PRICE T ROWE GROUP INC
Form 10-K
February 05, 2015
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UNITED STATES
SECURITIES AND EXCHANGE COMMISSION
Washington, D.C. 20549
FORM 10-K
ANNUAL REPORT PURSUANT TO SECTION 13 OF THE SECURITIES EXCHANGE ACT OF 1934
For the fiscal year ended December 31, 2014
Commission file number 000-32191
T. ROWE PRICE GROUP, INC.
(Exact name of registrant as specified in its charter)

Maryland	52-2264646
State of incorporation	IRS Employer Identification No.

100 East Pratt Street, Baltimore, Maryland 21202
Address, including zip code, of principal executive offices
(410) 345-2000
Registrant’s telephone number, including area code
Securities registered pursuant to Section 12(b) of the Act:

Common stock, $.20 par value per share	The NASDAQ Stock Market LLC
(Title of class)	(Name of exchange on which registered)

Indicate by check mark if the registrant is a well-known seasoned issuer, as defined in Rule 405 of the Securities Act. [X] Yes [ ] No
Indicate by check mark if the registrant is not required to file reports pursuant to Section 13 or Section 15(d) of the Act. [ ] Yes [X] No
Indicate by check mark whether the registrant (1) has filed all reports required to be filed by Section 13 or 15(d) of the Securities Exchange Act of 1934 during the preceding 12 months, and (2) has been subject to such filing requirements for the past 90 days. [X] Yes [ ] No
Indicate by check mark whether the registrant has submitted electronically and posted on its corporate website every Interactive Data File required to be submitted and posted pursuant to Rule 405 of Regulations S-T during the preceding 12 months. [X] Yes [ ] No
Indicate by check mark if disclosure of delinquent filers pursuant to Item 405 of Regulation S-K is not contained herein, and will not be contained, to the best of registrant's knowledge, in definitive proxy or information statements incorporated by reference in Part III of this Form 10-K or any amendment to this Form 10-K. [X]
Indicate by check mark whether the registrant is a large accelerated filer, an accelerated filer, a non-accelerated filer, or a smaller reporting company. See the definitions of “large accelerated filer,” “accelerated filer” and “smaller reporting company” in Rule 12b-2 of the Exchange Act.

Large accelerated filer	[X]	Accelerated filer	[ ]
Non-accelerated filer	[ ]	Smaller reporting company	[ ]

Indicate by check mark whether the registrant is a shell company (as defined in Rule 12b-2 of the Act). [ ] Yes [X] No
The aggregate market value of the common equity (all voting) held by non-affiliates (excludes current executive officers and directors) computed using $84.41 per share (the NASDAQ Official Closing Price on June 30, 2014, the last business day of the registrant’s most recently completed second fiscal quarter) was $21.6 billion.
The number of shares outstanding of the registrant's common stock as of the latest practicable date, February 3, 2015, is 260,726,853.
DOCUMENTS INCORPORATED BY REFERENCE: In Part III, the Definitive Proxy Statement for the 2015 Annual Meeting of Stockholders to be filed pursuant to Regulation 14A.
Exhibit index begins on page 57.

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PART I

Item 1. Business.

T. Rowe Price Group, Inc. is a financial services holding company that provides global investment management services through its subsidiaries to individual and institutional investors in the sponsored T. Rowe Price mutual funds distributed in the United States and other investment portfolios. These other investment portfolios include separately managed accounts, subadvised funds, and other sponsored investment portfolios, including collective investment trusts, target-date retirement trusts, Luxembourg-based funds offered to investors outside the United States, and portfolios offered through variable annuity life insurance plans in the U.S.

The late Thomas Rowe Price, Jr., founded our firm in 1937, and the common stock of T. Rowe Price Associates, Inc. was first offered to the public in 1986. The T. Rowe Price Group corporate holding company structure was established in 2000.

