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PRESENTATION

Operator

Good day, ladies and gentlemen and welcome to Victory Capital's Third Quarter 2018 Earnings Call. (Operator Instructions) As a reminder this conference is being recorded.

I would now like to turn the conference over to Lisa Seballos, Director of Finance. Ma'am you may begin.

Lisa Seballos ***Victory Capital - Director of Finance***

Good morning. Before I turn the call over to David Brown, I would like to note that today's discussion may contain forward-looking statements, and as such, includes certain risks and uncertainties. Please refer to our press release and our SEC filings for more information on the specific risk factors that could cause our actual results to differ materially from the projections described in today's discussion.

While a recording of this call will be made available by us on our website, any forward-looking statements that we make on this call are based on assumptions as of today, and we undertake no obligation to update these forward-looking statements to reflect new information or future events that occur or circumstances that exist after the date on which they were made.

In addition to U.S. GAAP reporting, we report certain financial measures that do not conform to Generally Accepted Accounting Principles. We believe these non-GAAP measures enhance the understanding of our performance. Reconciliations between these GAAP and non-GAAP measures are included in the tables found in our earnings release and the slide presentation accompanying this call, which can be accessed on the investor relations portion of our website located at ir.vcm.com.

Now I would like to turn the call over to David Brown, Chairman and CEO.

David Brown ***Victory Capital - Chairman & CEO***

Good morning and welcome to Victory Capital's third quarter 2018 earnings call. I am joined today by Terry Sullivan, our Chief Financial Officer, and Mike Policarpo, our Chief Operating Officer.

We are excited to spend some time this morning discussing our planned acquisition of USAA Asset Management Company as well as our third quarter results. Following our prepared remarks, Terry, Mike and I will be available to take questions.

We'll start by highlighting key points to be covered in today's discussion, which can be found on Page 4. Let me start by saying how pleased we are to be working with USAA. USAA is an organization that is synonymous with honesty, integrity and service -- core values that we admire and strive to live by. We are honored that USAA has chosen Victory Capital to serve the investment needs of their members going forward.

The acquisition of USAA Asset Management Company is a significant step in the evolution of our business. It significantly diversifies our AUM base and substantially increases our size and scale. It also expands our investment capabilities, specifically in the fixed income and solutions asset classes. Moreover, it provides us entry into a new member-based channel with attractive growth and retention rates.

USAA is a nationally recognized and well-respected brand and we are thrilled to introduce them on to our platform. The acquisition is financially compelling. It fits squarely into our stated acquisition strategy with the addition of several complementary strategies with strong organic growth potential that are designed to solve issues in client's portfolios. Target date and target risk strategies and active fixed income ETFs are just a few examples of these capabilities.

Looking at the third quarter results, we delivered strong investment performance and posted record quarterly highs across several financial operating metrics, despite continued forceful headwinds for our industry. Total AUM grew to $63.6 billion as of September 30, 2018, an 8% year-over-year increase and the highest quarter-end total that we've reported in our history. We also achieved quarterly record high levels of revenue, EBITDA, and operating margins. Our free cash flow yield is quite compelling and our average fee rates continue to be healthy.

Gross flows for the quarter were $2.9 billion, while overall net flows were negative $672 million. Total net flows were mildly disappointing given our strong investment performance and compelling product set. We've experienced client rebalancing activity during the quarter as well as some delays in our won but not yet funded book. However, our new sales pipeline remains healthy and we continue to earn new product placements with our key distribution partners.

Finally, in September, we announced the acquisition of Harvest Volatility Management, a leader in derivative investing, specializing in yield enhancement overlay, risk reduction, alternative beta and absolute return strategies. Harvest is a high-quality business with a strong organic growth history and a differentiated product set that will introduce new capabilities on to our platform, including alternatives.

Now, I will turn it over to Terry to discuss our third quarter financial results in more detail.

Terence Sullivan ***Victory Capital - CFO & Head of Strategy***

Thanks Dave. The financial results review for the third quarter 2018 begins on Page 6. Relative investment performance across our Investment Franchises and our Solutions Platform remained strong with 69% of our AUM outperforming its respective benchmarks over the trailing 1 year period and 75% over the trailing 5 year.

