To Our Shareholders

The Moment of Truth for Active Asset Management

At some point, every industry faces a defining moment—a reckoning that fundamentally alters the market landscape. It’s a way of purging stale business models to make room for the next generation. Those who anticipate and position themselves for the sea change have a chance to survive and even thrive. Those who don’t are relegated to the dustbin of history alongside Eastman Kodak and Blockbuster.

That moment has arrived.
It is time to acknowledge the truth. Long-only active asset management in its current form is no longer a growth industry.

While growth opportunities do exist, particularly in specialized investment strategies, the mass consumption of actively managed long-only products is in secular decline. Investors, disillusioned with the number of high-fee active managers who have failed to deliver outperformance and/or downside protection, continue to shift toward passive index-tracking strategies. Active strategies are also taking a hit as aging baby boomers, who cannot afford significant downside risk, cut back on core equity allocations in favor of lower-risk, income-focused investments and absolute-return strategies.

Coincidentally, barriers to entry are rising as more power is concentrated in the hands of distributor gatekeepers and asset consultants, who continue to cull the number of managers on their recommended lists. Most new investment flows are going to the managers on these lists, producing a small number of big winners. And with the Department of Labor’s proposed fiduciary rule, wealth advisors are focusing more on controlling the all-in cost of financial planning. As a consequence, managers are facing heightened expectations to outperform—and to do it at a lower cost to the investor.

At the same time, the costs for providing these services are rising, putting pressure on margins. Expenses are being driven higher on multiple fronts: an onslaught of new regulations, the consolidation of major distributors, as well as increased spending needs from compliance, distribution, marketing and IT. In addition, distributors are now requiring higher levels of seed capital to initiate and promote new strategies.

These growing headwinds come at a time when the global market environment isn’t exactly cooperating. The equity cycle is maturing, now seven years since the bottom in March 2009. Economic uncertainty is high, market volatility is extreme and weak commodity markets continue to undermine efforts to stoke inflation. Central banks aren’t in a position to be of much help, with monetary policies already at or near maximum accommodation. The result: investor conviction is low, risk aversion is high and the pressure on managers to deliver is through the roof.

Given the difficulties of executing in this environment, not everyone will succeed. Not everyone can be above average, let alone stand out. Many storied firms run by smart people will fall victim to the market’s secular transformation. Yet through the process of elimination and consolidation, managers who are well positioned for the new era should emerge even stronger.

**Who will struggle?**

- Managers who cannot deliver performance—from long-only managers crowded into mega-cap stocks to high-cost hedge funds that aren’t living up to promises of absolute returns
- Large firms weighed down by legacy core style-box strategies, which are especially vulnerable to market-share erosion by passive alternatives
- Small managers who lack the scale to gain market share and who are burdened by increasing regulatory costs and barriers to distribution
- Providers of alternatives or ETFs that try to create greater liquidity than what actually exists in the underlying assets—leaving investors exposed in times of market stress, when liquidity is most important

**Who will succeed?**

- Managers with strong brands and a track record of consistent outperformance
- Specialists focused on inefficient markets or unique strategies with records of high alpha generation
- Companies in the sweet spot: big enough to penetrate growth markets and absorb regulatory costs, yet small enough to see a meaningful impact from select growth opportunities
- Well-managed firms that develop and retain a deep bench of talent, with clear succession planning
- Those with a disciplined but flexible operational strategy that aligns headcount, compensation and other expenses with a volatile organic-growth environment
- Managers with strong and diverse global distribution

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At Cohen & Steers, we see this as a time for bold action. That does not mean radical change—we believe we have the right direction, the right approach and the right people in place to carry us forward. What it does mean is acting with conviction on our strategic plan.

Here is how we plan to do it.

We will continue to build on our strong Real Assets brand. These strategies fulfill a critical yet underserved role in investor portfolios, offering the potential for uncorrelated returns, growing income, inflation protection and capital appreciation.

We will remain focused on specialty asset classes that are well suited to active management, where the strength of our platform offers a distinct competitive advantage. As more investors adopt a core-satellite approach to portfolio construction and manager selection, we believe alternative strategies stand to gain share in asset allocations.

We will investigate opportunities to develop strategies that are both timely and timeless around our core competencies. For example: our low-duration preferred securities strategy for investors seeking income with reduced interest-rate sensitivity; or our opportunistic energy strategy for institutions with a long-term horizon, providing access to discounted assets.

We are committed to raising the bar on performance and consistency, mining all sources of potential alpha and reinvigorating our investment culture on active share. We will not rest on past successes. We will make every effort to improve in areas that don’t live up to our standards. This commitment extends to our thought leadership, presenting high-conviction insights to our clients.

Recognizing that strong investment performance starts with our people, we have made talent development an integral part of our culture and are now in our third year of succession planning.

