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PRESENTATION

Operator

Good morning. I would like to welcome everyone to the Focus Financial Partners 2021 Third Quarter Earnings Call.

Joining today's call are Rudy Adolf, Founder and CEO; Jim Shanahan, Chief Financial Officer; Rusty McGranahan, General Counsel; and Tina Madden, Head of Investor Relations and Corporate Communications. Mr. McGranahan, please go ahead.

John Russell McGranahan - *Focus Financial Partners Inc. - General Counsel & Corporate Secretary*

Good morning, everyone. Before we begin, let me remind you that during the course of this call, we may make a number of forward-looking statements. We call your attention to the fact that Focus' results may, of course, differ from these statements. These statements are based on assumptions made by and information currently available to Focus Financial Partners and involve risks and uncertainties that could cause the results of Focus to materially differ from these statements. Focus has made filings with the SEC, which list some of the factors that may cause its results to differ materially from these statements, including, without limitation, uncertainties surrounding the COVID-19 pandemic. And finally, Focus assumes no duty and does not undertake to update any such forward-looking statements.

With that, I will turn it over to our Founder and CEO, Rudy Adolf. Rudy?

Ruediger Adolf - *Focus Financial Partners Inc. - Founder, CEO & Chairman*

Thanks, Rusty, and good morning, everyone. We appreciate you joining our call today.

We delivered another strong quarter in Q3, and we are having an exceptional year across every dimension of our business. Our financial performance exceeded our expectations on all measures, positioning us for another record year.

We generated third quarter revenues of $454.5 million, adjusted net income, excluding tax adjustments per share, of $0.84, and tax adjustments per share of $0.14. Our last 12-month cash flow available for capital allocation grew 54.4% year over year, to $299.7 million, reinforcing not only our strong performance, but also the economic value of our tax shield.

Our high-growth business is complemented by a resilient, tax-efficient financial model that has consistently delivered strong results across market cycles. We are also proud that 10 of our U.S. RIA partner firms were recently included in the Barons 2021 list of America Stop 100 RIA firms, with most achieving this ranking for many years in a row, reflecting the consistently high quality of the firms in our partnership.

Our M&A momentum continued to accelerate in the third quarter, as we closed 2 new partner firms and 7 mergers on behalf of our partners, including a merger for connectors in Australia. The first quarter to date, we have closed another 12 transactions and announced 3 that are pending closing. This brings our year-to-date total to 31 transactions, which included 9 new partner firms, 22 mergers for our partners, including 8 mergers for connectors across 4 countries. Our expanding international footprint is an important source of revenue diversification.

Our value proposition continues to resonate strongly, and we are seeing an extraordinary level of potential transactions, both in terms of new partner firms and mergers on behalf of our partners. Connectors also continues to experience significant interest in the U.S. and international. We have a good mix of transactions in our pipeline and are seeing new opportunities to expand our business. Our partnership stood at 79 firms as of November 1. I've never been more excited about the caliber of firms we are attracting. Not only are they industry leaders in their own right, but they further complement and diversify our partnership through their track records of growth, as well as their deep expertise in wealth structuring and client service.

Ancora, Cardinal Point and Ullman, 3 recent partner firms we have closed or announced, are great examples of this. Combined, these -- they oversee approximately 11 billion in client assets, and we anticipate that they will add approximately $60 million in annual revenues and approximately $22.5 million in annual acquired base earnings. Here's a little context on each.

Ancora, which closed October 1, is a premier wealth advisory and investment management firm in Cleveland, Ohio, with over $9 billion in client assets. The firm is a scaled wealth manager that has differentiated itself through its diversified service model, which is complemented by an impressive investment team and performance track record spanning more than 15 years. Ancora is particularly well known for its deep investment management expertise, offering its clients an array of proprietary solutions in equity, fixed income, mutual funds and alternative investments.

Cardinal Point, which closed November 1, is a Toronto-based wealth manager with approximately $1.1 billion in client assets. Over more than a decade, Cardinal Point has built a reputation as a leader in cross-border wealth management. The firm addresses the complex needs of clients who are domiciled in both Canada and the U.S. through their highly integrated approach it has developed over time. Cardinal Point brings a unique value proposition to the Focus partnership, enhancing our existing network while also expanding Focus' presence in Canada.