Additionally, as of September 30, 68% of AUM in our mutual funds and ETFs earned 4 or 5 star overall ratings from Morningstar, and 79% earned 4 or 5 stars over 5 years. In our focused asset classes, 69% of AUM outperformed its respective benchmarks over the trailing 1 year period and 75% over the trailing 5 year.

Finally, 20 of the 34 funds and ETFs in our focused asset classes earned 4 or 5 star overall ratings from Morningstar as of September 30. We are very pleased with these investment results and this is another proof point that our business model is working.

AUM ended the period at $63.6 billion, an increase of 2% in a quarter in which we experienced positive market action that was partially offset by net outflows. Revenue increased 4% to $108.1 million and is up 6% from the third quarter of last year. Our EPS was $0.45, up year-over-year by 22% and our EBITDA margin was 40.1%, marking a 180 bps expansion year-over-year. Overall, Victory achieved record quarterly financial results on AUM level, revenue, adjusted EBITDA, profit margin and EPS metrics in a challenging industry backdrop.

On the capital management front, we delivered on our balanced, strategically aligned approach that we believe will drive shareholder value over time. We allocated capital towards our M&A growth strategy with the Harvest transaction, we also reduced our debt balance and we returned capital to shareholders with our ongoing share repurchase program. We reduced our Term Loan B debt outstanding to $280 million, a 13% decrease from June 30th bringing our current net debt to EBITDA ratio to 1.6x.

Third quarter '18 prepayments resulted in $1 million in annualized interest expense savings. We also repurchased 291,600 of our shares for a total of $2.8 million over the course of the quarter. Moreover, we generated strong cash flow of $40.3 million in the third quarter and our free cash flow yield is at the top of our peer universe. The fundamentals of our business remain solid and we believe we did a very good job executing against our financial plan during the quarter.

Slide 7 provides a snapshot of our scorecard, which we believe provides strong evidence that our unique culture and our platform are working for our investment franchises and, in turn, for our clients.

Slide 8 provides a financial summary of the third quarter. Third quarter net flows were negative $672 million, resulting from a few factors. We continue to see client rebalancing away from our strong performing products. We did see some softening relative investment performance in our U.S. Mid Cap and Commodity asset classes which did have an impact on flows with some clients choosing to redeem from certain strategies. And finally, we had several delays in client mandates which we expected to fund in the third quarter. We should see these materialize in the coming quarters.

Taking a longer term view, the last 12 month focused asset class net flows were positive $640 million and we continue to have success in several other asset classes and franchises. Our ETF business, VictoryShares, had positive net flows of $287 million in the third quarter, bringing year-to-date net flows to $939 million. We continue to be pleased with the strong momentum and market share gains we are seeing in VictoryShares and we note that our ETFs have achieved positive net flows every quarter since we entered the business in 2015.

Global Non-U.S. asset classes posted positive net flows primarily driven by strong results in our Trivalent Investments and Sophus Capital Franchises. We continue to be pleased with the evolution of future flow leaders in our business, most notably with VictoryShares, Trivalent Investments, Sophus Capital and RS Growth.

Importantly, the underpinning of the positive organic growth we are seeing in these franchises is based on attractive asset classes and strong, consistent relative investment performance, 2 critical elements of success in a broader challenging organic growth environment. As we look forward, we are confident in the fundamentals of our business and believe our competitive investment performance results are providing a strong foundation for potential organic growth. Our won but not yet funded book is high quality and we expect the previously mentioned delayed mandates to fund in the near-term.

Revenues grew 6% year-over-year, with 9% average AUM growth. Quarter-over-quarter revenues were up 4%, driven primarily by a higher average AUM level and one extra day in the quarter. Expenses decreased 9% year-over-year, reflecting operational efficiencies driven by our integrated platform. Expenses increased 2% quarter-over-quarter, primarily driven by increases across personnel and operating expenses which moved in line with higher revenue and earnings.

Our controllable expenses were essentially flat quarter-over-quarter which enabled us to deliver margin expansion. Non-operating expenses decreased 58% from third quarter '17, reflecting refinancing and subsequent paydowns of our debt balance. The third quarter was flat to the second quarter, reflective of a more normalized level of interest expense related to our debt.