We derive the vast majority of our consolidated net revenue and net income from investment advisory services provided by our subsidiaries, primarily T. Rowe Price Associates and T. Rowe Price International Ltd. Our revenues depend largely on the total value and composition of assets under our management. Accordingly, fluctuations in financial markets and in the composition of assets under management impact our revenues and results of operations. At December 31, 2014, we had $746.8 billion in assets under management, including $477.6 billion in the Price funds and $269.2 billion in other investment portfolios.

Our assets under management are accumulated from a diversified client base across four primary distribution channels: third-party financial intermediaries that distribute our managed investment portfolios in the U.S. and other countries; individual U.S. investors on a direct basis; U.S. defined contribution retirement plans; and institutional investors globally. As of December 31, 2014, nearly forty-five percent of our assets under management are sourced from our third-party financial intermediary distribution channel with the remaining three distribution channels comprising the balance. We have taken steps to broaden and deepen our distribution reach in overseas markets and with financial intermediaries. These initiatives are part of multi-year plans designed to further diversify our assets under management and client base. In 2014, we made key hires and continued to make investments in infrastructure to support these initiatives over the long-term.

The assets we manage are a broad range of U.S. and international stock, blended asset, bond, and money market mutual funds and other investment portfolios that are designed to meet the varied and changing needs and objectives of individual and institutional investors. Investors select mutual funds based on the distinct objective that is described in each fund’s prospectus and can exchange balances among the funds as permitted when economic and market conditions and their investment needs change. The investment objectives and investment management approaches employed in our other investment portfolios are similar to those in the Price funds. We also offer specialized advisory services, including management of stable value investment contracts and a distribution management service for the disposition of equity securities our clients receive from third-party venture capital investment pools.

Investment objectives for our managed investment portfolios, including the Price funds, accommodate a variety of strategies. Equity investment strategies may emphasize large-cap, mid-cap or small-cap investing; growth, value or core investing; and U.S., global, multi-regional and regional international, emerging market, and sector investing. Our fixed income strategies may focus on high yield, U.S. taxable bond, taxable low-duration, international, and municipal tax-free investing. We also combine strategies across asset classes to create solutions that help our clients achieve a single investment objective. To this end, we offer systematic, tax-efficient, blended equity, and asset allocation investment strategies, including target-date retirement investment portfolios.

We employ fundamental and quantitative security analysis in the performance of the investment advisory function through substantial internal equity and fixed income investment research capabilities. We perform original industry and company research using such sources as inspection of corporate activities, management interviews, company-published financial and other information, financial newspapers and magazines, corporate rating services, and field checks with suppliers and competitors in the same industry and particular business sector. Our research staff operates primarily from offices located in the U.S. and England with additional staff based in Australia, Hong Kong, Japan, and Singapore. We also use research provided by brokerage firms and security analysts in a supportive capacity and information received from private economists, political observers, commentators, government experts, and market analysts. Our securities selection process for some investment portfolios is based on quantitative analysis using computerized data modeling.

From time to time, we introduce new funds and other investment portfolios to complement and expand our investment offerings, respond to competitive developments in the financial marketplace, and meet the changing needs of our investment advisory clients. We will introduce a new investment strategy if we believe that we have the appropriate investment

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management expertise and that its objective will be useful for investors over a long period. Since the beginning of 2014, we have launched three new equity products—Asia Opportunities, Frontier Markets, and International Concentrated Equity—and three new fixed income products—Dynamic Global Bond, Credit Opportunities, and Intermediate Tax Free High Yield. Two additional fixed income products were opened in January 2015. We typically provide seed capital for the new investment portfolio to enable the portfolio manager to begin building an investment performance history in advance of the portfolio receiving sustainable client assets. The length of time we hold our seed capital investment will vary for each new investment portfolio as it is highly dependent on how long it takes to generate cash flows into the portfolio from unrelated investors. We attempt to ensure that the new investment portfolio has a sustainable level of assets from unrelated shareholders before we consider redemption of our seed capital investment in order to not negatively impact the new investment portfolio's net asset value or its investment performance record. At December 31, 2014, approximately 39% of our investments in sponsored portfolios and other investments is considered seed investments.

Conversely, we may also limit new investments into a mutual fund or investment strategy in order to maintain the integrity of the investment strategy and to protect the interests of its existing fund shareholders and investors. At present, the following mutual funds and affiliated other investment portfolios are closed to new investors.