Ullman Wealth Partners, which is expected to close in late first quarter, is an RIA based in Jacksonville Beach, Florida, with approximately $700 million in client assets. Ullman's dynamic, multi-generational principal group make it a preeminent firm to partner with in the attractive Florida market.

Each of these firms, as well as Sonora Investment Management, which closed October 1, joined Focus because we are much more than just financial acquirers. We are permanent investors, offering a unique combination of entrepreneurship, growth capital, and value-added services. I've said this before and it is worth reemphasizing. Having Focus as a long-term strategic partner, with the resources, intellectual expertise, and scale advantages that enable our partners to become stronger businesses, grow faster, and serve their clients better is an important competitive distinction.

The value-added services we provide are an essential element of what makes us attractive to their firms to join us. These are services that our partners have specifically identified as a need, and we are working closely with them to build adviser-friendly solutions that leverage our scale and purchasing power. The most recent example of this is trust services. This quarter, we began to offer dedicated trust services under the stewardship of Ted Simpson, who recently joined us to head Focus Fiduciary Solutions, our trust and estates offering for our partner firms and their clients. These services will create a significant opportunity for our partners' advisers to expand and retain multigenerational client assets.

Similar to the approach we took with our cash management and credit solutions, we are leveraging a network of third parties, in this case, advisor-coordinated, independent trustees, who have the scale and expertise to meet the diverse needs of our partners' clients and can do so at highly competitive pricing. That team works on a consultative basis with our partners to develop solutions that are tailored to their client needs.

As we turn our sights to the fourth quarter, I have no question that Focus will continue to generate outstanding business growth and financial performance, driven by the combination of 5 elements. First, we are the market leader in arguably the most attractive segment of financial services. There's no other firm that has our track record in independent wealth management and operates globally with our scale, scope, expertise, and resources. Since our first partners joined us in 2006, we have been at the forefront of the industry, but we are actually just getting started. We are a pure-play partnership, capitalizing on industry consolidation that is in its early innings, a trend that we believe will accelerate further and will characterize this space for the foreseeable future.

Second, our 3 M&A models -- direct partnership at the holding company level, mergers on behalf of our partners, and connectors acquisitions -- comprehensively serve the needs of this industry. And as a result, we are attracting many of the best firms. As such, we expect that we will have a sustained pipeline of high-quality domestic and international M&A opportunities for many years to come.

Third, the continued growth of our partner firms. They are operating as entrepreneurs, but are also benefiting from our value-added services, which are enabled by our unique scale and expertise. Their performance track records demonstrate the caliber of their businesses, which was particularly evident during the onset of the 2020 pandemic crisis. Our third quarter year-over-year organic revenue growth of 28.8% underscores this point.

Fourth, a tax-efficient financial model that derives its stability from its reliance on fee-based and recurring wealth management revenues that are not subject to fee pressure the way the asset management industry is. Our financial model is also CapEx-light, with a highly variable expense base.

And fifth, a prudently managed capital structure, with acquisitions funded by a combination of increased cash flow in low-cost debt, and by selectively using equity consideration for transactions and earnout payments.

With that, let me turn the call over to Jim. Jim?

James Shanahan - *Focus Financial Partners Inc. - CFO*

Good morning, everyone, and thank you for joining us today. Our third-quarter results reflect the strong performance of our business, and we have continued to build momentum into Q4. Our partner firms performed well in Q3 and delivered another quarter of strong growth. We have a long track record of acquiring excellent firms that are value accretive, capitalizing on a rapidly growing market that is consolidating quickly. Embracing the entrepreneurship that make these firms industry leaders is central to everything we do, and we provide them with breadth and depth of resources unavailable through any other acquirer in the market.

We manage our business and growth in a disciplined way, and the strength and consistency of our financial performance is a testament to that. We have a substantial market opportunity ahead of us, not just here in the U.S., but internationally as well, which will fuel our expansion for years to come. We have demonstrated success in not only taking advantage of the opportunity set immediately in front of us, but also at identifying where the market is evolving to and adapting our business to capitalize on what the future opportunities will be.