Year-over-year EPS increased 22% to a quarterly record of $0.45 per share, primarily driven by higher revenues, EBITDA margin expansion and reductions in our interest and tax expense related to the 2017 Tax Cuts and Jobs Act. Adjusted EBITDA was $43.3 million, up 10% year-over-year and 6% from second quarter '18. Our adjusted EBITDA margin expanded 180 basis points year-over-year and 110 basis points quarter-over-quarter. Our ability to expand our margin given our position amongst industry leaders on this measure is evidence of the scaling power of our integrated business model.

As a final point, we would note the adjustments as a percentage of total ANI with tax benefit dropped to 36%, a trend consistent with our view of these adjustments being nonrecurring and relatively short term in nature.

Now, I will turn it back over to Dave to review the acquisition of USAA Asset Management Company.

David Brown ***Victory Capital - Chairman & CEO***

Thank you, Terry. Slide 10 provides an overview of USAA Asset Management Company, which includes USAA's mutual fund and ETF businesses as well as a 529 college savings plan. As of September 30, 2018, USAA Asset Management Company had $69.2 billion in assets under management invested across a diverse product set that includes taxable and tax exempt fixed income funds, asset allocation funds, target date and target risk portfolios, ETFs, Index and Money Market Funds as well as a range of equity funds, including sub-advised and multi-manager strategies.

USAA Asset Management Company has experienced steady AUM growth and has achieved positive net flows for the period January 2014 through September 30, 2018. USAA's direct channel, which exclusively serves members of the military community and their families, has a very loyal client base with attractive retention rates.

Our entry into this distribution channel is a unique opportunity to expand relationships with the more than 1.5 million USAA members who own at least one investment product today and to build relationships with as many as 11.5 million members who do not yet own USAA mutual funds and ETFs. Additionally, USAA Asset Management Company has begun to establish a solid footprint in the retail intermediary and RIA channels, which has strong potential to accelerate with the support of Victory Capital's well established distribution platform.

USAA is a nationally respected brand that has been recognized by the industry for its strong performance track record. USAA Asset Management was named the 12th best fund family of 2016 by Barron's and the 23rd best fund family of 2017. USAA's well established fixed income platform was also recognized by Barron's, ranking 3rd in the taxable bond category for 2016 and 5th for 2017. USAA was also named "Best Institutional ETF User" of 2016 by etf.com. USAA was one of etf.com's 5 finalists for "New ETF Issuer of the Year" for 2017. Finally, the USAA 529 College Savings Plan was ranked first for investment performance over 10 years by savingforcollege.com.

Slide 11 outlines the 4 key reasons that we believe the acquisition of USAA Asset Management Company benefits our clients and creates value for our shareholders. First, the acquisition significantly diversifies our AUM and expands our investment capabilities in areas that complement our current platform and that our clients are demanding.

Second, the acquisition increases our size and scale. When the acquisitions of USAA Asset Management Company and Harvest close by mid next year, our pro forma AUM will be $144 billion. Third, the acquisition provides a very unique opportunity to deliver investment products and

services to USAA's loyal direct member based channel. Finally, we believe this is an extremely financially compelling transaction that is a strategic fit with our stated acquisition strategy. We'll spend just a few minutes on each of these points.

Slide 12 illustrates the significant diversification that this transaction will bring to our asset base. We have made significant progress in diversifying our AUM over the past several years through acquisitions and intentional expansion of our existing product platform. When we complete the acquisition of USAA Asset Management Company, active U.S. equities will make up less than half our pro forma AUM. Importantly, our Solutions Platform, which we believe represents a high demand asset class today and for the future, will make up 26% of our pro forma AUM.

Fixed income and cash will increase to 26% as well. We'll also add new product capabilities in target date and target risk portfolios, which should further increase our penetration with retirement plan advisors and participants. We'll also expand our rapidly growing ETF platform with the addition of 6 USAA ETFs, including 2 active fixed income ETFs.

In conjunction with the USAA transaction, Victory Capital will pursue its active ETF exemptive order, which we believe will further strengthen our position as a leading specialist ETF provider, allowing us to amplify our product penetration within the ETF industry. This type of diversification is important to our business as it positions us to be successful in changing market environments.

Turning to slide 13. The acquisitions of USAA Asset Management Company and Harvest are expected to more than double Victory Capital's assets under management to $144 billion on a pro forma basis. This is critical when we think about the importance of scale to our integrated multi boutique business model. Our model is built to provide centralized, but not standardized, support to our investment franchises so that they can focus solely on managing money for their clients without the operational distractions faced by many investment firms.