Fund	Date Closed
Institutional Mid-Cap Equity Growth Fund	December 8, 2003
Mid-Cap Growth Fund	May 31, 2010
Mid-Cap Value Fund	May 31, 2010
High Yield Fund	April 27, 2012
Institutional High Yield Fund	April 27, 2012
Institutional Small-Cap Stock Fund	December 31, 2013
New Horizons Fund	December 31, 2013
Small-Cap Stock Fund	December 31, 2013
Capital Appreciation Fund	June 30, 2014

We also provide certain administrative services as ancillary services to our investment advisory clients. These administrative services are provided by several of our subsidiaries and include mutual fund transfer agent, accounting, distribution, and shareholder services; participant recordkeeping and transfer agent services for defined contribution retirement plans investing in our sponsored mutual funds; recordkeeping services for defined contribution retirement plans investing in mutual funds outside the T. Rowe Price complex; brokerage; and trust services. Substantially all of our administrative and distribution and servicing fee revenues in 2014 were determined based generally on the recovery of our related costs to provide these services. Therefore, changes in our administrative fees, distribution and servicing fees, and related expenses generally do not significantly affect our net operating income or net income.

In 2014, we made a long-term strategic decision to change our delivery of certain administrative services, including fund accounting and other investment recordkeeping operations. We are currently in negotiations with BNY Mellon to perform these services. If a formal agreement is reached, we do not expect that the impact on our future operating results will be material.

2014 DEVELOPMENTS.

U.S. equities, as measured by the S&P 500 Index, rose in 2014 for the sixth consecutive year. The S&P 500 Index and the NASDAQ Composite Index, which is heavily weighted in technology companies, returned 13.7% and 13.4%, respectively, in 2014. Equities in developed non-U.S. markets declined in dollar terms in 2014, as a stronger U.S. dollar versus other currencies reduced overseas returns to U.S. investors. Emerging markets equities, in aggregate, declined in dollar terms but held up better than developed non-U.S. markets. Global bonds produced mostly positive returns in 2014.

Our 2014 results include net revenues of nearly $4.0 billion, net income of $1.2 billion, and diluted earnings per share of $4.55, an increase of 16.7% from the $3.90 per share earned in 2013. Investment advisory fees earned in 2014 are up 14.6% over 2013 as average assets under our management increased $90.9 billion, or 14.3%, to $724.7 billion. The average annualized fee rate earned on our assets under management was 47.8 basis points during 2014, virtually unchanged from the 47.7 basis points earned in 2013.

Six Price funds - Growth Stock, Equity Income, Mid-Cap Growth, Blue-Chip Growth, Value, and Capital Appreciation - accounted for 27% of our investment advisory revenues in 2014, and 23% of our assets under management at December 31,

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2014. Our largest client account relationship apart from the Price funds is with a third-party financial intermediary that accounted for about 4% of our investment advisory revenues in 2014.

Assets under management ended 2014 at a record $746.8 billion, an increase of $54.4 billion from the end of 2013. Market appreciation and income, net of distributions not reinvested, added $50.7 billion and net cash inflows added $3.7 billion in assets under management during 2014. Net cash inflows of $11.8 billion into the Price funds were partially offset by net cash outflows of $8.1 billion from our other investment portfolios. These net cash outflows were primarily from a few institutional and subadvisory clients who redeemed significant amounts from a small number of equity and fixed income strategies. The mutual fund and other investment portfolio 2014 cash flow amounts are each presented net of $5.3 billion in assets clients transferred from the mutual funds to other sponsored investment portfolios during the year, primarily our target-date retirement trusts.

Our target-date retirement funds and trusts, which provide shareholders with single, diversified portfolios that invest in underlying T. Rowe Price funds and T. Rowe Price collective investment trusts, continue to be a significant source of our asset growth. In 2014, our net cash flows include $17.7 billion that originated in these portfolios, including $13.2 billion in our target-date retirement funds.