With that, let's turn to the highlights of our Q3 P&L. Our revenues were $454.5 million, up 37.1% year over year, and slightly above the top end of our estimated range of $440 million to $450 million, as organic revenue growth across the partnership was 28.8%, exceeding the 27% high end of our estimate.

Our Q3 adjusted EBITDA was $113.5 million, up 45% year over year. Our adjusted EBITDA margin was 25%, in line with our estimate. We continue to expect that our margins will expand over time, due to the scale-driven operating leverage of our business. Year-to-date September 2021, our adjusted EBITDA margin expanded by approximately 1.8% compared to the prior-year period.

Our adjusted net income, excluding tax adjustments per share, were $0.84, 33.3% higher year over year, which reflected the effect of the incremental interest expense associated with prefunding of our acquisition activity in the second half of this year. As a reminder, we drew down $650 million of our $800 million term loan raise on July 1.

Our tax adjustments per share were $0.14, up 16.7% for a comparable period, reflecting our strong M&A momentum. It is important to note that our tax-efficient structure of M&A transactions continues to provide a significant benefit to shareholders in the form of tax savings, and frees up additional capital for the execution of our acquisition strategy. As of September 30, our gross unamortized tax shield was over $2 billion, the details of which are in our earnings supplement. Almost every acquisition we make increases the value of this tax shield.

Our M&A momentum was strong in Q3, and as Rudy noted, that has continued into Q4. We closed the acquisition of 2 new partner firms, ARS on July 1, and Badgley Phelps on August 1. These 2 firms contributed a total of $5.4 million in revenues and $2.1 million in adjusted EBITDA in Q3, or about 38% in adjusted EBITDA margin. Based on mid-quarter activity, we estimate Q4 full-quarter revenues and adjusted EBITDA of $7.3 million and $2.7 million, respectively, from these closings.

Additionally, Q4 to date, we have closed on 3 additional partner firms and have one signed and pending close, which we estimate will contribute a total of $69 million in annual revenues and $24.9 million in annual adjusted EBITDA, or about 36% in adjusted EBITDA margin. Based on mid-quarter closings, we estimate $15 million in revenues and $5.3 million in adjusted EBITDA in Q4 for these firms.

Now turning to our Q3 expenses and cash flow, management fees were $127.2 million, or 28% of revenues, relatively in line with the prior quarter. Our noncash equity compensation was 1.3% of Q3 revenues, in line with our expectation, and we estimate this expense will also be approximately 1.3% of estimated Q4 revenues. As a reminder, our GAAP results are impacted each quarter by the remeasurement of our earnout liabilities. This remeasurement, which is estimated use in Monte Carlo simulations, resulted in an increase in the noncash change in the fair value of estimated contingent consideration of $36.2 million for Q3, reflecting future growth of our partner firms.

Additionally, in Q3, we also issued approximately 64,700 Class B units in connection with an earnout obligation. As we have said previously, we selectively issue equity in connection with acquisitions and earnout payments.

Regarding cash flow, our LTM cash flow available for capital allocation as of September 30 was $299.7 million, 54.4% higher year over year, reflecting the growth of our partnership, as well as the addition of 10 new partner firms and 21 mergers during this LTM period. We paid cash earnout obligations of $33.7 million, in line with our Q3 estimate. We anticipate that we will pay cash earnouts of approximately $35 million in Q4.

Now for a quick review of our Q4 expectations. We estimate that our Q4 revenues will be in the range of $475 million to $485 million. We estimate a Q4 organic revenue growth rate of 17% to 20%. Our Q4 expectations also reflect the contributions of new partner firm additions.

We anticipate that our Q4 adjusted EBITDA margin will be approximately 25%. As I've mentioned previously, we will update our long-term adjusted EBITDA margin target at our Investor Day on December 9, as part of our overall review of our business strategy and long-term growth targets.

Now for a few comments on our balance sheet. We ended Q3 with approximately $2.3 billion of debt outstanding and a net leverage ratio of 3.54x, in line with our Q3 estimate. Assuming markets stay constant at current levels, we anticipate that our Q4 net leverage ratio will be between 4x and 4.25x. We remain committed to our net leverage ratio range of 3.5x to 4.5x, which we believe is the most appropriate range, given the highly acquisitive nature of our business.