Increased size will enable us to continue to invest in areas that are critical to the long term success of our platform, such as technology, operations, client service and investment support, and to leverage those investments across a broader base of assets. We'll be even more efficient than we are today and the support that we provide to our investment franchises will continue to be best in class.

As a larger platform, we'll be well positioned to continue to develop and enhance the product set that we offer to our clients. As a larger company with a nationally recognized brand on our platform and an expanded suite of investment capabilities, we'll have greater financial stability and resilience and increase our relevance with clients across all our distribution channels.

Slide 14 highlights some of the distinct strengths and benefits of the USAA direct member based channel. USAA's mission is to provide their members, all of whom are members of the military community and their families, with highly competitive products and services. It has established a distinguished reputation for the high level of service that it provides to its members. As a result, USAA has built an extremely loyal member base that really can't be compared to that of any other financial services organizations. To illustrate this point, USAA's mutual fund business has achieved an 82% retention rate over the last 5 years. In the direct mutual fund channel, the average customer has been invested with the company for 11 years.

USAA's direct channel represents a tremendous opportunity to further grow relationships with the more than 1.5 million USAA members who own at least one investment product today and to establish relationships with the remaining 11.5 million members who do not yet own an investment product. Among members who are already investors, 24% have elected an automatic investment plan, which represents a meaningful opportunity for those members to achieve steady and consistent account growth over time.

Additionally, USAA has made critical investments in technology that today support an environment in which members primarily purchase mutual funds through its proprietary self-service digital and mobile platforms. We intend to continue to support this type of buying experience because we believe it is preferred in today's technology-driven environment. It will also enable us to achieve efficiencies in servicing this channel over time.

USAA also offers a 529 college savings plan, which has an impressive AUM retention rate of 86% over 5 years. The average 529 plan client has been invested with USAA for 7 years. Not surprising, automatic investment plans represent 60% of gross sales for the 529 plan.

One last, but very important point is that Victory Capital will be managing this business with a strong link back to the USAA organization. USAA's makes it a priority to ensure that it's members have a positive experience, including with services delivered by its partner firms. So USAA has committed to work with us to ensure that members can seamlessly access investment services alongside USAA's other products and services. As I said earlier, we are extremely honored to work with USAA and intend to continue USAA's long-standing tradition of putting members needs first.

Now, I'll turn it back to Terry to cover the financial impact of the acquisition.

Terence Sullivan ***Victory Capital - CFO & Head of Strategy***

Thanks Dave. Turning to Slide 15, we are pleased to outline the attractive expected financial results of this acquisition for Victory shareholders alongside the compelling strategic rationale Dave just discussed.

We will be paying $850 million in purchase price with additional contingent payments of up to $150 million over 4 years based on future business performance. We expect EPS accretion to be approximately 90% in 2020 which would represent the first full year of our ownership. For illustrative purposes, full year 2019 EPS accretion is approximately 60%.

However, assuming a mid-year 2019 closing, EPS accretion will be approximately 30% in 2019. We expect an IRR on the acquisition of approximately 30%. The purchase multiples on EBITDA are attractive at 6.9x, 3.8x with expected synergies and 3.2x with expected synergies and tax benefit, reflective of our thesis of buying down purchase multiples through expected synergies and structure. Underpinning these financial metrics are several assumptions on how we will bring USAA Asset Management into our business.

We expect to add $69 billion in AUM, which excludes $11 billion of AUM from the Managed Money product, delivering $224 million of EBITDA to our business, comprised of $124 million in acquired EBITDA and $100 million of expected expense synergies net of certain investments we will make as part of our integration plan. Our synergy assumption is 32% of the 2018 expense base of the USAA entities being acquired and 17% of the pro forma combined existing cost base and, to be clear, this does not include any revenue synergies.

We estimate that these cost synergies will be fully phased in by year-end 2020. In fact, we expect that $42 million of the expense synergies will already be in place by closing, $83 million will be achieved within 6 months of closing and the full $100 million within 12 to 15 months of closing. The integration will come at a onetime expected cost to us of $50 million of which approximately 1/3 will be capitalized. The synergies will primarily be achieved through middle and back office consolidation and outsourcing actions, administrative function consolidation and gaining scale and efficiencies in a number of other areas. We have structured the transaction in a manner in which we will achieve a tax step up thereby creating annual tax savings in the $14 million to $16 million range.