Details of our assets under management (in billions) at December 31, 2014, are as follows:

Assets under management by investment portfolio	
Sponsored U.S. mutual funds	$477.6
Other investment portfolios	269.2
Total	$746.8
Assets under management by mandate	
U.S. stocks and blended asset	$496.9
International stocks and blended asset	83.0
Total stock and blended asset portfolios	579.9
U.S. fixed income	149.5
International fixed income	17.4
Total fixed income portfolios	166.9
	$746.8
Assets under management by account type	
Retirement accounts and variable annuity portfolios	$511.2
Other	235.6
	$746.8

Our target-date retirement portfolios account for 19.9% of our managed assets at December 31, 2014, compared with 17.5% at the end of 2013. The assets under management in these portfolios totaled $148.5 billion at December 31, 2014, including $126.0 billion in target-date retirement funds and $22.5 billion in target-date retirement trusts.

Non-U.S. dollar denominated securities held in client accounts are $100.7 billion, or 13.5% of our total assets under management at December 31, 2014. Investors domiciled outside the U.S. represent 5.6% of total assets under management at the end of 2014. We service clients in 36 countries around the world.

Investment Performance.

Strong investment performance and brand awareness is a key driver to attracting assets and to our long-term success. As of the end of 2014, 74% of the T. Rowe Price U.S. mutual funds across their share classes outperformed their comparable Lipper averages on a total return basis for the three-year period, 80% outperformed for the five-year period, 88% outperformed for the 10-year period, and 73% outperformed for the one-year period. In addition, T. Rowe Price stock, bond and blended asset funds that were given an overall rating of four or five stars from Morningstar at December 31, 2014, account for 82% of the assets

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under management in our rated funds. The performance of our institutional strategies against their benchmarks was substantially similar. Our target-date retirement funds continue to deliver very attractive long-term performance, with 100% of these funds outperforming their comparable Lipper averages on a total return basis for the three- and five-year periods ended December 31, 2014.

Capital Resources.

At December 31, 2014, we remain debt-free with substantial liquidity and resources, including cash and fund investment holdings of $3.4 billion. During the full year of 2014, we expended $415.5 million to repurchase 5.3 million shares of common stock. We generally repurchase shares of our common stock over time to offset the dilution created by our equity-based compensation plans. We presently plan to declare and pay quarterly cash dividends in 2015 that, taken together, will exceed the $1.76 per share in annual regular dividends declared and paid in 2014; however, there can be no assurance that we will continue to pay dividends at increasing rates or at all.

We also invested $126 million during the year in capitalized technology and facilities from existing cash balances. We currently expect total capital expenditures for facilities, equipment, and technology development for 2015 to be up to $175 million, which will be funded from operating resources.

Our substantial liquidity and resources also allow us to take advantage of attractive growth opportunities; invest in key capabilities, including investment professionals, technologies, and new investment strategy offerings; and, most importantly, provide our clients with strong investment management expertise and service both now and in the future. In the coming years, we expect to increase funding for long-term initiatives to sustain and deepen our investment talent, expand capabilities through enhanced technology, and broaden our distribution reach globally.

Additional information concerning our revenues, results of operations and total assets, and our assets under management during the past three years is contained in the Management's Discussion and Analysis of Financial Condition and Results of Operations in Item 7 of this Form 10-K as well as our consolidated financial statements, which are included in Item 8 of this report.

PRICE FUNDS.

We provide investment advisory, distribution, and other administrative services to the Price funds under various agreements. Investment advisory services are provided to each fund under individual investment management agreements that grant the fund the right to use the T. Rowe Price name. The boards of the respective funds, including a majority of directors who are not interested persons of the funds or of T. Rowe Price Group (as defined in the Investment Company Act of 1940), must approve the investment management agreements annually. Fund shareholders must approve material changes to these investment management agreements. Each agreement automatically terminates in the event of its assignment (as defined in the Investment Company Act) and, generally, either party may terminate the agreement without penalty after a 60-day notice. The termination of one or more of these agreements could have a material adverse effect on our results of operations. Independent directors and trustees of the Price funds regularly review our fee structures.