To close, we continue to deliver strong growth and financial performance in Q3, and we anticipate that this will continue into 2022 and beyond. We are uniquely positioned to benefit from the large and growing independent wealth management industry, which according to an investment report, stood at approximately $6 trillion in 2019 in the U.S. alone and is expected to grow to $9 trillion by 2024, expanding at a compound annual growth rate of 10%. According to several sources, the addition of international markets, just in the countries we're invested in, adds another approximate $4 trillion to this total.

It bears repeating and their Focus is a pure-play investor in the growth and consolidation of this industry globally. No other acquirer in this space, public or private, offers our track record and value proposition, which is supported by the benefits of permanent capital investment, or has anywhere near our scale. It takes time to build these capabilities, and we have a distinct first-mover advantage. Taken together, all of these attributes contribute to outstanding and sustained financial performance, industry-leading growth, and enduring competitive differentiation that creates sustained long-term value for their shareholders.

With that, let me turn the call over to the operator for Q&A. Operator?

QUESTIONS AND ANSWERS

Operator

(Operator Instructions) Our first question is from Owen Lau with Oppenheimer.

Kwun Sum Lau - *Oppenheimer & Co. Inc., Research Division - Associate*

Could you please talk about the outlook for acquisitions, and how would the potential change in tax rate impact the pace of your M&A?

Ruediger Adolf - *Focus Financial Partners Inc. - Founder, CEO & Chairman*

Owen, thanks for your question. Yes, as we said, the overall pipeline could not be stronger. We are very pleased with both quality, the diversity, the -- both domestic and international -- probably working on more deals than I can ever remember that we have. And yes, tax may, may not have some implication here in the U.S. -- obviously, has no implication in international. But let's always keep in mind that the fundamental driver of industry consolidation, the fundamental driver of the -- ultimately, our acquisition business -- is really the aging of the founders and the founding generation. You have heard the statistic before: 50,000 advisers just in the U.S., 65 years and older, managing $3 trillion in client assets. Yes, these forces are so much stronger than just taxes here or there, so we have no question that our momentum in next year and in the years after is going to continue to be very, very strong.

Kwun Sum Lau - *Oppenheimer & Co. Inc., Research Division - Associate*

Got it. That's very helpful. And then, Rudy, you touched on cash and credit program, and also, the new trust services. Could you please give us a little bit more color on these value-added services? Any numbers you can give it out? And then, any other potential value-added services you think could be material longer term?

Ruediger Adolf - *Focus Financial Partners Inc. - Founder, CEO & Chairman*

Yes. Yes. So we have pretty much the type of services that we want to offer. It's now about depth, deeper penetration, increasing sophistication, increasing scale and purchasing power in all the services that we are offering. Maybe there's one or 2 others that we can think of, but I think we have what we need.

Cash credit continues to be a very successful program. We have participated, consultative advice to help with the closing of $2 billion in transactions here since program inception. And we view this as just using the scale, the aggregate scale of our organization, using our purchasing power to create better solutions than any of our partners, or quite frankly, anybody in the industry could provide for the end client and for our partners, so very good momentum.

We announced earlier this year the Orion joint venture, you may remember in the cash and credit area. Just did a conference call with like 500 of their clients, which was, again, very, very successful and well received. Early days, but we believe this is a high differentiation program. Trust, we just launched. It's now about education, and again, lining up the right trust companies to provide preferred solutions for our clients and our partners. We have a very good roster right now, with about 10 of them, both domestic and international, and certainly, early indications are very positive.

The key theme for all of these value-added programs is ultimately about equipping our partners with all the capabilities, all the skills of a high-end private banker, without any of the package. But we are really going beyond the private banker in the sense that we have introduced the concept of open architecture to the high end of the credit market, which certainly, to my knowledge, has never been done before. Yes, you have Quicken Loans and so on in the mass market, but a curated, sophisticated lending solution using a whole number of different banks as preferred providers in passing this through to clients is really a new solution, and we are very pleased where we are at this point.

Operator

Our next question is from Alex Blostein from Goldman Sachs.