Turning to slide 16, the transaction will be financed through a combination of debt and cash on the balance sheet at closing. We have received committed debt financing from our bank financing sources. We expect our Net Debt to EBITDA ratio to be 3.2x at transaction close. We would note that this leverage ratio is at a level where we have operated before and given the projected cash flow generation of the pro forma business, we expect to continue our focus on deleveraging which should occur at a rapid pace.

In closing, I would highlight a few financial attributes that result from the transaction that we believe will help drive long term shareholder value for Victory Capital. At $144 billion in AUM, 11 differentiated investment franchises and a Solutions Platform, 130 plus investment strategies and the addition of a new distribution channel, the combined organization will have a transformed financial profile. Generating approximately $900 million in revenue, $420 million in EBITDA at 45% plus margin, the combined organization will deliver size, scale and diversification which we believe is critical in today's investment management environment.

Given our significant past M&A integration experience, we are confident in our ability to seamlessly integrate the 2 organizations in a manner that fully achieves the cost synergies and incremental EBITDA previously mentioned without business disruption, thereby leveraging our integrated multi-boutique model and positioning our business for success in the future. Our integrated multi-boutique model is set up and designed to integrate businesses like the USAA Asset Management Company and our team is excited to get going on it.

This concludes our prepared remarks. I will now turn it over to the operator for questions.

QUESTIONS AND ANSWERS

Operator

(Operator Instructions) Our first question comes from Michael Carrier with Bank of America.

Jeff Ambrosi ***Bank of America - Analyst***

It's actually Jeff Ambrosi filling in for Mike. Just first on the 90% accretion. I just want to make sure I'm getting the right base on that. Is that referring to the consensus of like $1.97 right now which I think is partially reflective of Harvest?

Terence Sullivan ***Victory Capital - CFO & Head of Strategy***

Yes, so let me walk you through the methodology there. So first of all, the accretion is very much driven by the transformed financial profile that we have set forth. If you think about it, we're more than doubling our EBITDA and therefore our earnings. So as we think about the baseline calculation, we started with what I would say is Victory core 2020 consensus. We've previously given guidance on Harvest accretion and so we've added that in as the baseline. And then from there you add in the expected earnings from USAA plus synergies which includes phase in and the cost to achieve. And then obviously some frictional costs associated with financing and that's how you get to the accretion number.

Jeff Ambrosi ***Bank of America - Analyst***

And then maybe just one on organic growth. I know you guys gave some, I guess, longer term flow history for USAA, but just curious maybe what the flow has been like more recently maybe year-to-date?

David Brown ***Victory Capital - Chairman & CEO***

Year-to-date they've been about flat. This is Dave Brown -- they've been about flat. We're really excited about the organic growth opportunity for the USAA funds through the direct member channel and through taking some of their products to the RIA intermediary channels through our distribution platform, very excited about that. I'd also point you back to the longer term organic growth rate, which I think we referenced in our prepared remarks being 3x what the industry is -- has been.

Operator

Our next question comes from Michael Cyprys with Morgan Stanley.

Michael Cyprys ***Morgan Stanley, Research Division - Executive Director and Senior Research Analyst***

Just on the direct channel, just curious if you could talk a little bit about that a bit more. Are there any third party platforms, any third party firms on this direct platform? Just trying to get a sense of what portion of the 1.5 million members have their mutual fund products with USAA versus other managers there?

David Brown ***Victory Capital - Chairman & CEO***

So the direct member channel is a really unique channel. The direct member channel does not have any other competitors within the direct member channel. Those 1.5 million members are members that have USAA funds. As we said in our prepared remarks, there's another 11.5 million members that do not own a mutual fund or own investment products.

Michael Cyprys ***Morgan Stanley, Research Division - Executive Director and Senior Research Analyst***

And then can you also just talk a little bit about the client profile? I think you mentioned that they're trying to expand their footprint into other intermediaries. Maybe just what portion is of the assets or with the direct, with the USAA members versus what's in wire houses and other channels?