We will continue to strengthen our global footprint and select distribution outlets. We expect regulation to open up the defined contribution market, which is under-allocated to real assets. In Europe, we have implemented new leadership to address its highly fragmented market. We continue to build on Cohen & Steers’ strong brand presence in Japan and Taiwan, serving markets that are starved for yield and primarily focused on active management. We view the anticipated emergence of active, nontransparent ETFs as a key growth opportunity for the firm in the future.

Every offense needs a stout defense. We have taken steps to strengthen our already strong balance sheet to provide a cushion against volatility and to put us in a position to potentially take advantage of strategic acquisition opportunities.

We will take a hard look at costs we can control. But there are some areas where we refuse to cut corners, such as compliance and client service, which are critical to our reputation and are not open to compromise.

Never in our 30-year history have we shied away from a challenge, and we’re not about to start now. After Cohen & Steers was founded in 1986, it took seven hard years before the market was ready for what we were offering. Through perseverance and conviction, we pressed forward until investors finally came around. By that time, we had established a track record and were positioned as the leader in U.S. REIT investing.

The challenges we face today remind us a lot of those early days. More complex, to be sure. But the principles that guide us are the same. We are confident that Cohen & Steers will be among those to emerge stronger—ready to help investors face the next generation of challenges head on.
2015 Review

Cohen & Steers achieved record revenues of $329 million in 2015, representing a 4.7% increase over $314 million in 2014. Net income attributable to common shareholders was $65 million, or $1.41 per diluted share, compared with $76 million, or $1.66 per diluted share, in 2014. Operating earnings per share were $1.72, versus $1.66 in the prior year. Our operating margin remained consistent year over year at 38.8%. Unrealized losses on our seed investments, primarily in energy-related and commodities strategies, accounted for the difference between operating income and pretax net income.

Assets under management (AUM) totaled $52.6 billion at year end, compared with $53.1 billion a year earlier, while average AUM for the year was $52.7 billion, up from $50.6 billion for 2014. The 1% decrease in ending AUM reflected net outflows of $1.0 billion and market appreciation of $0.4 billion. By contrast, the previous year was defined by sizable market appreciation, which more than offset net outflows. Excluding market appreciation, our −1.8% organic AUM growth in 2015 was an improvement from −4.1% in 2014, aided by 3.6% organic growth in the final quarter—our first quarter of net inflows since the first quarter of 2013. Notably, our pipeline of awarded but unfunded mandates grew to reach $1.35 billion at year end.

Overall, our investment performance was strong, with seven of our ten core strategies outperforming their benchmarks.

In terms of notable core strategy contributions, AUM in our preferred securities strategy increased 21% for the year. This reflected a total return of 7% and net inflows of $1.2 billion. For context, fund flows into preferred securities open-end mutual funds for the entire industry were $1.5 billion in 2015, according to Morningstar. The preferred securities investment team had another excellent year—the strategy outpaced its benchmark for the 12th consecutive year. On the development front, in November, we launched the Cohen & Steers Low Duration Preferred and Income Fund, a pioneer concept that takes a limited-duration approach to an asset class commonly perceived to have high interest-rate sensitivity.

Our U.S. real estate strategy produced a relatively strong return of 6%, outpacing the broader U.S. equity market and significantly outperforming major REIT benchmarks. Despite positive absolute returns and strong relative performance, the strategy had a 2% decline in AUM due to net outflows that were partially offset by appreciation. And while our global/international real estate strategies also outperformed their benchmarks, they had a 7% decrease in AUM, likewise due primarily to net outflows.

Our global listed infrastructure strategy had net inflows of $300 million, but experienced a 10% decline in AUM due to market depreciation. Amid the plunge in oil and natural gas prices, pipeline companies experienced significant declines that overwhelmed generally positive returns in other infrastructure subsectors. Despite the difficult year of performance, institutional adoption of listed infrastructure continued to grow. July saw the launch of Argo Global Listed Infrastructure Limited, an Australian listed investment company that we sub-advised. In September, we launched the Cohen & Steers SICAV Global Listed Infrastructure Fund, a new fund in our series of Luxembourg-domiciled offerings that delivers our listed infrastructure strategy to retail and institutional investors outside the U.S.

For the seventh consecutive year, we increased our regular quarterly dividend, from $0.22 to $0.25 per share, in March 2015. In December, we paid a special dividend of $0.50 per share—the sixth such special dividend in six years, bringing aggregate special dividends over this period to $7.00 per share. We ended the year with a strong balance sheet, with no debt and $143 million in cash and cash equivalents.

In a year marked by growing headwinds for the active asset management industry, Cohen & Steers had many strategic accomplishments. Despite adverse market conditions that challenged our financial performance in 2015, we ended the year with strong momentum. As we look ahead to our 30th anniversary this year, we remain firmly dedicated to executing our vision with conviction, discipline and an unwavering focus on providing value to our clients.

Mark Cohen
Chairman

Robert H. Steers
Chief Executive Officer

Joseph M. Harvey
President