Alexander Blostein - *Goldman Sachs Group, Inc., Research Division - Lead Capital Markets Analyst*

A question, I guess, on the pace of M&A transactions for you guys, really robust activity over the last several months, several quarters now. When we think about the constraints, the financial constraints, obviously being the leverage, you guys, I think, are guiding to a little bit of a 4x debt-to-EBITDA into the fourth quarter. Not surprisingly, that's ramping, given the old activity. So do you still generally expect to be below 4.5% as a kind of target over year and longer term? And to what extent does that affect kind of the pace of activity? So could we anticipate a moderation as you kind of get into the fours or the other things you're doing that could kind of keep you on a similar pace that we've seen recently?

Ruediger Adolf - *Focus Financial Partners Inc. - Founder, CEO & Chairman*

Yes. Yes. Thanks, Alex. The momentum is just incredible. There's no other way to put it. We have 31 deals announced year to date. And our reality is we were always committed. We are committed to the 3.5% to 4.5% range. That is what we believe the right range for us operating as a public company. And clearly, when you look at our performance last -- sorry, this year, and particularly in the -- or in the second quarter last year, it was always extremely strong, and it demonstrated the resiliency of this business model, so we think 3.5%, 0.5% is the right range.

You have seen already now, but also in a number of future transactions, as we always said, we are willing to use equity. And yes, we have a number of transactions where there's an equity component. In fact, our equities is seen as a very attractive currency these days. And then, of course, as you know, our cash generation is just extremely strong, about $300 million this year, growing at a very, very significant pace. So we believe that we, on the one hand, certainly are not opportunity constrained, meaning that there is so many opportunities out there. But the combination of our cash flow, of course the tax shield, our ability to use equity gives us all the flexibility that we currently need. And as I said, told Owen before, I don't see next year or any of the coming years here some significant change in the pace of M&A, that M&A opportunities that we see.

James Shanahan - *Focus Financial Partners Inc. - CFO*

Just to make -- add to that is we clearly have dry powder with the undrawn term loan and our revolver and so forth. But the cash element continues to grow on an LTM basis, and success begets success, and this cash flow limits our use of leverage for future periods. And then, as we continue to structure transactions in a tax-efficient manner, the tax deductions also shelter the cash flow. So we think the future is bright, and we have great opportunity here with the M&A pipeline, but we'll continue to be prudent in terms of managing our leverage and our guidance.

Alexander Blostein - *Goldman Sachs Group, Inc., Research Division - Lead Capital Markets Analyst*

Great. My second question is around operating leverage dynamics, and I appreciate, Jim, you guys are going to give us updated targets on EBITDA margins at the Investor Day in December. But really just kind of trying to better understand what's going on [underneath the] surface over the last couple of quarters here. So when I look at the sort of EBOC margin, right, so kind of consolidated margin in the business, it's been improving nicely over the last 3 to 4 quarters and kind of goes in line with scaling of your partner firms, so that makes a ton of sense. But then, if I look at the EBITDA margins, it's been coming down a little bit, and that's really just a function of the management fee kind of payout and the expense growing as a percentage of that EBOC number, if you guys kind of follow what I'm saying. So is that a function of the leverage is coming from some of the larger firms and you have less equity in those firms, and therefore, the expense ratio is skewing the wrong way, keeping the EBITDA margins flattish, as opposed to you sort of participating in operating leverage from your management team partners? I'm just trying to kind of better understand the scaling of the affiliates relative to the scaling of Focus.

Ruediger Adolf - *Focus Financial Partners Inc. - Founder, CEO & Chairman*

Yes. Yes. So let me talk about the operating leverage here. So first, just the fundamental trend. In 2015, the EBITDA margin was 19.7%. And yes, Q3, we reported 25.3% EBITDA margin, so the mega trend from a margin improvement kind of couldn't be stronger. And it's really on multiple levels. One is, yes, our partner firms -- and you are correct, really many of the larger partner firms ultimately see margin improvement. And this, then, just translates through our percentage of ownership into our P&L.

But quite frankly, in the small firms, they scale very fast, and we see a partner level operating margin. Quite frankly, our thriving merger business is an important contributor to this. Still a little bit small, but, well, coming exactly with the pace that we expected. Connectors is also going to be a higher-margin business, as we discussed on prior calls.

