THOMSON REUTERS

EDITED TRANSCRIPT

Q4 2018 Victory Capital Holdings Inc Earnings Call

EVENT DATE/TIME: FEBRUARY 06, 2019 / 1:30PM GMT

CORPORATE PARTICIPANTS

David Brown *Victory Capital Holdings, Inc. - Chairman & CEO*
Matthew J. Dennis *Victory Capital Holdings, Inc. - Director of IR*
Michael Policarpo *Victory Capital Holdings, Inc. - COO*
Terence F. Sullivan *Victory Capital Holdings, Inc. - CFO & Head of Strategy*

CONFERENCE CALL PARTICIPANTS

Christopher Shutler *William Blair & Company L.L.C., Research Division - Research Analyst*
Jeffrey Drezner *Keefe, Bruyette, & Woods, Inc. - Equity Research Associate*
Kenneth S. Lee *RBC Capital Markets, LLC, Research Division - Analyst*
Michael J. Cyprys *Morgan Stanley, Research Division - Executive Director and Senior Research Analyst*
Shaun Calnan *BofA Merrill Lynch, Research Division - Research Analyst*
William V. Cuddy *JP Morgan Chase & Co, Research Division - Analyst*

PRESENTATION

Operator

Good day, ladies and gentlemen, and welcome to the Victory Capital Fourth Quarter 2018 Earnings Call. (Operator Instructions) As a reminder, this conference call is being recorded. I would now like to turn the conference over to Matt Dennis, Director of Investor Relations. Sir, you may begin.

Matthew J. Dennis ***Victory Capital Holdings, Inc. - Director of IR***

Thank you, Shannon. Good morning. I would like to introduce myself. I am Matthew Dennis, the new Director of Investor Relations for Victory Capital, and I'm thrilled to be joining Victory at such an exciting time. Before I turn the call over to David Brown, I would like to note that today's discussion may contain certain forward-looking statements, and as such, includes 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 Holdings, Inc. - Chairman & CEO***

Thanks, Matt. Good morning, and welcome to Victory Capital's Fourth Quarter 2018 Earnings Call. I'm joined today by Terry Sullivan, our Chief Financial Officer; Mike Policarpo, our Chief Operating Officer; as well as Matt Dennis, our new Director of Investor Relations. I'm going to spend a few minutes discussing our fourth quarter results as well as some business highlights. Then I will turn it over to Terry, who will review our financial results for the quarter in more detail. Following our prepared remarks, Terry, Mike, Matt and I will be available to take questions.

We'll start on Slide 5. I'm pleased to report that Victory Capital delivered strong investment and financial performance during the fourth quarter. The fourth quarter was a period of unprecedented volatility and we experienced a significant market pullback, especially during December.

Strong operating margins, cash flow generation and expense control during the volatile quarter highlighted the strength and sustainability of our integrated multi-boutique business model. Our model provides diversification across asset classes, investment return streams, product types and business channels and has enabled us to build scale in operations, administration and technology.

As a result, we've been able to continue to reinvest efficiently in the business and allocate the resources necessary to seek to provide superior returns and service to our clients and our investment franchises.

Starting with investment performance. 57% of our AUM outperformed its respective benchmarks over the trailing 1-year, 68% over the 3-year, 74% over the 5-year, and 88% over the 10-year periods ended December 31, 2018.

Total AUM decreased to $52.8 billion as of December 31, 2018, due primarily to market depreciation. Gross flows for the quarter were strong at $4 billion, while net flows were negative $1 billion as many investors retreated from higher-risk asset classes and rotated into cash.

Going into December, we were net flow positive for the quarter as a firm. With the market volatility and dislocation that intensified in December, we saw elevated levels of redemption in the asset classes we manage, which resulted in outflows for the quarter.

Moreover, the fundings of some of our won-but-not-yet-funded accounts were pushed back into 2019. That said, we're seeing a more normalized environment in 2019, and in fact, preliminary assets under management have climbed back to approximately $57 billion as of the end of January. Overall, our pipeline for 2019 is healthy as are our sales prospects, fueled by our investment performance and diverse product set.

Momentum in our VictoryShares ETFs remained strong with net flows of $121 million for the quarter and $1.1 billion for the year ended December 31, 2018. We continue to think VictoryShares represents an exciting and differentiated part of our product platform.