David Brown ***Victory Capital - Chairman & CEO***

So there's a number of their products. They really have been under marketed outside of the direct member channel. It represents about 10% to 12% of the overall assets that we're acquiring. We think taking those products outside of the direct member channel -- again, they've been really under marketed -- we think there's a great opportunity to take our distribution platform and distribution team and marketing team, use what we've learned and what we do every day, and take those products and introduce them to a number of our already partners.

Michael Cyprys ***Morgan Stanley, Research Division - Executive Director and Senior Research Analyst***

And just quickly follow up question just that, it seems like you're tilting a little bit more towards fixed income and money markets a little bit here, which are not part of your focus asset classes. Can you just talk a little bit how you're thinking about that? And is your -- do you focused asset classes evolving?

David Brown ***Victory Capital - Chairman & CEO***

So, pro forma our focused asset class is the -- we'll have about 2/3 of our assets still in our focused asset classes. We talked about diversification. We think it is very important to be diversified and increasing our fixed income and then adding money market. We think it's healthy. We think it provides for a sustainable platform. As I've said in the past, the focused asset classes are areas where we think we're seeing a lot of client demand. And we think in today's environment, the investor demands are demanding products like that. The non focus asset classes, just to be clear, are not asset classes we don't think we can grow. We still think we can grow those. So the way we look at it, this provides us, by the way, a lot of diversification, adds a number of new products to our focus asset classes. It increases our ETF. It adds active ETFs. It adds target date, target risk, asset allocation funds, a 529 college savings plan, which we think really, when you look at it broadly, allows us to be better diversified and then provide us new product capabilities. And really allows us, as we see investor sentiment changing, to be in all areas to capture those assets as they move around in client's portfolios.

Operator

Our next question comes from Ken Worthington with JP Morgan.

Kenneth Worthington ***JP Morgan Chase & Co, Research Division - MD***

In the presentation, I guess, we've talked about mobile and digital, the USAA funds are going to continue to have access. How long will they have access to the USAA insurance clients and is there any cost to that access? And then, what kind of access do you get to the 11.5 million USAA members that don't own USAA fund products today? And do you have access -- like, can you reach out to those clients by phone calls or e-mail or traditional mailings? Like, how much can you market the existing USAA products to again, those who don't own them? And then I'll tack one more on. Like, to what extent can you market the non-branded USAA funds to USAA insurance clients? Is their provisions that allow for that sort of access as well and how deep can you go?

David Brown ***Victory Capital - Chairman & CEO***

Hi, Ken, number of questions there, I'll try to address them all. First from a cost perspective, there is no additional cost other than what's in the purchase price to get access to the other 11.5 million members that don't own an investment product today. As I said in my prepared remarks, the goal of USAA and for us is to provide a seamless integration, so the -- to the members in that -- those 1.5 million members and the other 11.5 million members. They will be able to access the USAA fund as they've always had through their client portal, through their website. And as far as our ability to access the other 11.5 million members, we will go and introduce the USAA funds just as they've been introduced today, as if the transaction has never occurred. We'll do it through their client portal, we'll do it through direct methods, through mailings, through other methods we think where we can gain attention. Lastly, I would say that we are hoping, and I think the goal of the transaction, if you think about USAA's mission of providing top financial products to their members, the goal is to actually increase the number of members that the USAA funds -- the members are invested in USAA funds. So that is one of the primary goals from USAA's perspective is to be able to introduce these funds to more of their members.

Kenneth Worthington ***JP Morgan Chase & Co, Research Division - MD***

And then maybe just secondly. You've got 2 live deals with Harvest and USAA, what are the challenges of integrating 2 deals at the same time? And given you're much bigger with these deals, does it makes sense to insource certain functions that previously you have been outsourcing given your increased size and scale?

David Brown ***Victory Capital - Chairman & CEO***

So, I'll take the last part of that question first. We, of course, are evaluating as we do with every transaction whether to insource, outsource or to do a mix. So we'll evaluate that, and it's an ongoing evaluation. On the first part of the question is around integrating 2 transactions at the same time. Our business model is really built for this. The way we set the company up, our history and experience of integrating acquisitions, we're very well experienced at it. We have the same management team that's been doing it over the last 5 plus years. And these integrations are very different. Harvest is a one location, less employee, smaller firm, very focused on a few products. And obviously, the USAA acquisition is much larger and it's very different. But we're fully qualified to integrate both, and we're more than excited to get going. And as you can see through some of the information we've shared, we've done a lot of due diligence on both of the acquisitions and spent a lot of time ensuring that we can do this in a seamless way.