So again, I wouldn't read too much into quarter-over-quarter trends. I think it's the long-term trend that really matters here. And yes, Jim and I are not ready to give you the numbers. You have to come to Investor Day in December, but we are going to revise our 2025 and beyond margin target upwards. And, well, I'm not ready to give you the number yet, Alex.

Alexander Blostein - *Goldman Sachs Group, Inc., Research Division - Lead Capital Markets Analyst*

Okay. Fair enough. We'll see you in December.

Operator

Our next question is from Kyle Voight with KBW.

Kyle Kenneth Voigt - *Keefe, Bruyette, & Woods, Inc., Research Division - MD*

Could I please ask a follow-up on Alex's question. Rudy, I know you've selectively used equity in transactions in the past, strategically, especially for tax purposes. But I still think a very high percentage of your deals over the past few years have been done with cash consideration. So as you look ahead, and just given the commentary on equity consideration, I'm just wondering if I'm inferring correctly that you're -- are you more willing to use a higher percentage of equity consideration on an ongoing basis now, or am I just -- am I inferring incorrectly there?

Ruediger Adolf - *Focus Financial Partners Inc. - Founder, CEO & Chairman*

Yes, no, Kyle, you're inferring correctly. With cash being so cheap for us at the blended rate of 2.5%, of course, is highly, highly attractive. But then, at the same time, too, we've quite frankly got a lot of flexibility on the equity side. It will be for larger transactions, and we have historically used it for larger transactions. And quite frankly, of course, there's a lot of interest in the equity. And then we have this unique ability, Kyle, where we can issue upstairs equity and where we can use downstairs equity for -- obviously, through our UP-C structure, which actually is a real competitive advantage, because when you have the downstairs equity, again, it's for larger deals. Basically, it's a tax-free exchange on the LSC side, which is very, very unique. And I don't think anybody else can offer in the same format as we can, so it's a very powerful currency.

So yes, you're hearing correctly. From time to time, particularly for larger transactions, we are going to use some of our equity currency options, but the majority will continue to be ultimately cash.

Kyle Kenneth Voigt - *Keefe, Bruyette, & Woods, Inc., Research Division - MD*

Understood. And just a question on the leverage ratio. You've guided to that 4% to 4.25% range by the end of the year, just over 3.5 turns now. I guess when we take into account the organic growth in 4Q, and we also take into account the run rate pro forma EBITDA related to the deals that you've announced that are expected to close in that quarter, we're still struggling to maybe see how there would be more than a half a turn added to the net leverage ratio in the fourth quarter specifically. So I don't know, Jim, maybe you could help us kind of bridge that gap a little bit. Is there anything that we're really missing? And then also, maybe we could get a little more color on recent purchase multiples and if those have changed at all.

Ruediger Adolf - *Focus Financial Partners Inc. - Founder, CEO & Chairman*

Yes, so let me talk about the multiples first, and Jim, you can jump in on the leverage guidance. And obviously, for every quarter, we give very narrow guidance. We have precise guidance, and so we can basically help you with your model there.

But on the multiple side, quite frankly, we like what we see. We always have the ability for very -- for high-quality, fast-growing firms to flex on the upside. Yes, we have -- for smaller firms, for mergers, some of our international deals, we see very attractive multiples. Ultimately, we will give you, again, on Investor Day, an update on the returns that we are generating, and they continue to be very, very attractive, so we are very comfortable where we are. We use the flexibility that we have when we have to, but first and foremost, just look at the quality of the firms that we are bringing in. Thirty-one deals year to date, this is going to be our most successful M&A year, and we expect to achieve, again, very, very attractive returns on the -- on, let's say, the 2021 or what we expect will be the 2022 vintage of partners joining us.

James Shanahan - *Focus Financial Partners Inc. - CFO*

Yes. I think we closed this quarter, Q3, at 3.5x on the net leverage ratio. We've disclosed in the Q we've deployed over $400 million of cash for transactions. We've closed I think 13 transactions already in Q4, and we have a range of 4% to 4.25% is the guidance for Q4 at this time, and we continue to work on transactional activity.

Operator

Our next question is from Craig Siegenthaler with Bank of America.