Looking ahead, we intend to grow organically by leveraging the diverse capabilities of our investment franchises and our solutions platform, coupled with our well-established distribution system.

Our organic growth potential will be impacted somewhat by the investing environment, which as I stated earlier, has begun to normalize, which is quite encouraging. We also intend to grow inorganically through acquisitions and believe the consolidation of the industry will only increase in the years to come.

We believe we are as well positioned as any firm in the industry to benefit from consolidation, given our platform and our experience.

On that front, we announced 2 acquisitions in 2018. In September, we announced plans to acquire Harvest Volatility Management, and in November, we announced plans to acquire USAA Asset Management Company, which includes its mutual fund, ETF and 529 college savings plan businesses.

Together, these 2 acquisitions will significantly diversify our AUM and investment capabilities and add many new and distinct products to our current line up. They will also give us substantial opportunities to expand our distribution platform, including the addition of the direct channel for USAA members.

The acquisitions will also transform our business in terms of size and scale, thus giving us the ability to continue to reinvest at a pace that will prepare us for the future during this phase of rapid change for our industry.

Both Harvest and USAA Asset Management performed as expected in the fourth quarter, given the difficult market environment.

Harvest did experience an investment performance drawdown for some of their investment strategies, but this performance was comparable to other like investment strategies. Harvest's flagship strategy, CYES, was competitive relative to its benchmark. We believe the Harvest investment products continue to serve as an important component of a well-diversified portfolio built for the long term.

Generally speaking, USAA's investment strategies held up nicely during the volatile quarter and illustrated the power of a product set that is well diversified across a number of different asset classes. We're excited to bring this group of products from Harvest and USAA to our platform and offer them through our distribution system.

Plans to integrate Harvest and USAA Asset Management company are on track. Each firm's mutual fund Board of Trustees approved the respective transactions, which is a step in bringing the transactions to close.

Additionally, mutual fund proxies for both transactions have been filed with the SEC and will come to market shortly.

Specific to USAA, the Board of Trustees of USAA Mutual Funds Trust approved the addition of several Victory Capital Investment Franchises and our Solutions capabilities to provide investment management services to specific USAA funds, as well as an alignment of certain service providers that support our integrated multi-boutique model.

As Terry will go through later, we have committed financing for both transactions and we are on schedule to execute on these transformational acquisitions.

This includes our ability to accomplish the $100 million synergy goal within the timeframe that we initially laid out at the announcement of the USAA transaction.

Based on the information we have at this point, we expect to close both these transactions in the second quarter of 2019.

We believe the current market dynamics support consolidation through M&A as firms of all sizes continue to evaluate their businesses and how they fit into the future landscape of the asset management industry.

We aim to be the consolidator of choice given our experience and the benefits offered by our integrated multi-boutique business model.

Our M&A pipeline remains strong, and we continue to have focused conversations with investment managers that fit our platform, and we are very excited about the prospects for our M&A activity in the coming quarters and years.

Now we'll turn to Slide 7. The foundation of our business is built on the 4 key pillars that you see here, which exemplify our culture and our commitment to our clients.

Our commitment to these pillars has helped to create a very unique employee ownership culture that we believe serves as a key driver of our success, both today and in the future.

We are very proud to report that our current base of 264 employees has more than $100 million invested in the products that we manage.

We invest at full fees alongside our clients, so we are clients as well. This is all done by personal choice, not by any type of corporate mandate to do so. As a result, our interest and our clients' interests are aligned.

Let's turn to Slide 8. This slide illustrates our diversification from multiple perspectives, including by business, distribution channel, by product type and by asset class.

That's important when we think of the health and sustainability of the business through all market cycles. Approximately 56% of our AUM is from institutional clients and 44% from retail clients as of the end of the quarter.

We expect our two planned acquisitions to significantly enhance the diversification characteristics of our platform through expansion of our investment capabilities, product set and distribution system.

Slide 9 provides a snapshot of our scorecard, which we believe provides strong evidence that our unique culture and platform are working for our investment franchises, and in turn, for our clients.

Slide 10 illustrates our short and long-term outperformance relative to benchmarks. Some select examples that I would like to highlight at the investment franchise level include Sycamore Capital, RS International, INCORE and Munder, all of which had one or more funds ranked in the top quartile by Morningstar for the trailing one-year period ended December 31, 2018.