Advisory Services.

Investment advisory revenues earned from the Price funds are determined daily based on the net assets managed in each fund. The advisory fee paid monthly by each of the Price funds is computed on a daily basis by multiplying a fund's net assets by its effective fee rate. Details of each fund's fee arrangement are available in its prospectus.

For the majority of the Price funds, the fee rate is equal to the sum of a tiered group fee rate plus an individual fund rate. The tiered group rate is based on the combined net assets of nearly all of the Price funds. If the combined net assets of these Price funds exceed $400 billion, the weighted-average fee across pricing tiers is 29.5 basis points for the first $400 billion of net assets plus 27.5 basis points for net assets in excess of $400 billion. To the extent that the combined net assets of the funds included in the group rate calculation increase, the group charge component of a fund's advisory fee rate and the resulting advisory fee rate paid by each fund will decrease.

The individual fund rates are generally flat rates that are set based on the fund’s specific investment objective. Several funds, including the Blue Chip Growth, Equity Income, Growth Stock and Mid-Cap Growth funds, have an effective tiered individual fund rate in which their base individual flat rate is reduced by about 15% on net assets in excess of $15 billion. The New Income and Value funds have their base individual flat rate reduced by about 20% on net assets in excess of $20 billion. The effective fee rates for the stock and bond funds on which we earned annual advisory fees of at least $6.0 million in 2014 varied

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from a low of 39 basis points for the Maryland Tax-Free Bond, Tax-Free Short-Intermediate, and Short-Term Bond funds to a high of 104 basis points for the Emerging Markets Stock, International Discovery, and Latin America funds.

The fee rate of several of the Price funds, including the Index and Summit funds as well as specific funds offered solely to institutional investors, do not include a group fee component but rather an individual fund fee or an all-inclusive fee. An all-inclusive fee covers both the investment management fee and ordinary operating expenses incurred by the fund. Each of the funds in the series of Spectrum Funds and in the series of target-date retirement funds that we offer invests in a diversified portfolio of other Price funds and has no separate investment advisory fee; rather, they indirectly bear the expenses of the funds in which they invest.

Each Price fund typically bears all expenses associated with its operation and the issuance and redemption of its securities. In particular, each fund pays investment advisory fees; shareholder servicing fees and expenses; fund accounting fees and expenses; transfer agent fees; custodian fees and expenses; legal and auditing fees; expenses of preparing, printing and mailing prospectuses and shareholder reports to existing shareholders; registration fees and expenses; proxy and annual meeting expenses; and independent trustee or director fees and expenses.

We usually provide that a newly organized fund’s expenses will not exceed a specified percentage of its net assets during an initial operating period. Generally, during the earlier portion of the period, we will waive advisory fees and absorb other mutual fund expenses in excess of these self-imposed limits. During the latter portion of the period, we may recover some or all of the waived fees and absorbed costs, but such recovery is not assured.

In 2014, we continued to voluntarily waive advisory fees and other fund expenses of all of our money market funds and trusts in order to maintain a positive yield for investors. Total fees waived in 2014 were $58.4 million, or about 2% of total investment advisory revenues earned during the year, compared to $51.2 million in 2013. We expect that these fee waivers will continue in 2015.

Assets under Management.

At December 31, 2014, assets under our management in the Price funds aggregated $477.6 billion, an increase of 9.7% or $42.3 billion from the beginning of the year. The following table presents the net assets (in billions) and the year of formation of our largest Price funds (net assets in excess of $1.0 billion at December 31, 2014) at December 31.

	2013	2014
Stock and blended asset funds:		
Balanced (1991)	$3.7	$3.9
Blue Chip Growth (1993)	22.8	26.4
Capital Appreciation (1986)	19.1	22.9
Dividend Growth (1992)	4.1	4.6
Emerging Markets Stock (1995)	7.1	7.6
Equity Income (1985)	29.5	29.8
Equity Index 500 (1990)	20.2	24.4
European Stock (1990)	1.5	1.4
Global Technology (2000)	1.0	1.6
Growth & Income (1982)	1.5	