Craig Siegenthaler;BofA;Managing Director

I just had a question on your alternative investments. I believe your largest L.A.-based affiliate has a pretty robust [wealth] platform, and they're in the process of leveraging their platform to help some of your other partners get brought access to alts. Can you update us on this effort and just see how it's been progressing?

Ruediger Adolf - *Focus Financial Partners Inc. - Founder, CEO & Chairman*

Yes. Yes, absolutely. You're referring to FCS, which is actually a Boston- and L.A.-based firm and New York-based firm. And yes, we certainly believe their alternative program is one of the very best in our industry. It's well above $10 billion, with a terrific track record behind it, so it's about 1/3 of the asset base. And we call the program a portfolio optimization, where we make these solutions from FCS, but also other firms, like Kovitz in Chicago has very high-quality real estate investments, hedge funds and other solutions. And there will be other partners who will have the ability to participate.

So through portfolio optimization, other Focus partners can tap into these programs. The example I used in the past and that's going very well is California-based firm, Vista. It was kind of guinea pig. They are a silicon value-based firm and really were very interested in reaching their investment solutions. And in the moment, they could tap into the FCS program, not just could they broaden their value proposition in ways that they could have never done any other way, because it takes years and years an enormous scale to build a program like this. And quite frankly, it resulted in larger clients converting with larger, by definition, alternative asset percentage of allocations and just a very, very attractive mix that they needed to serve an increasingly ultra-high-net-worth clientele that they are serving.

And we are making this program more broadly available at this point. In fact, we are heading to our partners meeting next week, to our first in-person partners meeting, which is very exciting, actually. And there, we have a pre-session, where all the CIOs of many of our partner firms come together and talk about their unique solutions, and basically, make them available to other partners' firms who may be in interest. And of course, FCS will be one of the future speakers there, and we expect a very high level of interest in what they can offer.

Now here's the important thing, Craig, and thanks for your question. So this is not a distribution model, so this is not what a wire house would do or asset managers, who basically, if you want, push underperforming overpriced products down the throats of their clients. That is absolutely not what we're doing. We are basically creating, simply, access -- access to high-quality solutions, where our partners, at their choice, can access these if they want to. This is very much in the spirit of entrepreneurship and decentralization. But whether it is alternatives, whether it is cash credit, what we discussed before, whether it is trust solutions, multifamily office solutions, valuation programs and other things, they all ultimately are a result of the -- by the standards of this industry -- enormous scale that we have built. And the scale simply creates better outcomes for our partners and for their clients, and alternatives is at the very top of this list.

Craig Siegenthaler;BofA;Managing Director

And maybe Tina will chime in and correct us on this one, but I believe you generally pointed us to a rough client AUM mix of 50-50 equity to bonds, like when we're running stress scenarios. But do you know what the rough mix of client AUM invested in alts is today inside of that mix? I imagine it's probably in that equity side?

Ruediger Adolf - *Focus Financial Partners Inc. - Founder, CEO & Chairman*

Yes. So usually, we are saying between 50% and 55% equities and the balance, noncorrelated. And the alternative component, we don't really break out. But given that we are serving the -- and yes, it would be the non-correlated, that's correct, part of the asset mix. But of course, given that we are serving high-net-worth, ultra-high-net-worth families, the overall level of alternatives is actually pretty high. I mentioned before, FCS is a $30 billion firm. Over $10 billion are alternatives. That probably is one of the highest allocation and it's driven by the sophistication that they have in this area. But from an overall perspective, particularly in this low-yield environment that we are currently in, alternatives are a very important part of serving our clients in a sophisticated way.

Operator

Our next question is from Michael Young from Truist Securities.

Michael Masters Young - *Truist Securities, Inc., Research Division - VP & Analyst*

Wanted to ask just a question on M&A, maybe kind of 2 parts. One, as your AUM base is getting larger, do you plan to run faster with more M&A deals at a similar size or look at larger deals? And then 2, just kind of what are you seeing in terms of interest and demand out there in terms of acquisitions by the 3 buckets? Is there more demand for Connectus or becoming a partner firm, et cetera?