Additionally, I'd like to call out the strength of our overall 3- and 5-year performance track records, as most clients use these timeframes when evaluating whether to hire and also retain investment managers.

The results delivered by our VictoryShares platform were also compelling with 57% of our ETFs ranked in the top quartile over the trailing one-year period. 5 of our ETFs were ranked in top decile by Morningstar over the one-year period, and three were ranked in the top decile over the 3-year period.

Looking at our full suite of mutual funds and ETFs on Slide 11, 65% of AUM in those products was ranked 4 or 5 stars by Morningstar on an overall basis for the period ended December 31, 2018.

56% of AUM was ranked 4 or 5 stars over 3 years, 64% over 5 years and 72% over 10 years.

Slide 12 highlights a strong momentum that we continue to achieve with our solutions platform, particularly our VictoryShares ETFs. Since we introduced ETFs on our platform in 2015, our ETF AUM has grown from $198 million to $3 billion as of December 31, 2018.

At the end of the December 2018, VictoryShares was ranked 26 in overall ETF AUM among 144 issuers and 21st out of 144 ETF issuers in year-to-date net flows according to Morningstar.

Year-over-year, our ETF market share has increased by 33%.

Before we move into our financial results, I would like to briefly discuss an organizational change we will be implementing over the next month. Michael Policarpo, our Chief Operating Officer will be promoted to our President, Chief Financial Officer and Chief Administrative Officer. Our current Chief Financial Officer, Terry Sullivan, will be leaving the firm. Mike has been with Victory Capital for 14 years and has served in various senior capacities over his tenure, including our prior Chief Financial Officer before Terry's arrival. Mike's institutional knowledge, industry experience and direct involvement in the sourcing and execution of our acquisition strategy positions him very well for a seamless transition into this new role. Terry has been a valued contributor to our company over the last few years as our Chief Financial Officer. For many years prior to that, he was a trusted advisor to me while at a previous firm. We wish him well in his next career opportunity and know he will stay a friend of the firm and to me personally.

Now I'll turn it over to Terry to discuss our financial results for the quarter.

Terence F. Sullivan ***Victory Capital Holdings, Inc. - CFO & Head of Strategy***

Thanks Dave for your kind words. Mike, I wish you the best of luck, and I'm committed to a smooth and seamless transition. I would like to add to Dave's comments that I truly enjoyed my tenure at Victory. We've accomplished a lot strategically, organizationally and financially over the past couple of years, and I am proud to have been a part of an exceptionally talented team.

I have the utmost confidence that Victory is on path for tremendous success in the future, and agree with Dave's comments that with the long-term previous relationship and what we've accomplished together that I will always be a friend of this firm.

The financial results review for the fourth quarter of 2018 begins on Slide 14. AUM ended the period at $52.8 billion. This is a decrease of 17% in a quarter in which we experienced extreme market volatility that resulted in negative market action and net outflows, and thus impacted our P&L.

Revenue decreased 11% to $96 million quarter-over-quarter, and is down 9% from the fourth quarter of last year.

Our EPS was $0.38, down 3% and 16% from 4Q '17 and 3Q '18, respectively, and our EBITDA margin was 37.9% flat to 4Q17's measure and down 220 basis points from 3Q18's measure. Overall, we believe we did a good job executing against our financial plan in a quarter that was preceded by record results in the third quarter, and where we saw unprecedented market volatility, a severe market pullback and challenging environment for the investment management sector. Though the challenging markets impacted our quarterly results, we are pleased with the progress we made against our full year-over-year financial goals.

Taking a longer-term viewpoint, Victory Capital posted measurable full year-over-year growth across revenue, EBITDA, adjusted net income with tax benefit and EPS.

More specifically, EBITDA margin expanded 230 basis points and ANI with tax benefit grew 41% from 2017, reflective of both the operating and capital management levers existing in our business.