Operator

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

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

I guess, first question I have is, a lot of the USAA products, I think particularly the equity products are sub-advised by third parties. So, can you maybe -- what's you're thinking about that part of their business. Who's going to kind of make the decisions about who stays or not over time related to those sub-advisors? And is that something you think of internally where it's appropriate there's an opportunity to maybe replace the most subadvisors or do you think that's really just -- you can leverage your third party marketing and even if they are sub-advised that, could give a broader product profile?

David Brown ***Victory Capital - Chairman & CEO***

So we have sub-advised funds today, so we're fully aware of how to use them. I would say that the fund board will ultimately approve any sub-advisor changes. We'll work with them and evaluate the opportunity to see if there's other better sub-advisors for those funds. We've evaluated them in our due diligence. We think a lot of those sub-advised funds are very competitive, but we'll continue to look at them as we get to close and eventually make recommendations to the fund board.

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

And then maybe a follow up on the deal structure and contingent payment. So, I mean, understanding, once the deal is done you kind of want to pay down debt at a rapid pace. But just kind of curious about how you're thinking about kind of debt structure, pretty much all bank debt, or you're thinking about some combination of trying to turn out a big chunk of it just to kind of fix financing, and then, on the contingent payments over 4 years, what are some of the business metrics that those are dependent upon? Is it EBITDA growth, is it AUM growth, is it flows, just trying to get a sense for what kind of would trigger those payments?

Terence Sullivan ***Victory Capital - CFO & Head of Strategy***

Sure, Rob, I'll start with the second question first. As we've mentioned in our prepared remarks, the contingent payment is $150 million that could be paid over 4 years. And it's based on business performance, specifically revenue retention. And then in terms of capital structure, as we've set forth the structure will be 100% debt alongside some cash on the balance sheet that will be there at closing. The pro forma leverage ratio will be about 3.2x or roughly $1.4 billion. It will be tending to our existing Term Loan B outstanding, the Harvest financing, as well as this financing. And I think what we would say around this is that the -- we're comprehensive in a way that we think about this structure, so these contingent payments would be taken care of through cash flow of the business which as we discussed will be quite powerful in the pro forma organization. And we are quite familiar with the debt structure that we're setting forth, this Term Loan B, which is a market that we're active in today. And obviously, we've operated the business at forward levels like this and we have proven over the last several years that we will be very focused on deleveraging with the cash flow that will be generated.

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

And if I could maybe just one quick follow-up, since I'm not familiar with the USAA direct distribution channel. Is it just USAA funds available on there or are there other third parties? And post transaction, is USAA intending -- while you'll still be there with the brand -- are they at all intending to kind of open that up to other parties if that's not the case now?

David Brown ***Victory Capital - Chairman & CEO***

So the direct member channel is just USAA funds and they are not planning to open up to other parties.

Operator

Our next question comes from Chris Shutler with William Blair.

Andrew Nicholas ***William Blair - Analyst***

This is Andrew Nicholas filling in for Chris. First, I think in the presentation there's about $21 billion of AUM at USAA that you classify within your Solutions category. Just hoping you could break that down a little bit more and be helpful to better understand these types of strategies and/or the capabilities in that bucket, and how you expect them to augment Victory's current product suite?

David Brown ***Victory Capital - Chairman & CEO***

So the breakdown at a high level is the target date, target risk, the ETFs, the asset allocation, the 529, and some of the index products.

Andrew Nicholas ***William Blair - Analyst***

Okay, and then, separately from USAA, you mentioned there were some delays in your won but not yet funded pipeline. Just hoping you could talk little bit more about those, where you're seeing the delays, the size of those mandates, and whether or not you expect them to fund in the fourth quarter?

David Brown ***Victory Capital - Chairman & CEO***

So where we're seeing some delays have been in our focused asset classes, and we do expect them to fund in the fourth or first quarter. But I would tell you that those dates are based on what clients want to do and they can change, but from what we know today, they're fourth quarter-, first quarter-type fundings.

Andrew Nicholas ***William Blair - Analyst***

And then just one last question on Harvest. Obviously, October was a little bit choppier of a month with some rising volatility, just curious if you have any insight on how Harvest strategies performed in the month or how that outlook has changed since the last deal announcement?

