for opportunities to take advantage of the market dislocation. There will be winners and losers, but with more extreme results than we have seen in the past 3-4 years.

Performance as of December 31, 2007

Index	Total Return 2H07	Total Return 1 Year	Total Return Annualized 3 Yr	Total Return Annualized 5 Yr
S&P 500	-1.4%	5.5%	8.6%	12.8%
NASDAQ	1.9%	9.8%	6.8%	14.7%
FTSE 100	-2.3%	3.8%	10.3%	10.4%
LBGC*	6.2%	7.2%	4.4%	4.4%
HRFI Fund**	2.3%	10.0%	10.7%	12.1%

*Lehman Brothers Govt./Credit Index

** Hedge Fund Research Institute Fund Weighted Composite

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Indices at 12/31/07:

DJIA	13,264
Nasdaq	2,652
S&P 500	1,468
FTSE 100	6,457
10 Year US Treasury Bond Yield	4.03%
USD per GBP	\$1.98
USD per EUR	\$1.46

Summary:

- **Deal Activity / M&A:** 2007 had a record number of deals at 213 versus 170 in 2006. Total deal AUM at \$1.3 trillion was down from \$2.2 trillion in 2006, a result of the large transactions in 2006. However median deal size in 2007 reached an all-time high
- **Credit Turmoil:** we outline losers (SIV managers, MMF bailouts, etc) and potential winners (SWF's, BDC lenders, distressed debt managers), as well as the capital flows in PE funds (70% CAGR) and CDO issuance (95% CAGR) leading up to the crisis
- **Real Estate:** Global REITs lost nearly 20% and trade at 20% NAV discounts, but don't count real estate out yet – it is an important asset class that is internationalizing fast
- **Alternatives:** there were 64 deals, and the average size grew exponentially as a wave of established firms struck deals (DE Shaw, Blackstone, Och-Ziff, Grosvenor)
- **Sovereign Wealth:** news has been focused on replenishing bank capital but they have also been gently working the asset management segment; expect more of this to come
- **Valuations:** public valuation levels have been most volatile for alternative firms, while public traditional firms have suffered less; private transaction valuations remain more stable

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