We believe our results punctuate a theme Dave mentioned earlier, which is our integrated multi-boutique model is durable and built for these types of environments. Furthermore, the announced acquisitions of Harvest and USAA Asset Management provide proof points of the powerful M&A capability and value proposition our model offers in what we view as an industry with continuing consolidation on the horizon. On the capital management front, we earmarked capital for our M&A growth strategy with Harvest and USAA Asset Management acquisitions, we continued to return capital to shareholders with our ongoing share repurchase program, and we accumulated cash as part of our acquisition financing strategy. Our cash balance is $51.5 million, and our Term Loan B debt outstanding is $280 million. Our net debt-to-EBITDA ratio dropped to 1.5x from 1.6x in the prior quarter. We repurchased approximately 499,000 shares over the course of the quarter, which represents a 70% increase quarter-over-quarter. Finally, we generated cash flow of $34.4 million in the fourth quarter, delivering a free cash flow yield that is amongst the leaders in our peer group.

Slide 15 provides a snapshot of our AUM over time. Our AUM decreased 17% from 3Q '18 primarily from market action and some outflows. Focused asset classes are currently 78%, and we continue to see the benefits of our purposeful commitment to these strong performing, value-added, in-demand, higher fee and higher margin asset classes.

Our mutual fund and ETF AUM finished the fourth quarter at approximately $33.4 billion in AUM, including $3 billion in ETFs.

We continue to operate a well-diversified platform relative to our AUM size and are quite pleased with our scale and growth potential.

Slide 16 provides a perspective on our organic growth performance over the last several quarters. 4Q outflows were $1 billion, resulting from a few key factors. Outflows accelerated in December as the extremely volatile market led some investors to the sidelines, resulting in higher-than-expected outflows in several asset classes. This investor move to the sidelines intensified in December, and as such, Victory moved from a quarterly net flow positive position through November to an outflow position in December.

That said, we continue to have success in select asset classes and with several franchises. Our ETF business, VictoryShares, had positive net flows of $121 million in the fourth quarter, bringing full year 2018 net flows to $1.1 billion. We continue to be pleased with the strong momentum and market share gains we're seeing in VictoryShares and note that we have experienced positive net flows every quarter since our acquisition of the business in 2015.

Global non-U.S posted positive net flows of $659 million and $1.5 billion for the quarter and full year, respectively, primarily driven by strong results in our Trivalent Investments and Sophus Capital Franchises.

We continue to see encouraging progress among our future flow leaders, most notably with VictoryShares, Trivalent, RS Growth, Sycamore and Sophus. Lastly, our separate accounts and Other channel posted $367 million of fourth quarter flows, reflecting the positive momentum we had with institutional clients in turbulent market conditions. We were pleased with our gross sales results of $4 billion for the quarter and $14.1 billion for 2018, as they provide evidence of the strength of our distribution platform, attractiveness of our investment strategies and competitiveness of our investment performance.

Gross sales for the quarter were up $1.1 billion, or 39% when compared to the prior quarter.

While the fourth quarter's market volatility created an extremely challenging investment environment and drove sizable investor outflows across the industry, we feel confident that our franchises are navigating the markets on behalf of our clients effectively.

Furthermore, with these market conditions come opportunities to outperform and gain market share by leveraging our attractive asset classes and strong, consistent and relative performance. As we look forward, we believe our franchises continue to provide us with a strong foundation for organic growth as supported by a high-quality pipeline across several franchises and distribution channels.

Slide 17 provides a snapshot of quarterly revenues. Quarterly revenues decreased 9% year-over-year and 11% from the third quarter, reflecting average AUM decreases from the fourth quarter market decline and fee rate decreases resulting from asset mix shift. We ended the full year of 2018 up modestly on revenues from 2017 levels.

Turning to Slide 18, expenses decreased 15% year-over-year, reflecting lower AUM and revenue levels that reduced variable costs, operational efficiencies driven by our integrated platform, and lower interest expense resulting from our debt refinancing and deleveraging efforts. Expenses decreased 5% quarter-over-quarter, driven by decreases across personnel and operating expenses that were partially offset by transaction-related costs.

Personnel expenses decreased 11% quarter-over-quarter and 9% year-over-year.

Operating expenses decreased 5% quarter-over-quarter and 12% year-over-year, driven by the impact of lower AUM and revenue levels on variable costs, reductions in broker-dealer distribution expense and platform distribution fees and continuing run-off of legacy intangible amortization.