David Brown ***Victory Capital - Chairman & CEO***

We're really very happy with the way Harvest has performed. We know that they've performed better than most of their competitors. It was a very challenging month for these types of products, and they've done well against their competitors. Very much their active overlay has really benefited their strategy and we're more than excited about bringing them on. We think that this is going to be a great product and we're really excited to introduce it to our clients, and we think it has real organic growth potential, especially when it's partnered with our distribution.

Operator

Our next question is a follow-up from Michael Cyprys of Morgan Stanley. Your line is open.

Michael Cyprys ***Morgan Stanley, Research Division - Executive Director and Senior Research Analyst***

Just hope you can give us a little bit of context as to how this deal came about, how long you guys were in discussions for and how competitive was this?

David Brown ***Victory Capital - Chairman & CEO***

So it was extremely competitive, and I would tell you that that we have been working on this for quite some time. USAA and Victory really do share a lot of the same culture, really a foundation from a cultural perspective, we're very similar. And I think that really came to the forefront and that's really one of the reasons why we were able to win this deal. And I think that they recognized our business model, our platform, our investment excellence and really our ability to serve their members. And I think that was the most important thing to them. And we really felt that we could come through on serving their members and really evolving how they serve their members. But it was an extremely competitive opportunity. But as I said in the past, I think our platform and our business as it is as well positioned as any business in the industry to really be a consolidator as we think about the industry moving forward. I think what we've done in the last 60 days is a real testament to that. And I think the quality of this business and the quality of Harvest shows the type of businesses that we can attract to our platform.

Michael Cyprys ***Morgan Stanley, Research Division - Executive Director and Senior Research Analyst***

And then just on the leverage point, 3.2x a little bit more, highly levered versus from the peers. Can you just talk about your confidence and how levering an asset like this, particularly late in cycle, and maybe help us frame and think through how quickly you could de-lever perhaps 12 months post close, where that 3.2x could drop to?

Terence Sullivan ***Victory Capital - CFO & Head of Strategy***

I think as it pertains to the leverage level, I'd offer a couple of perspectives there. First of all, when you think about the pro forma business profile here, we think that this is very helpful. And it's also very much improves the financial profile vis-Ã -vis leverage. We've got diversification. We've got scale and we've got size. And these are all very helpful to our financial profile. Secondly, we've operated this business at these levels before, and I think we have experience on our side and we will be able to continue to focus on deleveraging and have proven that out as we have before. We do think that when you look at the pro forma free cash flow of this business, it's quite powerful. There are synergies in there that as we set forth in our prepared remarks, can be achieved quickly and contribute immediately. So we have overall confidence in the business and the financial profile that comes with it. As it goes to deleveraging, we're not going to provide specific guidance on how that trails down, but if you look at sort of historically how we've trended down, we think that that path is consistent with what you would see here.

Operator

Thank you. (Operator Instructions) And next follow-up comes from Robert Lee with KBW.

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

I guess I actually have a question too on the current business. Could you maybe just update as you'd mentioned that the commentary on the pipeline -- new business pipeline. I don't know if there's any quantification you give on that. I know you said you expect some of it to fund over the near-term after being somewhat pushed out. But any color on kind of the size or mix of the pipeline, and that'd be helpful?

David Brown ***Victory Capital - Chairman & CEO***

We don't give guidance on the pipeline going forward, but what I'll say is, we think it's healthy, it's widespread. The foundation for it is our investment performance in the asset classes that we're in. But we feel really good about as we look forward, feel even better with Harvest coming on, and USAA coming on. We think, we'll have a compelling organic growth profile as we look forward. As I said, in my prepared remarks, we were mildly disappointed with the flows this quarter, given our investment performance and our asset classes. But there were a lot of pockets of positive. Our VictoryShares, our global non-U.S. really was strong. And we think that as we look forward, we're going to be in a very good position to grow our business organically.

Operator

Thank you. And I'm currently showing no further questions at this time. I'll turn the call back over to David Brown for closing remarks.

David Brown ***Victory Capital - Chairman & CEO***

Thank you for taking the time today to participate in our earnings call. If you have any additional questions, please don't hesitate to contact us. We look forward to updating you on our progress in the future. Thank you.

Operator

Ladies and gentlemen, this concludes today's conference. Thank you for your participation, and have a wonderful day.