Ruediger Adolf - *Focus Financial Partners Inc. - Founder, CEO & Chairman*

Yes. Yes. Thanks, Michael. So I never believed -- and when you look through Focus' history -- in kind of elephant hunting, the big, flashy deals, we continue to see the biggest opportunity in the north of $1 billion and probably a $5 billion range. Of course, we do to transactions larger, like Ancora was a $9 billion firm.

But yes, first and foremost, we look for firms that simply are aligned with our vision, you want to protect your clients through continuity of advice, you want to have access to value-added services. You want permanent capital, and you want to operate in an entrepreneur way? Quite frankly, Focus the on the game in town, and we are looking for firms where this resonates.

So I don't see us getting into the -- in need or in being it attractive to be in this elephant business, which is the implication of your question, Michael, is, yes, we simply do more deals in our sweet-spot range -- occasionally also some larger deals, occasionally some smaller deals. But we have the largest M&A team in this industry. We are operating on a global scale or in multiple markets. And quite frankly, I have no question that we can, by keeping the mix quite comparable as it has been for a number of years, to basically meet our objectives and stay on the absolute forefront of industry consolidation and, ultimately, creating value to clients and advisers through the scale and sophistication of the model that we have.

Michael Masters Young - *Truist Securities, Inc., Research Division - VP & Analyst*

Okay. And my second question, I don't know if this is a better one for Rudy or Jim. But just, as we think about kind of the macro pressure of inflation and therefore, higher rates headed into potentially 2022 or 2023, I'm just trying to think of how that flows through kind of your business model and any reviews you've done to that effect, particularly as it relates to maybe operating margins and management fees. I'm not exactly sure how those behave kind of in an inflationary environment.

James Shanahan - *Focus Financial Partners Inc. - CFO*

Yes. I think from the revenue standpoint, as we've often said, our revenues are fee-based, recurrent in nature. It's wealth management, holistic service, so we don't have interest revenue as a component. The interest expense is more driven on rates for our P&L, and we constantly evaluate our fixed and variable exposure.

We have $850 million of our term loan is hedged at this point; 648 of it is a 50-floor, so that operating cost is already being incurred. And we'll continue to moderate what the Fed does in terms of the long-term interest rates, but we don't think it's anything significant that will limit our goals at this point.

Ruediger Adolf - *Focus Financial Partners Inc. - Founder, CEO & Chairman*

Yes. And Michael, just strategically, and I said before, just stay tuned. We will update our return numbers at the Investor Day, and they will be very, very strong. And of course, from a pure macro perspective, there should be an inverse relation between interest rates and multiples. And it's the overweighted cost of average -- weighted average cost of capital that, of course, is critical. But then also, what's the returns that you're generating based on the multiples and the growth that you are paying?

So quite frankly, any smaller changes from a macro perspective have very little impact on what we are doing. And if there was some more dramatic changes, that's the power of our business model and this entrepreneurial, decentralized structure that we have. We can adapt to different rate environments, different market environments, extremely fast. And if there's anything we have demonstrated second quarter last year is this business model is just extremely resilient and very flexible to ultimately adjust to just about any reasonable scenario that macro could throw at the business.

Operator

We have reached the end of the question-and-answer session, and I will now turn the call over to Rudy for closing remarks. Rudy?

Ruediger Adolf - *Focus Financial Partners Inc. - Founder, CEO & Chairman*

Yes. Thank you. To conclude, I'm extremely proud of the level of growth and momentum our business is achieving. We are firing on all cylinders, and our results this quarter are reflective of that. This outcome could not have been possible without our partner firms, who continue to perform exceptionally well, deliver outstanding service to their clients, and define leadership in this industry.

It would also not have been possible without our holding company team. We have said many times that we have the best team in every facet of our business, and our results this quarter are again reflective of that.

We're extremely well positioned, not only for a strong finish to -- in our second quarter, but also to deliver strong, sustained growth and execution for years to come. We look forward to telling you more about that at our Investor Day on December 9. And many of our partner firms will be there, as well as they will -- there's no better way than they conveying the Focus story, and we are very much looking forward to seeing many of you at Investor Day. Thank you all for your interest.

Operator

This concludes today's conference, and you may disconnect your lines at this time. Thank you for your participation.