Non-operating expenses increased by $2.4 million from the third quarter related to 2 noncash items. Year-over-year non-operating expenses were down 43%, primarily driven by reduced interest expense resulting from our debt refinancing and deleveraging efforts, partially offset by the previously mentioned 2 non-cash items.

Lastly, our controllable expenses within our integrated multi-boutique model were essentially flat again quarter-over-quarter, which enabled us to effectively buffer industry-wide margin pressure resulting from market volatility.

I would point out that our ability to prudently manage our controllable cost has not impaired our ability to invest in our platform for the future, as we made great strides in enhancing our technology, marketing and distribution capabilities over the last few years to support our business growth.

We present our non-GAAP earnings, EPS and margin metrics on Slide 19. EPS decreased 3% year-over-year and 16% quarter-over-quarter, driven by reduced quarterly revenues and EBITDA resulting from the market downturn.

Full year 2018 ANI with tax benefit and EPS grew 41% and 20%, respectively, from 2017 levels, primarily driven by higher revenue, EBITDA margin expansion, reductions in our interest expense and lower tax expense related to the 2017 Tax Cuts And Jobs Act, partially offset in the case of EPS by share issuance related to our 2018 IPO.

Adjusted EBITDA was $36.4 million, down 9% year-over-year, and 16% from 3Q '18. We're able to maintain a high 30s adjusted EBITDA margin percentage throughout 2018, including in the volatile fourth quarter, a level that positions us amongst the leaders in the industry and provides another proof point of the scaling power of our integrated model.

Turning to capital management, slide 20 outlines several key balance sheet items and metrics. Overall, we believe we delivered on our balanced, strategically aligned approach to capital management. We developed a fully committed debt financing strategy with our relationship bank partners for the Harvest and USAA Asset Management acquisitions that we believe is optimized for shareholder value creation. Our net debt balance stands at $236 million, yielding a net-debt-to-credit-EBITDA ratio of 1.5x. We have $51.5 million in cash as we accumulate cash to finance the acquisitions. We continue to execute on our share repurchase program by buying in approximately

499,000 shares over the course of the quarter, which represents a 70% increase quarter-over-quarter.

As we've said before, we feel the buyback program demonstrates thoughtfulness and proactiveness on the capital management front, reflects our confidence in our long-term business strategy and is a useful tool to have in the toolkit to drive long-term shareholder value.

We generated strong cash flow from operations of $34.4 million in the fourth quarter, which enables us to strike the right balance across our capital management priorities and implies a free cash flow yield for Victory Capital amongst the leaders in our peer group.

This concludes our prepared remarks. I would now like to turn the call over to the operator for questions.

QUESTIONS AND ANSWERS

Operator

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

Shaun Calnan ***BofA Merrill Lynch, Research Division - Research Analyst***

This is actually Shaun Calnan, on for Mike. Just on the transition, given Terry's extensive background in M&A, should we expect less acquisition activity in the near term, as Mike transitions into the new role?

David Brown ***Victory Capital Holdings, Inc. - Chairman & CEO***

This is Dave. No, Mike has been with us for 14 years and has been involved in really every aspect of the transactions from a sourcing perspective, from an integration perspective, from a closing perspective. I wouldn't at all assume because Terry is moving on that we would change our acquisition philosophy or really how we're positioned in the market to grow inorganically.

Shaun Calnan ***BofA Merrill Lynch, Research Division - Research Analyst***

Okay. And then I just had one on the management fee rate. So it's a little bit more than expected in the quarter, and we're just wondering if that was mostly driven by mix? And if it could potentially recover a bit going into this quarter with the strong to quarter-to-date market?

Terence F. Sullivan ***Victory Capital Holdings, Inc. - CFO & Head of Strategy***

Sure. It's Terry. Yes, I would say that is -- as you think about the fee movement, it is driven by asset mix shift -- that if you think about it, was a bit magnified in the fourth quarter given the volatility. I think it's important to focus on mixed shift versus erosion because that is truly what we're seeing here. It's about the asset classes that we're having momentum in. And I would also say that it is not a permanent movement. We have asset classes, and therefore fees that range quite broadly, as we've discussed in the past. And we have seen and would expect to see momentum in some of those asset classes that higher -- have higher fees, and therefore, could move it in the other direction.

Operator

Our next question comes from Ken Worthington with JP Morgan.

William V. Cuddy ***JP Morgan Chase & Co, Research Division - Analyst***

This is Will Cuddy filling in for Ken. First, Terry it's been great working with you, best of luck in your next role. And Mike, congratulations on the role change. Turning to questions. Could you please provide USAA AUM at the end of the year and the latest available? And based on some of the market movements, how should we be thinking about any potential revisions or expectations for synergy -- sorry, for accretion relative to what you provided in the fall?

Terence F. Sullivan ***Victory Capital Holdings, Inc. - CFO & Head of Strategy***

Sure, it's Terry, Will, and thanks for your kind words and wishes. Let me maybe talk a little bit about, or holistically about, the transaction and the financial update. It's important to consider the framework that we're operating in. Remember we set forth some guidance earlier on, we're more than doubling the AUM revenue and EBITDA of the business. It also is bringing significant diversification and scale, which has driven the strategic and financial thesis and also it's been transformative to our financial profile. Dave mentioned earlier that the business as well as Harvest for that matter are both performing as expected. Obviously, the market volatility has had some impact, but it's not changed the long-term view and thesis that we have both strategically and financially on the acquisitions. In terms of thinking about the numbers, best way to frame it is to, and the way we're thinking about it at least is, it's really a revised starting point on AUM. And so we provide specific guidance around pro forma EBITDA of $420 million. As we look at the markets at the end of the year, we would estimate that, that number has decreased call it 5% to 7%, however, I would note that the recovery in January has been significant and gives us comfort that we're trending well against our overall goals. As it pertains to EPS guidance, we would say that we -- our guidance that we have provided remains unchanged. We're still in the same range. Actually, and probably the numbers have bounced up a few points, just the way the math works, call it the denominator effect where Victory the core existing business has a little bit more exposure to the equity markets relative to the other business.

William V. Cuddy ***JP Morgan Chase & Co, Research Division - Analyst***

Okay, great. And would it be possible a specific AUM number for the end of the year? Or just take the 5% to 7% down?

Terence F. Sullivan ***Victory Capital Holdings, Inc. - CFO & Head of Strategy***

I think you should -- I think that the 5% to 7% to be clear is on EBITDA. And we're not providing guidance on the AUM. We certainly will be back with that information holistically, when we have more information to provide.

William V. Cuddy ***JP Morgan Chase & Co, Research Division - Analyst***

Okay, great. And then turning to some other organizational changes, Mike and Terry could you maybe talk about how you split responsibility, both the Harvest and USAA transactions? How would you characterize your respective focuses on each transaction?

Terence F. Sullivan ***Victory Capital Holdings, Inc. - CFO & Head of Strategy***

Sure. I'll start. It's Terry again, I would say it's complete partnership. As we've talked about in the past, we are -- M&A is a core driver of our business, but we are first and foremost operators of the business. And if you have that foundation, it really makes for a group of executives that work seamlessly across the various elements to come with, with really sourcing, evaluating, diligence and ultimately executing M&A. That starts at the beginning and then carries to announcement. And then after that, that's where in a lot of ways as operators, the real work begins from an integration standpoint, which goes without saying needs to be seamless and fully partnered.

Michael Policarpo ***Victory Capital Holdings, Inc. - COO***

Yes, its Mike. I would add that Terry and I have worked very closely on both the Harvest and the USAA transactions, from the beginning through now through execution, and I think it has been a very seamless partnership where we've worked together.

David Brown ***Victory Capital Holdings, Inc. - Chairman & CEO***

And the last part, it's Dave, is I would say, the organizational change has been thought about and I would say that, we don't see any issues at all and any issues impacting the closing or the integration of Harvest or USAA at all. And we feel very confident about that.

Operator

Our next question comes from Kenneth Lee with RBC Capital Markets.

Kenneth S. Lee ***RBC Capital Markets, LLC, Research Division - Analyst***

Just want to echo my thought, good luck Terry, it's been great working with you and congratulations again Michael. In terms of the Harvest, that you mentioned that there was a drawdown in the fourth quarter, would you be able to sort of quantify that? And maybe remind us again, how the flagship strategies will typically perform in terms of client demand in volatile markets?

David Brown ***Victory Capital Holdings, Inc. - Chairman & CEO***

So let me take the 2 pieces to that question. Let me first say that, our thesis on Harvest, that it is a value-added portion of a well-diversified portfolio has not changed. We're very excited about what Harvest's product set brings to not only our product set, but to clients' product sets, potential clients product sets. Their flagship strategy, and they have multiple strategies, but their flagship strategy performed very similar to what the benchmark is, and how they bench themselves. It did have a slight investment drawdown. They did see some outflows in the fourth quarter, but have recovered very, very nicely in January from a flow perspective as well as from a performance perspective.

Kenneth S. Lee ***RBC Capital Markets, LLC, Research Division - Analyst***

Great. And then in terms of the global and non-U.S. equity flows, you mentioned briefly about strong performance within Trivalent and Sophus. I'm wondering whether there are any particular sizable, institutional inflows that were driving the strength in the flows in the fourth quarter?

David Brown ***Victory Capital Holdings, Inc. - Chairman & CEO***

So we've had several mandates that have been awarded to us with both of those franchises. We did see a sizable mandate won within Sophus. But we're very excited about that asset class. We have really good investment franchises with really good investment performance over the short and long-term. And we've a lot of open capacity there. And as you noted, we've seen positive flows there. And we think that those 2 franchises will be contributing to really our transition to future flow leaders as we think about our organic growth opportunities in the future.

Operator

Our next question comes from Michael Cyprys with Morgan Stanley.

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

Just wanted to see if you can elaborate a bit further on the high quality pipeline that you're seeing. You mentioned some wins were pushed into 2019, if you could help quantify that, talk a little bit about the pipeline on both the institutional side. But also if you could talk a little bit about the retail side, some of the initiatives there with the different channels.

David Brown ***Victory Capital Holdings, Inc. - Chairman & CEO***

Yes, so, it's Dave. Won-but-not-yet-funded accounts, we don't control the timing, obviously the clients do. We've been notified by a number of potential clients that they're going to award us mandates. We've worked through contracts and completed the contracts and awaited, and really are waiting for the clients to award us the dollars. They're significant, and they're with a few franchises, and we anticipate that in the fund within the first half of 2019. They really are not specific to any channel. I would point out that maybe where we've seen the most momentum, is in the sub-advisor channel. We feel that, that's a channel where we have grown and we continue to grow and it happens to be where some of our won-but-not-yet-funded is. On the retail side, for your question on the retail side, we continue to see great progress with our ETFs, with VictoryShares, as we've noted the growth in that part of our business since we bought into the business in 2015. That is integrated into our platform from a sales perspective, from an operational perspective, so it's really part of our business, it's not a separate business. We've seen really good opportunities there. And then I would say, for a number of our franchises in our focused asset classes, U.S. small-cap, we feel like our performance has really driven us to an opportunity to grow in the retail side with those products.

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

Great. And then just a follow up, I think you had mentioned the USAA board had encouraged some of your franchises to provide Asset Management services. Can you quantify how much AUM that has been approved there? And how much you're baking in to your accretion guidance related to that? And just how you're thinking about the opportunities set longer-term for that?

David Brown ***Victory Capital Holdings, Inc. - Chairman & CEO***

So let me start off and say that any of our franchises participating in a multi-manager product and the removal of one of the sub-advisors is really net into our synergies number. So it will -- it's in that $100 million synergy number that we had stated earlier, which is on track and really on time. We don't have a dollar amount, an AUM amount. What was approved was the ability to participate in the multi-manager products, but we don't have a specific dollar amount. As we get closer or as we close, we'll share that with you, but that is not final at this point.

Operator

Our next question comes from Robert Lee with KBW.

Jeffrey Drezner ***Keefe, Bruyette, & Woods, Inc. - Equity Research Associate***

This is Jeff Drezner, on for Robert Lee. I was wondering if you can give us an update on flows for Victory, since the quarter end?

David Brown ***Victory Capital Holdings, Inc. - Chairman & CEO***

We did update for January AUM. We don't update for flows intra quarter. But I would go back to my prepared remarks to say that the operating environment, the flow environment for us has normalized. And I will go back to the comments we said about our pipeline in our won-but-not-yet-funded accounts.

Jeffrey Drezner ***Keefe, Bruyette, & Woods, Inc. - Equity Research Associate***

Okay. And then was just wondering also about expected costs or savings in regards to the move to San Antonio? And how we can think about that?

Terence F. Sullivan ***Victory Capital Holdings, Inc. - CFO & Head of Strategy***

Yes, I would say a couple of things about the relocation. Firstly, reiterate some of the remarks that we made in the January press release about the strategic nature of that development. As it pertains to the financial consequences, I'd say a couple of things. The operating costs associated with the relocation are effectively baked into the $100 million synergy number that we previously disclosed. There's probably an inherent question around tax consequences there as well. And what we'd say right there is that we've done some preliminary work. We do see that there's potential positive impact but again, it's a pretty preliminary and likely marginal as taxes at that level are apportionment driven from a revenue standpoint.

David Brown ***Victory Capital Holdings, Inc. - Chairman & CEO***

Yes and I -- it's Dave. I would add just a few things to that. Victory moving its headquarters to San Antonio is all about the future. It really is going to allow us to cost effectively build out our operational infrastructure, while also really being able to recruit top talent and maintain our talent. The idea of having a city where we can recruit technology people, operational people is we feel really gives us a leg up on the competition to recruit top talent.

Jeffrey Drezner ***Keefe, Bruyette, & Woods, Inc. - Equity Research Associate***

That's helpful. And then just if I can get one more. If there is any way to quantify the pipeline to won-but-not-yet-funded business?

David Brown ***Victory Capital Holdings, Inc. - Chairman & CEO***

We don't quantify, but I'd say that we feel like it's impactful to our flow picture.

Operator

Our next question comes from Chris Shutler with William Blair.

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

So the -- I just wanted to confirm Dave what I think you said, which is that the sub-advisory changes were already in the synergy estimates?

David Brown ***Victory Capital Holdings, Inc. - Chairman & CEO***

Correct.

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

Okay. And then thinking about the M&A pipeline, in a more broad way, I think you said it's still active, but can you talk about how you're thinking about leverage in the current environment? And does having USAA and that direct distribution channel change at all how you think about M&A? In other words, might you be willing to look at some even smaller managers because you can plug them into that distribution network?

David Brown ***Victory Capital Holdings, Inc. - Chairman & CEO***

Let me take -- start off with your last part of your question about M&A and the direct channel. In general, as I said in my prepared remarks, we're still having a lot of conversations, focused conversations. We feel like we're very well-positioned, if not, the best positioned in the industry to take advantage of the consolidation that is happening and we think will intensify as we move forward in the future quarters and years. Our platform, the integrated multi-boutique, as we've spoken to a number of potential partners, really is attractive with what as how the industry is shaping out. The direct channel will allow us to potentially look at smaller managers that could be maybe, in today's -- in our structure today, we would not look at, it will open up maybe some smaller managers that we would speak to, so I would say, yes on that. And as far as the leverage, Terry maybe you want to go through that.

Terence F. Sullivan ***Victory Capital Holdings, Inc. - CFO & Head of Strategy***

Yes, sure. I think in summary, we would tell you that we're comfortable with our overall financing plan and comfortable with our leverage levels, as we do think it optimize -- it's optimized for driving shareholder value. And there's a number of reasons that underpin that view. First of all, as Dave mentioned earlier, the financing is fully committed and secured so from an execution standpoint, we are ready to go and that's important. I'd also point to the pro forma financial profile of this business, the attributes, the diversification. If you think about it then in the context of the fourth quarter, we've effectively we think performed very well in a somewhat stressed environment, which also is important when you think about leverage. The pro forma financials that we will be looking at are -- offer a very powerful free cash flow yield, and when we combine that with our history of deleveraging and the discipline and prudence that we demonstrated there, we think that there's a nice glide path in trajectory from a deleveraging standpoint. We've been accumulating cash as we go towards the months -- through the months -- towards closing, which will also contribute. And if you think about some of the numbers that we're broadly giving guidance on around that $420 million I mentioned earlier, we don't see a material move in the debt-to-EBITDA ratio that we had previously disclosed. And again, we'll see how things evolve. There's obviously a positive tilt in January that bodes well for the future as we march towards closing.

Operator

And I'm showing no further questions at this time. I'd like to turn the call back over to David Brown for closing remarks.

David Brown ***Victory Capital Holdings, Inc. - Chairman & CEO***

Thank you. 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. And 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.